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Promoting Agriculture, Climate and Trade Linkages in the East African Community

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Briefing Paper

The Continental Free Trade Area: Enhancing Economic Development in Africa

By Elodie Arnell

Summary

Africa is well endowed with a large share of the world's natural resources as well as two thirds of unexploited arable land. Nonetheless, the continent remains a marginal player in global trade, a situation exacerbated by very low intra-African trade. As other regions conclude mega-regional free trade arrangements, and with negotiations at the multilateral level stalling, African countries risk being further marginalized in terms of trade. Accelerating work on the Continental Free Trade Area (CFTA) provides an opportunity for the region to mitigate these risks. This briefing paper discusses merits of the CFTA and its potential to enhance economic development in Africa.

CUTS International GENEVA

PROMOTING AGRICULTURE, CLIMATE AND TRADE LINKAGES IN THE EAST AFRICAN COMMUNITY – PHASE 2

The PACT EAC2 project builds capacities of East African stakeholders for climate-aware, trade-driven and food security enhancing agro-processing development in the region. Web: www.cuts-geneva.org/pacteac2

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Background

The African Union (AU) is comprised of 54 countries of which there are 34 Least Developed Countries (LDCs). It aims to develop a continental integration through six phases as laid out by the Abuja Treaty (1994) The AU succeeded the Organisation of African Unity (OAU). AU's Agenda 2063 for *"The Future we want for Africa"* provides an action plan aimed at ensuring positive socioeconomic transformation within the next 50 years[1].

Despite being endowed with the larger share of natural resources in the world, intra-African trade remains only around 13 percent compared to 60 percent and 40 percent intra-regional trade achieved by Europe and North America, respectively[2].

This briefing paper discusses the potential for economic development through continental integration that would contribute to the structural transformation of Africa leading to inclusive growth and sustainable development.

Regional integration: an African commitment

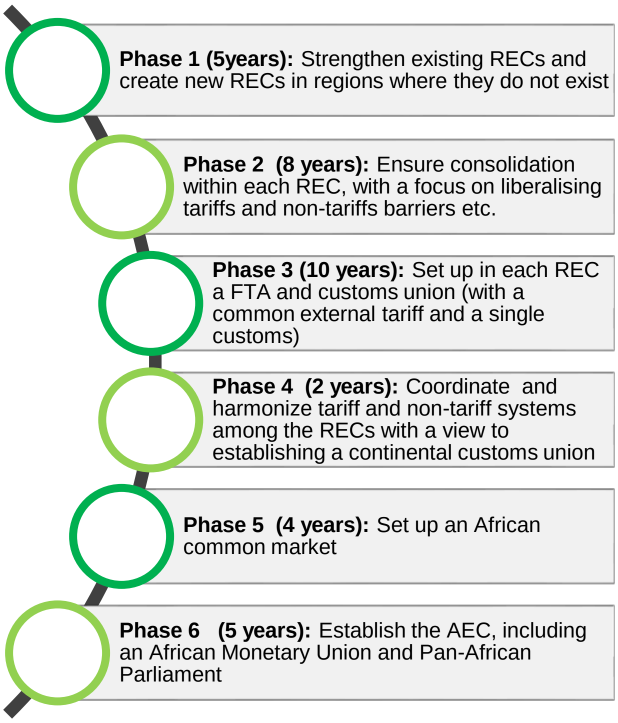
Since the independence of most African nations in the 1960's, regional integration and cooperation has been a development strategy of the continent. This commenced with establishment of the OAU in 1963.

Efforts to integrate the African continent economically go back to the Lagos Plan of Action of 1980, followed by adoption of the Abuja Treaty (1991) that concretized this plan in the form of the African Economic Community (AEC).

The AEC is comprised of six phases (Figure 1) and aims to increase the pace and impact of Africa's development, i.e. improving the living standards of African's, maintaining economic stability, and establishing peaceful relations between member states.

The Abuja Treaty's strategy was to create Regional Economic Communities (RECs) as *building blocks* for the eventual Continental trade block. Currently, there are eight RECs[3] approved by the AU. Ultimately, it's envisaged that the CFTA will lead to reduced poverty and promote regional value chains, as well as integration of African countries in global value chains, in order to contribute to inclusive growth and sustainable development.

