Submission to the Inquiry into Africa Free Trade initiative (AFTi)

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The views expressed here are not necessarily those of the World Bank Group or its Executive Directors. This submission outlines three aspects of the importance of regional trade integration in Africa for development and poverty reduction. First, there are great challenges, but consequently there is enormous untapped potential through regional integration in Africa to deliver poverty reduction and development gains. Second, we must take a fresh look and reinvigorate some regional integration initiatives if the continent is to become better integrated. Finally, that the World Bank Group and other development partners should be ready to intensify support for those governments and regional communities that are committed to use deeper regional integration as a key tool to drive economic diversification and poverty reduction.

1. The challenge being faced - and the opportunities that exist if these challenges can be overcome

Regional trade integration has long been a strategic objective for Africa yet, despite some success in eliminating tariffs within regional communities, the African market remains highly fragmented. A range of non-tariff and regulatory barriers still raise transaction costs and limit the movement of goods, services, people and capital across borders throughout Africa.

Barriers to trade continue to limit integration in all African regional groupings. By imposing unnecessary costs on exporters these barriers raise prices for consumers, undermine the predictability of the trade regime, and reduce investment in the region.

Two concrete examples highlight this[1]:

- If the residents of San Francisco faced the same charges in crossing the Bay Bridge to Oakland as do residents crossing the Congo River between Kinshasa and Brazzaville, a similar distance, the cost would be more than $1200 for a return trip. The high cost of the Kinshasha-Brazzaville crossing means that passenger traffic at this obvious focal point for cross-border exchanges between the two Congos is around five times smaller than that between East and West Berlin in 1988. This is, of course, before the dismantling of the Berlin Wall!
- In southern Africa, licences and other requirements mean that a truck serving supermarkets across a border may need to carry up to 1600 documents. Slow and costly customs procedures and delays caused by agencies operating at the border raise the costs of trading. For example, one supermarket chain in Southern Africa reports that each day one of its trucks is delayed at a border costs $500, and it spends $20,000 per week on import permits to distribute meat, milk, and plant-based goods to its stores in one country alone.

[1] Drawn from Brenton, P. and Isik, G. (eds.) (2012) "De-Fragmenting Africa: Deepening Regional Trade Integration in Goods and Services," Washington, DC: World Bank.

It is estimated that intra-African trade costs are around 50% higher than in East Asia, and are the highest of intra-regional costs in any developing region[2]. The result of these high costs is that Africa has integrated with the rest of the world faster than with itself, with many export-oriented efforts focused on trade with distant markets rather than neighboring countries in the region.

A reflection of this greater focus on extra- than intra-regional trade is that recent export growth in Africa has been driven primarily by commodities, with limited impacts on employment and poverty. This is of particular concern now that traditional markets in Europe are stagnating and the relative slow-down in the Chinese economy has heralded the end of the commodity price super cycle.

Some of the opportunities that could come about through greater regional integration include:

- Bringing staple foods from areas of surplus production across borders to growing urban markets and food deficit rural areas. Indeed, Africa has the potential to feed Africa. But at present only 5% of Africa's imported cereals come from other African countries.
- A significant amount of cross-border trade takes place between African countries at small scale and is not measured in official statistics. Allowing these traders, many of whom are women, to flourish and gradually integrate into the formal economy would boost trade, as well as the private sector base for future growth – as well as having swift impacts on poverty.
- With rising incomes in Africa there are emerging opportunities for cross-border trade in basic manufactures such as metal and plastic products that are relatively costly to import from the global market.
- The potential for regional production chains to drive global exports of manufactures, such as those in East Asia, has yet to be exploited. There are also opportunities to develop regional value chains around mineral commodities such as phosphates for fertilizers and regional processing of nickel and copper.
- And cross-border trade in services offers untapped opportunities for exports as well as better access for consumers to critical services such as health and education and firms to services such as accountancy and other professional services that boost productivity.

2. Taking a fresh look at African integration in terms of poverty impacts

The incidence of barriers to regional trade fall most heavily, and disproportionately, on the poor. Poor farmers in rural areas are denied access to markets in neighbouring countries that would deliver higher returns. The opportunities for them to raise their productivity by using higher yielding seeds and greater application of fertilisers are stymied by restrictions which prevent the emergence of more efficient regional markets in crop inputs. Barriers at borders particularly afflict small-scale traders, preventing them from earning a living in activities where they have a comparative advantage—catering for smaller, local markets across borders. Most of these small

[2] Based on the WB-UNESCAP Trade Costs Database. See Chapter 2 in OECD/WTO (2015), *Aid for Trade at a Glance 2015: Reducing Trade Costs for Inclusive, Sustainable Growth*, OECD Publishing, Paris

scale, poor traders are women and their trading activities provide an essential source of income to their households. Their profit margins are small, and are reduced by every delay or extra charge they face. They are also vulnerable to abuse. Hence tackling barriers to intra-African trade can have disproportionate, positive effects on the poorest people. This makes greater African trade integration central to the goal of ending poverty and to the aspirations of African governments and communities.

To end extreme poverty, policies to increase the contribution of intra-regional trade to growth will need to be matched with a new effort to maximize the gains of trade for the poorest. This entails tackling constraints faced by the extreme poor – including those generated by rural poverty, gender inequality, fragility and conflict, and the nature of the informal economy. These issues were explored in detail in the joint flagship publication by the WTO and World Bank Group, *The Role of Trade in Ending Poverty*, published in June 2015[3].

Regional integration can play a key role in maximizing the benefits of trade opportunities for the extreme poor in a number of ways:

- in linking rural communities to markets to improve access to new technologies, such as higher yielding seeds, and to markets for the goods and services they produce,
- in leveraging trade and cross-border exchange to generate solidarity between communities in fragile states and enhance opportunities for sharing the benefits of growth and increasing prosperity.
- In providing a route for small firms to grow and increase their capacity to leave the informal sector and thrive in the economy.
- In assisting women in dealing with poverty by providing more opportunities for jobs and better returns from cross-border trading activities[4].

