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Executive Summary

Effects of the AfCFTA for German and European Companies

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Effects of the AfCFTA for German and European Companies

In May 2019, the African Continental Free Trade Area (AfCFTA) agreement entered into force. In numerous respects, the AfCFTA can be considered a historic milestone towards trade liberalization on the African continent. Following ten rounds of official negotiations beginning in June 2015, the agreement now spans 55 African Union Member States of which 43 have already deposited their instruments of ratification.[1] By connecting these economies, AfCFTA has become the largest trading bloc in the world in terms of market size, covering more than 1.3 billion consumers with combined GDP of USD 2.5 trillion. The AfCFTA's core objective is to deepen the economic integration of the African continent by creating a single market for the movement of goods, services, capital and natural persons. In the study "Effects of the AfCFTA for German and European companies", we assess the status quo of trade within AfCFTA economies and between AfCFTA and EU economies, and outline three hypothetical future outcomes of AfCFTA for different levels of trade liberalization.

[1] Information as of May 2022.

Status quo of African trade relations

The status quo of intra-African trade integration remains shallow. Figure 1 shows the African continent to have a very low share of intra-continental trade, both in terms of imports and exports, as compared to Europe, Asia or the Americas. In fact, the share of internal trade on the European continent is almost seven times as high as on the African continent, and still only a quarter of intra-American trade. Furthermore, no clear upward trend is visible.

For AfCFTA member states, the European continent remains a major trading partner. However, in recent years it has increasingly seen competition by Asian countries, most notably China (Figure 2). The agreement's successful implementation is therefore a strategic priority in the EU's evolving relationship with Africa and offers an opportunity to arrest the gradual decline in its relative importance as a trading partner for African economies.

In terms of traded products, African exports are dominated by commodities and raw materials (Figure 3). This industrial structure is markedly different from that of the EU and therefore reduces the likelihood of intra-African integration diverting trade away from the EU.

For the EU itself, the African continent is — in overall economic terms — a relatively minor trading partner. Its share of exports to African economies in total exports persistently stays around 2%. This trade concentrates heavily in few economies, most notably in the geographical north of the continent as well as South Africa. Within the EU, Germany is the second largest exporter to and third largest importer from AfCFTA members. Importantly, its trade relationship with African economies is unique in a number of ways: Compared to overall imports from the EU, African economies source industrial goods such as machinery, electrical appliances, vehicles and transport equipment much more intensively from Germany (Figure 4). This pattern is also observable in AfCFTA exports to Germany.

Even though these patterns are mainly driven by South African-German trade, especially in motor vehicle-related goods, they provide a good example for potential benefits of deeper trade integration with other African countries.

