Who will gain from Africa free trade agreement promises?

By Etienne Vlok

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The African Continental Free Trade Area, with its promises of a move away from a colonial trade model to real development on the continent, faces the risk of fraud and abuse by unscrupulous traders. ETIENNE VLOK sets out what must be done to ensure that the winners are the countries that are party to the agreement and not the drivers of international trade. He made this presentation at an Institute for African Alternatives Forum.

MOTIVATIONS FOR AfCFTA: LARGER MARKETS, MORE INTRA-TRADE, INDUSTRIALISATION

Many African countries and heads of state now recognise that there is great potential opportunity in the fact that there are 1.3 billion people on the African continent at present, and this is projected to grow to 2.5 billion by 2050. Their eyes light up when they realise that the African Continental Free Trade Area (AfCFTA) could create a much larger market, compared to the very small markets they currently produce for, which could provide real opportunities for job creation, deepened industrialisation, better economies of scale and enhanced competitiveness.

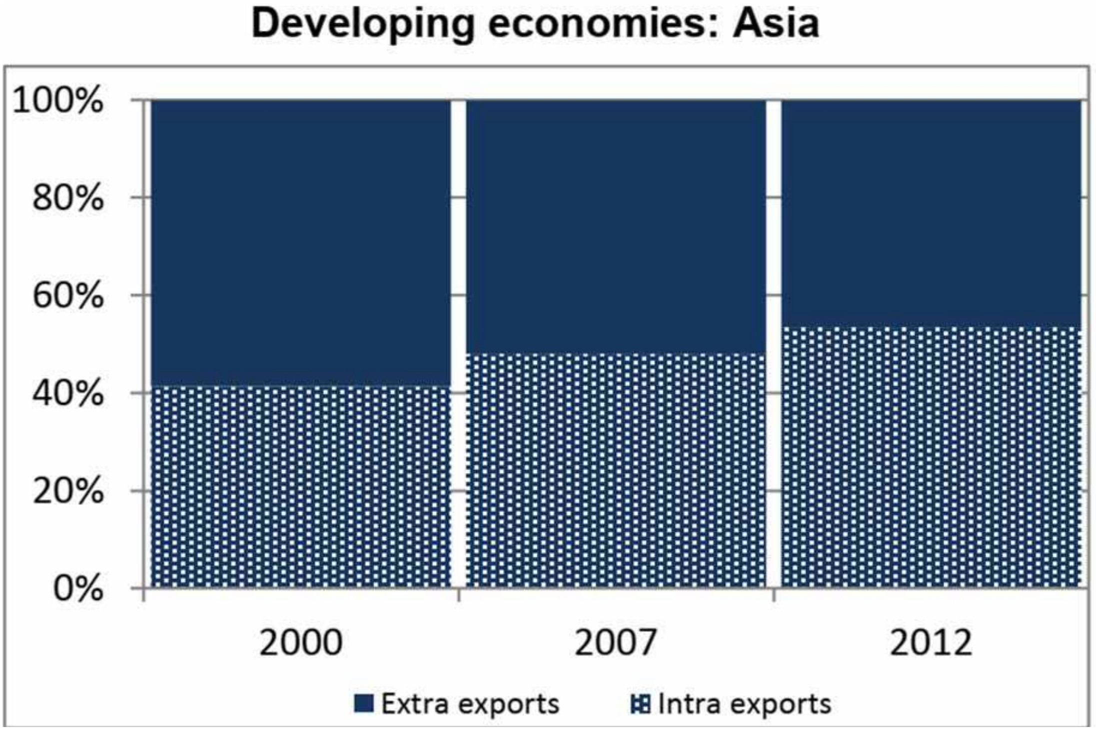
At present South Africa's exports sustain about 2.6 million jobs, or 22% of formal sector employment, according to figures from the Industrial Development Corporation (IDC). African exports currently constitute about 10% of these, or just 250,000 jobs. South Africa believes there is an opportunity to increase this number by expanding the African market and exporting more manufactured products and less raw materials and minerals.

