



Briefing Paper

The African Continental Free Trade Agreement: Opportunities and Challenges

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Summary

This briefing paper aims to inform delegates and governments of Member States of the AfCFTA of the challenges and opportunities of the treaty. In particular, this analysis encompasses the following topics: (i) the structure and objectives of the African CFTA; (ii) the economic impact of the treaty; and (iii) the challenges and issues. This paper is based on a CUTS study by Théophile Albert titled “The African Continental Free Trade Agreement: Opportunities and Challenges”, available at <https://bit.ly/2PGvSe8>.

Introduction

The African Continental Free Trade Agreement is the largest free trade agreements, consisting of 54 African country. The Organization of African Unity (OAU) was founded in 1964 and had the clear objective of fostering cohesion and solidarity among African countries. In 1980 the OAU adopted the Lagos Plan of Action which call for the integration of the continent based on self-reliance, endogenous development and industrialisation.

In 1991 the OAU adopted the Abuja Treaty which was a progressive approach to regional integration. It called for the establishment of Regional Economic Communities (REC's) and African Economic Communities by 2028. The Abuja Treaty's pathway can be summarized by the following steps; (i) establish Free Trade Areas in each REC; (ii) create customs unions for the RECs; (iii) create a common market place; (iv) form a Monetary Union.

At the beginning of the 2000's eight REC's had already been established and were headed to regional integration. In 2011 the Tripartite Free Trade Agreement (TFTA) consisting of the EAC, COMESA and SADC was launched which merged overlapping RECs. In January of 2012, the Economic Commission for Africa made a strong case to the African Union (AU), the successor OAU, to launch negotiations for the CFTA (Continental Free Trade Agreement) which was agreed upon during the 18th ordinary session of the Assembly of Heads of State and Government of the AU.

In 2015 the AU launched their 50 year visions for 2063 which coved many topics of which the two main topics are creating a prosperous Africa through durable growth and sustainable development, increased standards of living and quality of life. The other main topic was to do with a unified continent based on idea of Pan-Africanism and a continental customs union, which will be

established after the implementation of an African Common External Tariff (ACET). Currently 54 out of 55 states have signed the AfCFTA.

This brief note draws from a recent paper titled "African Continental Free Trade Agreement: Opportunities and Challenges", and is aimed at highlighting the main issues discussed therein.

Structure and Objectives of the AfCFTA

Institutional Structure and Mechanism

There are three layers to the AfCFTA agreement the first layer covers the purpose, intentions and the primary definitions and outlines. The second layer covers protocols regarding trade in goods and services and, rules and procedures for the settlement of disputes, competition policy and IP rights. The third layer consists of an annex, guidelines and instructions for protocols.

The decision-making process of the AfCFTA on substantive issues is based on consensus, where negotiators will aim for an agreement that satisfies the position and interests of all parties, despite this being the fairest method it is time consuming. Decisions regarding procedures are to be made based on a simple majority of eligible state party votes.

Main Goals and Objectives

The main goals of the AfCFTA agreement includes the removal of a majority of tariffs, enhanced investment facilitation and free movement of capital and people, inclusive trade policies and improved economic competitiveness. The AfCFTA faces the challenge of resolving the issue of multiple overlapping REC memberships and accelerating integration processes on the regional and

continental scale.

The AfCFTA compels the countries to remove 90 percent of tariffs on goods; create a single market for goods and services; facilitate free movement of persons; all of which would in turn strengthen economic integration of the African continent.

The call for promotion of industrial development that would enhance economic competitiveness of state parties at the continental and global level. This would be through diversification, regional value chain development, agricultural development, food security, and investment in quality infrastructure.

The Agreement provides guidance to achieve these goals as the following; eliminate tariff and non-tariff barriers, adopt a developmental integration approach, cooperate better on investment, intellectual property rights and competition policy, and the creation of a dispute settlement body. The Agreement will be implemented in two phases. Phase I will consist of providing a framework for trade liberalisation in goods and services and a mechanism for dispute settlement, while phase II will cover competition policy, investment, and intellectual property rights.

