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Role of Tariffs in the Implementation of African Continental Free Trade Area Agreement (AFCTA)

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Introduction

A tariff is a tax imposed by the government on imported commodities. In general, a country imposes tariffs for two reasons: to increase government revenue or to reduce the import of specific goods. Tariffs measure trade cost and price on imports, as well as being an indicator of a country's openness. For this reason, tariffs are often used to measure the effects of trade liberalization.

Tariff reduction is a quintessential feature of PTAs as member countries aim to gain better access to each other's market. However, member countries often pursue "deeper integration" through agreements on non-tariff matters as well. Non-tariff measures (NTMs) typically cover competition policies, product standards, regulatory regimes, investment codes, environmental policies, labor standards and so on.

The trade effect of NTMs can be either positive or negative. On the one hand, legally binding agreements can reduce uncertainty for traders arising from unilateral policy interventions (Bagwell and Staiger, 2002). On the other hand, some member countries may use NTMs to protect import-competing industries, especially those with strong lobbying power. Under the General Agreement on Tariffs and Trade (GATT), PTAs are allowed as an exception to the clause of Most Favored Nation (MFN) only if all duties are eliminated on "substantially all" trade between the member countries within a reasonable length of time. As such, countries wanting to protect specific industries can only resort to non-tariff barriers (NTBs) disguised as GATT-complying NTMs (Limao and Tovar (2011) show that tariff commitments in trade agreements increase the likelihood and restrictiveness of NTBs.

NTBs have risen during the mid-1990s to 2000 and then again after the Global Financial Crisis (WTO, 2012). Consequently, there has been a steady increase in sanitary and phytosanitary (SPS) measures and technical barriers to trade (TBTs) notifications by WTO members since 1995 (Bacchetta and Beverelli, 2012). The GATT and WTO have already reduced tariffs substantially, as evident in the merely five percent average duty worldwide, tariff reduction arising from future PTAs will be moderate; consequently, NTMs may become increasingly important in determining the impact of PTAs.

African Continent Trade Landscape

The African continent accounts for less than 3 percent of world trade (UNCTAD Stats, 2018). Commodities and natural resources continue to dominate Africa's export basket, and the continent's participation in the global value chain has been minimal. In terms of intra- African trade, Africa continues to trail other regions which have drawn on vibrant cross-border trade to sustain growth and economic development, as well as integration into the global economy. At

about 15 percent, Africa compared unfavorably to Europe (68 percent), North America (37 percent), and Latin America (20 percent).

Over the past few decades, the African continent has experienced a proliferation of sub-regional agreements, including the East African Community (EAC), the Common Market for Eastern and Southern Africa (COMESA), the Economic Community of West African States (ECOWAS) and the Southern African Development Community (SADC). That proliferation has raised concerns over the potential costs imposed by the fragmentation of the continent's trading system into exclusive blocs, especially in a context of low intra-regional trade performance. Cognizant of the importance of intra-regional trade, the 18th Ordinary Session of the Assembly of Heads of State and Governments of the African Union, held in January 2012, endorsed the framework and road map for the establishment of the African Continental Free Trade Area (AFCTA) by an indicative date of 2017through negotiations on the liberalization of trade in goods and services

African Continental Free Trade Area Agreement (AFCTA)

The AFCTA is a consolidation of the Tripartite Free Trade Area and other regional free trade areas and is expected to create the largest free trade area in Africa. It covers a wide scope of formal trade measures, including Trade in Goods, Trade in Services, Investment, Intellectual Property Rights, Competition Policy, and Rules and Procedures on the Settlement of Disputes. The AFCTA is meant to lay the foundation for the establishment of a continental customs union, which will advance regional economic integration on the continent. It fills an important lacuna in the Lagos Plan of Action and Abuja Treaty, which conceived continental integration at the level of a customs union. A Continental Free Trade Area is an important precursor and stepping-stone to the continental customs union. The CFTA comprises the 55 member states of the African Union (AU) and 8 AU-recognized RECs with varying trade liberalization legal frameworks, plus a tripartite trade integration initiative for 3 of those regions.

