

Imperial™

beyond possibility

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**The African
Continental Free
Trade Area Agreement -
unlocking value on the African continent**

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About Imperial:

Imperial is an African focused provider of integrated market access and logistics solutions.

With a focus on the following key industries - healthcare, consumer, automotive, chemicals, industrial and commodities - we take our clients' and principals' products to some of the fastest growing and most challenging markets in the world. Ranked among the top tier global logistics providers and listed on the JSE in South Africa, we seek out and leverage new technology to deliver innovative, end-to-end solutions. Through our significant African footprint and international expertise, and with the support of our 25,000 people, Imperial's purpose is to connect Africa and the world - and to improve people's lives with access to quality products and services.

The African Continental Free Trade Area Agreement - unlocking value on the African continent

Prior to the onset of the COVID-19 pandemic, Africa displayed significant economic growth, approximately 3.4% annually, and was home to six out of ten of the fastest growing economies in the world. Although the pandemic has placed strain on economic activity on the continent, medium and long-term economic prospects remain promising. This is complemented by positive demographics on the continent, with the United Nations forecasting that the population of Africa is expected to increase to 1.7 billion in 2030 and 2.5 billion by 2050, with 26% of the world's working-age population predicted to be living in Africa by 2050. These fundamentals bring immense opportunities for African countries, and the timeous implementation of the African Continental Free Trade Area Agreement (AfCFTA), which was enacted in 2018 and came into effect in January 2021, is therefore a necessity.

The AfCFTA envisages seamless trade, travel and transport and a single African passport for all African Union member nations. The objective is to phase out tariffs on 90% of goods within ten years and create a continent-wide single market for goods and services with free movement of business, people and investments. Another important goal of the AfCFTA is to create jobs, particularly for women. According to the United Nations Economic Commission for Africa (UNECA) and the African Trade

Policy Centre, women are estimated to account for around 70% of informal cross-border traders¹.

As of early October 2021, 41 countries have complied with their domestic requirements for ratification of the AfCFTA, and 38 of those countries had ratified the agreement, 9 of which are Southern African Development Community (SADC) member states – Angola, eSwatini, Lesotho, Malawi, Mauritius, Namibia, South Africa, Zambia and Zimbabwe.

The COVID-19 pandemic and vaccine roll-outs have highlighted the importance of the logistics industry in Africa, as well as the opportunities this industry presents in terms of connectivity, distribution and supply chain efficiencies in key industries. The growing consumer base and increased access to the consumer in Africa are particularly appealing to both multinational and local organisations. However, logistics presents a major challenge, including the cost of moving products into and out of Africa being exorbitant in comparison to other continents, and getting those products to consumers in Africa remains complex. As one of the largest logistics players on the continent, and with logistics being integral to facilitating trade, Imperial believes that the AfCFTA will play an important role from a logistics and transport perspective as countries start embedding trade links.

¹Mail & Guardian



A Platform for Improving Trade in Africa

The AfCFTA represents the world's largest free trade area due to the number of countries participating. By 2030, Africa is set to have a potential market of 1.7 billion people, a combined expected GDP of approximately USD3 trillion and a total consumer and business spending projection of USD6.7 trillion². With an expected consumer market as large as China, added to the mineral and natural resource endowment of Africa, the full potential of the AfCFTA is extraordinary. It is anticipated that trade facilitation measures to cut red tape and simplify customs procedures would drive USD292 billion of the USD450 billion in potential income gains by 2035. The AfCFTA will provide a platform to not only boost trade within Africa, but also the quality of trade in terms of improved efficiencies, more markets, among other benefits. Currently only 16% to 18% of goods produced in Africa go to other African countries; African countries imported R8 trillion worth of goods in 2019, only R1 trillion of which came from other African countries³. The AfCFTA is also expected to lift around 68 million people out of poverty, a critical element as African countries look inward for solutions to the continent's socio-economic challenges.