Economic Impact of the Treaty

Current State of Trade in Africa

The AfCFTA provides an opportunity to drive African development and intra-African trade, which is very low in comparison to intra-regional trade with other regions. Only 15% of all African exports currently go to African countries. Intra-African trade is hindered by high-tariffs, colonial-era infrastructure, and overlapping REC's which obstruct trade standardization and enforcement.

African economies are characterized by their lack of requisite infrastructure, currently there is a need for US\$170Bn of investment in infrastructure every year in the domains of communication, energy supply, and digital infrastructure.¹

Through 2000 and 2017, intra-continental trade was primarily of manufactured goods and food, exporting mainly palm oil, sugar, maize, rice and tobacco. Total intra-African agricultural trade was valued at US\$24.4Bn (which represents 19% of total intra-continental exports and 18% of total intra-continental imports).

In 2017, main intra-African exports were of minerals (25%), chemicals (11%), and food, beverages and tobacco (9%). In comparison African exports outside of Africa consisted of primary products and raw materials which contributes to 60% of total exports, while 70% of imports consisted of mineral products, chemical products, manufactured goods, machinery and transport equipment.

The AfCFTA provides investment plans, trade facilitation measures, and trade related infrastructure measures, which, if implemented would result in facilitated trade and economic growth.

Potential Positive Impacts

- In the long run a full elimination of tariffs would lead to an overall welfare gain of US\$16.1Bn for African countries.
- An assessment by the Economic Commission for Africa found that the AfCFTA will lead to an increase in exports by 3% and an increase of around 1% of the GDP. The increase is not as

¹https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2018AEO/African_Economic_Outlook_2018_-_EN_Chapter3.pdf

high as initially expected, however the limited export growth can be attributed to fact that 83% of African exports are directed to outside of Africa.

- An increase by 53.3% in intra-African trade is anticipated by the year 2022 which is expected to transpire from the cutting of tariffs by 90% and the harmonisation of trade rules. Intra-Africa trade for industrial products would increase by 25%-30% (US\$36Bn - US\$44Bn), food and agro by 20%-30% (US\$9.3Bn - US\$17Bn), energy and mining by 5%-11% (US\$4.5bn - US\$9bn).
- Lower trade costs would lead to economic stimulation domestically and internationally as a reduction of tariffs produces lower importing prices therefore increased purchasing power and consumption. Cutting quotas and reducing trade barriers subsequently allows for access to a greater range of products.
- Due to cuts in production costs caused by minimal or no tariffs, countries importing raw material should expect lower cost which would increase the competitiveness of domestic producers and help them integrate in the global value chain.
- Trade liberalisation for domestic firms also means access to bigger markets and would allow them to gain economies of scale. However if larger companies benefited from the economies of scale it would prevent SME's from accessing the market.
- Trade liberalisation also increases competitiveness and efficiency. For African firms this means increasing investment in R&D for new technology, production methods, and to innovate.
- To improve intra-Africa trade, the AfCFTA set

up investment strategies which can be supported through national investment plans. There is a need for the implementation of national investment strategies that can target complementary measures and key trade opportunities.

- The AfCFTA will lift restrictions on foreign investments. Allowing investors to add capital would expand local industries and boost domestic businesses. The inflow of foreign capital will stimulate banking systems, lead to more investment and consumer lending.
- The aforementioned benefits of the agreement would also impact employment, which will also benefit from the agreement as it would present an opportunity to catalyse inclusive growth enhancing women and youth in key sectors of the economy. Never the less, for this outcome to be realised, complimentary policies and a requisite regulatory framework will be required
- The AfCFTA should encourage MSME economic activity. Currently 80% of the GDP and 50% of employment is provided by MSME's in Africa, however the lower cost of trade mean SME's can enter foreign markets where there are more opportunities and areas to trade.
- With a common external tariff, African nations have larger influence and power in negotiations. Intra-African trade under AfCFTA will mitigate the costs of adverse global economic shocks, a larger and more effective domestic market would protect member states from global volatility and disruption

Differential Treatment

Trade liberalisation has to be disproportionate, in order to support smaller economies, while also coordinating building productive capacity, and enhancing cross-border infrastructure. The

AfCFTA will impact each state differently, for that reason a differential schedule of liberalisation was established to protect small venerable economies and fragile economies from being negatively affected by the bigger economies.

