



# CORPORATE FINANCE MANAGEMENT FACULTY Newsletter



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## AFRICAN CONTINENTAL FREE TRADE AREA (AfCFTA): IMPLICATIONS FOR BUSINESS AND CORPORATE ENTITIES

### INTRODUCTION

The establishment of the AfCFTA is a priority project of the African Union's Agenda 2063, a blueprint for attaining inclusive and sustainable development across the continent over the next 50 years. This trade agreement specifically aims to improve

competition policy. It was reached following the meeting of African leaders from 44 African nations at the African Union (AU) Summit held in Kigali, Rwanda, on the 17<sup>th</sup> – 21<sup>st</sup> March, 2018. As at date, Eritrea remains the only country of the 55 AU Organization (WTO). The trade bloc will affect over 1.2 billion people with a combined GDP of more than US\$3.4 trillion. The AfCFTA main objectives are to create a single market for goods and services, facilitate the movement of persons, promote industrial development, support sustainable and inclusive socioeconomic growth, as well as to resolve the issue of multiple membership, in accordance with Agenda 2063. It is aimed to be a model of cross border cooperation in an era of growing isolationism (Kende-Robb (2021)).



intra-African trade by providing a comprehensive and mutually beneficial trading agreement among the member states. The agreement covers exchange in goods and services, investment, intellectual property rights and

member states that has not signed the AfCFTA agreement (the Agreement). The AfCFTA, which became operational on 1<sup>st</sup> January, 2021, has been termed the largest free trade area (by countries participating) after the World Trade

The UN Economic Commission for Africa (UNECA) estimates that the implementation of the agreement could increase intra-African trade by 52% by 2022 (compared with trade levels in 2010) and double the share of intra-African trade (currently around 13% of Africa's exports) by the start of the next decade.

### STRUCTURE AND OBJECTIVES OF THE AGREEMENT

The AfCFTA agreement is a framework covering trade in goods and services following protocols: Trade in Goods and Services,

Intellectual Property Rights, Competition Policy, Investment and Dispute Settlement.

The agreement aims to progressively reduce and eventually eliminate customs duties and non-tariff barriers on goods as well as liberalize trade in services. Concerning trade in goods, the goal is set for 90% of products at zero duty across the continent.

The different protocols are negotiated in two phases. Phase 1 focused on three protocols: trade in goods with its nine (9) annexes; trade in services with its three (3) annexes and dispute settlement. Phase two (2) negotiations will focus on the protocols on competition, intellectual property rights and investments.

According to the AU 2018 report, the Agreement has a number of objectives which could be streamlined as general and specific. The General objectives are the visions as set out in Article Three (3) which include:

1. Develop a single market for goods and services via encouraging the movement of persons in order to deepen the economic integration of the African continent;
2. Create a liberalized market for goods and services through successive rounds of negotiations;

3. Encourage investments, building on the initiatives and developments in the State Parties and Regional Economic Communities (RECs), while contributing to the movement of capital and natural persons;
4. Lay the foundation for the establishment of a Continental Customs Union; and
5. Promote and attain sustainable and inclusive socio-economic development, gender equality and structural transformation of the State Parties.



The specific objectives in line with Article four (4) of the Agreement include:

1. Progressive elimination of tariffs and non-tariff barriers to trade in

- goods;
2. Progressive liberalization of trade in services;
3. Cooperation in all trade-related areas including investment, intellectual property rights and competition policy;
4. Cooperation on customs matters and the implementation of trade facilitation measures;
5. Establishment of a mechanism for the settlement of disputes concerning the rights and

obligations of members; and

6. Establishment and maintenance of an institutional framework for the implementation and administration of the AfCFTA.

### WHAT IMPACT WILL THE AfCFTA HAVE ON AFRICAN BUSINESSES?

The AfCFTA Agreement will benefit World. Some of the benefits of the the member states in various Agreement include:

forms as Africa hopes to grow with the a.) **COST REDUCTION**

Member states will benefit from cost reduction for consumers and producers. This cost reduction will include both administrative and compliance costs. The Agreement has promised to reduce tariffs which eventually will result in lower prices for imported goods for consumers, as well as for producers using intermediate inputs. Also, there are non-tariff barriers (NTBs) like burdensome administrative procedures and various technical requirements that may be eliminated in the adoption of AfCFTA.



Compliance costs which arise as a result of differences in standards and regulations between member countries in most cases constitute trade barriers. With AfCFTA, these costs will likely be reduced or totally eliminated. The reduction of trade costs will bring about trade facilitation measures that will improve inter-country trading. With the elimination



operating model of the AfCFTA, as trade barriers and cost are eliminated, countries will benefit by trading with each other. This opens up Africa to future possibilities. AfCFTA will benefit those countries that are already relatively open to their own liberalization with more access to other markets. Excess protection may hinder some level of benefits.

or reduction in the respective costs, prices of goods and services will decrease and become less expensive. AfCFTA also expects to enhance the principles of comparative advantage enabling the consuming nations to be vested with opportunities to invest in production and enjoy the benefits accruing from competition. Also, member states will enjoy faster productivity gains by taking advantage of economies of scale in the larger market, as well as attract foreign