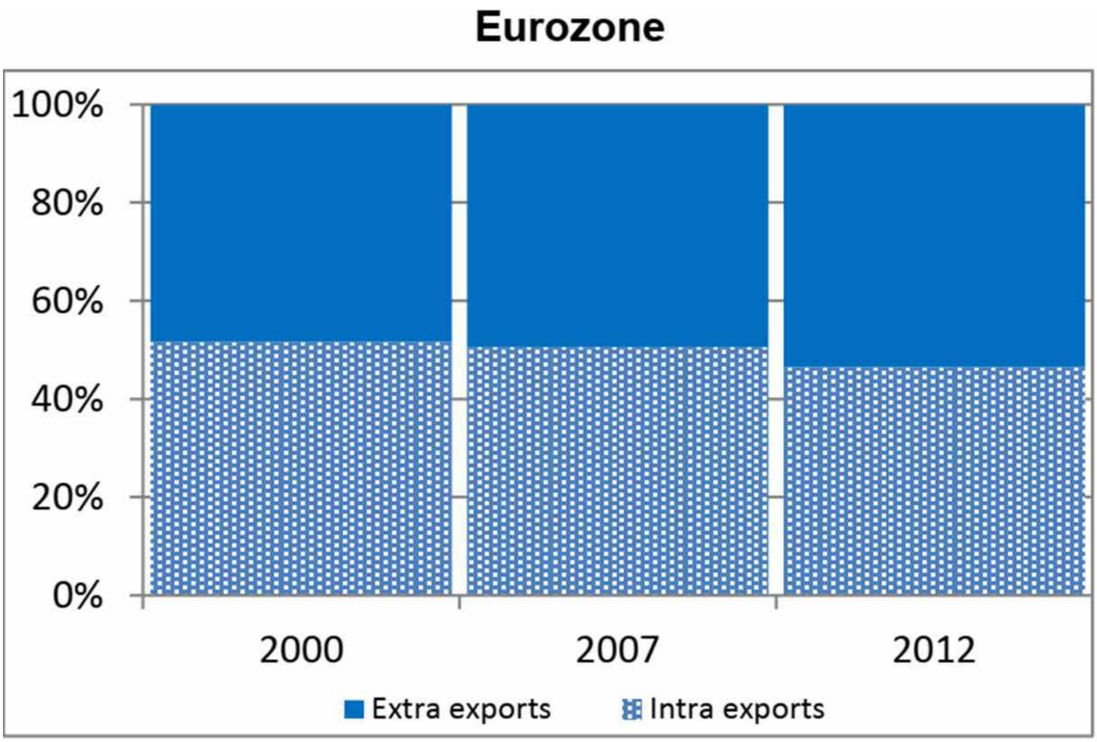
The AfCFTA presents the possibility of greater opportunity for African countries and blocs to engage in trade with each other. At present Africa's intra-trade remains stagnant and low. There are many reasons for this lag. One is that the market remains fragmented. There are barriers to the flow of goods between countries such as infrastructure deficiencies [broken roads, no rail, bad air and sea ports], inadequate economic diversification [many countries produce the same things and have no real need to trade with one another] and non-tariff barriers [complex phytosanitary regulations, unnecessary customs clearance procedures, sometimes requiring bribes]. All this stops the sort of intra-trade that happens in similar developing continents and blocs. These barriers stop the growth of supply chains across countries. They keep markets separated and fragmented.

The African Development Bank says that two out of every three countries in Africa find that they experience greater difficulties trading with their neighbours than they do with the rest of the world!