Figure 1 : The AU Continental Integration Agenda: the AEC's establishing in 6 phases



Source: Soininen, 2014

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[1] agenda2063.au.int/en//vision
[2] http://www.au.int/en/ti/biat/about
[3] Arab Maghreb Union (AMU, 5 countries), Common Market for Eastern and Southern Africa (COMESA, 19 countries), Community of Sahel-Saharan States (CEN-SAD, 28 countries), East African Community (EAC, 6 countries), Economic Community of Central African States (ECCAS, 11 countries), Economic Community of West African States (ECOWAS, 15 countries), Intergovernmental Authority on Development (IGAD, 7 countries), Southern African Development Community (SADC, 14 countries)

State of play of the CFTA's establishment

Initially, the Abuja Treaty road map did not include the establishment of the CFTA in any of its six stages[4]. However, a Continental Customs Union was expected in Phase 4, through the consolidation of the RECs' Customs Union and the harmonization of their Common External Tariff.

In order to address the lacuna of the Abuja Treaty, in January 2012, in South Africa, the 18th African Union Summit adopted a decision[5] and a declaration[6] *"on boosting intra-African trade and the establishment of the CFTA"* to hasten and deepen the continent's market integration. As of today, Phase 3 (2008-2017) is still ongoing; and the CFTA establishment will help to fulfil it.

African leaders agreed on a roadmap for establishing the CFTA indicatively by 2017 and still recognized the use of RECs as *building blocks.* In June 2015, the Tripartite Free Trade Area (TFTA) agreement was launched; it unites 26 member states of three RECs: EAC, COMESA and SADC. It represents an important step towards the CFTA process and accounts for close to 60 percent of AU's GDP and population.

As reported by the AU, *"the main objectives of the CFTA are to create a single continental market for goods and services, with free movement of business persons and investments, and thus pave the way for accelerating the establishment of the Customs Union. It will also expand intra-African trade through better harmonization and coordination of trade liberalization and facilitation and instruments across the RECs and across Africa in general. The CFTA is also expected to enhance competitiveness at the industry and enterprise level through exploitation of opportunities for scale production, continental market access and better reallocation of resources"*[7]. According to the United Nation Economic Commission for Africa (UNECA) calculation, the CFTA could increase intra-African trade by $35billion, or 52 percent above the baseline of 2017 by 2022. Imports from outside of the continent would decrease by $10billion per year, and agricultural and industrial exports would increase by $4billion (7 percent) and $21billion (5 percent) above the baseline, respectively (Soininen, 2014).

Negotiations of the CFTA will pursue a two-step approach. It will cover: (1) agreements with commercial value on trade in goods and trade in services; and (2) other issues like investment, intellectual property rights, movement of business persons and competition policy (Figure.3). It should also be guided by principles such as: "RECs FTAs building blocks for the CFTA", "flexibility", "special and differential treatment", and "transparency" amongst others. Figure 2 below lists the specific issues to be covered:

Figure 2 : Scope of the CFTA

(1) Trade in goods
• Tariff liberalisation, • NTBs, • Trade facilitation, • Transit & Transit facilities, • Trade remedies, • Safeguards, • Standards, • Technical barriers to trade, • Sanitary and phytosanitary, • Dispute settlement, • Institutional arrangements
Trade in services
• Transportation (Air, Maritime) • Financial Services (banking, insurance) • Tourims • Energy
(2) Other issues
• Competition policy • Intellectual Property Rights • Insvestment • Movement of business persons

Source: Sebahizi, 2016

[4] http://unctad.org/meetings/en/Presentation/ditc-ted-09032016-accra-paper-Fajana.pdf
[5] Assembly/AU/Dec.394 (XVIII)
[6] Assembly/AU/Decl.1 (XVIII)
[7] http://www.au.int/en/ti/cfta/about

