Adam Smith is dead: Africa's future in a neo-mercantilist world

Benedict Oramah
Afreximbank

Richman Dzene
Afreximbank

Introduction

The Group of Seven (G7) industrialised Economies made a significant move recently that could upend globalisation as we know it. The G7 Economies announced new policy measures targeted at some developing countries, including export controls and restrictions, designed to protect G7 domestic industries. These far-reaching actions, part of a broader trend since the turn of the 21st century towards protectionism and economic nationalism, mark the rebirth of mercantilism and could potentially become the coup de grace of internationalisation. This paper discusses the devolving global order from the Adam Smith's prescribed Laissez Faire system to a neo-protectionist and mercantilist system and the possible implications for developing economies, particularly Africa.

A devolving global order

The resurgence of neo-mercantilist policies, a significant evolving swing in the conduct of global trade, can mark the beginning of the death of the reign of free market economic doctrine of Adam Smith (1723–1790), an economist and philosopher and the "father" of modern economics. This shift, which harkens back to 15th-century mercantilism, marks a significant departure from the principles of global cooperation, multilateralism, and free markets that had become the mainstay of global trade policy following the Great Depression and the second world war. These pillars lifted global trade during the second half of the 20th century and facilitated industrialisation and technological advancement in developing economies. Indeed, it is this system, which fostered globalisation and led to the pulling of over 800 million people out of poverty in China. The potential consequences of this shift, therefore, includes an increase in global poverty and a decline in gross domestic product (GDP) growth.

In 1776, Smith's seminal work, The Wealth of Nations, sounded the death knell for mercantilism, arguing that the benefits from trade were not finite but could accrue across multiple countries and parties. This was contrary to the zero-sum game (i.e., one person's gain is another person's loss) and tit-for-tat economic dogma that mercantilists Thomas Mun[1] and others had promoted. In particular, Smith posited that two or more countries engaged in international trade could maximise their benefits if each specialised in the production and export of the goods in which they had an absolute advantage. His works state: "The most advantageous method in which a landed nation can raise up artificers, manufacturers, and merchants of its own is to grant the most perfect freedom of trade to the artificers, manufacturers, and merchants of all other nations" (Smith 1776, 170). Of course, David Ricardo (1817) and others have since refined and developed this fundamental concept.

Between the 14th and 19th centuries, countries conducted trade under zero-sum or beggar-thy-neighbour policies (i.e., mercantilism), with the United Kingdom and France leading the conquest. In these countries, the essence of national policy was to suppress, and dominate other territories while usurping and stockpiling vital resources from them to build local industries for one-sided export trade, thereby ensuring that the balance of trade was permanently favourable to them.

These 17th to 18th-century anti-globalisation tendencies have returned, most visible in the last decades of the 20th century and the beginning of the 21st, and ironically led by advanced economies that were the principal proponents of a free market economy. This marked an obvious reawakening of the discourse and sentiment around dissipation of geopolitical and economic power (see Figure 1). Globalisation and free market trade policies triggered the rapid growth and diffusion of innovations and technological advancements across developing countries in Asia, Latin America, and elsewhere. Its unintended consequence—in the eyes of originators—was the rise of developing and small economies. The World Trade Organisation, founded in 1995, gave the free market an additional boost, providing unbridled market access to many of these economies. Oramah and Dzene (2019) analysed this phenomenon in some detail from the perspective of the trade wars that had emerged between the US and China.

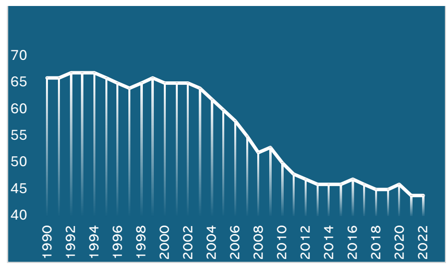

Figure 1: G7 share of Global GDP (%)

The generalised economic progress and wealth creation (i.e., what Smith called "universal opulence") supported the steep decline in global poverty during the last two centuries (figure 2). The proportion of the world's population living in extreme poverty fell from more than 80% in 1820 to less than 20% by 2015 (Beauchamp 2014). Similarly, global GDP per capita rose from US$1,120 in 1820 to US$14,700 in 2015, with most of the significant gains occurring during the period of rapid globalisation and technological advancements in the second half of the 1900s (Hasell et al. 2022) (figure 3).