Various protocols of the agreement cover legal arrangements that are meant to boost intra-African trade. Key among these are arrangements related to tariff and non-tariff barriers (NTBs), rules of origin, services liberalization and regulation, investment and cross-border movement of persons, and trade remedies, as well as monitoring and evaluation.

The Boosting Intra-African Trade (BIAT) Action Plan was endorsed at the 18th Ordinary Session of the Assembly of Heads of State and Government of the African Union, in January 2012. The Action Plan aims at deepening integration and increasing the volume of intra-African trade. It highlights the constraints that encumber growth of intra-African trade and outlines policies and programmes to overcome each one. Some of the obstacles identified include differences in trade regime, inadequacies of trade-related infrastructure, trade finance and trade information, constricting customs, administrative and technical barriers, limited productive capacity, lack of factor market integration and inadequate focus on internal market issues.

Both the AFCTA and the BIAT Action Plan form part of broader initiatives under the African Union's Agenda 2063.2 Together, these initiatives offer a comprehensive framework to drive economic growth, industrialization and development across Africa. The AFCTA is a time bound

project, whereas BIAT is continuous, with tangible milestones marking progress on doubling intra-African trade flows from 2012 to 2022 (AU,). These two decisive initiatives by the Assembly of Heads of State and Governments of the African Union present great opportunities, as well as challenges, for boosting intra-African trade and create feasible avenues to deliver prosperity to all Africans.

The benefits of the AFCTA, which is intended to eventually incorporate all 55 African countries with a population of 1.2 billion and a combined GDP of $2.5 billion are expected to be substantial. This study was undertaken to gain a better understanding of the potential implications of the AFCTA for boosting intra-African trade.

The CFTA aspires to liberalize trade between African countries across the continent and to build on the considerable successes already achieved within Africa's regional economic communities (RECs). By doing so, the CFTA is set to facilitate intra-African trade; foster regional value chains that can facilitate integration into the global economy; and energize industrialization, competitiveness and innovation—and thereby contribute to African economic and social progress and development.

The World Trade Organization

The WTO was formed in 1995, the original intention was to create a third institution to handle the trade side of international economic co-operation. The objective of the WTO and GATT has always been to lower trade barriers to help trade flow as freely as possible because increasing trade is seen as important for economic development. This neoliberal view of global trade is based on the belief that unrestricted flows of goods and services will sharpen competition, motivate innovation and breed success in participating countries. The WTO has three major functions: to host negotiations between member countries, to remove obstacles to trade, to resolve conflicts of interest between member countries.

The WTO has not only enhanced the value and quantity of trade but has also helped in eradicated trade and non - trade barriers. WTO has also broadened the trade governance scope to trade in investment, services and intellectual property. It has emerged as a greater institution than GATT and expanded the agenda by including developmental policies which further helped in settlement of disputes and improved monitoring by introducing the Trade Policy Review and the World Trade Report as well as increased transparency by removing green room negotiations.

WTO also encouraged sustainable trade developments. As trade expands in volume, in the numbers of products traded, and in the numbers of countries and companies trading, there is a greater a chance that disputes will arise. The WTO system helps resolve these disputes peacefully and constructively - in reality, a lot of international trade tension is reduced because countries can turn to organizations, in particular the WTO, to settle their trade disputes. The fact that there is a single set of rules applying to all members greatly simplifies the entire trade regime. The WTO cannot claim to make all countries equal. But it does reduce some inequalities, giving smaller countries more voice, and at the same time freeing the major powers from the complexity of having to negotiate trade agreements with each of their numerous trading partners.