Figure 1 Share of internal imports and exports by continent

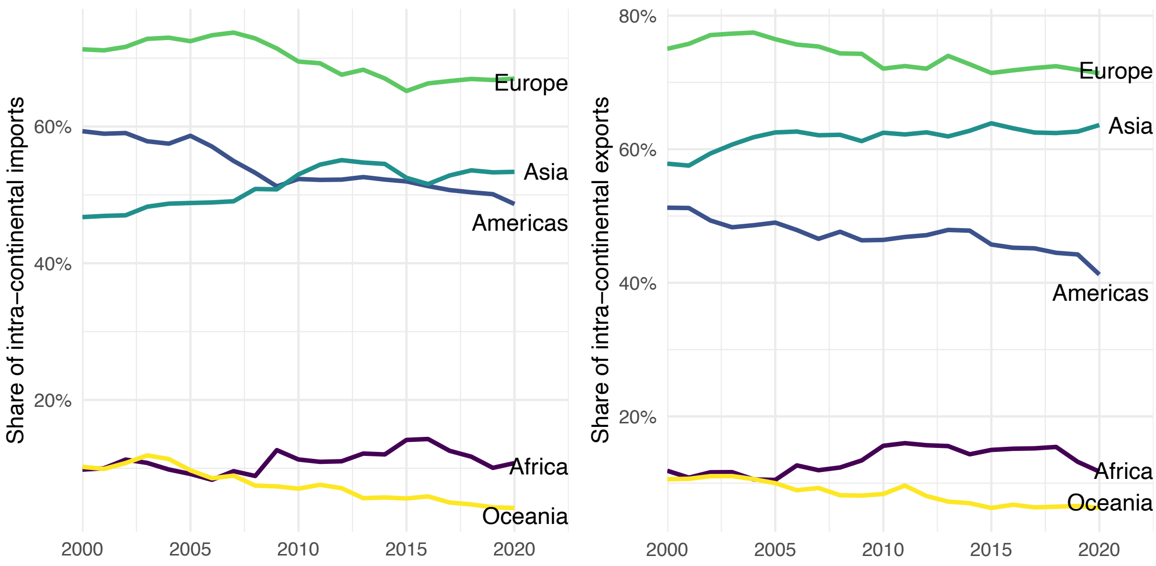


Figure 2 African export destinations and import origins over time

