



POLICY BRIEF

AFRICA'S DIVERSIFICATION AND ITS TRADE POLICY TRANSFORMATION



Task Force 1
TRADE, INVESTMENT AND GROWTH

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موجز السياسة اتجاه أفريقيا نحو التنويع وتحول سياستها التجارية

فريق العمل الأول
التجارة والاستثمار والنمو



المؤلفون

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ABSTRACT

This policy brief discusses Africa's diversification and trade policies for improved intra-African and international trade, economic and social transformation, as well as promoting win-win G20-Africa economic relations. The brief presents the imperatives to broaden Africa-G20 cooperation through improved trade and restructured global value chains that will enhance competitive production, diversification, and economic transformation. Ultimately, the G20 and African leadership are urged to support effective implementation of the African Continental Free Trade Area, trade policy reforms, and broadened partnerships. This will speed up Africa's economic diversification and integration into regional and global value chains.

يناقش موجز السياسة هذا اتجاه أفريقيا نحو التنويع وتحول سياستها التجارية لتحسين التجارة الداخلية والتجارة الدولية فيها، ونتائج التنمية الإيجابية، والعلاقات الاقتصادية بين مجموعة العشرين وأفريقيا المربحة للطرفين. ويوصي الموجز بتوسيع دائرة التعاون بين أفريقيا ومجموعة العشرين نحو تجارة محسنة وإعادة هيكلة مزايا سلسلة القيمة العالمية التي ستؤثر في الإنتاج التنافسي والتنويع والتحول الاقتصادي.

وفي نهاية المطاف، يحثّ الموجز مجموعة العشرين والقيادة الأفريقية على دعم التنفيذ الفعال لمنطقة التجارة الحرة القارية الأفريقية (AfCFTA)، وذلك لتسريع وتيرة اتجاه أفريقيا نحو التنويع، إضافةً إلى تعزيز شرعيتها ومصداقية سياساتها في التحول الاقتصادي الهيكلي وأهميتها للتنمية العالمية من خلال العلاقات التجارية المستقبلية.



CHALLENGE

The recently established African Continental Free Trade Area (AfCFTA) is an African initiative toward achieving pan-African economic integration. The AfCFTA also offers a new entry point for cooperation with Africa, including at the multilateral level, under the auspices of the G20. This free trade area raises hope for the expansion of intra-African trade through better harmonization and coordination of trade liberalization among its signatories. At the same time, it entails risks and challenges that include policy and procedural constraints that might create bottlenecks at the regional level. For instance, while increasing intra-African trade will facilitate diversification and economic transformation, it must also strike a balance to avoid “too much” trade diversion with the rest of the world owing to further intra-African tariff cuts. At the same time, it must create sufficient preferential treatment among African countries to allow for the establishment of regional value chains (RVCs) and diversification.¹ The G20 should not only provide support to manage the downsides and leverage the potential of the AfCFTA, but also use the integration project to leverage win-win G20–Africa economic interdependencies and boost Africa–G20 cooperation.

The AfCFTA addresses a range of inter-related policies for African economies. Intra-African trade liberalization could allow for the establishment of RVCs, thereby promoting intra-African trade. In the long term, this could enable diversification of economic activity and allow African economies to enter into global market arrangements. All these are key elements of economic transformation wherein a region or a country moves to a more diverse and complex production and trade structure. This transformation helps mitigate volatility; it also provides a more stable path for sustainable growth, competitive production, and development. These elements are now especially critical, given the expected uncertain global growth owing to the COVID-19 pandemic as well as the imperative to increase the number and quality of jobs in developing countries. Thus, the goal is to foster sustainable and inclusive development in line with Africa’s 2063 agenda and the 17 global goals enshrined in the 2030 Agenda for Sustainable Development.

