PEGNet
Policy Brief

Regional Integration, Trade and Industry in Africa

Helmut Asche

KEY POINTS

- The African Continental Free Trade Area (CFTA) has the potential to overcome major problems of economic integration in Africa, but it is not a panacea and far from being operational.
- A number of the major African RECs are not well integrated despite being officially labelled as customs unions.
- The underlying problem: Working regional integration needs diversified manufacturing industry (and agriculture), as much as industry needs bigger regions to flourish.
- In order to solve the twin problem of creating integrated regions and industry in sync, smart common industrial policy (CIP) is essential, even more than in RECs of advanced economies.
- Important African RECs consider CIP but such policy needs a whole system of institutions, regulations, and financial capacity to work. New Aid for Trade can help.
- Global North-South integration shall not go deeper and further than South-South integration- The Economic Partnership Agreements of the European Union with Africa try exactly this and should be revamped.
- By introducing the double challenge of Industry 4.0 and sustainability into the framework, an outlook of future Green Regions in Africa is provided.

With the advent of the African Continental Free Trade Area (CFTA), regional economic integration in Africa has captured international attention and raised high hopes. In the new book “Regional Integration, Trade and Industry in Africa”, the present state of economic integration on the continent is explored in the context of global trade and plans to foster industrialization. This policy brief summarises the book’s main findings.
The CFTA project has the potential to overcome major shortcomings of regional economic integration so far:

- The market size even in the bigger traditional Regional Economic Communities (RECs) remains below minimum efficient scale for key industries.
- The degree of trade liberalization on the continent is often lower than for third parties, e.g., vis-à-vis the European Union, as there are no free trade agreements between important RECs or single African states.
- Present-day REC overlaps (known as the “Spaghetti bowl”) hinder trade liberalization.

Partly as a consequence of these problems, intra-African trade hovers at around 15% of total trade in goods. The CFTA can help to solve such problems. In addition, the parallel track of CFTA negotiations (in Phase I) on goods and services (along with dispute settlement) is more adequate given today’s realities in which few ‘goods only’ are traded.

However, CFTA design and negotiation mode – as far as it is currently known, thus *under-researched* – are marred by some of the same problems which the underlying RECs in Africa are facing, such as detailed case-by-case market access offers instead of generics, including those for rules of origin. Sensitive product or exclusion lists contain important exceptions from complete internal trade liberalization. Very long transition periods (10-13 years minimum) make such exceptions from African free trade last. Technically, the different liberalization lists and timelines for two or three special country groups violate the established common external tariff (CET) of the existing RECs. More fundamentally, it can be argued with insights from New Economic Geography that full continental trade liberalization would not even be desirable for Least Developed Countries (LDCs), without an effective compensation mechanism, as adverse industrial agglomeration at the poles of the existing regional hegemons (Egypt, Nigeria, Kenya, South Africa) looms. The proposed compensation fund would thus have to cover not only financial tariff losses and adjustment costs but allow for proactive creation of industrial units in a more decentralized pattern. The regional hegemons in turn fear trade deflection of third country imports namely from China and India. Finally, it is important to understand the political economy reasons why the CFTA will never become a customs union and will thus not replace the existing RECs in Africa which strive to become ones (see chapter 6).

The problems enumerated mean in actual practice: As no tariff schedule is agreed, let alone domestication issues solved, trade under the new CFTA scheme has definitely not started January 1, 2021, let alone free trade. With regard to trade, „*there will be no Africa without borders. You may call this trade realism*“ (p. 103).

Part I: the Economic Regions in Africa

The state and prospects of the CFTA project send analysts back to the major existing RECs, meant to be building blocks for the CFTA anyway. Here we observe, on the one hand, the said “Spaghetti bowl” of numerous overlapping RECs used to ridicule African RECs or economic regionalism at large (see chapters 1-5). On the other hand, the African Union (AU) ’officially recognizes’ just eight of these RECs but without giving proper reasons (UMA, COMESA, CEN-SAD, EAC, ECCAS, ECOWAS, IGAD, SADC). Thus, demystification of the existing RECs is badly needed.