² Brookings

³ Freight News



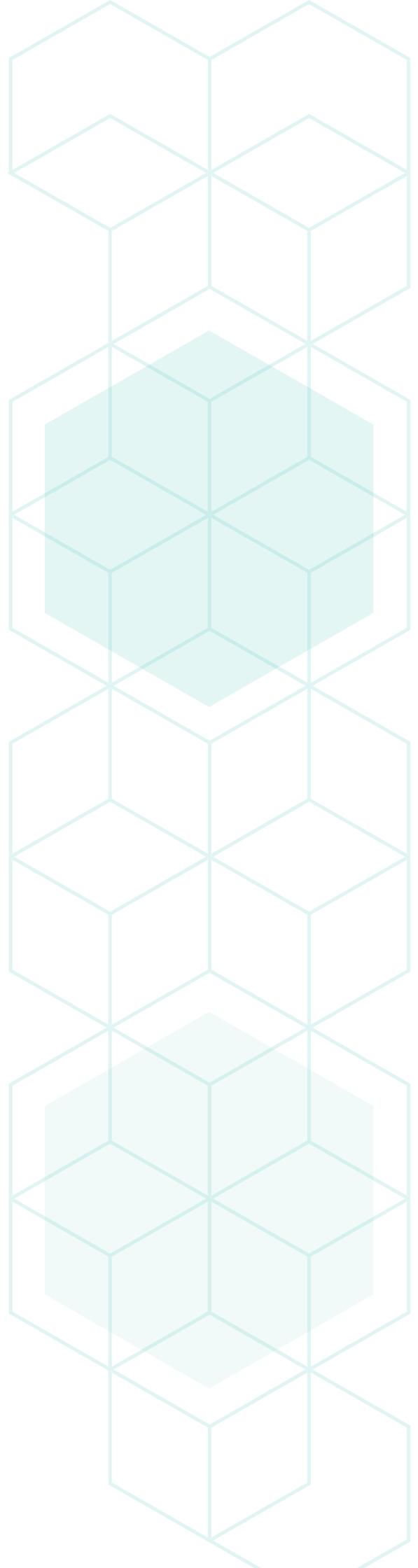
Current Challenges Facing African Trade

The AfCFTA negotiations are scheduled to include a protocol on eCommerce, which could present an opportunity for African countries to collectively establish common positions and leverage the benefits of eCommerce, as well as potentially harmonise digital economy regulations.

Currently, the lack of reliable online payment systems is limiting cross-border eCommerce. Complicated and time-consuming payments are compounded by foreign exchange restrictions and controls. In addition, not having payment guarantees means high costs related to debt recovery and write-offs. Generally, consumers are concerned about security of payments and the risk of being defrauded, which also contributes to their reluctance to embrace African cross-border eCommerce. Cross-border trade law enforcement is deemed to be weak, which further negatively affects consumer demand for eCommerce. However, those companies that have developed a good reputation for working in Africa over time, instil confidence in their customers and have thereby enjoyed eCommerce success⁴.

Another big challenge for countries in Africa is infrastructure interconnectivity to enable trading. While South Africa has one of the best road and rail networks on the continent, many other countries have poor road and rail links and excessive border bureaucracy, which hampers efficient cross-border trade. Poor land infrastructure means that air and sea

⁴ Supporting Economic Transformation (SET)



freight are most commonly used, but these present challenges. For example, air freight is costly and does not effectively cater for large volumes, while sea freight takes longer, and landlocked countries must still rely on road infrastructure to get products from neighbouring countries. Better rail and road infrastructure will mean lower cost-to-serve and more efficient service. The Africa Finance Corporation recently secured USD250 million in financing from the U.S. Development Finance Corporation to help fund infrastructure projects on the continent, which bodes well for the AfCFTA⁵.