The main thrust of the policy brief is that Africa’s diversification strategies and trade policy transformation are prerequisites for economic transformation, inclusive growth, and stability as well as for deeper G20–Africa economic interdependencies. Effective implementation of the AfCFTA would accelerate economic transformation (i.e., prod-

1. On the one hand, the global competitiveness of African firms and products will depend on access to the most cost-effective services and products. On the other hand, Africa requires significant volumes of investment and competitive production; thus, intra-African investment will not be sufficient.

uct diversification, competitive production, restructuring of the global value chain mechanism, and geographic diversification of exports). The brief outlines the role of the G20 and African countries in leveraging this endeavor. This is both in terms of collective legitimate governance and as part of the G20's efforts toward global rebalancing to promote capital flows from surplus countries to opportunities in sustainable infrastructure and climate finance that have high returns. Most G20 core policies that seek to rebalance economies (e.g., by improving services productivity or promoting social protection) will affect African interests.

Trade policy trends and its implications for Africa's diversification and structural transformation

Africa's share in total world exports and imports has been relatively low but stable over the past two decades, averaging only 2.7% for both exports and imports (United Nations Conference on Trade and Development 2019; Mevel and Karingi 2012). This diminished role of Africa in global trade can largely be explained by the poor diversification of the continent's trade. Between 1998 and 2018, more than 70% of Africa's exports to the world comprised fuels and other primary commodities. Such strong concentration of exports in low-value products has severely undermined Africa's development potential. However, it should be noted that the composition of trade tends to strongly vary by the destination of Africa's exports—whether it is the African market or the rest of the world. While primary commodities accounted for more than 75% of Africa's exports outside the continent during 1998–2018, manufactured goods dominated intra-African exports, with a share of about 45%, and primary commodities barely amounted to one-third. While the share of intra-African trade (exports) has remained relatively low (compared with other main regions) at around 13% on average over the last 20 years, it nevertheless signals promising characteristics for Africa's industrialization and development.

The AfCFTA, once realized, is expected to become the largest trade integration project in the world in terms of participating countries since the formation of the World Trade Organization (WTO). The agreement establishing the AfCFTA has been signed by 54 African Union member states, of which 30 have ratified it. Once implemented and appropriately managed, the AfCFTA offers substantial potential in manufacturing and industrial development, tourism, intra-African cooperation, and economic transformation (Signé 2018). Among other benefits, the Agreement is bound to expand intra-African trade, enhance the net welfare of African households, economic communities, and countries, as well as facilitate the harmonization and coordination of trade-related measures within the continent by enabling coherent policy in Africa.

Broadly, the expanded markets for African goods and services, coupled with unobstructed factor movements, restructured global value chain processes, and the reallocated resources, should promote economic diversification, structural transformation, technological development, and the enhancement of human capital.

Promoting economic diversification and boosting intra-African trade would simultaneously function as drivers for eradicating poverty and fostering sustainable and inclusive development of African countries, which is consistent with the agenda of the African Union and the Sustainable Development Goals (Songwe 2020).

As demonstrated in the empirical assessment of the AfCFTA modalities on trade in goods by the UN Economic Commission for Africa (ECA), intra-African trade could increase by 15% (\$50 billion) to 25% (\$70 billion) in 2040, depending on the ambition of the liberalization reform (Mevel and Karingi 2012). Indeed, the ECA's analysis finds that the current relatively low share of formal intra-African trade² could increase by around 50% after the AfCFTA reform; more than two-thirds of the gains in intra-African trade would be captured by industrial sectors, with textile, wearing apparel, leather, wood and paper, vehicle and transport equipment, electronic, as well as other manufacturing sectors expected to benefit the most. Gains in agriculture and food sectors would also be substantial—particularly for meat products, milk and dairy products, sugar, beverages and tobacco, vegetables/fruit/nuts, and paddy and processed rice.