The system shields governments from narrow interests. Governments are better placed to defend themselves against lobbying from narrow interest groups by focusing on trade-offs that are made in the interests of everyone in the economy. It is the world's only international organization that supervises 95% of the world's global trade. The WTO agreements include numerous provisions giving developing and least-developed countries special rights or extra leniency special and differential treatment. Among these are provisions that allow developed countries to treat developing countries more favorably than other WTO members. The General Agreement on Tariffs and Trade (GATT, which deals with trade in goods) has a special section (Part 4) on Trade and Development which includes provisions on the concept of non-reciprocity in trade negotiations between developed and developing countries — when developed countries grant trade concessions to developing countries they should not expect the developing countries to make matching offers in return.

Both GATT and the General Agreement on Trade in Services (GATS) allow developing countries some preferential treatment. The least-developed countries receive extra attention in the WTO. All the WTO agreements recognize that they must benefit from the greatest possible flexibility, and better-off members must make extra efforts to lower import barriers on least developed countries' exports. In addition, liberalization under the WTO boosts global GDP and stimulates world demand for developing countries' exports.

Critique of WTO

WTO lies in the fact that it is highly dominated by some developed nations which questions its democratic nature. In looking at how decisions are made, there is clearly not an equality of decision making power in the WTO, as the 'trading system is still to a large degree a power-based as opposed to a rules-based system'. Whilst there is formally a one member, one-vote system in the WTO, it has never been used, and as is the case in most international governance institutions, the interests of the powerful dominate.

The WTO's fierce defense of 'Trade Related Intellectual Property' rights (TRIPs) patents, copyrights and trademarks comes at the expense of health and human lives. WTO has protected for pharmaceutical companies' 'right to profit' against governments seeking to protect their people's health by providing lifesaving medicines in countries in areas like sub-Saharan Africa, where thousands die every day from HIV/AIDS.

In developing countries, as many as four out of every five people make their living from the land. But the leading principle in the WTO's Agreement on Agriculture is that market forces should control agricultural policies-rather than a national commitment to guarantee food security and maintain decent family farmer incomes. WTO policies have allowed dumping of heavily subsidized industrially produced food into poor countries, undermining local production and increasing hunger.

WTO takes too long to arbitrate and settle disputes - it can take over five years from the initial receipt of a complaint from one member to the final panel ruling. Despite the WTO operating as a multilateral organization, many member countries and trading blocs favor bilateral discussions

with partners or competitors. This is because bilateral negotiations can be fully focused and relatively quick to complete. The result is that many countries prefer to bypass the WTO process, and deal directly with other countries. The failure of the most recent round of WTO negotiations, the Doha round, is widely regarded as evidence of the inherent problems of multilateral discussions.

African Regional Blocs

Africa has many policy initiatives that express commitments to continental integration, the framework that provides both legitimacy and inspiration is the Treaty Establishing the African Economic Community (the Abuja Treaty), which entered into force in 1994. The following subsection reviews the progress towards realizing the commitments of that Treaty. Roadmap towards an African Economic Community shows the stages of integration to which African countries committed themselves under the Treaty.

According to the Economic Commission for Africa (ECA) (2016), The first stage has now been completed, with eight RECs formally recognized by the African Union. These are the Arab Maghreb Union (AMU), Economic Community of West African States (ECOWAS), East African Community (EAC), Intergovernmental Authority on Development (IGAD), Southern African Development Community (SADC), Common Market for Eastern and Southern Africa (COMESA), Economic Community of Central African States (ECCAS) and the Community of Sahel-Saharan States (CEN-SAD). The second stage has not been fully completed because progress by the RECs and by members within the RECs has been uneven. The third stage is under way in a number of RECs but not all. Only three of the eight recognized RECs have both a FTA and Customs Union (ECOWAS, EAC and COMESA), although with varying degrees of implementation.

Currently there are four functioning free trade areas by AU recognized RECs: COMESA, ECOWAS, EAC and SADC. Further intra-African trade is liberalized through mechanisms beyond the AU-recognized RECs, including the Pan-Arab free trade area, the Central African Economic and Monetary Community (CEMAC) and the Southern African Customs Union (SACU).