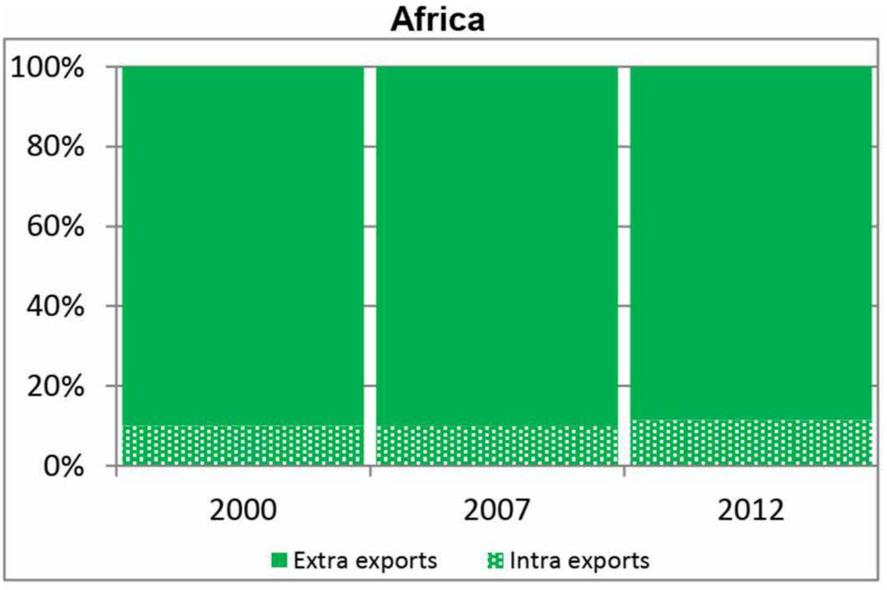
When a country encounters difficulties in sending products to neighbouring countries, compared to countries thousands of kilometres away, there is clearly a problem.

There is a significant amount of intra-trade exports among the developing countries in Asia, amounting to about 50% of exports in Asia in 2012. In the Eurozone there has been a slight downturn in recent years, but about half of the exports of Eurozone countries go to other Eurozone countries. ››





The problem is that Africa is not trading with itself. Instead it is largely trading with other countries. Only about 10% of its exports are moving between African countries (against the 50% benchmark for Europe and Asia). This discrepancy was major motivation for African countries to enter into agreements to launch the AfCFTA.

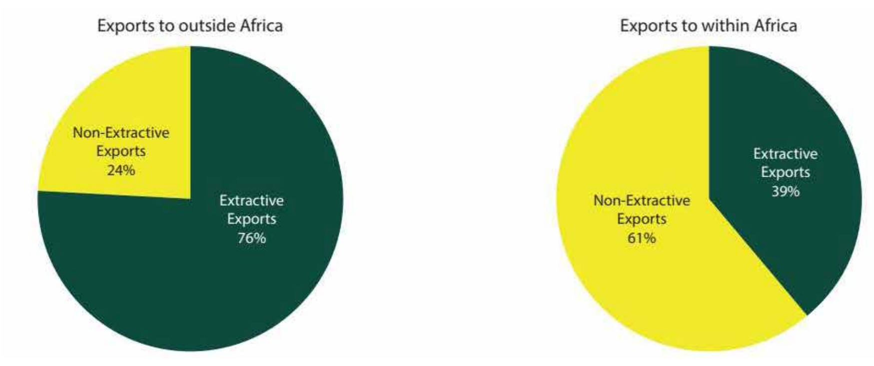


Source: Trade report: Export opportunities for South Africa in selected African countries, May 2014, Industrial Development Corporation

> **African governments see this as an opportunity to move away from a colonial model of trade which largely involves the exports of extractive commodities.**

At Nedlac we identified industrialisation as another significant motivation for the AfCFTA. Trade forecasts suggest African industrial exports will benefit the most from the trade agreement. African governments see this as an opportunity to move away from a colonial model of trade which largely involves the export of extractive commodities such as raw agricultural product, timber, oils and minerals and the import of finished goods. The aim is to increase exports of manufactured goods produced inside the continent and decrease reliance on the exportation of extractive commodities. Until now, 76% of Africa's exports outside the continent have been extractives, while from 2012 to 2014 only 39% of intra-African trade were extractives.

