United Nations
Economic Commission for Africa

The Case for the African Continental Free Trade Area

The AfCFTA, Africa's trade flows and industrialization

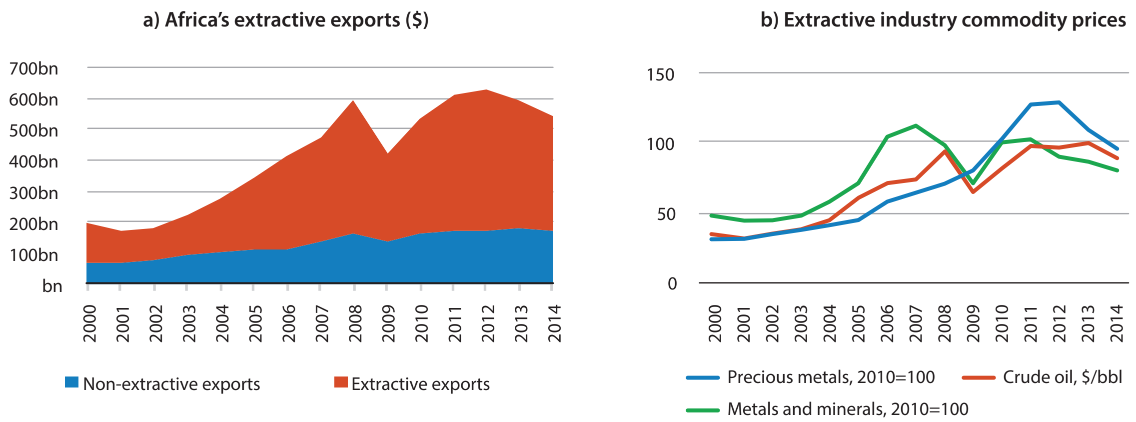
The prevailing story of Africa's exports since 2000 has been that of the strong impact of the commodities super-cycle. As Figure 1 shows, the bulk of Africa's impressive almost-three-fold increase in exports, from $194 billion in 2000 to $544 billion in 2014, is due mostly to the expansion of extractive exports and the commodity price boom. This has contributed to Africa's headline growth figures but has not been conducive to the economic transformation Africa requires to industrialize and realize long-run sustainable growth.

In sharp contrast is the composition of Africa's intra-African trade. Figure 2 shows that intra-African trade comprises a disproportionately large share of non-extractive exports. Looking at the most recent three-year average, this included $17 billion in processed industrial supplies, $10 billion in capital goods, $8 billion in processed food and beverages, $7 billion in transport equipment, another $7 billion in consumer goods, $4 billion in primary food and beverages and $2 billion in primary industrial supplies.

The growth of intra-African trade has helped to promote Africa's industrial export sectors since 2000. Despite amounting to just 18 per cent of Africa's total exports, intra-African exports have accounted for 57 per cent of the growth in Africa's exports of capital goods, 51 per cent of processed food and beverages, 46 per cent of consumer goods, 45 per cent of transport equipment, and 44 per cent of processed industrial supplies as shown in Table 1.

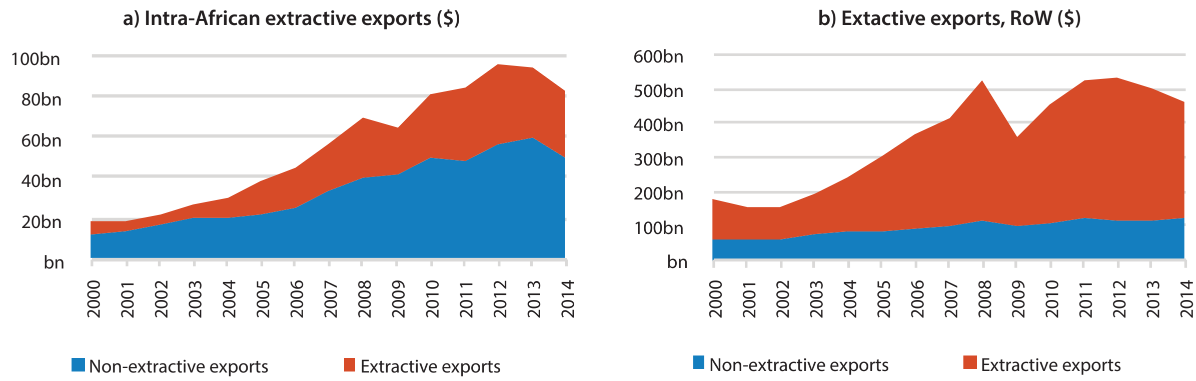
The exceptional value of this intra-African trade for Africa's industrialized economic transformation provides the foundational logic behind the AfCFTA. The fundamental rationale of the AfCFTA is to promote this trade through the removal of tariff and non-tariff barriers.