Most observers wonder why such universal opulence has caused discomfort in parts of the advanced world. The truth is that the free-market system did not entirely wiped out the mercantilist footprints. Industrial policies that prioritised building local industries while restricting foreign competition drove the industrial progress of most advanced economies of the late 1800s and early 1900s,[2] and have, in recent years, regained prominence among developed countries in response to the rise of competition from unexpected places, leading to a badly bruised global system. The gains of globalisation during the 20th century are rapidly eroding, and the economies of countries deeply integrated in global value chains are beginning to slow. GDP per

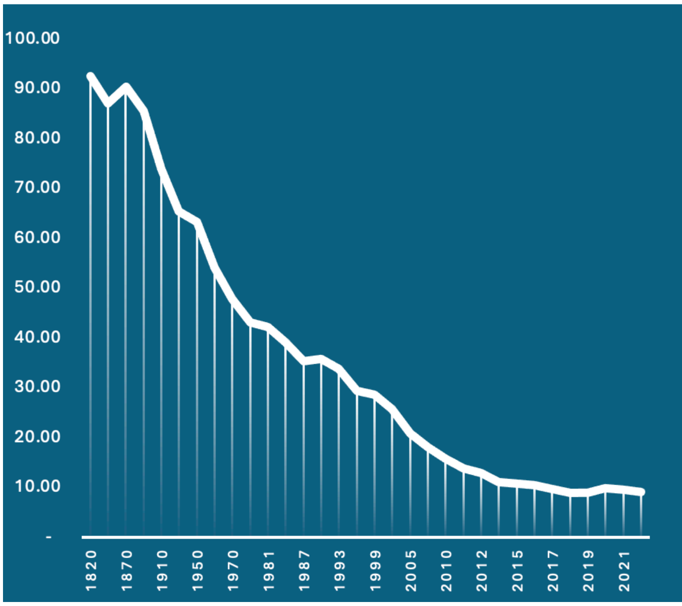

Figure 2: Proportion of the World Population Living in Extreme Poverty (%)
Sources: UNDESA (2015); Madison (2008); World Bank (undated); Hasell et al. (2022)

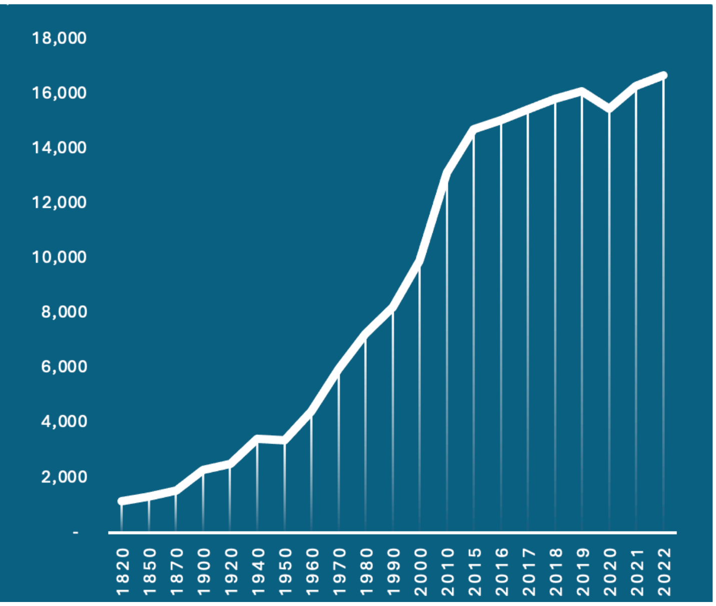

Figure 3: World Per Capita GDF (in current USD)
Source: Hasell et al. (2022)

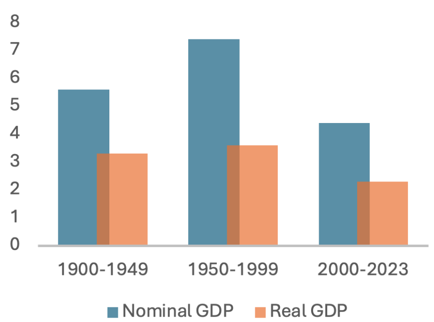

Figure 4: Long Run Global Growth (%)
Source: Economy-GDP-R-By-Decade.pdf (crestmontresearch.com)