A first exercise of applying a matrix of (1) general vs (2) sectoral/issue-related and of (3) functional vs (4) non-functional unions, results in a far clearer pattern of functioning general economic integration schemes, with some borderline cases admitted to the picture (see Figure 1):

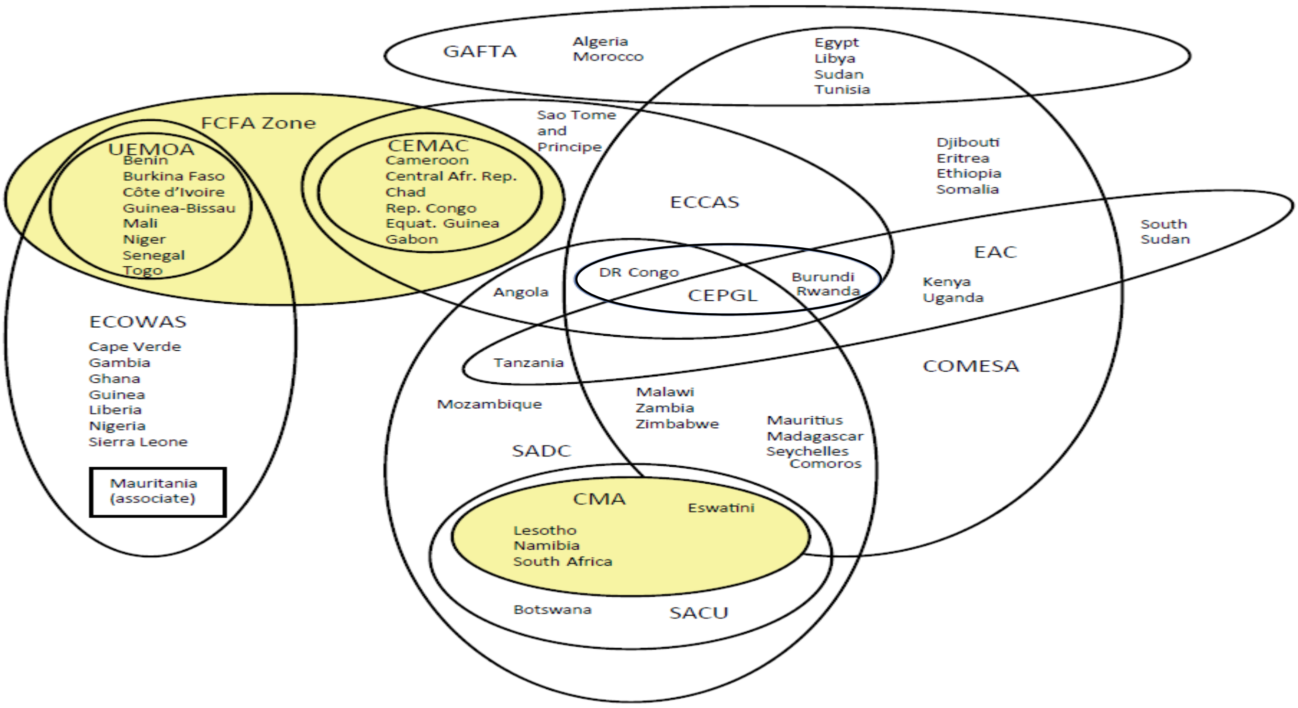
PEGNet
Poverty Reduction, Equity and Growth Network

KIEL INSTITUTE FOR THE WORLD ECONOMY
Kiellinie 66 | 24105 Kiel

E pegnet@ifw-kiel.de
www.pegnet.ifw-kiel.de

@PEGNetKiel

Figure 1 A consolidated picture of African RECs (2021)



Source: Own representation.

- Three of the eight 'official' RECs (UMA, IGAD, CEN-SAD) of the AU have disappeared from the picture, because showing no sign of life or being rather oriented on political issues, such as peace building
- Three economically relevant RECs are re-introduced, incidentally the three post-colonial customs/monetary unions (marked in yellow), and a new one in North Africa (GAFTA)
- As the only country left alone now appears Mauritania, just (re-) associated to ECOWAS
- With the Economic Community of the Great Lake Countries (CEPGL) and the Economic Community of Central African States (ECCAS) being shallow schemes, a "**great vertical trade rift**" in Africa appears (corresponding to Africa's East-West infrastructure gap)