Common Market for Eastern and Southern Africa (COMESA)

COMESA launched its Customs Union at its 13th Summit of Heads of State and governments in Victoria Falls, Zimbabwe on 8th June, 2009 - five years after the originally agreed date. The member states agreed to submit their lists of products with rates that are the same as those under the Common External Tariffs (CET) (that is, the rates of 0, 10 and 25 percent), as well as their lists of sensitive products where current national rates would be aligned to the CET rates during the transition period.

The Summit agreed that the transition period for the implementation of the COMESA CET would be three years, but could as well be extended to a period not exceeding five years. There would be a mid-term review after one and a half years to take stock of the progress made by member states in implementing the Customs Union. The three tariff bands cover raw materials and capital goods

at 0 percent duty, with about 2,709 tariff lines which is about 39 percent of the total 6,903 CET lines. The second band which covers intermediate goods is at 10 percent, with a total of 2,196 tariff lines (that is, 32 percent of the total lines). The last band being finished products at 25 percent, with a range of 1,998 tariff lines or 29 percent of the total lines. The COMESA member states with substantial number of tariff lines of more than 30 percent below corresponding CET duty include Libya, Madagascar, Mauritius and Seychelles.

The Economic Community of West African States (ECOWAS)

The ECOWAS Common External Tariff came into force on 1 January 2015. Ten out of 15 ECOWAS members were implementing it by 2016 (Ghana Revenue Authority, 2016). ECOWAS has created the following mechanisms to ensure that their member states implement the common external tariff:

1. A customs valuation mechanism, to ensure that all member states apply the same system of customs valuation.

2. Regulations to ensure that inputs for the manufacture of zero-rated products do not face tariffs significantly above those placed on the final product.

3. Safeguard, trade, defense and anti-dumping measures: These include supplementary protection measures allowing member states to deviate from the common external tariff for a maximum of 3 per cent of the tariff lines identified in it.

East African Community (EAC)

In January 2005 Kenya, Tanzania and Uganda launched the EAC Customs Union (CU). Burundi and Rwanda joined in mid-2007, and the CU was transformed to a Common Market (CM) on 1st July 2010. The goods sectors were fully liberalized through the elimination of internal tariffs under the EAC customs union, except for Kenya that underwent asymmetry tariff liberalization for a period of five years from 2005 to 2010 for products listed in category B with a three band common external tariff of 0, 10 and 25 percent. However, the commodities in the sensitive list have varying tariff rates between 35 - 100 percent. The category B products included 443 and 880 product lines for Uganda and Tanzania respectively.

Under the CM protocol, some services sectors underwent liberalization reforms. However, there are still prevailing barriers within the protocol on issues of work and residence permits, stay of students, right of establishment and the unbound commitments on market access and national treatment by all partner states on other key services sectors:

Burundi, for example, did not make commitments on some services sectors including legal services, accounting, auditing and booking services, data processing services, data base services, research and development services in natural sciences, social sciences, humanities, interdisciplinary research and development services, life, accident and health insurance and telecommunication services;

Tanzania remains closed to financial leasing, credit reference bureau (CPC 8133), midwives and nurses (CPC 93191), medical and dental services (CPC 9312) are restricted to specialized hospitals and diagnostic centers, courier services (CPC 7512) are subject to shareholding of 35 percent by locals, telecommunication services are subject to shareholding of 35 percent by locals, and also 51 percent shareholding by locals is required in radio and television transmission services (CPC 9613);

1. Kenya remained unbound in the sub-sectors of postal services, telecommunication and maintenance and repair of vessels (CPC 8868);
2. Rwanda maintains restriction on commission agents (CPC 621), franchising (CPC 8929) and wholesale service and retail;
3. Uganda remains closed to wholesale, retail and travel agencies, tour operators and guides, as well as hotels and restaurants including catering (CPC 641-643 which is subject to economic needs test).