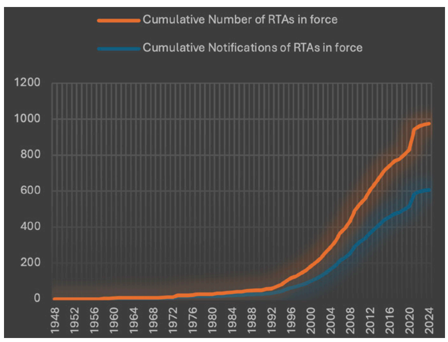

Figure 5: Regional Trade Agreements (Count)
Source: WTO (2024)

Figure 6: Africa's Share of Global Trade (%)

capita seems to be flattening since the 2010s (figure 3). Indeed, the long-run average global economic growth between 2000 and 2023 at 2.3% is much slower than the average of 3.6% seen between 1950 and 1999, the hey days of globalisation (figure 4).

Implications of a changing global order on global growth and development

What will become of a fractured world in the years ahead? Even precise science cannot predict the future in this sense, but history and the current trend toward protectionism suggests a return to a mercantilist system. Experts in geopolitical dynamics, history, and policy suggest that the Ukraine–Russia conflict is merely a proxy war for major powers to showcase their military might, and economic strength given that direct confrontation would be catastrophic. Beyond the slowing wars are fundamental issues of economic and overall global power equilibrium that affects international relations. Proxy wars will likely become pervasive in the decades ahead, as evident in increased military spending and investment between 2022 and 2023. Expansionist militarisation may become an essential weapon for attaining economic supremacy, creating global conflict and instability. This should be a cause for concern and a stark reminder of the importance of global cooperation and the dangers of reverting to mercantilist policies.

Neomercantilism may become pervasive, particularly as the Dispute Settlement Body of the World Trade Organization (WTO) remains in an uncertain state. If this is not resolved, trade retaliatory measures would rise, significantly impacting global trade and investment flows. The UN (2024) reveals a startling rise in the number of antidumping and countervailing duties imposed by WTO members between 2015 and 2021 (up from 600 to about 2,200). China is expected to impose some form of trade restrictive actions on the United States in response to recent tariffs imposed on its exports of electronic vehicles, steel, and medical supplies. [3]The same could happen if the European Union also decides to move in this direction. This alarming shift towards extreme forms of protectionism and isolationism is detrimental to global growth and trade-led innovations and may lead to a stagnation of the global economy.

A rift between or among major economies in this new era will generate shocks that would reverberate beyond their immediate economic confines. Developing countries that have relied on a liberal system as a source of growth and wealth generation will have to find alternative means to propel their economies, underscoring the urgent need for regional cooperation. Regionalism, which assumed some significance in foreign and trade policy circles in the 2000s, will become important again. As the fractures deepen and global supply chains are torn apart, realignment of production and trade partnerships and new forms of collaboration become increasingly important. The WTO received about 508 notifications of regional trade agreements during the first two decades of the 21st century, and 286 are currently in force (WTO 2024) (figure 5). Adam Smith would have frowned upon such bilateral or regional trade treaties as they yield sub-optimal resource allocations, higher prices, lower trade volumes, and limited welfare impacts. However, regional cooperation offers a glimmer of hope, under the emerging neo-mercantilist world providing a path towards economic integration and stability despite a retreat from multilateralism.

In this neo-mercantilist world, investment in technology, research and development innovations, and inventions will determine who wins and who loses. It is worth noting that the terms such as losers and winners abound in this era. The pace of technological diffusion that has accompanied growth in trade and investments has slowed and is expected to falter even further as such transmission links through globalisation are disrupted.

What does a mercantilist system mean for Africa? What should our policy choices be?

