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# ASG Analysis: The AfCFTA's Potential for Economic Recovery, Opportunity, and Unity

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*This ASG Analysis is the last in a three-part series on the African Continental Free Trade Area (AfCFTA). The first piece focused on the agreement's status, purpose, and early implications for investors. The second explored ways in which the success of AfCFTA may be complicated or challenged. Here, we look to the agreement's future and potential.*

## Key takeaways

- The African Continental Free Trade Area (AfCFTA) has been lauded as the main post-Covid-19 economic driver for African countries, and will enable them to emerge from the pandemic as a single market.

- While the continent faces a long road to recovery, the AfCFTA creates new opportunities that in some cases build on pandemic-era changes, such as new investment in local vaccine production and increased reliance on e-commerce. We see particularly strong opportunities in manufacturing and digital technology.

- The social impacts of the AfCFTA – such as improved governance, freedom of movement, and the sharing of ideas – could contribute to strengthening democracy and improve market predictability across the continent.

- Africa can learn from the European Union model of a continental single market and, if implemented effectively, the AfCFTA could eventually follow in the footsteps of the EU to even out economic development across nations and unite countries around a common passport, currency, and institutional norms.

Watch Senior Advisor and former Ambassador of South Africa to the United States **Ebrahim Rasool** break down the AfCFTA's implications for investors and economic recovery in this **ASG Reality Check** video.

## Prospects for post-Covid-19 economic recovery

Trading under the AfCFTA, which began in January 2021, came at a crucial time for the African continent, as it sought to begin to recover economically from the ongoing effects of the pandemic. We anticipate that the agreement will play an important role in Africa's long-term economic recovery, enabling countries to rely on regional partners for trade and investment and increasing manufacturing and digitization that will spur economic growth. Upcoming negotiations on digital protocols are likely to pave the way for an increasingly digitized continent and enable e-commerce to play an expanded role. Early signs indicate that African countries will experience a challenging but steady recovery; in the long term, investor-friendly markets like Kenya and Cote d'Ivoire will recover relatively well, and larger economies could see marginal growth in the early days of the AfCFTA if it is well-implemented.

Still, the spread of the delta Covid-19 variant coupled with the slow uptake of vaccines means that African countries will continue to be impacted by the virus for the foreseeable future and points toward a drawn-out recovery across the continent. To date, about 5.5 percent of Africans have received at least a first dose of the Covid-19 vaccine, compared to the global average of 42.6 percent, and only 3.3 percent of Africans are fully vaccinated, compared to the global average of 31.5 percent. According to the World Health Organization (WHO), around 80 percent of African countries will not meet the global target of vaccinating 10 percent of their population by the end of September 2021. Until most of the population is fully vaccinated against the coronavirus, African economies remain at risk.

## Long-term opportunities for investors

### Manufacturing

The AfCFTA creates strong economic opportunities for a post-Covid-19 Africa, which will come out of the pandemic as a single market. The agreement makes Africa a key destination for manufacturing, particularly for companies seeking to diversify their supply chains in the wake of the pandemic. The World Bank estimates that by 2035, Africa's manufacturing exports could increase by 110 percent for intra-African trade and 46 percent for non-African trade. Nonetheless, most African countries still face challenges when it comes to critical infrastructure, which is something that will need to be addressed in order to fully benefit from the expanding manufacturing sector.

Four key markets are emerging as particularly strong targets for the global manufacturing industry: Ghana, Rwanda, Nigeria, and South Africa. Between 2015 and 2018, $3.8 billion of the total $11.7 billion in foreign direct investment (FDI) in Ghana went to manufacturing, and we expect this trend to continue as the AfCFTA widens access to markets closer to the country. While Rwanda's manufacturing industry is small, it is becoming increasingly diversified as more value-added manufacturing – processing and/or transformation of raw materials into finished products – takes place. In the first quarter of 2021, Nigeria's manufacturing sector grew at a rate of 3.4 percent. South Africa has also seen growth in its manufacturing sector with an increase of 12.5 percent year-on-year in June of 2021. These upward trends will likely continue as the AfCFTA is implemented.