There seems to be scepticism about the pace of change under the AfCFTA agreement. One of the biggest problems is that Africa's efforts to attract foreign investment to boost development and industrialisation have not had much success. The continent is still marginalised in the global political economy, attracting barely 5% of global foreign direct investment (FDI) flows. The COVID-19 pandemic has had a significant impact on FDI flows into Africa, with a decline of 16 in 2020 compared to 2019, and recovery is threatened by weak economic growth and slow vaccine roll-out programmes⁶. However, to mitigate these adverse effects, Africa needs to ensure greater policy consistency, develop a strong regional integration agenda and through savvy economic diplomacy, countries should utilise the changing geopolitical and investment landscape for commercial and political benefits, in line with their strategic objectives, while also playing a strong role in alleviating socio-economic challenges faced throughout the continent.

In addition to some of the challenges mentioned above, the implementation of AfCFTA in certain regions across the continent will be impacted to some degree by various global supply chain disruptions and bottlenecks (e.g. port congestion, container imbalances, global trade volume imbalances, freight rate increases, driver/labour shortages and the shortage of semi-conductors) that are currently being experienced globally, some of which are expected to continue into 2022. Port congestion and container imbalances are negatively affecting trade flows across the globe and unfortunately Africa is not considered a priority destination for many shipping lines at the moment. In fact, the lack of cargo in the Port of Mombasa has created a "price war" amongst transport companies. Many empty containers are currently sitting in certain African ports and are not being collected by the shipping lines, which is compounding the container imbalance situation.

⁵ Africa Finance Corporation

⁶ UNCTAD





Opportunities for Growth

For the past ten years, South Africa has been the main player in terms of inter-African trade and already has customs arrangements in place - the duty-free Southern African Customs Union (SACU) and the Free Trade Agreement (FTA) in the SADC region - and is ready to start trading under the AfCFTA.

At present, most intra-African trade comes from the SADC, hence the AfCFTA will open the north and west African markets, where South African companies have not been competing successfully due to high trade duties. For example, Ghana levies customs duties of between 20% and 35% for consumer products. In the absence of an Africa trade agreement, local trade in this region is limited to Economic Community of West African States (ECOWAS) countries with no import duty, as imports from SADC countries are not competitive. Within ECOWAS countries, most trade utilises road transport, however, with the AfCFTA, logistics costs will remain low within Africa due to the availability of sea transport. Key countries that have domestic manufacturing capabilities, such as South Africa, Egypt and Nigeria, may benefit the most through exports to smaller African countries, which are currently dependent on Asian imports. The AfCFTA should increase the market size for any investment consideration, as Africa's population size is comparable to that of China or India.

The private sector in Africa will play a critical role in speeding up

industrial development and economic diversification, particularly in the context of the ongoing pandemic and other development challenges. The private sector accounts for approximately 80% of total production, 67% of investment, 75% of credit and employs 90% of the working age population. Several determining factors, including an enabling business environment, affordable connectivity, accelerated digitalisation and opportunities to forge strong public-private partnerships are crucial to ensuring businesses' commitment to trade and investment in the AfCFTA⁷.

South Africa plans to improve access to African markets with the upgrade of its six busiest border posts, the first being the 92-year-old Beitbridge border post, which was last upgraded in 1995. Imperial believes that while the AfCFTA provides a framework for improvement, the agreement alone cannot improve the efficiency, capacity and systems of customs authorities and border posts. It can also not prevent government interference, poor policies or restrictive tax regimes. We have a presence in over 20 countries across the African continent, through a combination of our footprint of in-country operations and our partnership network, and many of these countries are landlocked where logistics costs depend as much on the efficiency of neighbouring transport services and border processes, as their own⁸.

There are vast distances between markets on the continent, which also means that transferring products at different levels of the value chain can be costly.

This challenge is further exacerbated by the lack of enabling infrastructure connecting countries, especially rail, which can provide cost-effective transportation. In 2019, Africa had fewer kilometres of road than it had 30 years ago, and the highest costs of transporting goods in the world. Due to these logistical challenges, including poor road infrastructure and a lack of rail infrastructure, some companies find it more cost-effective to ship goods from an African country to another continent and then on to another African country. Given that in order to build effective regional value chains, raw materials and intermediate goods may need to move across multiple countries (for production) and finished goods may be sold in many markets on the continent, costs can build rapidly if transportation between countries is costly and inefficient due to poor transport infrastructure that causes delays⁹. The need to accelerate one-stop border posts on the continent at large can therefore not be over-emphasised.