An earlier empirical study by ECA (see Mevel and Karingi 2013)³ shows that once parallel reforms aimed at reducing trade costs through effective discipline of inefficient border processes are implemented, they would amplify the expected trade and real income benefits from the AfCFTA for all countries. This was confirmed in a recent analysis by the United Nations Conference on Trade and Development.⁴ It estimated that the gains following a reduction of non-tariff barriers could be three to four times larger than the gains after only tariffs elimination within Africa. Trade facilitation measures are also essential to increase productivity; along with efficient services sectors throughout Africa, they can facilitate the building and upgrading of RVCs and make

2. Informal trade is thought to be significant in Africa, but not captured in official trade statistics.

3. See https://www.ilo.org/wcmsp5/groups/public/---ed_emp/documents/genericdocument/wcms_212864.pdf

4. See https://unctad.org/en/PublicationsLibrary/ser-rp-2017d14_en.pdf

Africa competitive. Similarly, recent studies by the African Economic Research Consortium⁵ find two salutary effects of AfCFTA implementation: (1) a positive effect on new trade (or trade creation), including an increase in intra-Africa trade, and (2) improved welfare in the Southern African Development Community and the Economic Community of Central African States regions.

The level of diversification is unevenly distributed across African countries (Fosu and Abass 2019). Further, the AfCFTA is likely to have an amplifying effect on this scenario. The enhanced integration efforts may enable comparatively mature hubs, such as Kenya or South Africa, to attract the bulk of intra-African manufacturing production in the short run at the least. The periphery would be limited to export activities that are less beneficial for economic development. This way, the gap between “winners” and “losers” of regional integration is expected to increase. If such patterns in roles are reinforced, it would ultimately undermine the acceptance of the AfCFTA among members. Thus, mechanisms for structural adjustment facilitation and policy measures that support economic transformation appear to be vital for equal and sustainable participation.

Beyond the invaluable opportunities for industrialization and development for member states, successfully establishing the AfCFTA could reshape trade relations with the G20 by ascribing more importance to the African market. The Agreement offers the G20 a vehicle for reciprocal and mutually advantageous trade and investment frameworks. For instance, around 83% of Africa’s total exports are currently directed outside the African continent (particularly to EU countries, China, India, the US, and the UAE).⁶ With a combined GDP of over \$2.3 trillion and a population of 1.2 billion—of which most are below the age of 30—African countries would be part of the G20’s efforts toward global rebalancing to promote capital flows from surplus countries toward profitable opportunities in sustainable infrastructure, climate finance, services productivity improvements, and social protections that affect African interests. Given these tangible trade and investment benefits for all parties involved, external partners should play a reciprocal role in supporting the AfCFTA implementation process. In this policy brief, we focus on the role of the G20. Notably, the AfCFTA is a vehicle for upgrading and intensifying cooperation between Africa and the G20.

5. The African Economic Research Consortium network has completed three studies under the auspices of a collaborative research project on “Rethinking Regional Integration in Africa for Inclusive and Sustainable Development.” The studies were undertaken by researchers from the European Centre for Development Policy Management, Addis Ababa University, and University of Zimbabwe.

6. ECA’s computations based on UNCTADStat (accessed March 24, 2020); average for 2016–18.



PROPOSAL

Africa–G20 cooperation is currently limited to a few single initiatives and an observer status for the African Union and New Partnership for Africa's Development. This level of engagement should be enhanced to focus on the current global challenges and strong economic interdependencies between African and G20 countries.⁷ With a focus on “beyond aid” issues, the AfCFTA presents opportunities for both G20 and African leadership to add value to African development and boost their legitimacy, credibility, and relevance to global development. Further, the economic interdependencies among African and G20 countries imply that G20 policies such as rebalancing trade and consumption have mutually reinforcing development effects. Clearly, Africa–G20 cooperation should go beyond the current state of play and, in light of the AfCFTA, renew attention toward shaping the future of trade relations characterized by strong linkages to competitive production, economic diversification, and economic transformation.

Promoting AfCFTA implementation

The G20 should promote AfCFTA implementation, and, through it, strengthen intra-continental trade flows. This can be realized through two measures: first, by boosting financial and technical support for building the capacities of African member states to implement AfCFTA; and second, through investments in physical infrastructure (roads, railways, ports, and airports), services, and logistics to reduce transportation and transaction costs, facilitate trade by more strongly orienting G20 expertise and aid programs toward trade facilitation in Africa, and potentially substitute revenue losses.