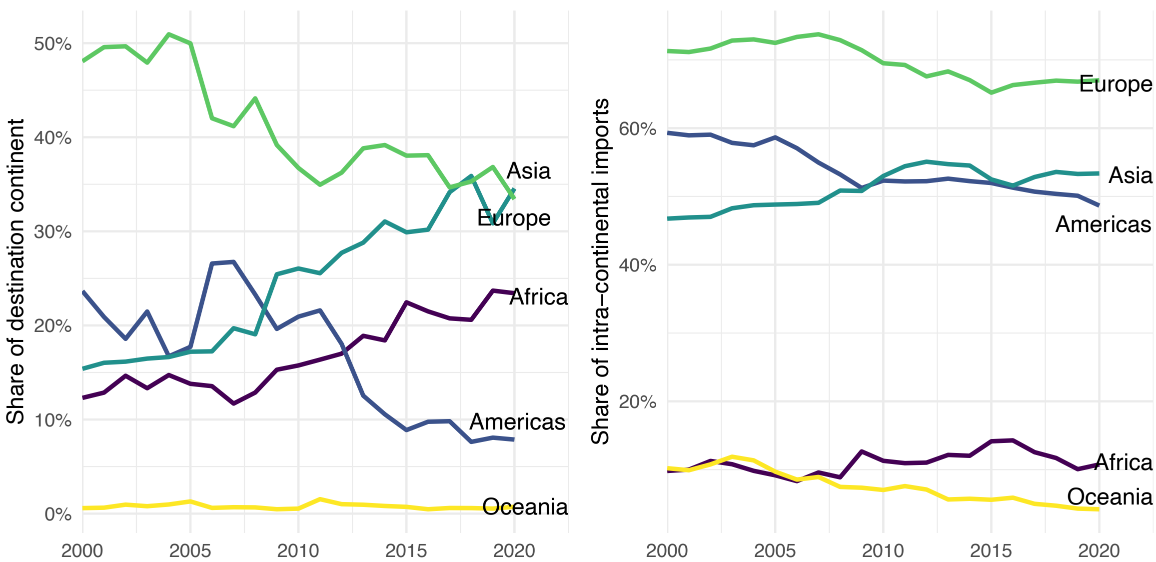


Figure 3 Top African export sectors in 2019

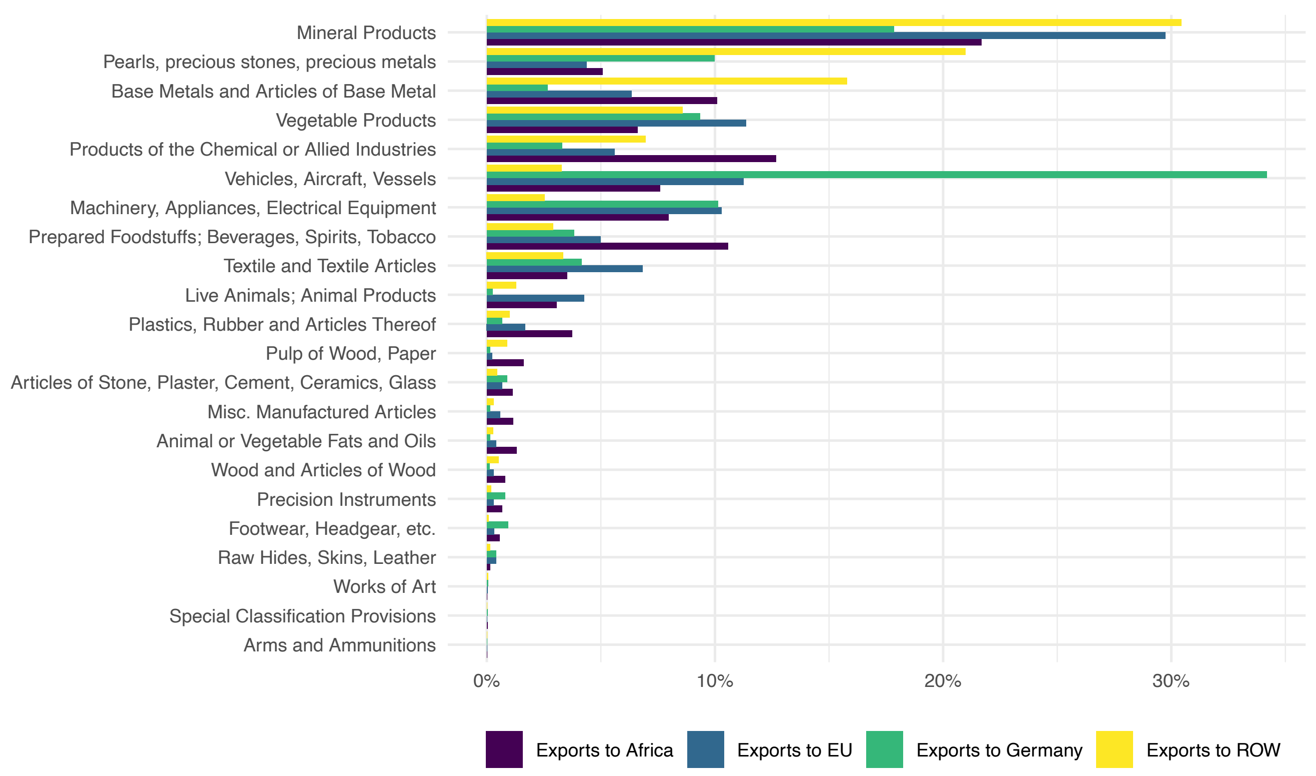
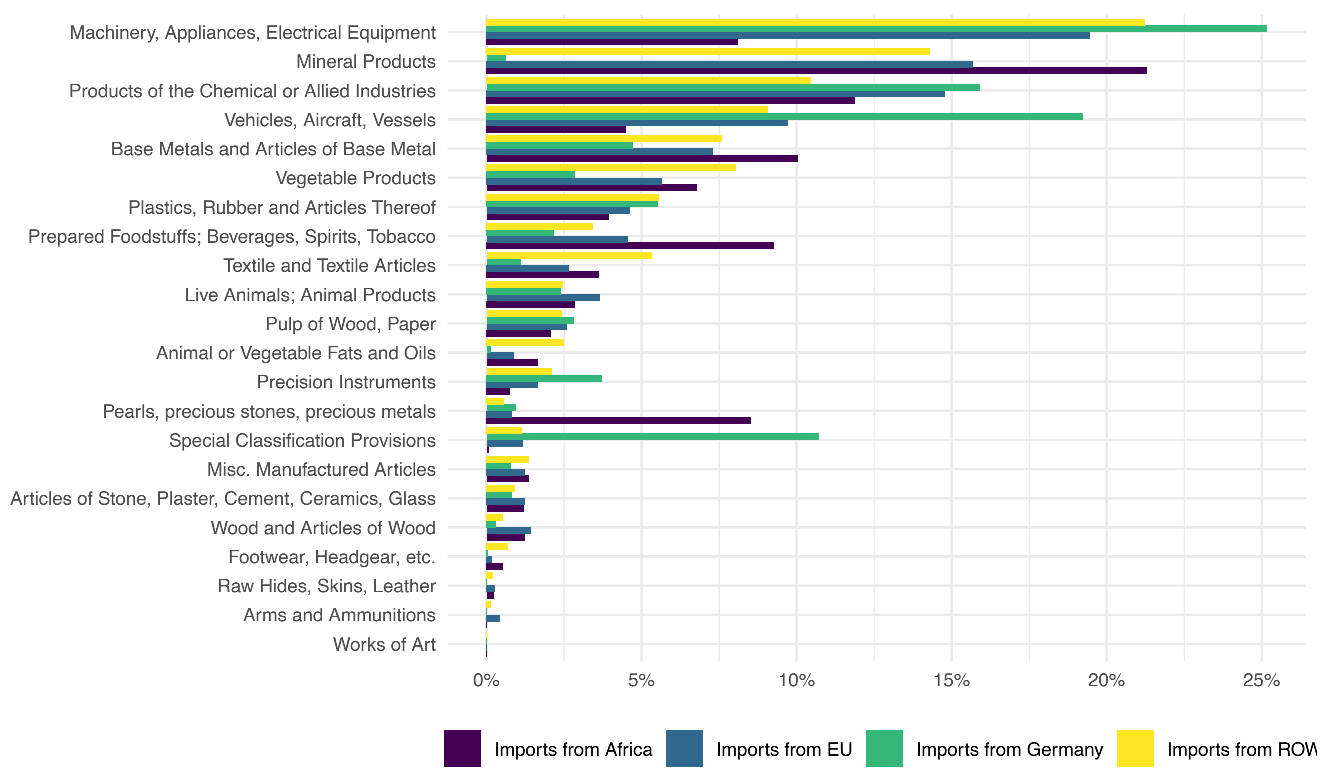