We have seen how conditions-of-entry regulations currently differ from country to country, and this impacts the operations of many businesses across Africa, including delays at certain border posts and ongoing issues along strategic points across corridors such as Beitbridge. Imperial believes that technological advancements will play a key role in tackling some of these and other big issues that have prevented trade from growing in Africa, including reducing red tape and easing supply-chain bottlenecks. Governments will also need to provide

⁷ Africa News

⁸ International Trade Centre

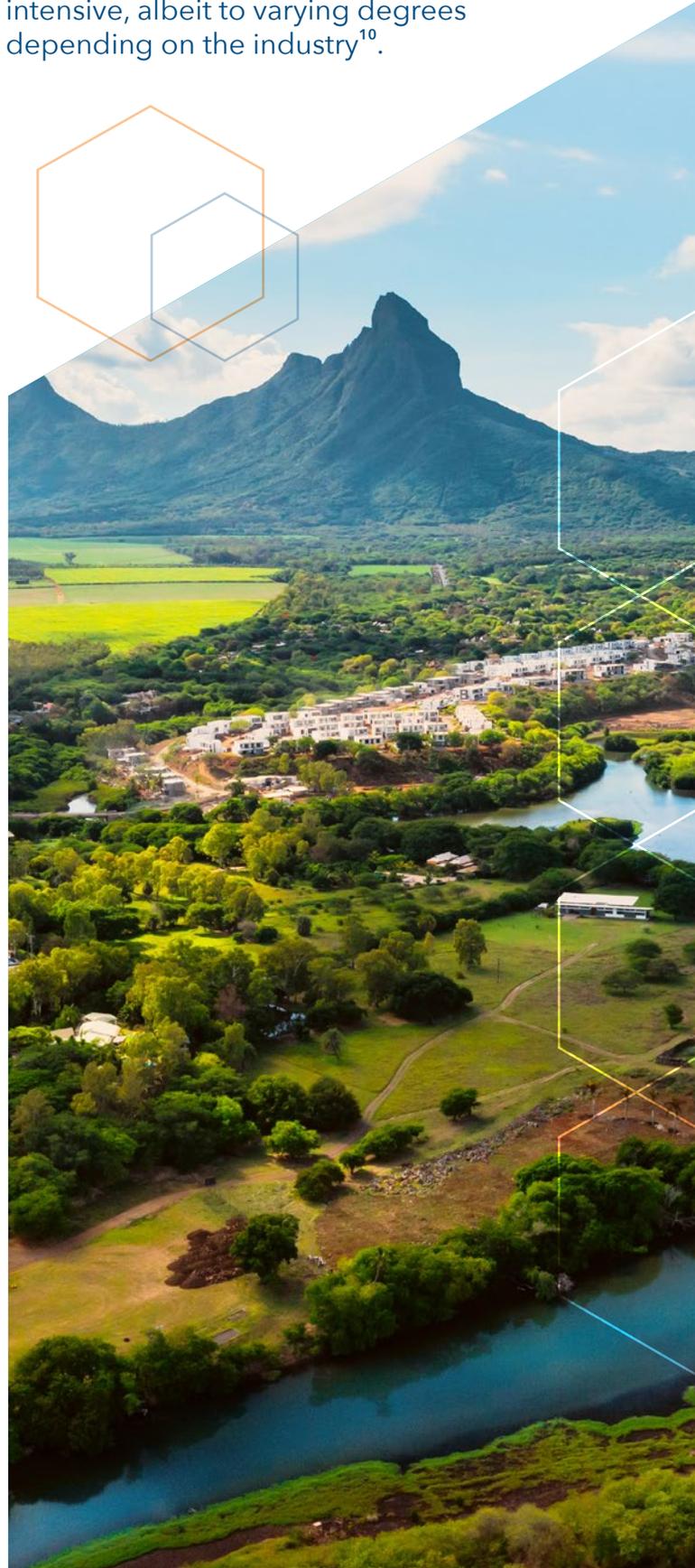
⁹ World Economic Forum

support by building infrastructure because true operational benefits will only be achieved after significant infrastructure investment is made in road, rail and port facilities. In addition, governments have to ensure that regulations do not serve as a constraint.