Due to difficulties securing vaccines on the global market, African countries are also investing in domestic manufacturing to localize vaccine production and supply. Senegal, Morocco, Uganda, and South Africa have partnered with the U.S. and European countries to invest in scaling up local vaccine manufacturing capacity. Within the context of the AfCFTA, we'll be watching Phase 2 negotiations on intellectual property rights to see if they create conditions conducive to the establishment of further health-related manufacturing in Africa. This could help African countries access more Covid-19 vaccines and enable them to produce inoculations and medicines for other diseases on the continent, although it will take time for countries to build up their health manufacturing capacity and the continent will continue to face shortages in the meantime.

### Digitization

The pandemic has highlighted the need to further develop digital infrastructure, as African countries have had to turn to the digital world for solutions to problems related to transactions and trade. Through fintech companies and digital currencies, African countries see ongoing potential to streamline cross-border payments and boost intra-continental trade. One example is Senegal's launch of a blockchain-based digital currency known as the e-CFA, which will be equal in value to the West African Franc (CFA Franc). The West African Economic and Monetary Union (WAEMU) plans to launch the digital currency in other countries that use the CFA. In addition, over the last year, digital banking has become more prevalent, which has in turn spurred the growth in digital payments and e-commerce that created four African fintech unicorns: Fawry in Egypt and Interswitch, Jumia, and Flutterwave in Nigeria.

The AfCFTA's goal of creating an essentially continent-wide single market for digital trade especially boosts the e-commerce sector's potential for growth. Analysts estimate that in most African countries, less than 5 percent of the population buy online. If countries and companies can use the AfCFTA to tap into the remaining 95 percent, they can create a large, significant market of cross-border traders. E-commerce provides a short-term solution to pandemic related obstacles for consumers, but also could expand cross-border trade within the AfCFTA and provide broader access to goods for consumers in the medium to long term. The digital protocols for the AfCFTA are still being negotiated, so countries could take some time to get on the same page in this regard.

Increased internet and mobile penetration, a growing youth population, and a push from countries to improve their digital infrastructure will lay the foundations for a digitized Africa. If African countries can leverage the reduction in tariffs and the trade liberalization of the AfCFTA to boost digitization and e-commerce, the continent's digital economy will grow rapidly. As ASG wrote previously, Phase 2 and Phase 3 AfCFTA negotiations, which include digital polices and protocols, will be key to this.

## What's on the horizon?

### Potential for worker benefits

If properly implemented, the AfCFTA will increase Africa's income by $450 billion and contribute an additional $76 billion to the world's economy. Free movement of people will create opportunities for both skilled and unskilled workers, providing jobs for millions of unemployed African youth who will be able to more easily move to cities with better-paying jobs and high demand for skilled labor. The International Monetary Fund (IMF) predicts that the AfCFTA will lead to substantial wage gains for African workers, with wages of skilled workers increasing by about 9.8 percent and wages of unskilled workers increasing by about 10.3 percent. Women will see their wages increase by an average of 10.5 percent and men will see their wages increase by 9.9 percent. This growth, along with increased contributions from young people to the workforce, could prove to be a major economic boost.

| Type of Worker | Wage Increase |
|---|---|
| Skilled workers | 9.8% |
| Unskilled workers | 10.3% |
| Women | 10.5% |
| Men | 9.9% |

**Fig. 1**: IMF predictions for wage increases under the AfCFTA.

### Possibility of improved governance

The AfCFTA could also play an important role in connecting African countries politically and socially. Increased freedom of movement will enable access to better training and services, but also could increase the flow of political and social ideas across borders. The AFCFTA integration is intended to move countries to trade beyond their domestic markets and could eventually include the delivery of regional public goods, leading to improved infrastructure and predictability for investors. Transport corridors, cross-border digital connections, and disease control systems are all potential areas of multinational collaboration. Increased sharing of resources and ideas might lead to the strengthening of democratic ideals across the continent, and populations that have lacked public freedoms or open discourse in their own social contexts might be exposed to fairer practices in other parts of the continent. Improved governance would naturally lead to stronger market confidence. At the same time, we will be watching closely to see if grassroots protectionist sentiment, especially in major economies with large informal sectors like Nigeria and South Africa, is leveraged as a form of anti-establishment backlash.