Figure 4 Top African import sectors in 2019



Three Scenarios for AfCFTA Implementations

To quantify and evaluate the effects of the entry into force of the AfCFTA for its members, Germany and other EU countries, we compare a baseline simulation scenario (i.e. a world without AfCFTA) to three counterfactual states of the world economy in which the level of trade liberation under the AfCFTA varies:

Scenario 1

All intra-AfCFTA tariffs are eliminated whereas the external tariffs, i.e. tariffs for non-AfCFTA economies, remain as in the status quo.

Scenario 2

Intra-AfCFTA NTBs are lowered by 10% in addition to eliminating all intra-AfCFTA tariffs. External tariffs and NTBs remain unchanged.

Scenario 3

IIn addition to the liberalizations from Scenarios 1 and 2, NTB reductions by 10% are extended to all trading partners, while extra-AfCFTA tariffs remain in place.

Table 1 summarizes the simulated economic outcomes of the different AfCFTA implementation scenarios:

Table 1 Economic impact of the three different scenarios for AfCFTA member countries

	Scenario 1 Tariffs only	Scenario 2 Tariffs + bilateral NTBs	Scenario 3 Tariffs + multilateral NTBs
Change in Global Exports	0.37 %	17.4 %	22.9 %
Change in intra-African Exports	0.38 %	23.0 %	19.9 %
Change in Exports to EU	-0.56 %	-21.6 %	36.3 %
Change in Tariff Revenue	-6.42 %	-38.7 %	15.5 %
Change in Income	≈ 0	11.6 %	18.7 %
Change in Production (real)	0.3 %	24.0 %	29.9 %

The results of Scenario 1 show that tariff elimination alone provides only a marginal boost to AfCFTA's global exports. Almost all the gains come – not unexpected – from within-African trade. These gains are mainly offset by a significant reduction in tariff revenues, however.

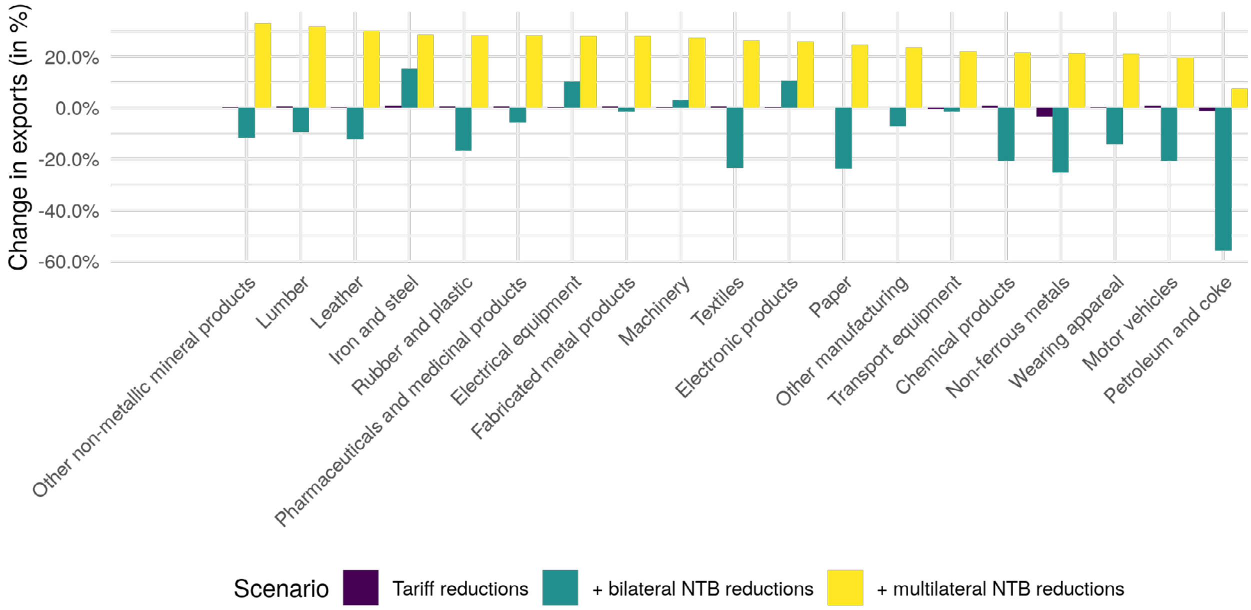
The results of Scenario 2 and Scenario 3 show that the main boost to trade comes from a reduction in NTBs. If intra-AfCFTA's NTBs are reduced by 10% (Scenario 2), members would experience global export growth by up to 17.4% and steep growth in intra-AfCFTA exports (23%). Tariff revenues are seen to decrease by 38.7%, as trade is diverted away from other economies such as the EU and towards AfCFTA partners for whom tariffs have been eliminated. However, these tariff declines are fully offset by export growth resulting in real output growth of 24%.