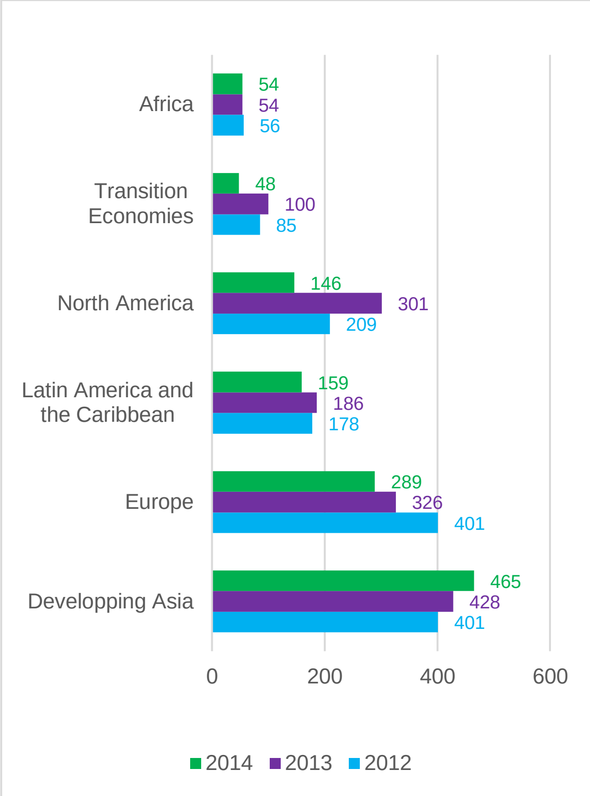
Africa's Trade Scenarios

Given the continents natural resources endowments and vast arable land, the CFTA presents an opportunity to spur the regions agriculture and manufacturing sectors. Agriculture is already the main economic sector for the majority of the African countries. It is the major source of revenue, employment and foreign exchange earner, yet many of African countries are net importers of food and agricultural products (including food aid) from outside Africa. The manufacturing sector largely remains at infant stage with most of capital and high end goods such as machinery, motor vehicles etc. being imported.

According to the Economic development in Africa Report (UNCTAD, 2013), the informal sector is large in African countries; it accounts for 37.6 percent of GDP in Sub-Saharan Africa and 27.3 percent in Middle-East and North Africa compared to 17.5 percent and 13.4 percent in East Asia and Pacific, and High-income OECD, respectively. Therewith, firm sizes in Africa are either micro- or small and they choose to stay informal because of perceived high level of costs in doing business otherwise, which slows their growth since they do not benefit from economies of scale needed to be competitive.

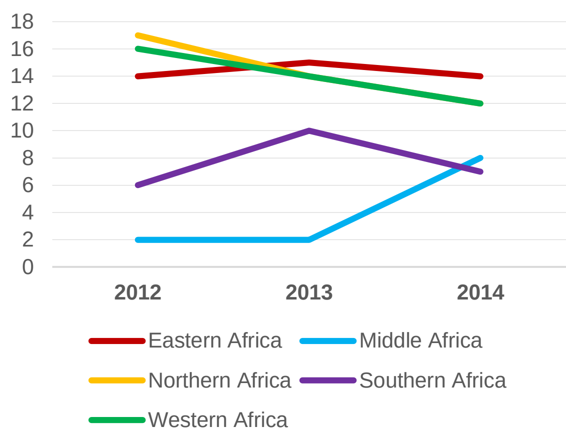
Africa being rich in natural resources is very attractive for foreign direct investments (FDI). However since 2012, Africa's overall FDI inflows have remained flat at $54billion while Asia is the only region where a raise is observed (Figure 3). Despite the world economic instability and the politic uncertainty, in some African regions' FDI have increased. In 2015, investment from China to Africa decreased from about 84 percent during the first quarter of the year[8] which threatens the African growth. The share in world of the Africa's FDI inflows is 4.4 percent.

Figure 3 : FDI inflows, by region 2012-2014 (USD Bn)



Source: Data from UNCTAD, WIR, 2015

Figure 4 : FDI inflows, African regions 2012-2014 (USD Bn)



Source: Data from UNCTAD, WIR, 2015

[8] http://www.agenceecofin.com/investissement/2810-33445-les-investissements-chinois-en-afrique-ont-chute-de-84-durant-le-1er-semestre-2015

Africa's share of global trade remains at 3 percent and despite participating in the multilateral trading system and benefiting from initiatives such as African Growth and Opportunity Act (AGOA), Everything but Arms (EBA) and Economic Partnerships Agreements (EPAs) the region is yet to successfully integrate into the global economy[9].

CFTA Potential towards Economic Development

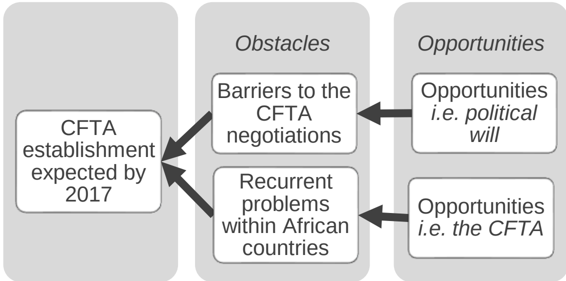
Africa's 54 countries have different levels of development which need to be taken into consideration in negotiating the CFTA, in order to ensure outcomes benefit the continent as a whole.

Given the slow progress in multilateral trade negotiations, as well as proliferating mega-regional trade agreements such as the Trans Pacific Partnership and Trans-Atlantic Trade and Investment Partnership agreements, Africa was at risk of further marginalisation from global trade. The CFTA is therefore an opportunity to mitigate this situation.

The United Nations Economic Commission for Africa (UNECA) estimates that with reduction or elimination of tariff and non-tariff costs and integration of informal trade, intra-African trade will increase from 20 to 30 percent. In order to achieve this, political will across the continent, harmonisation of trade policies to reinforce linkages between the agricultural and non-agricultural sectors of their economies, building up local capacities within the continent, strengthening the regulatory framework and the agriculture development, improving infrastructure including energy access is a prerequisite.