Challenges Facing AFCTA Mission Realization

Africa remains far behind the world on its efficiency of document and border processing requirements for trading across borders (World Bank, 2017a), despite significant recent progress. The time and cost of importing and exporting for various African countries. For both document and border processing requirements remains a challenge, the best-performing countries and territories in the global dataset achieved a cost of less than one U.S. dollar and a processing time of one hour or less (World Bank, 2017b and 2017c).

Data on services trade are notoriously weak, with woefully poor coverage on both what is being traded and with whom, and questionable reliability of the meagre data that are available. Moreover, drawing on balance-of-payments data, services trade data essentially ignores investment flows. Notwithstanding improvements in the collection of services trade data over the past 15 years, the macro- and micro- level services data needed for meaningful economic analysis simply do not exist (Primack, 2016).

If large firms gain a dominant position in the African market, they may crowd out small and medium-size firms. This suggests a need for complementary policies, including consumer protection and competition policies, to ensure a smooth transition.

Higher heterogeneity and political costs can be expected as a result of countries' diverse cultural, political and economic arrangements if some countries' preferences for public goods and policies are incompatible with the preferences of other countries or sub-regions on the continent. Heterogeneity can also be source of value in the AFCTA area if differences across the continent stimulate economic agents to specialize in the production of different rival goods and services, whiles simultaneously learning from each other. And when there is little heterogeneity, conflict may arise because interest groups may have similar preferences for particular rival goods.15 In the case of heterogeneous choices over non-rival goods (common institutions), greater political costs and a higher probability of strife at the country level can be expected.

There could be losers under AFCTA, at least in the short term when some countries are unable to access the markets of member countries or experience reduced intra- African exports as a result of an increasingly competitive environment. However, intra-African trade remains very low and therefore offering great prospects for expansion and growth. At the same time, export growth losses contemplated could, be countered by the growth of domestic production through the economies of scale from the lower cost of intermediate imports, consumer surplus from the consumption of quality low- cost imported products and net welfare gains.

Lessons from Regional Blocks for Implementing AFCTA

Evidence from world factories in Asia, Europe and North America demonstrates that there is value of building regional value chains for participation in global value chains by increasing the market for exports and imports (UNCTAD, 2017). The intra-industry trade effects of AFCTA could engender a change in the way a country uses productive resources to serve both domestic and regional markets. For example, a representative African country that exports primary products and depends on manufactured and processed imports can use intermediate imports from the region to invest in the domestic production of different varieties of products (within the same product classification of its import and export). Abolishing trade barriers, therefore, not only benefits firms, households and government, but it also generates opportunities for countries to access intermediate imports for investment to boost productivity in related sectors for domestic consumption and exports.

The Southern African Customs Union (SACU) region has the highest gain in terms of intra-African export flow, US$18.4 billion (inclusive of intra-SACU trade), with about 46 percent of it (US$8.4 billion) into the Southern African region, 19 percent (US$3.5 billion) into East Africa, 14.8 percent (US$2.7 billion) into West Africa and 11.8 percent (US$2.1 billion) into Central Africa. Gains in intra-SACU trade amounts to US$876 million (UNCTAD, 2018).

Impact of AFCTA on Movement of Goods between Member States of AFCTA

The removal of tariffs and trade barriers to free up trade and deepen intra-African trade and regional integration is an important tenet of the AFCTA. The AFCTA is also likely to lead to shift in technology frontier as well as improvement in productivity spill overs within African countries that will result from trade creation. The AFCTA ultimately aims to boost the economic performance of African countries in ways that enhance welfare as well.

The AFCTA commits African economies to the removal of trade barriers on imports (tariffs and quotas), which will reduce import costs and, consequently, consumer prices. Consumers will benefit by being able to consume a larger variety of African products in the single market. These supply and demand effects together engender welfare gains in the form of consumer surpluses in importing African countries (Saygili et al. 2017).