When extending the AfCFTA's NTB reductions to third countries (Scenario 3), the positive impact of the agreement on the bloc's economic outcomes are further magnified. Besides, global exports, income and production also show their highest growth rates when NTBs are reduced on a multilateral basis. Therefore, by reducing NTBs towards non-AfCFTA exporters as well, the bloc's own gains from the AfCFTA are amplified.

The results for German and other EU companies show that intra-AfCFTA tariff elimination alone (Scenario 1) leads to virtually no change in EU exports to AfCFTA economies. Moreover, reducing NTBs only among AfCFTA countries (Scenario 2) has a negative impact on EU exports and imports due to trade diversion resulting from the increased trade within the AfCFTA bloc.

For EU exports to AfCFTA members to grow, NTB cuts must be multilateralized (Scenario 3). Under this scenario, EU exports to AfCFTA increase by 32.1% over the long run vis-a-vis a situation without the AfCFTA. For Germany, this export growth from AfCFTA is substantial in all key German sectors such as motor vehicles, pharmaceuticals and chemical products (Figure 5).

Figure 5 Change in German exports by sector and scenario



Stakeholder action for a successful implementation of AfCFTA

The simulation results show that this ambitious agreement has the potential to address the chronically low levels of intra-African trade observed today and to spur economic growth across African economies. The agreement also presents a valuable opportunity for the EU to stem its declining share in African economies' trade baskets. However, in order to capture the full benefits of economic integration, AfCFTA members must ensure that NTBs are effectively and irreversibly reduced during the agreement's implementation phase, where-ever possible in a multilateral fashion.

The results also show that the gains from the AfCFTA are far from automatic. With China's increasing influence in the region, the EU should bolster efforts to renew and modernize its long-standing economic partnership with African economies. By assisting in the agreement's implementation, the AfCFTA offers a valuable opportunity for the EU and Germany to demonstrate their support of Africa's economic growth and development. Businesses in the EU and Germany have a uniquely important role to play here. With their considerable knowledge and experience of African markets and persistent trade frictions, they can inform ongoing efforts in both the EU and AfCFTA economies to reduce these critical NTBs.

The studies lays out that public and private sector actors in Germany should focus on the agreement's provisions concerning NTBs, carefully monitoring future negotiations between AfCFTA members on NTBs and if feasible, provide technical support to AfCFTA economies in lowering NTBs on a multilateral basis. For instance, sharing best practices, technologies and information to modernize customs procedures in AfCFTA economies can lower costly red tape and documentation burden faced by German businesses. In addition, European and German companies should consider geographically diversifying their exports to Africa, tapping into new markets within the continent. This suggestion is motivated by the finding that multilateral NTB reductions produce high rates of revenue growth for German companies in economies that currently do not feature prominently in its export basket.

Beyond increasing engagement with AfCFTA states, German companies with experience of operating in African economies can provide ground-level insights to the EU on key trade bottlenecks. This can support the development of EU's strategy towards Africa and inform the EU's plans for infrastructure investment under the newly launched Global Gateway Initiative. Such EU-level investment in building and maintaining quality infras-tructure in Africa offers new opportunities for German companies active in the construc-tion/engineering/logistics sectors besides reducing costs of doing business in Africa more broadly for all German and European companies.