When Africa trades with itself there are far fewer extractive exports and a much bigger proportion of non-extractive exports, which are goods to which some value has been added, on the continent. Clearly for African governments the possibility of adding value to goods is an attractive option. Developing manufacturing industries is far more likely when the continent trades with itself.



Source: African Continental Free Trade Area: Questions & Answers by African Trade Policy Centre (ATPC) of the Economic Commission for Africa (ECA)

South Africa's exports to China, for example, are almost exclusively raw materials, minerals, etc. But as soon as South Africa starts to trade with sub-Saharan African countries, more finished manufactured goods enter the picture, for instance trucks, vehicles, pumps for liquids and machinery. As soon as we trade more within Africa we can move away from the colonial model of trade.

FREE TRADE AGREEMENTS VERSUS PREFERENTIAL TRADE AGREEMENTS

We traditionally have reservations about free trade agreements (FTAs). They usually require the removal of protective import duties, take away the policy space of governments to decide their own developmental paths, and obstruct developmental opportunities to grow local industries, jobs and ultimately economies. FTAs also aften result in damage to new and vulnerable industries and can set in place a downward push on wages and employment conditions. Countries then start competing on low wages and inevitably the losers are the workers and working-class communities.

Preferential trade agreements (PTAs) are much more palatable to our minds. They usually involve a smaller, restricted group of products in the trade agreement and within that there is significant space created for defensive positions to protect vulnerable jobs and industries. In other words, there is space to say we are better at exporting certain products and are prepared to put those products into a trade agreement, but we are not interested in trading in products from smaller, vulnerable industries and we exclude them from the trade agreement. What a PTA typically does is take into account the various levels of development in countries that enter into trade agreements.

We believe that in conceptualising and negotiating the AfCFTA, industrial policy has not led trade policy. Countries first have to identify what they need to grow their industries and jobs. That should set the agenda for a trade agreement. But in the AfCFTA negotiations, political considerations have exerted pressure to conclude this agreement as soon as possible, especially in 2016, 2017 and 2018, even though it was not, and still is not, ready. Many details remain unsettled. We think that negotiations have largely been led by geo-political considerations, which could result in a greater negative impact on jobs and industry in the future.

However, what distinguishes the AfCFTA slightly from other free trade agreements is that there is still significant space for exclusions of certain products and for other products to phase duties down over longer periods to allow sectors to adjust. Within the AfCFTA, 10% of industrial tariff lines can be identified as sensitive and receive special treatment. This means they can either be totally excluded from the agreement and the requirement to reduce tariffs or they can be given a longer period to phase down, which means more time to reduce their duties to zero percent.

But we believe that the present exclusions aren't sufficient. We have made this argument often as Cosatu and Sactwu, saying that we need more space to protect sensitive industries and sensitive jobs. We think that at least 15% of industrial trade lines need to be regarded as sensitive and we have asked government to increase this, or we are at risk of losing thousands of jobs and significant industrial capacity.

WHAT CHALLENGES FACE THE AfCFTA?

While we hear of potential huge new markets of 1.3 billion people, and new countries to export goods to, we think the picture being presented is way too rosy. The opportunities for trade depend on the purchasing power of consumers. The African Development Bank estimates that although we have 1.3 billion people on the continent, the middle class comprises fewer than 350 million people. KPMG, an accounting firm, using a higher threshold, estimates that only about 36 million people on the continent can be described as middle class. This means that there may be significantly less purchasing power for the kind of products that countries will be exporting. Of that middle class, about half resides in South Africa and an additional approximately one million people live in each of five other countries – Ghana, Ethiopia, Kenya, Ivory Coast and Uganda.