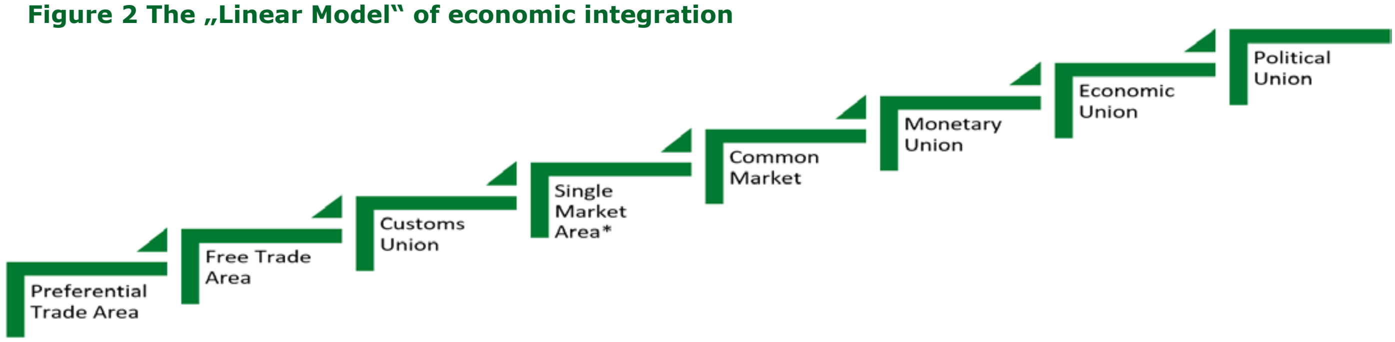
In a second exercise of approximation, REC implementation can be assessed by the "Linear Model" of economic integration (see Figure 2), which is admittedly not linear, much too European, perhaps not desirable as to its ultimate goals, but practical as a yardstick.
With day-to-day reality of trading still *under-researched*, it is safe to say that all major African RECs stand somewhere between formal stages 1, 2 and 3 – blended with elements of higher integration such as a monetary union (see chapter 3), because:

1. Numerous challenges of domestication of the free trade arrangements remain
2. A pervasive "Logic of Exceptions and Exclusions" for specific products prevails, both in the interior of the Free Trade Agreements/Currency Unions and in the application of the common external tariff
3. Non-tariff barriers (NTB) are just partly removed and pop up over and again within the RECs, replacing earlier tariff hurdles
4. In addition, bilateral country-to-country treaties within/across RECs still exist, and some REC overlaps hinder a simple tariff structure, too.

In consequence, there is little unfettered intra-group trade. Instead, we have considerable informal cross-border trade, with strange effects, including a trade-proximity paradox: "The ratio of non-recorded trade in Africa *increases* with every *lower* level of analysis: from global to intra-African, to intra-REC trade and finally to pair-wise cross-border trade of immediate neighbours within one REC, where it seems to be highest."(p. 51)

At an overarching level, a virtuous cycle of regional integration and industrialization does not unfold. Although it is said that most of the (limited) intra-continental trade is in manufactured goods, a closer examination reveals that it consists mainly of processed agricultural goods. Hence, a beneficial industrial division of labour barely evolves, and the aforementioned trade hurdles reflect competition in the same few categories of goods. Low-level diversification among African countries prevails. In consequence, we have **contested regions**, for which the institutions-heavy, protective type of RECs that emulates the 'linear' EU model is called into question by one strand of trade economics, as it produces little additional trade and industry. A lighter model of integration is suggested by institutes such as Tralac (Trade Law Centre for Southern Africa), concentrating more on practical issues of standards, dispute settlement and regulation of services. These critical observers do have a case.
Can the 'classical' RECs in Africa that start with internal liberalization of goods and maintain some external protection nevertheless be defended? This is difficult but not impossible. In the first place, African RECs are in need of a **higher-order project** of integration (p. 108 sqq.), which does away with the logic of exclusions and exceptions, thus achieves full internal trade liberalization and a solid, predictable CET vis-à-vis external partners. Similarly, it would have to fully do away with discretionary NTBs which do not serve any higher developmental purpose (a new NTB typology is offered; p. 28). Then, a free trade area truly becomes a free trade area, and a customs union becomes a customs union. Very much the same applies to the CFTA. Therefore, the CFTA while being pan-African is not in itself of higher order but has to avoid the same pitfalls of discretionary exceptions and exclusions from its own rules.