Downstream manufacturers in importing countries also stand to gain through declining production costs as the costs of imported raw materials and intermediate inputs falls. This may improve the competitiveness of domestic producers and enable African economies to integrate into global value

chains. Competitive pressures resulting from the AFCTA can enhance the efficiency of domestic firms by requiring improvements in resource allocation and in innovation to compete in the liberalized environment. Thus, implementing the AFCTA has the potential to enhance the efficiency of African firms.

The AFCTA would allow African domestic firms to access a 1.2 billion strong market (including a growing middle class) and thus to benefit from economies of scale. Expanding markets offer important opportunities to develop regional value chains that can enhance diversification and competitiveness and consolidate and integrate production infrastructure and processes across borders. Constrained access to markets limits the growth of firms.

Therefore, for domestic firms, getting rid of local market constraints may improve growth prospects and access to finance and technology in the global economy.

Small and medium-sized enterprises are key to growth in Africa. They account for around 80 per cent of the region's businesses. These businesses usually struggle to penetrate more advanced overseas markets, but are well positioned to tap into regional export destinations and can use regional markets as stepping stones for expanding into overseas markets at a later point. Before exporting cars overseas, for example, large automobile manufacturers in South Africa source inputs, including leather for seats from Botswana and fabrics from Lesotho, under the preferential Southern African Customs Union trading regime.

Women are estimated to account for around 70 per cent of informal cross-border traders in Africa. When engaged in such an activity, women are particularly vulnerable to harassment, violence, confiscation of goods and even imprisonment. By reducing tariffs, AFCTA makes it more affordable for informal traders to operate through formal channels, which offer more protection. This can be further enhanced by simplified trading regimes for small traders, such as the Simplified Trade Regime in the Common Market for Eastern and Southern Africa (COMESA), which provides a simplified clearing procedure alongside reduced import duties that provide particular help to small-scale traders.

While African countries that are relatively more industrialized are well placed to take advantage of the opportunities for manufactured goods, less-industrialized countries can benefit from linking into regional value chains. Regional value chains involve larger industries sourcing their supplies from smaller industries across borders. AFCTA makes the formation of regional value chains easier by reducing trade costs and facilitating investment.

Agricultural countries can gain from satisfying Africa's growing food security requirements. The perishable nature of many agricultural food products means that they are particularly responsive to improvements in customs clearance times and logistics that are expected of AFCTA.

The majority of African countries are classified as resource rich. Tariffs on raw materials are already low and so AFCTA can do little to further promote these exports. However, by lowering intra-African tariffs on intermediates and final goods, AFCTA will create additional opportunities for adding value to natural resources and for diversifying into new business areas.

The cost of being landlocked includes higher costs of freight and unpredictable transit times. AFCTA provides particular benefits to these countries: in addition to reducing tariffs, the AFCTA is set to include provisions on trade facilitation, transit and customs cooperation.

Conclusions and Way Forward.

AFCTA would be an important framework to help lockout some of the prevailing challenges such as non-tariff measures (NTMs) on goods, infrastructural problems and trade facilitation, multiple membership and rules, rules of origin, defensive interests of some members states and eliminate member states restriction on the movement of natural persons and service consumers. This would require pursuance of a deeper integration framework taking into consideration the economic development needs of other members. Within the AFCTA framework, there is a need to provide a mechanism to finance infrastructure development among member countries, compensate members who incur costs in terms of tariff revenue as a result of the establishment of the AFCTA by establishing a trust fund.

The committees need to examine specific barriers in the respective sub-sectors especially in services, including domestic regulations in individual member states on goods and services, cultivate deeper understanding of the sectors and possible measures. This is important because it will give a direction in dealing with the interests of members who are already in multiple agreements.

Harmonization of technical regulations, standards and conformity assessments procedures are necessary in the negotiations. Member states need to devote more attention to building a mechanism under which there would be mutual recognition of standards and conformity assessments. This would require establishment of a standard development center to support uniformity of standards, testing and certification requirements.

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