The extent to which trade leads to increased economic activity in the areas and sectors in which poor people earn their livelihoods is critical for poverty reduction. Rather than exporting minerals and fuels to distant markets, greater intra-African trade of goods and services would support more employment-intensive activity than exports from extractive industries. Greater intra-African trade is likely to have a more direct impact on poverty by creating opportunities for the poor who both produce and trade the basic foodstuffs dominating intra-regional trade.

However, there is typically insufficient attention to the goal of eliminating extreme poverty and sharing prosperity in the design and implementation of regional trade agreements – and no attempt to monitor the impact and contribution of regional integration towards achieving these objectives. While increasing the share of regional trade in total trade is the headline objective that most policy makers like to discuss it tells us very little about whether commitments in regional trade agreements to reduce trade costs are actually being implemented to the benefit of the poor. Indeed, the popular indicator of successful regional integration can be very misleading -

[3] World Bank Group and World Trade Organization, 2015. *The Role of Trade in Ending Poverty*. World Trade Organization: Geneva

[4] For further detail see Brenton, P., Gamberoni, E., Sear, C. (eds); (2013) *Women and trade in Africa: realizing the potential*. Washington, DC: World Bank.

recent declines in commodity prices are likely to be reflected in increases in the share of regional exports in total exports for a number of countries in Africa! What we need is to build indicators from data that measure directly the trade costs face by the poor.

In addition to renewing the focus on poverty reduction, our experience also points to a number of ways in which policymakers and the regional community can increase the impact of regional integration efforts. Looking ahead, our experience and analysis suggests a number of key messages to guide implementation of regional agreements in Africa:

- Effective regional integration is *more than removing tariffs—it is about addressing on-the-ground constraints that paralyze the daily operations of ordinary producers and traders*. To deliver integrated markets that attract investment in agro-processing, manufacturing and new services activities, we must work together to move beyond tariff reduction toward a more holistic process of deeper regional integration.
- This calls for *regulatory reform and, equally important, for capacity building among the institutions that are charged with enforcing the regulations*. This entails engagement with national institutions as well as those at the regional level.
- The integration agenda must cover *services as well as goods*. Why? Because services are critical, job-creating and productivity-enhancing inputs into the competitive edge of almost all other activities and are of particular importance in allowing firms to participate in regional and global value chains.
- *Action is required at both the supra-national and national levels*. Regional communities can provide the framework for reform, for example, by bringing together regulators to define harmonized standards or to agree on mutual recognition of the qualifications of professionals. Imagine the benefits of allowing African doctors, nurses, teacher, engineers and lawyers to practice anywhere in the continent, regardless of the African country they come from. But responsibility for implementation lies with each member country.

Beyond this we have recently looked at political economy factors and identify four key issues that are likely to lie behind successful regional integration[5]:

a. *Lead government or governments* – successful integration typically requires at least one government to drive and coordinate the process
b. *A key role for the private sector* – successful integration needs strong and broad based private sector support
c. *Simplicity over complexity* - Complex negotiations across range of government agencies provides groups opposed to integration scope to block progress – and strains the capacity of many governments
d. *Flexibility over rigidity* – a rigid top down approach through the RECs can constrain integration when states have divergent integration priorities. Implementation of specific

[5] Brenton, Paul and Hoffman, Barak (eds) 2015. *Political Economy of Regional Integration in Sub-Saharan Africa*. Washington DC: World Bank.

commitment by for subset of countries may be more effective – with other partners following when ready.

3. The role of the World Bank Group and other Development Partners

The World Bank together with its development partners can play an important role in helping Africa integrate with itself and in supporting effective implementation of regional agreements, the Tripartite Agreement and the Continental Free Trade Area - working in partnership with regional secretariats, the African Development Bank, the African Union, the United Nations Economic Commission for Africa, among others. The specific contribution of the Bank lies in delivering just-in-time technical advice for capacity building and in leveraging the available financing instruments, regional investment operations and a new instrument a “Regional Development Policy Operation” to countries that decide to jointly implement policies leading to mutual trade integration.

Trade facilitation is a strong focus of World Bank Group’s work and that of other development partners: more than half of our trade-related assistance is devoted to trade facilitation. Lowering trade logistics costs are vital to efforts of developing countries to integrate more closely in global and regional markets. Of particular importance is to complement investments in infrastructure with support for the policy and procedural reforms that deliver lower trade logistics costs. This may often have to be supplemented by an effective competition policy that ensures that competition between trade logistics service providers so that the benefits of improved infrastructure and trade procedures are passed on, especially to poor consumers and producers.

The Bank is ready to work with development partners such as DfID to support countries and regional communities to monitor the impacts of regional integration so that policy makers are better able to assess progress and fine-tune the regional integration reform agenda where necessary. In particular, we are focusing on measuring trade costs for the poor to ensure that regional initiatives deliver benefits for the poorest. We are also providing concrete support to the institutions of regional integration to enhance their capacity to monitor and assess the effective implementation of regional liberalization efforts. Effective monitoring will have to have a gender lens and capture how regional integration is better connecting the poor to new opportunities through trade in rural areas, in the informal sector and in fragile states.

But, finally, we also recognize that while trade openness and deeper regional integration are critical, alone they may not be enough. A range of complementary policies helps maximize the gains from trade integration for the poor – including policies related to human and physical capital, access to finance, governance and institutions and macroeconomic stability. To achieve this will require deeper cooperation across sectors, better coordination across government ministries and agencies and that a wider range of stakeholders work effectively together.