The CFTA faces a number of challenges likely to hinder its effectiveness upon agreement, these can be categorised as "recurrent problems" and "barriers to CFTA negotiations" as highlighted in Figure 5 and expounded upon thereafter.

Figure 5 : Obstacles and Opportunities to the CFTA establishment



Source: Author's own illustration

Recurrent problems within African countries

Africa is the most electricity poor region (World Energy Outlook, 2015) and people with less access to energy live in rural areas especially in Sub-Saharan Africa (10. 635million or 53 percent of the population without electricity access lives in Africa and 754 million or 68 percent of the population relying on traditional use of biomass are from Africa).

Other well documented challenges include poor infrastructure (e.g. ICT infrastructure, road network); the low level of manufacturing and production; the high level of tariff and non-tariff barriers (e.g. transport cost and distance to its market), limited labour market and goods market efficiency, and the poor macroeconomic environment (e.g. high and unsteady interest rate, currency appreciation, obstacle to global demand, disconnection of capital flows from the real economic activities) and others.

Further, although many African countries benefit from Food aid, its paradoxical in that it does not systematically help Africa to develop or sustain a transformation for the well-being of everyday Africans, instead it supports indirectly unfair

[9] http://www.cuts-international.org/ARC/Accra/IVORI/pdf/Regional_Integration_in_Africa.pdf

[10] http://www.worldenergyoutlook.org/resources/energydevelopment/

competition to farmers by exposing them to price volatility. In addition subsidies often given in developed countries lead to dumping on world markets which exacerbates the problem. Moreover a statistic review shows that *"The profits that Ghana, Mali and Burkina Faso lost because of US cotton subsidies are much more than the total amount of aid (including food aid) these countries have received since they were independent"*[11]. Thus, the ability to access food is reduced because profits received from sold products by Africans in the global market are less than expected; farmers' are non-competitive and received less than needed to feed themselves and their families and poverty as well as hunger keep being a widespread issue.

On the other hand, African countries face instability issues whether it is political, ethnical and religious tensions as well as insecurity issues, especially in Sahel caused by the presence of armed group, and often hit by act of terror. This insecurity and instability encourage illicit trade and customs (e.g. corruption) as well as informal cross-border trade (e.g. in SADC, informal cross-border trade could amount to $17.6billion per year, representing 30 to 40 percent of total intra-SADC trade (UNCTAD report 2014). Despite the creation of the African Peace and Security Architecture (APSA) in 2001, the continent is still dependent of external solutions. In this way, establishing the CFTA is an ambitious plan took by the AU.

Barriers to the CFTA negotiations

Foremost, the negotiations process is complex because of the number of participants; the AU is comprised of 54 countries and eight RECs including 34 LDCs as well as economic powerhouses such as Nigeria and South Africa. Poorest countries have expressed concerns on the fact that larger economies might dominate the CFTA both in terms of negotiations as well as outcomes. Thereby, the negotiating framework has to take into consideration the fact that their level of development and capacities building are different.

Besides, African countries participate to several RECs or other agreements which offer better terms to external partners than to each other. Tariff, non-tariff and bilateral tariff costs are higher within Africa than within the rest of the world and it often appears to hit regional trade disproportionately.

In addition parallel to CFTA negotiations, RECs are undertaking other negotiations such as with the EU for economic partnership agreements (EPAs); on 10 June 2016[12], SADC signed an EPA with the EU. Other negotiations can lead to negative impact on the negotiation of the CFTA given the likelihood of issue conflict and resource challenges.

All in all the CFTA provides immense opportunities for Africa, not only to mitigate possible negative repercussions from the other mega regionals and delayed multilateral trade negotiations, but to overcome intra-Africa trade challenges, which would spur the regions sectoral development.

[11] http://theafricaneconomist.com/food-aid-does-not-help-africa-it-is-the-problem/#.V16C49T5jQA

[12] http://ec.europa.eu/trade/policy/countries-and-regions/regions/sadc/

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United Nation Economic Commission for Africa, History and background available at: http://www.uneca.org/oria/pages/history-background-africas-regional-integration-efforts

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This note is authored by Elodie Arnell. CUTS briefing papers are to inform, educate and provoke debate on specific issues. Readers are encouraged to quote or reproduce material from this paper for their own use, provided due acknowledgement of the source is made.

37-39, Rue de Vermont, 1202 Geneva, Switzerland
geneva@cuts.org ● www.cuts-geneva.org
Ph: +41 (0) 22 734 60 80 | Fax:+41 (0) 22 734 39 14 | Skype: cuts.grc

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