How does Africa navigate this maze? The world stage will no longer become a conducive source of growth and development capital for its vulnerable economy. Thus, drawing on lessons from the last few decades will prove useful in its further development. While poverty levels have dipped across the developing world, Africa's share of the global economy, trade, and industrial value-added has plateaued or declined over the last three decades. For instance, Africa's share of global trade fell from about 3.5% to 2.5% between 2012 and 2022 (Figure 6). The same is true for manufactured exports, which have averaged under 1% for the last three and half decades (Figure 6).

Despite benefiting the least from globalisation, Africa remains a strong advocate for global cooperation and is rightfully wary of de-globalisation. Market-driven globalisation has fuelled significant capital flows into Africa and other developing regions for high returns. Data from UNCTAD suggests that the stock of foreign direct investment rose 172 times from US$60 billion in 1990 to US$1.05 trillion in 2022 (UNCTADSTAT, 2024). However, these and other financial flows have hardly supported sustainable and productive sector development. Primarily, such investments have supported commodity extraction and exports, with hardly any linkages to local economies. To achieve change, instead of remaining a milking ground for raw materials and dumping ground of global manufactured goods, African countries should dictate the nature, size, and destination of foreign capital inflows, insisting they be channelled into manufacturing, agricultural, and tech-based industries.

Africa should urgently prepare for its economic transformation by implementing policies that prioritise local value addition and granting transient protection to critical growth industries. These measures should be backed by significant investments and governance structures that support corporate and operational independence. Lessons from prior attempts show that failures mainly result from undue external political influence. Fears of retaliation should not be of major concern; after all, the nature of the new world is shifting as advanced economies kick away the ladder of economic development from developing countries (Chang 2002).

African countries must instigate and determine the nature of the partnerships necessary to support industrial growth and economic transformation, taking advantage of the African Continental Free Trade Agreement established in 2018. Some countries are already doing so. For example, through their partnership with African Export-Import Bank (Afreximbank)—a pan-African multilateral trade finance institution created in 1993 and headquartered in Cairo, Egypt as well as an industrial infrastructure company, Arise Integrated Industrial Platform (Arise IIP) and Africa Finance Cooperation (AFC)—Gabon has transformed from an exporter of raw wood into a continental hub for furniture and wood products, while Benin went from being an exporter of seed cotton to a hub for integrated textiles manufacturing. Industrial complexes operated by Arise IIP and supported by Afreximbank are also beginning to sprout in other parts of Africa, including Botswana, Chad, Cote d'Ivoire, Malawi, Nigeria, and Kenya, among others. It is the outcome of about 2 billion in investments that Afreximbank has made available for towards the development of those industrial complexes.

Investments from Afreximbank, Africa Finance Corporation (AFC), African Development Bank and other regional development finance institutions represent the surest path to breaking the jinx of under-industrialisation on the continent. The expectant delocalisation of labour-intensive manufacturing jobs from Eastern Asia to Africa may be slow, partly because these modern factories now require more capital and skill to build (Economist 2024). However, Africa is well on its way towards achieving results, on the back of the AfCFTA.
Regional cooperation under a free trade agreement or similar arrangement will become necessary, even if sub-optimal substitutes. African governments must build domestic capital and financial markets while diversifying foreign currency reserve holdings. In a mercantilist world, a country's economic strength and resilience can only be backed by precious minerals. The new era of the gold standard may be lurking. Africa presently boasts of about 870[4] tonnes of gold reserves. It must use it to shore up its financial system and the growth of strategic sectors.

Africa must increase its economic resilience under a system that allows for independence and self-reliance. At the recently concluded 31st Annual Meetings of Afreximbank in Nassau—the first in the Caribbean region—participants recognised that a united African people connected around a shared economic vision would thrive, even during global turbulence. They called for the conception and birth of a Global Africa Commission, through which human, material, and natural resources are pooled to build prosperity for all Africans and the world. In a recent statement to the Eurogroup on a Strategy for European Competitiveness in Luxembourg, International Monetary Fund Managing Director Kristalina Georgieva said, "Europe's core strength is the single market: fundamentally, Europe derives its prosperity, its competitiveness, and—yes—its market power from its cohesion." If this is true for Europe, so is it for Africa. Its countries must rally together behind core principles, including promoting shared growth and prosperity and building a strong regional market.