Differential treatment would reap greater benefits for smaller economies and LDC's. Similarly more diversified economies are more likely to receive greater benefits from the Agreement.

Negative Impacts

- The Agreement in the short term may have an adverse effect on many economies. More competition would threaten MSMEs and small scale farmers while larger companies would benefit in this time period.
- Member states would undergo a transition period in which they would face adjustment costs. The less diversified and in-flexible countries suffer more from the adjustment costs in comparison to bigger and more diversified ones. Adjustment costs would be higher for MSMEs and for labour mobility in developing countries.
- Unskilled labour will likely be negatively affected by trade liberalisation in the short and medium run, for which compensatory measures must be taken, otherwise social tension will be created.
- A decrease in tariff revenue would also affect the government's budget which have implications on the government's capacity to invest in infrastructure, education, and social programs, crucial for sustainable development and decreasing inequality.
- If the financial sector and governance structure is not strengthened in addition to raising the education level, the level of poverty will not

decrease. Political and economic effort are required from states such as providing social security in case of negative outcomes from trade liberalisation such as loss of tariff revenue and loss of jobs.

- Although the AfCFTA provides economic opportunities, complementary measures must be implanted by prioritising strategic sectors in national investment plans, establish simple trading regimes, investing in trade related infrastructure, education and training to enhance skills.
- The AfCFTA could also have negative effects on the environment as more trade entails increased CO2 emissions. The Agreement includes a few environmental standards however there is need for more ambitious sustainable standards to minimise the negative effects.

Global Impacts

The AfCFTA strengthens the voices of African countries in international organisation. Additionally with the help of a common external tariff, African countries will be able to negotiate better agreements with a unified African voice.

The Agreement would generate 7.5 million jobs in G20 economies and an increased share of manufacturing in Africa's GDP would increase investment in the G20 economies by US\$485Bn and household consumption by US\$ 1.4 trillion. The indirect effects from increased exports would boost aggregate demand, create employment in rich and poor countries, and move the world towards better

international relations.²

Challenges and Issues

Unresolved Strategic Topics

- Conflicting RECS, as previously mentioned are one of the main challenges of implementing the Agreement. REC's must converge so as to become compatible with the AfCFTA
- Harmonising standards and certification is another issue that needs to be tackled as these non-trade barriers curtail trade in ways that are at times more complex than tariffs. To tackle this, trade facilitation policies should be implemented to reduce border regulations and corruption. Reducing trade barriers is not enough action, therefore members should implement trade facilitation policies, increase investment in infrastructure and improve standards harmonisation.
- The Issue of Rules of Origin (RoO) is slightly complicated, if the rules are transparent and predictable they can be a game changer otherwise they can be seen as another barrier to trade, which would discourage businesses and entrepreneurs from trading. If the RoO are too complicated products would be imported from outside of Africa, which would hinder the intra-African trade gains that comes from the AfCFTA. The RoO should account for inequalities among African countries
- Development of ecommerce is another major issue that requires a proper legal framework for digital trade and activities. Additionally issues of digital trust and competition policies in the digital sector, data privacy, protection and cyber

security needs to be tackled to implement cooperation among African stakeholders.

Inclusive Integration

The implementation of specific national plans will provide technical and financial support for MSMEs which will enable them to penetrate the cross border continental market. This is essential for the AfCFTA, as it provides an opportunity for entrepreneurs to enter new markets and increase their level of production. These national plans have to be applied to small scale farmers to help them integrate into the export market as they will be competing with larger and more competitive companies.

An indirect effect of the Agreement will be the economic empowerment of women. The AfCFTA should build capacity in women and youth to reinforce their inclusion within the trading and economic system.