Bank Group, 2020). According to the study by the World Bank Group, selected countries like Morocco, Namibia, and Senegal, will benefit substantially from improved market access in other AfCFTA markets and this will increase their welfare. The removal of administrative bottlenecks, NTBs and trade tariffs which initially is a constraint to trading among member states will boost the benefit realizable by states. Where only one of these constraints is removed, then there

### c.) IMPLICATIONS ON TAX REVENUE

The AfCFTA will impact the level of taxation in member states. Most of this will arise from the removal or the reduction of tariffs among member states. It should be noted that full trade liberalization could impact the level of revenue and may result in revenue losses in some cases; however, little evidence is available to prove this. The World Bank Group (2020) report indicated that losses resulting from the impact of liberalization of full trade may be small. A further study by the African Development Bank (ADB, 2019) listed some possibilities that could significantly reduce the level of revenue losses (ADB 2019; Laborde et al. 2019; UNECA 2017). In the interim, there is the expectation that the overall impact on import tariff revenue may remain positive to the member states over the long run.



direct investments (FDI).

### b.) REAL INCOME IMPLICATIONS

There are many real income gains arising from tariff liberalization coming from the implementation of the AfCFTA even though it may not be significant (World

will not be any sufficient condition for real income gains to materialize (World Bank Group, 2020). These gains may not be equally distributed among the member states; nevertheless, Africa will be on the pedestal to competing with the World in the nearest future. Trade. With improved

Although tariffs will decline, with the increase in the volume of imports and the increase in trade and economic activities, there is the opportunity that tax revenue may grow over time.

d). **TRADE IMPLICATIONS ON SMALL AND MEDIUM ENTERPRISES** The agreement will give SMEs an advantage to grow beyond their domestic market into regional ones. Other African professionals in various service industries (SMEs), are expected to largely benefit from AfCFTA because it entails lower or no tariffs and free access to market and market information. The instrument will indeed lead to removal of tariff restrictions and other barriers on intra-African trade. It will also be easier for Africans to establish businesses in different African countries. It will allow businesses to access cheaper raw materials and intermediate goods, while improving the conditions of regional value chains and access to global value chains.

The agreement will give SMEs an advantage to grow beyond their domestic market into regional ones. Other African professionals in various service industries (such as construction, engineering, technology, and financial services and already is experiencing intra-continental movement in labour) would see increased movement of such professionals to countries that demand for their services. In addition, labour-intensive trade across borders would require the services of low skilled workers and the free movement of persons guaranteed by the AfCFTA will bring with it the free movement of services that these persons will render.

e). **IMPACT ON EMPLOYMENT**

The AfCFTA also seeks to create a single liberalized market for trade in services for

**THE IMPLEMENTATION CHALLENGES OF THE AGREEMENT**

Experts have opined that the agreement must overcome certain implementation challenges to realize its many benefits. Two of such experts are Kende-Robb (2021) and Bavier (2021) of World Economic Forum (WEF). Some of the issues identified include



infrastructure (roads and rail links), political unrest, and excessive bureaucracy. These are perennial problems that have generally inhibited investment and trade in the continent. However, more peculiar challenges are discussed below:

a.) **Heterogeneity of the market, quality and standard regulations**

Africa is a huge continent with markets that have different sizes and characteristics. Nigeria, Egypt and South Africa contribute over half of the continent's cumulative GDP, while six of the small islands contribute only 1% of the Continental GDP. Market regulations also vary a lot from country to country. Therefore, the harmonization of the regulations will be a main challenge. Standardizing quality requirements for goods and services will not be an easy

task as well.

b.) **Small and Medium Scale Enterprises (SMEs)**

Due to the relative size and capacity of multinationals or foreign businesses, they tend to supply goods and services at lower rates than local SMEs causing the latter to lose market. This issue will be more evident since the Agreement offers reduced tariff on imported goods.

c.) **Labour issues**

Labourers may be forced to work with lesser rights and protection in order to win the competition. The Nigerian Labour Congress criticized the agreement labeling it as "a renewed, extremely dangerous and radioactive neo-liberal policy initiative".

d.) **Environmental issues**

The tough competition may also lead to

SMEs ignoring environmental regulations. In order to cut costs, SMEs may disregard such regulations during manufacturing or waste dumping.

#### e). Theft of intellectual property

The absence in most countries and the heterogeneity in others, of laws regulating theft of intellectual property may be a serious issue. The African Union should also address this issue in order to protect SMEs that may otherwise be reticent in Africa in investing in more creative ideas and researches.



#### CONCLUSION AND RECOMMENDATION

Even though the AfCFTA is a great step forward towards economic integration, there is still a long road ahead. African governments must commit to working hard so that the gains from the AfCFTA are distributed as fairly as possible, making sure no one is left behind, and ensuring that the AfCFTA becomes a catalyst for sustainable economic development for the continent as a whole. Amongst others, businesses should plan their structures, presence/location, product offerings and competition analysis as well as inhibitors to realizing the full benefits of the trade pact.



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