The neo-mercantilist-type of global prospects are not those we should desire in a world that has prospered for several decades through global cooperation. We must return Thomas Mun and his cohorts to their graves and bring back Adam Smith's ideas to our policy pages. In the midst of an ever-changing global order, it is obvious that whether global sanity is restored, or the current fractures deepens, Africa must determine its own future.

References

Maddison, Angus. 2003. The World Economy: Historical Statistics. Vol. 2. Paris: OECD.

Beauchamp, Zach. 2014. "The World's Victory over Extreme Poverty, in One Chart." Vox. December 14, 2014.

Chang, Ha-Joon. 2002. Kicking Away the Ladder: Development Strategy in Historical Perspective. London: Anthem Press.

Economist. 2024. "Will Services Make the World Rich?" Economist.com. https://www.economist.com/finance-and-economics/2024/06/24/will-services-make-the-world-rich.

Hasell, Joe, Max Roser, Esteban Ortiz-Ospina, and

Pablo Arriagada. 2022. "Poverty." OurWorldInData.org. https://ourworldindata.org/poverty.

Hunnicutt, Trevor, Jeff Mason, and David Shepardson. 2024. "New Biden Tariffs on China's EVs, Solar, Medical Supplies due Tuesday – Sources." Reuters. https://www.reuters.com/business/us-set-impose-tariffs-china-evs-certain-strategic-sectors-bloomberg-reports-2024-05-10/.

Oramah, Benedict Okey. 2020. "Export Credit Arrangements in Capital-Scarce Developing Economies." In The Handbook of Global Trade Policy, First Edition, edited by Andreas Klasen. New Jersey: John Wiley & Sons Ltd. https://onlinelibrary.wiley.com/doi/pdf/10.1002/9781119167402.ch19.

Oramah, Dzene (2019) Globalisation and the Recent Trade Wars: Linkages and Lessons https://doi.org/10.1111/1758-5899.12707

Reinert, Sophus A., ed. 2011. Antonio Serra, A Short Treatise on the Wealth and Poverty of Nations (1613). London: Anthem Press. (Translated by Jonathan Hunt.)

Ricardo, David (1817). On the Principles of Political Economy and Taxation. J. Murray. pp. 160–162.

Smith, Adam. 1776. An Inquiry into the Nature and Causes of the Wealth of Nations. London: W Strahan and T Cadell.

UN (United Nations). 2024. Key Statistics and Trends in Trade Policy 2023: The Importance of Unilateral Trade Preferences. UNCTAD/DITC/TAB/2024/2. Geneva: Division on International Trade and Commodities (DITC), UNCTAD Secretariat, UN. https://unctad.org/system/files/official-document/ditctab2024d2_en.pdf.

UNCTAD. UNCTADSTAT, accessed in June 2024

UNDESA (United Nations Department of Economic and Social Affairs). 2015. World Population Prospects: The 2015 Revision, Key Findings, and Advance Tables. Working Paper No. ESA/P/WP.241. Geneva: UNDESA Population Division. http://esa.un.org/unpd/wpp/Publications/Files/Key_Findings_WPP_2015.pdf".

World Bank. Undated. "DataBank, World Development Indicators." https://databank.worldbank.org/source/world-development-indicators#.

WTO (Word Trade Organization). "Regional Trade Agreements Database." Accessed June 23, 2024. https://rtais.wto.org/UI/charts.aspx#.

Endnotes

1. Adam Smith considered Thomas Mun to be the principal architect of mercantilism (https://en.wikipedia.org/wiki/Mercantilism). Other authors such as Friedrich List considered Antonio Serra to have written the first treatise on political economy with A Short Treatise on the Wealth and Poverty of Nations (1619) (Reinert 2011).

2. Export credit agencies were particularly designed to promote industrial and trade dominance by enabling exports into seemingly challenging countries—the Soviet Union at that time—while only facilitating imports of raw materials (Oramah 2020).

3. Announcements of these tariffs were widely reported. New Biden Tariffs on China's EVs, Solar, Medical Supplies due Tuesday - Sources | Reuters (Hunnicutt , Mason, and Shepardson 2024).

4. Africa Gold Advisory, Website of the United States Government, https://www.state.gov/africa-gold-advisory/#post-457135-footnote-2, accessed on November 16,2024.