We also think that talk about a significant market fails to look at the nature of the retail market on the continent. Half of all African retailing occurs in five countries, Nigeria, Egypt, South Africa, Algeria and Morocco. Together these five constitute just more than half of the retail market, which means that there are much less opportunities for export beyond those markets.

The other important feature of the African retail market is that it is overwhelmingly informal. The UN Economic Commission for Africa said that about 90% of African retail transactions occur in the informal sector. It would therefore be difficult to export new finished products into those markets.

For us, one of the major challenges with the AfCFTA concerns customs. We have doubts about the capacity of South African customs service, and those across the continent, to implement and police trade agreements in Africa. Often, when new trade agreements are set up, especially multilateral agreements involving many countries, there is an increase in customs fraud, including transhipment, misclassification and other types of fraud that are largely intended to abuse the preferences that only the countries party to such agreements should enjoy.

For example, African countries may enjoy a lower duty under the agreement, but traders from countries that are not part of the agreement may try to tranship their goods. They could do this by claiming that goods made in Bangladesh or France, for example, were produced in an African country. They then try to tranship these products into countries such as South Africa at low-level duties. Similarly, traders may misclassify high duty products as products at a lower duty level to minimise or even evade duty. We are concerned that neither South African customs services nor those in other countries have the resources to detect and stop such fraud. This will undermine the objectives of the agreement and the major winners would then not be the African countries but instead traders in other countries who are illicitly claiming the trade preferences in the AfCFTA.

We have suggested some safeguards be built in to ensure that this does not happen, such as beefing up customs services and increased cooperation between African governments to ensure that such fraud can be detected and illegal imports stopped. We have proposed some suspensive conditions

and a review mechanism to be applied when it seems that the AfCFTA is benefitting traders from elsewhere in the world instead of African countries. In such cases, we need to be able to pull up the handbrake and review our capacity to police this agreement.

The other major shortcoming of the AfCFTA is that it doesn't support a social clause or a labour clause. We believe it should include such a clause. Participation in the free trade area should be conditional on the enforcement of workers' rights (such as the right to organise free trade unions, to negotiate conditions of employment and to strike under legal protection). Except for the obvious benefits for workers of a social clause, there are other benefits for countries as well, such as helping create the mass market that the AfCFTA promises by ensuring higher wages for workers as consumers. It will help deal with inequality, which impedes growth. It will have a positive impact on development, allowing for the provision of education and health services. It will also create favourable conditions for a stronger African labour movement and encourage linkages between unions across the continent.

While there has been some interest shown by the South African government in such a clause, across the rest of the continent there has been widespread resistance to it. We in Sactwu and Cosatu believe there may still be space to include a social or labour clause and we have not stopped agitating for this. [This proposal was made by Cosatu in the 1990s before the formation of the World Trade Organisation, at a time when the trade union movement was much stronger than it is today. The proposal died an early death – editor's note.]

POSSIBLE NEGATIVE OUTCOMES OF THE AfCFTA: MITIGATING FACTORS

Like other free trade agreements we could well end up with workers and working-class communities as the main losers. How do we mitigate that? We could ensure sufficient space and rules of origin to protect vulnerable industries and jobs. Another mitigation strategy could be to introduce a social clause to stop a race to the bottom based on wages. A third mitigating factor could be an increased focus on industrialisation and the deepening of industrial value chains across countries, rather than just trading between countries.

Another possible outcome could be that all the promises the AfCFTA claims it will deliver could be undermined by various logistical problems. One of the major mitigating factors may be a significant focus on improving the quality and reach of industrial, trade and transport infrastructure within countries and also between countries. This will have a developmental outcome internally and will also assist countries trading across borders.

Finally, one of the major threats is transhipment and customs fraud with traders outside the continent benefitting from the AfCFTA. For us, the mitigating factor would be stronger and better customs management, cooperation between African countries and safeguards that can be triggered should we find that it is not African countries and African jobs that benefit but largely international traders. NA