Non-tariff barriers affect women's participation in trade. Informal cross border trade among women generates 40%-60% of the GDP in west and central Africa, despite the fact that women still suffer from stigmatization, violence, harassment, poor working conditions and lack of recognition for their economic contribution. By overlooking women's contribution in trading activities, African countries are neglecting a significant catalyst for trade and economic development.

The AfCFTA provides opportunities for women in agriculture, manufacturing, and service trade. Deliberate action by the AU must be taken to implement gender sensitive policies and target complementary measures; this includes national initiatives such as a gender-sensitive education,

²https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/African_Economic_Outlook_2018_-_EN.pdf

women-training programs, financial support for women entrepreneurs and the implementation of tax reduction for women-owned companies.

Sustainable Development

To comply and reach the Sustainable Development Goals 2030 agenda, action must be taken to eradicate poverty, reduce inequality, and protect the planet through sustainable agriculture and methods of production.

To address the impacts of climate change that are now prevalent throughout the continent, Member states must decrease carbon emissions, and the use of pesticides and veterinary medicine on agricultural products. Relevant stakeholders must support national and international public authorities, and the government, through incentives, tax reductions and technical support, should encourage industrial producers, farmers, and the civil society to change habits and do business and trade in a more sustainable way. The SPS regulations are essential, as the use of certain pesticides endangers public health, for which compliance will increase exports and protect African public health and biodiversity.

Next steps

AfCFTA entered into force May 30th 2019. To foster African cooperation and work towards African unity the following seven steps would ensure comprehensive integration:

- Step 1: Operationalize the AfCFTA by finalizing technical features and concluding schedules especially those countries that have recently ratified the treaty
- Step 2: Effectively implement the AfCFTA by operating the institutional structures and mechanisms.
- Step 3: Implement complementary measures to fully optimize and leverage the agreement.

- Step 4: Conclude phase 2 of negotiations (negotiations regarding level of investment, competition policy and IP rights)
- Step 5: Use the agreement as a tool for achieving a single African market
- Step 6: Creation of the African Monetary Union, which should be operational by 2023 as per the 2063 objectives
- Step 7: Creation of an African Political Union which involves deeper political cooperation and integration.

Developing countries have comparative advantage in several service sectors, but their services exports often face barriers in export markets which could be targeted in multilateral trade negotiations.

Unlike trade in goods, international commitments and disciplines on trade in services are relatively new and less developed. Since 2001, services negotiations aimed for establishing new rules in the areas of: (i) domestic regulations, to develop disciplines on qualification requirements and procedures, technical standards and licensing requirements and procedures; (ii) rules for emergency safeguard measures and subsidies; and (iii) market access for further liberalisation of trade in services.

Conclusion and Recommendations

AfCFTA offers opportunities to increase intracontinental trade and to strengthen the position of African countries in the international trading system. In order to efficiently and sustainably implement the AfCFTA, African policy makers must fully adopt and implement the agreement. If the AfCFTA is implemented successfully African countries will acquire substantial social-economic benefits.

Regarding Trade: include taking action to remove

non-tariff barriers, implement complimentary policies and protocol on e-commerce, taking commitments in accordance to a state's comparative advantage and working towards an African Single Market and an African Monetary Union.

Regarding Climate: implementation of incentives and tax reductions for sustainable activities, encourage compliance with SPS standards, protecting African biodiversity through creation of protected parks and development of green cities, and put in place investment plans for renewable energy and sustainable infrastructure.

Regarding inclusive growth and development: education and training for women and instituting a regulatory framework addressing gender imbalance is necessary, in addition to implementing incentives

and tax reductions for women and youth owned businesses. Inclusiveness of course goes beyond gender issues, other considerations such as the role of civil society organizations, private sector, marginalised communities etc. should be taken into account.

All in all, the AfCFTA is a positive step in the right direction of advancing development and emancipation of livelihoods in the African continent, while also contributing to global efforts in this regard. There is no doubt that if fully implemented, the agreement will immensely contribute to better economic and social wellbeing of the Member States.



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