Figure 2 The „Linear Model" of economic integration



(*) The Single Market Area (SMA) is singled out as a stage of its own, due to the enormous challenges of unifying rules and standards, not identical with the factor liberalization of the Common Market.
Source: Own representation.

The higher-order project of economic integration would have to comprise proactive structural or sector policies, also in service areas. This is what some analysts in Africa call „Transformative/ Developmental regionalism" (p. 115 sqq.) To accommodate such a move, trade theory has to evolve accordingly. Since the start with Vinerian distinction between trade creation and trade diversion, trade theory has had difficulties to model tariff effects other than consumer losses or unwarranted producer windfalls. When treating regional integration based on the assumption of "no imperfect competition / no increasing returns", thus mis-representing reality, the dynamic potential of developing-country RECs is systematically underrated. African RECs inevitably appear to be what they presently are: static. Several theoretical arguments in favour of dynamic effects indicate otherwise (see chapter 4). In the presence of imperfect intra- and extra-regional (global) competition, dynamic effects need intelligent sector policy to be reaped. This marks the transition into part II.

Part II. Industrial Policies in the African regions

From the empirical and theoretical scrutiny of the African REC experience a twin problem emerges: "Industry requires the region to flourish. The region needs industry to strive." (p. 121) Yet this works in neither direction for Africa as a whole. The twin problem turned positively gives the double rationale for an exogenous push, that is smart industrial policy for (a) delivery of industrial commons and (b) correction of market failures in the respective regions.

Industrial policy, however, is among the most difficult sectoral policies by any standard. After having been shunned by mainstream economics for decades, despite its obvious role in the successful catching up in East Asia, essentials of such a 'new', non-prescriptive industrial policy have become some kind of consensus over the last decade, with industrial self-discovery by public-private dialogue as a key element.[1]

Now, some African RECs consider even regional policies, e.g. a Common Agricultural or Industrial Policy (CAP, CIP), for which the EAC, ECOWAS, COMESA or SADC have ambitious strategy documents. However, this is not straightforward. The key question is: *"Should these be national policies within a region, or should truly regional, i.e., common policies of member states be defined? The one (regional policy) does not self-evidently follow from the other (regional problem)." (p. 122)*

As an example from the global North, the sector of Industry or most of Public Health were in the European Union longtime categorized as third-class policy areas (supporting competence), contrary to agriculture (second-class, shared competence) and trade (first-class, exclusive EU prerogative). Just now industry as a joint policy concern is gaining ground in the EU (and Public Health for pandemic reasons) but has not yet seen a lifting of its formal policy status. And in South-South RECs? Four arguments can be advanced why CIP in Africa is crucially needed for the RECs to succeed, even more so than in northern RECs:

1. Severe policy/planning capacity constraints in single, small developing economies
2. A recognized need for regional compensation of imbalances
3. Shrinking policy space for industrial nationalism when RECs deepen
4. A number of supporting policies that are regional by nature and have a bearing on industry or agriculture.

The last argument reads in plain language: RECs already do joint sector policy, mainly as trade policy (e.g., writing a CET or rules of origin, negotiating schedules with third parties); better they do it consciously and systematically. Thus, CIP/CAP is no science fiction in Africa.

Common industrial policy, in application of not less than sixteen design principles, comes with a meaningful concept of 'regional industries', production networks, regional value chains, industrial 'lighthouses', appropriate regional incentive systems, locational/spatial policies, a redesign of regional financial institutions and of regional development aid (see chapters 8, 9). Participation of key regional actors and business associations is needed for the industrial self-discovery to work.
Two small case studies illustrate why not every agro-industrial sub-sector fits the picture, even when these prerequisites are in place: the West African dairy business – not a promising regional industry – and a regional textile industry – which is difficult to mount, but potentially more than a mirage. The perspectives of creating regional value chains vary accordingly.