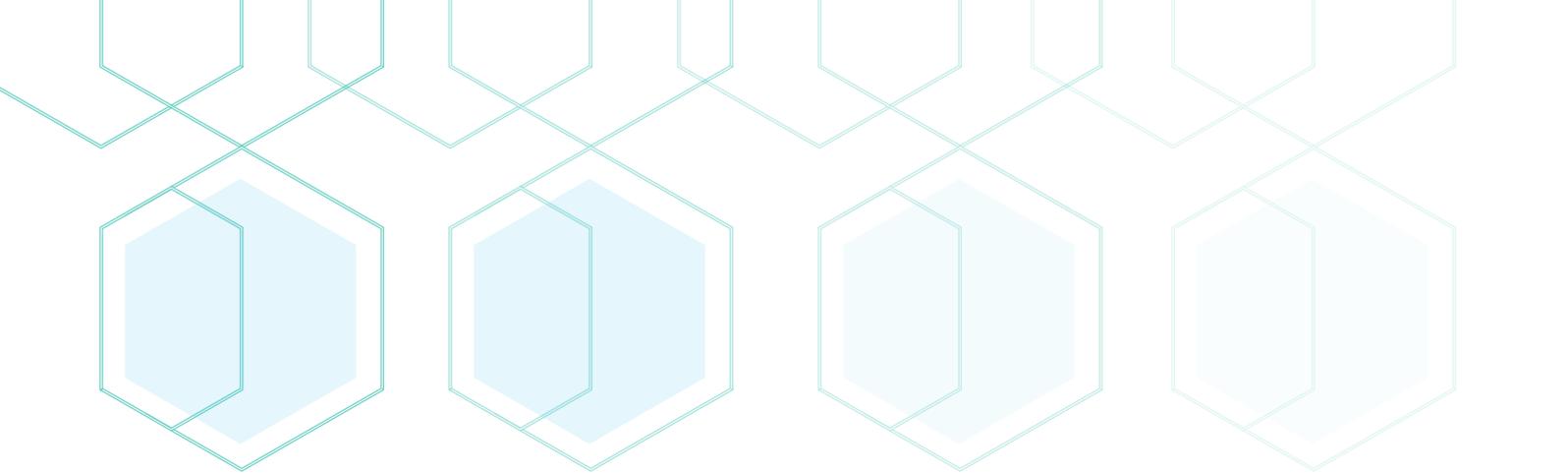
With Africa's emerging technological capabilities and the need to invest in infrastructure, digital services and solutions seem to offer the most logical and effective large-scale expansion opportunity. However, this would depend on successful negotiations to keep restrictions on cross-border services to a minimum, as well as investment. It is encouraging to note that negotiations are underway with representatives in select countries to open up the service sector, specifically business services, communication, financial services, transport and tourism.

From a transport and logistics perspective, Imperial believes that last mile delivery is the key to trade. The future of trade depends on full logistics/delivery solutions with minimal restrictions. Excessive bureaucracy can be avoided for transit stocks to landlocked countries if customs duties are not applicable. The AfCFTA does not currently provide any incentive to directly service industries such as transport, however, it does open up a larger market. Without customs duty, we expect cross-border transactions by unauthorised traders to reduce, and as the official distribution partner we can then better service our clients, principals and customers. An analysis conducted by the International Trade Forum estimates

that the transport sector will experience the greatest boost from AfCFTA a USD286 billion, followed by business services at USD207 billion, which are relatively income inelastic and low-skill intensive, albeit to varying degrees depending on the industry¹⁰.



