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Forty-four African countries sign Continental Free Trade Area agreement

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Executive summary

On 21 March 2018, 44 of Africa's 55 countries signed the Africa Continental Free Trade Area (FTA) agreement in Kigali, Rwanda during an African Union summit. Nigeria, Tanzania and Burundi are some of the countries that did not sign the agreement during the summit. The Continental FTA seeks to eliminate barriers to trade and investment.

This Alert highlights the objective of the FTA and what it provides to the signatories.

Detailed discussion

Objective of the FTA

Countries generally are not self-sufficient and may require trade with other countries to take advantage of the other country's competitive and/or comparative advantages which may be natural resources, expertise or even size/geographical coverage. The process of countries seeking to benefit from another economy's (or economies') comparative advantages leads to economic integration, under the following formats:

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1. Preferential trade area
2. Free trade area
3. Customs union
4. Common market
5. Monetary union
6. Political federation

An FTA, the second form of economic integration, seeks to remove barriers to the easy exchange of goods that exist between countries. Normally there are import duties of some sort as goods move from one country to the other and levels of other local taxes such as Value Added Tax (VAT) and excise duties that often differ between the countries. The aim, therefore, of an FTA is to reduce barriers to exchange so that trade can grow as a result of specialization, division of labor, and most importantly via comparative advantage. The theory of comparative advantage states that in an unrestricted marketplace (in equilibrium) each source of production will tend to specialize in that activity where it has a comparative (rather than absolute) advantage. Consequently, the net result will be an increase in income and ultimately wealth and well-being for everyone in the FTA.

Currently, the signatories to the Africa Continental FTA are also members of other regional economic communities. For instance, Uganda and Kenya are signatories to the East African Community (EAC) common market as well as the Common Market for Eastern and Southern Africa (COMESA) customs union. South Africa is a signatory to the Southern African Development Community (SADC) and South African customs union (SACU). Furthermore, another COMESA-EAC-SADC FTA agreement was signed and is in advanced stages of implementation/ratification by the member countries. Several deadlines towards implementation of the FTA have however been missed since 2015 when the agreement was sent for ratification by the signatories. Decisions on rules of origin criteria per trade bloc also have taken longer than expected.

Advantages of the FTA

With a combined gross domestic product of about US$2.5 trillion and 1.2 billion people, Africa currently trades more with continents or countries outside of Africa than with fellow African countries. Of the 55 African countries, 80% of exports are to other continents and these are mainly raw or semi-finished and undiversified exports. Free trade among the partner states would boost and increase trade for all countries involved. With a focus on comparative advantage, exports would be more diversified and would grow from raw/semi-finished to finished products.

Transport and infrastructure are some of the impediments/barriers to trade among fellow African countries. If these countries work towards FTA collaborations, "one-stop" border posts could potentially improve trade between the countries.

The fact that the Continental FTA could potentially be comprised of 55 countries promises more power and economies of scale than the EAC that has 6 member countries or SADC or COMESA with about 15 member countries.

However on the flipside, an FTA only serves to eliminate tariff (non–tariff) barriers to trade whereas a customs union (like SACU or COMESA) removes internal tariffs and creates a common external tariff to protect local industries of participating countries, and a common market advocates for free movement of labor, services, goods, capital and right of residence among member countries.

Next steps

The next step in the process of implementing the Continental FTA will be for the signatories to ratify the agreement and then implement the provisions of the agreement. Critical areas to consider include rules of origin to qualify for preferential taxes on imports from member countries as well as agreements of which physical barriers to trade are eliminated gradually.

The ultimate aim of the African Union is to become a political federation with one currency and one president across the whole continent.

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