Reforming G20 members' trade policies and broadening partnerships

The G20 could support and leverage the potential of the AfCFTA by influencing its members' trade policies and broadening trade partnerships with Africa. First, the G20 ought to spearhead world trading system reforms to promote the diversification of exports and trade-related support for African countries. Second, there is a need for capacity development with respect to African trade policies in order to address concerns over G20 protectionist tariffs (Kareem 2019a, 2019b; Evenett and Fritz 2019).⁸

7. See recent international policy discourse and recommendations by T20 at https://www.g20-insights.org/wp-content/uploads/2017/05/Policy-Brief-Africa_final.pdf and https://t20argentina.org/wp-content/uploads/2018/07/TF5-5-4-Africas-partnership-with-G20-and-others_final.pdf.

8. See https://ycsg.yale.edu/sites/default/files/files/Murky_Protectionism.pdf and other recent Global Trade Alert reports.

Third, the G20 should maintain and extend existing preferential trade measures and aid-for-trade assurances to the entire African continent (e.g., existing trade partnerships through the Economic Partnership Agreements with the EU, African Growth and Opportunity Acts by the US, and preferential schemes offered by China and India to Africa). Lastly, it is important to strengthen innovative trade and investment partnerships with Africa's main external trading partners—both traditional partners, such as the EU and the US, and emerging countries, such as China and the Republic of Korea. The G20 countries must also start considering Africa as “one” (e.g., trade and investment partnerships with external partners to be negotiated at the level of the African Union). It is also important to enhance coordination between the G20 and Africa for coherent policies toward regional and international economic integration, including the removal of the G20 and individual member policies that impede development in Africa. At the least, a “do no harm” approach should be guaranteed.

Economic diversification and integration into regional and global value chains

To increase Africa's diversification and integration into extant value chains (both regional and global), several strategies ought to be adopted by the African bloc, the G20, and private sectors. First, it is crucial to develop and implement harmonized technical standards or customs procedures. Second, there is a need to review and improve G20 trade policies, in particular tariffs and non-tariff measures, to increase Africa's export competitiveness. G20 countries' regulatory frameworks and the corresponding non-tariff measures (NTMs), such as Sanitary and Phytosanitary/Technical Barriers to Trade requirements, alter relative competitiveness in favor of exporters that are capable of efficient compliance with NTMs. This, in turn, penalizes exports originating in Africa and other least developed countries. Mutume (2006) argues that Africa's exports are prevented from reaching most G20 markets because of additional regulatory barriers, despite Africa's efforts to raise the quality of their commodities. The presence of NTMs has undermined Africa's potential to gain from exports, particularly the opportunity to create wealth and employment in the agricultural sector and among rural household producers (Fugazza 2013; UNCTAD 2013, 2016). Clearly, developing capacities and capabilities both on bilateral and multilateral levels would help minimize Africa's costs of compliance with stricter technical regulations. Other NTMs would be essential to facilitate the integration of African economies in the global economy. Finally, Africa should adopt internationally accepted trade facilitation standards as well as immigration rules and practices to develop RVCs that benefit from the higher end of major global value chains.

A key catalytic role for the G20 here would include the following: (1) Upgrading of production infrastructure and technical expertise to raise the quality of outputs for export, particularly to sophisticated advanced markets; (2) investment in research and development to propel innovations that are necessary for and sufficient to guarantee market access; (3) strengthening institutional capacities for enforcing product quality standards for entry into targeted export markets; and (4) an effort to reform the global value chain and balance the value toward producing centers of primary exports. The G20 countries should also support the productive capacity of African countries in order to benefit from the new AfCFTA opportunities. This can be done *inter alia* through G20 buyers, consumer preferences, and domestic incentives to restructure and focus the global supply chains in favor of African producers in an environmentally friendly and sustainable manner. Finally, the G20–Africa partnership ought to prioritize a strategy for engagement with the private sector in Africa’s quest for economic diversification through trade transformation.

Disclaimer

This policy brief was developed and written by the authors and has undergone a peer review process. The views and opinions expressed in this policy brief are those of the authors and do not necessarily reflect the official policy or position of the authors' organizations or the T20 Secretariat.



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