## Drawing inspiration from the EU

### EU single market helping smaller states

The African Union (AU) may take inspiration from the framework set up by the European Union to create a lasting single market and customs union. EU institutions provide checks and balances to prevent any single country from imposing its will on the common agenda, which has helped ensure that smaller nations benefit as much as wealthier Western European nations do. There are indications that the AU might aim to replicate this model within the AfCFTA to help smaller African countries grow and develop alongside larger economies. Additionally, before countries join the EU, they must meet certain criteria including but not limited to strong institutions, political stability, and respect for human rights. If implementation of the AfCFTA prioritizes similar institutional norms amongst member states, it could be a catalyst for encouraging better governance and stronger democratic processes across Africa. While the AU has several existing institutions to help drive economic development and joint political strategy, they need strengthening to be able to effectively develop policy and respond to continent-wide issues.

### AU passport

The AU passport is part of the AU's Agenda 2063 plan and is aimed at removing restrictions on Africans' ability to travel, live, and work throughout the continent. It promotes free movement for all African citizens between all African countries. The idea for an AU passport, like the EU passport, has gained further traction in discussions relating to the AfCFTA. It has several benefits, including boosting intra-Africa trade, commerce, and tourism; enabling Africans to have labor mobility and transfer their knowledge and skills throughout Africa; promoting an African identity that allows for social integration; and improving infrastructure and shared development across borders.

The proposed AU passport is not without its challenges; there may be pushback from larger countries such as Nigeria and South Africa, which could take a protectionist stance if they do not want to accept an influx of migrants from across the continent. They fear their markets could be flooded with Africans in search of more lucrative economic opportunities. However, if countries embrace the spirit of collaboration and invest in the vision of a continental free trade area with shared ideas, resources, and culture, then the AU passport could be another effective tool for creating a united Africa. Notably, the AU passport is a long-term goal of the AU and is unlikely to be realized in the near future, especially as issues such as the pandemic, economic recovery, and development continue to hold the focus of African leaders.

### Common currency

The AfCFTA Secretary General, Wamkele Mene, has indicated that a common African currency that can be used within the AfCFTA, much like the Euro in the EU, is a realizable goal. A common currency is a long-term aim for both the AfCFTA Secretariat and the AU, in the interest of promoting macro-economic convergence and facilitating intra-African trade. Given the priority placed on finalizing negotiations and ratification of the AfCFTA, however, it is unlikely that a common currency will come into effect in the next several years.

Until a common currency is realized, the AfCFTA has created the Pan-African Payment and Settlement System (PAPSS) to enable countries to carry out free trade in their local currencies. Currently there are 42 currencies on the continent, and it costs approximately $5 billion per year to convert these currencies. The PAPSS therefore plays an important role in establishing a functioning digital currency exchange and facilitating payments and saving conversion costs. The PAPSS is still in its pilot stage and is being tested in Ghana, Liberia, Nigeria, and Sierra Leone.

## Series conclusion

The AfCFTA is a momentous achievement for Africa, creating a continental market of over 1.3 billion people and with a GDP of $3.4 trillion. The eventual removal of 97 percent of tariffs will boost trade and foster the free flow of goods, services, and people across Africa. The AfCFTA will also provide opportunities for trade deals with external partners and foreign investors. Navigating the current overlapping regulations across the continent will be key to the AfCFTA's success. Infrastructure, security, and capacity shortfalls will challenge the implementation of the agreement, but political will from key African leaders can mitigate these risks, and early investors will be well positioned to benefit from the AfCFTA. The AfCFTA will play an increasingly important role in Africa's economic recovery from the effects of Covid-19 as manufacturing, digitization, and labor opportunities are likely to surge under the AfCFTA, with African youth poised to be major beneficiaries. Along with increasing connectivity around trade, the AfCFTA is likely to improve social and political connections between African countries that could lead to strengthening of democracy and governance.

African markets are likely to surge following successful implementation of the AfCFTA, and it is critical for investors to be positioned early to benefit from the trade area's upsides.

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## About ASG

Albright Stonebridge Group (ASG), part of Dentons Global Advisors, is the premier global strategy and commercial diplomacy firm. We help clients understand and successfully navigate the intersection of public, private, and social sectors in international markets. ASG's worldwide team has served clients in more than 120 countries.

ASG's Africa practice has extensive experience helping clients navigate markets across sub-Saharan Africa. For questions or to arrange a follow-up conversation please contact Pierre Tantchou.