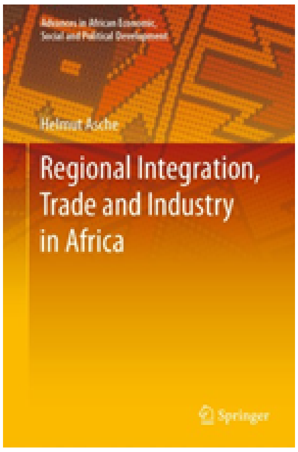
Part III. Global Dimensions of Regionalism

To succeed, regional economic integration among developing countries needs to be properly embedded in global trade processes, considering shallow and deep integration at global scale (see chapter 10). While South-South agreements such as the African RECs mostly remain 'shallow', concentrating on tariff liberalization for trade in goods, they are lured by the global North into deep integration exercises (liberalization of services and investment, etc.). Some trade policy scholars even suggest abandoning South-South treaties in favour of hub-and-spokes models, with the economic hub obviously located in

1 See H. Asche and M. Grimm (2017). "Industrialization in Africa – Challenges and Opportunities", PEGNet Policy Brief No. 8/2017.

Author

Helmut Asche
University of Mainz
PEGNet Advisory Board
asche@uni-mainz.de



the North. Instead, when acknowledging warnings by Stiglitz and others against any 'WTO-plus' agreements suggested to developing countries, a general rule of the global game can be defined: *North-South agreements should not go deeper or run faster than South-South agreements. (p. 196)*

Most obviously, North-South treaties should not outright undermine South-South agreements. The rule is not violated so far by the European trade agreements with Sub-Saharan Africa, as they are restricted to trade in goods and avoid liberalization in services or the so-called Singapore issues (e.g. trade and investment) – at a moment where the African regions just venture into these issues among themselves. The picture is less clear for the market access offers in comparison (see above, on the CFTA).

Regarding the evolution of current trade deals and those to come (including a revamped African Growth and Opportunity Act, which in strict sense is not a treaty but a unilateral US scheme) it should be closely followed how this problematic unfolds, as the global North seeks to apply the three overarching principles 1) Comprehensiveness, 2) Reciprocity and 3) Irrevocability, which taken together represent 'WTO-plus', that is more than developing countries are obliged to concede in GATT/WTO.

When among the number of EU trade regimes specifically the so-called Economic Partnership Agreements (EPA) are put to scrutiny (see chapters 11-13), problems of both country coverage and content become apparent. Regarding the final **country configuration**, the landscape of EPAs remains highly problematic:

1. Single country 'interim' agreements with African middle-income countries such as Côte d'Ivoire, Ghana, Cameroon, instead of full EPAs with the major RECs to which they belong
2. Agreements with REC-subgroups, or groups across REC boundaries
3. The Kenyan Market Access Regulation as a special regime in East Africa.

Not one of the full or interim EPAs, and none of the North African treaties with the EU, corresponds to an African REC. It is literally as if single EU member states concluded trade agreements with, say, ASEAN or other blocs. This petrifies the relapse of major African RECs from customs unions to free trade areas, which already looms with the ruling exceptionalism within African RECs.

Regarding the content of the EU trade agreements, about sixteen topical areas are to be examined, just for trade in goods, starting with the market access offers and comprising trade remedies, export duties, rules of origin, etc. Not all that is retained in the EPAs on these items is per se detrimental to the common policies defined in Part II. Yet, to various degrees EPA clauses are reducing the required policy space, especially for targeted support to new or revived agro-industrial ventures. This is illustrated by case studies on the problem of limiting imports of frozen chicken parts from the EU/US by trade remedies and the impact of export duty reduction on Mozambique's cashew production.

The general conclusion on EPA content is: many single clauses are copy and paste from GATT, seemingly inoffensive, e.g. on countervailing measures, but they drop the GATT's special and differential treatment of developing countries, which is often badly needed in self-defence, and make this turn irrevocable. Hence, EPAs mark a fundamental departure from GATT, and are on both country coverage and content, still untenable from a developmental point of view.

Conclusion & Outlook

Summing up over the three parts of the analysis, African countries face a **triple challenge** of imperfect regionalism, missing industrialization, and unfavorable North-South relations. Regionally inclusive growth, with balanced industrial division of labour supported by common regional policies can provide a remedy to the first two challenges. This is conditional on North-South treaties that do not reduce the required policy space in the South. The analysis contained in the volume presented did not distinguish between different kinds or levels of industry. It was all manufacturing. By introducing Industry 4.0 and sustainability issues into the analytical framework, we enter largely uncharted territories, that is the twin digital and ecological change in Africa. On the trajectory from the great unbundling to reshoring of industrial tasks, regional (re-)concentration combined with sustainable production lines may emerge as an unexpected chance for Africa's regional value chains, definitely another under-researched area: African **„Green Regions"** to come?!