¹⁰ International Trade Forum



Impact on the Healthcare Sector

With respect to goods, the sectors that should immediately benefit from trade liberalisation include agro-processing, automotive, pharmaceuticals, textiles, chemicals and mineral beneficiation. Imperial's experience in the healthcare sector, mainly through its Market Access business, indicates that patients do not have universal access to healthcare due to restrictive policies and regulations. Healthcare should be prioritised to benefit from free trade and liberation to boost the sector on the continent. The pharmaceutical industry in Africa is one of the fastest growing sectors of business in Africa, increasing in value from USD14.5 billion in 2010 to around USD60 billion in 2020¹¹. This makes Africa a prime market for multinationals and pharmaceutical companies seeking new growth opportunities as traditional markets stagnate. The rapid growth of the pharmaceutical industry in Africa also bodes well for African patients, who will now gain access to previously unavailable medicines.

Although pharmaceutical products are currently manufactured in South Africa, Kenya, Morocco and Egypt, as a whole, Africa currently imports more than 80% of its pharmaceutical and medical consumables¹², which, under current circumstances, is unsustainable. The AfCFTA, once successfully implemented, will address the challenge of small, fragmented markets that have long discouraged pharmaceutical manufacturing investors.

African pharmaceutical manufacturers that are currently operating in these markets cannot compete with their Asian counterparts that operate in vastly larger markets and therefore enjoy economies of scale. A pooled procurement mechanism will encourage leading global generic pharmaceutical manufacturers to build plants in Africa or partner with African pharmaceutical companies to manufacture generic products. Total delivered cost (up to 40%) of medicines in Africa is made up of supply chain, distribution and other non-core costs, which should see an improvement once the AfCFTA agreement is fully implemented, making pharmaceutical products more affordable to more African people. Increased cross-border volumes will improve economies of scale, particularly when it comes to dealing with volume imbalances on major corridors in the SADC region.

¹¹ United Nations Industrial Development Organization

¹² United Nations African Renewal Magazine



Looking Ahead

One of the agreement's ambitions is to double intra-African trade by 2035 from the current level of 18%. However, according to Francois Fouche from Growth Diagnostics, in collaboration with the North-West University Business School, not much has changed as yet¹³. Although many countries have reduced their taxes, making some goods eligible for lower tariffs, not all the customs processes have been finalised. As a result, South African goods are still attracting high tariffs. Fouche cited two examples - Kenya is a major flower exporter, but Nigeria imports flowers from the Netherlands. Nigeria produces palm oil, but Kenya purchases the product from Malaysia. Fouche believes that "African countries will not be trading with each other, free of import tariffs, for a considerable amount of time".

The uncertainty and the economic impact the COVID-19 pandemic has had on the continent remains a threat to the implementation of the AfCFTA. Participation in and the realisation of the AfCFTA is confronted with many challenges, and we believe that in order to maximise benefits of the AfCFTA, the continent must adopt a 'One Africa' inclusive approach that involves all key players such as governments, private sector and communities. In addition, technological advancements will be a key enabler of the AfCFTA as this is key to tackling some of the major issues that have prevented trade from growing in Africa.

Many of Imperial's clients and principals, including both multinationals and local companies, are looking at ramping up their manufacturing facilities in selected countries where Imperial will play a pivotal role in getting products to end-users across the continent. Over the years, Imperial has acquired well-established companies and capabilities, particularly in the healthcare and consumer industries, that are well positioned to take advantage of the benefits of the AfCFTA in terms of increased intra-regional trade. We are excited about the opportunities that the AfCFTA will unlock for the continent and its people, allowing Imperial to further demonstrate our purpose of connecting Africa and the world and improving people's lives with access to quality products and services.

¹³ Biashara Services and Products Africa Conference and Exhibition 2020

**For more
information:**

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