Figure 1: **Africa's extractive industry exports and world commodity prices**



Source: ECA calculations using CEPII-BACI trade dataset and World Bank Commodities Market Data.

Figure 2: Extractive composition of intra-African trade



Source: ECA calculations using CEPII-BACI trade dataset and World Bank Commodities Market Data.

Table 1: Share of Africa's export growth in non-extractive export categories, intra-African vs the rest of the world

	Import category	Share of export growth attributable to each market (%)	
		Intra-Africa	Rest of the world
Food and beverages	Primary	18	82
	Processed	51	49
Industrial supplies	Primary	15	85
	Processed	44	56
	Capital goods	57	43
	Transport equipment	45	55
	Consumer goods	46	54

Source: CEPII's BACI dataset. Values compare the export growth between three-year averages of 1998–2000 and 2012–2014, and calculate the proportion of export growth attributable to each market such that $Share\ Attributable_{i,j} = (Exp_{i,j,t} - Exp_{i,j,t-1})/(Total_{i,t} - Total_{i,t-1})$ *where i is the export category, j is the buying market, and t is the period. Exp is the value of exports of category i to market j while Total is the total value of exports from Africa of product j.*

Theoretical case for the AfCFTA

- Producers immediately gain from access to: cheaper inputs and intermediary goods from other African countries; a broader variety of inputs and intermediary goods; and larger markets for their products. This enables them to produce more efficiently and competitively and at greater economies of scale.

- Consumers immediately gain from: access to cheaper products from other African countries; and a broader variety of products. Both improve consumer welfare.

- Continental trade integration also helps eliminate the challenges associated with multiple and overlapping trade agreements in Africa.

- An enlarged regional market provides incentives for inward foreign direct investment (FDI) and cross-border investment. Most African markets are small, yet many industrial investments require large economies of scale to be profitable. An expanded African market creates the scale necessary for more investment.

- An integrated African market better facilitates competitive interaction between African firms, setting in motion dynamic gains from competition. In contrast, monopolies and oligopolies have little incentive to become more efficient, cut costs or innovate. Yet as monopolistic markets are pervasive across Africa, enabling African businesses to compete in each other's markets can unlock the competitive pressures necessary for long-run productivity growth.

- Better access to imported inputs and intermediary goods lowers the cost of innovation. Firms may innovate with new combinations and varieties of inputs.

- The AfCFTA may cause trade diversion to African countries at the expense of third countries. This can increase the relative price of exportables in

Africa, stimulating further investment, output and employment in these sectors.

- Trade diversification and a shift to trade in industrialized goods would improve Africa's long-run growth. Intra-African trade embodies a far larger share of industrial and value-added goods than Africa's trade with the rest of the world. Promoting such trade can generate industrial diversification in Africa and catalyse structural transformation.

Empirical case for the AfCFTA

Under the AfCFTA, intra-African trade is estimated to increase by 52.3 per cent ($34.6 billion), compared with a baseline scenario without an AfCFTA. Africa's industrial exports are forecast to enjoy the highest gains, expanding by 53.3 per cent ($27.9 billion). Real wages are estimated to increase for unskilled workers in the agricultural and non-agricultural sectors, as well as for skilled workers, and there is a small shift in employment expected from agricultural to non-agricultural sectors. Flanking the AfCFTA with trade facilitation measures is found to be important in maximizing the impact of the AfCFTA on Africa's industrialization and ensuring that all countries gain from the AfCFTA.

Three important messages derive from the empirical studies. First, the importance of complementary policies that go beyond tariff reductions. Complementary policies are necessary to maximize the gains of the AfCFTA but also to ensure that its benefits are shared equally to produce a win-win outcome for all countries. Such measures include the reduction of non-tariff measures and transaction costs, such as those associated with improved regulatory transparency, harmonization of sanitary and phyto-sanitary regulations, the accreditation and mutual recognition procedures for technical barriers to trade and improved administrative conditions in customs. With the inclusion of such measures, welfare gains are enjoyed by all African countries.

Second, the most important gains from the AfCFTA will be realized over the long run as the agreement contributes to the economic restructuring of African sectors towards more productive industrialized and export sectors, and to improved investments.

Third, the recognition that such studies likely underemphasize the range of benefits derived from the AfCFTA, as modelling exercises struggle to capture and quantify the full gamut of AfCFTA benefits. They frequently overlook gains such as those facilitating trade in food security products, improving the stability of fragile countries, enhancing firms' access to inputs and intermediary goods, reducing the cost of innovation, improving intra-African competition, addressing the challenges linked to overlapping African trade agreements and regional economic communities and providing a platform for cooperation and dialogue more broadly.

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