



## **DRAFT NOT FOR PUBLICATION**

### **INDUSTRIALIZATION AND ECONOMIC DIVERSIFICATION – KEYS TO UNLOCKING THE FULL POTENTIAL OF THE AFCFTA : A CASE STUDY FOR CENTRAL AFRICA**

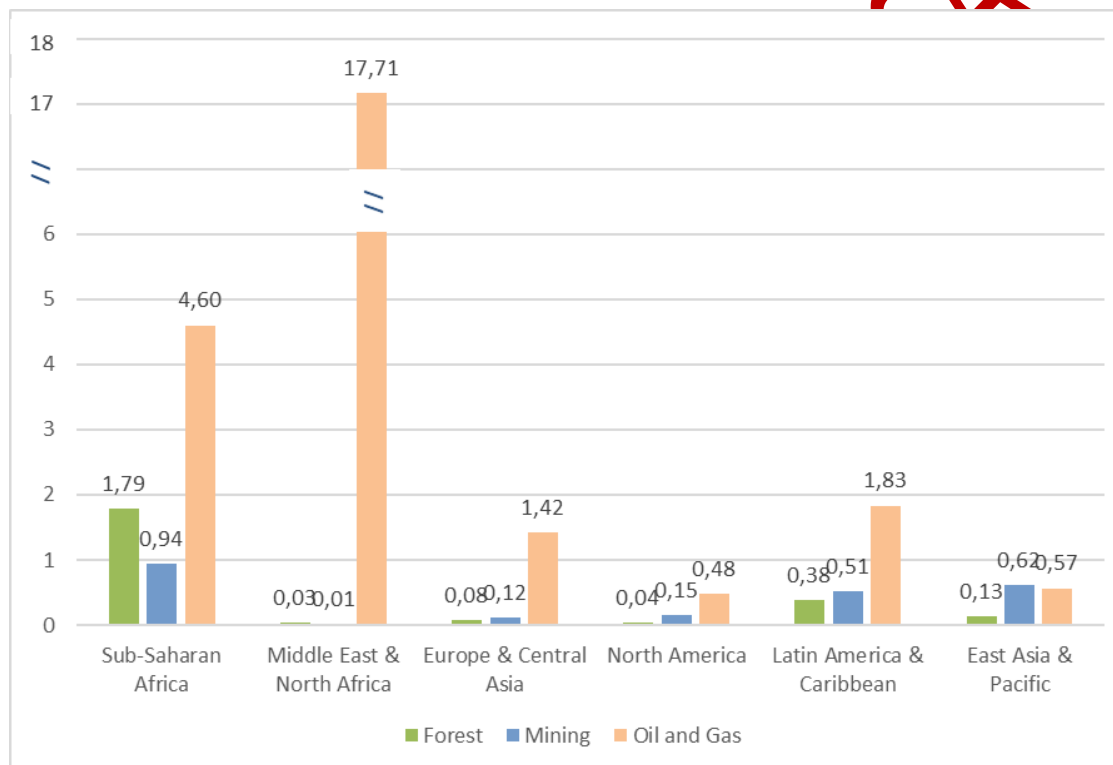
#### **ABSTRACT**

Established on 1 January 2021, the African Continental Free Trade Area (AfCFTA) is a key opportunity for Central African governments to build upon regional integration strategies, aligning their national trade strategies as well as industrial strategies, to enhance intra-regional trade as well as trade with continental partners. For an agreement as comprehensive as the AfCFTA, implementing evidence-based policies necessitate comprehensive analysis of plausible economic outcomes of policy strategies for the AfCFTA and in concordance with national industrialization strategies. In this paper, being the most comprehensive CGE analysis for Central Africa to-date, we model the impact of the AfCFTA on Cameroun, Tchad, the Congo, Gabon, and Rwanda, with consideration of three possible scenarios of structural change for the region.

# 1. Introduction

While natural resource abundance can provide opportunities for economic growth, natural resource dependency is often associated with stagnated growth (Badeep et al., 2017). Countries across Africa have faced the so-called natural resources curse, with natural resources rents accounting for over 7% of GDP across Sub-Saharan Africa, compared with less than 1% in North America, less than 2% in Europe & Central Asia and East Asia & Pacific, and less than 3% in Latin America & the Caribbean. The only region where natural resource rents surpass those in Sub-Saharan Africa is the Middle East & North Africa where Oil and Gas rents reach 17.17% (Figure 1).

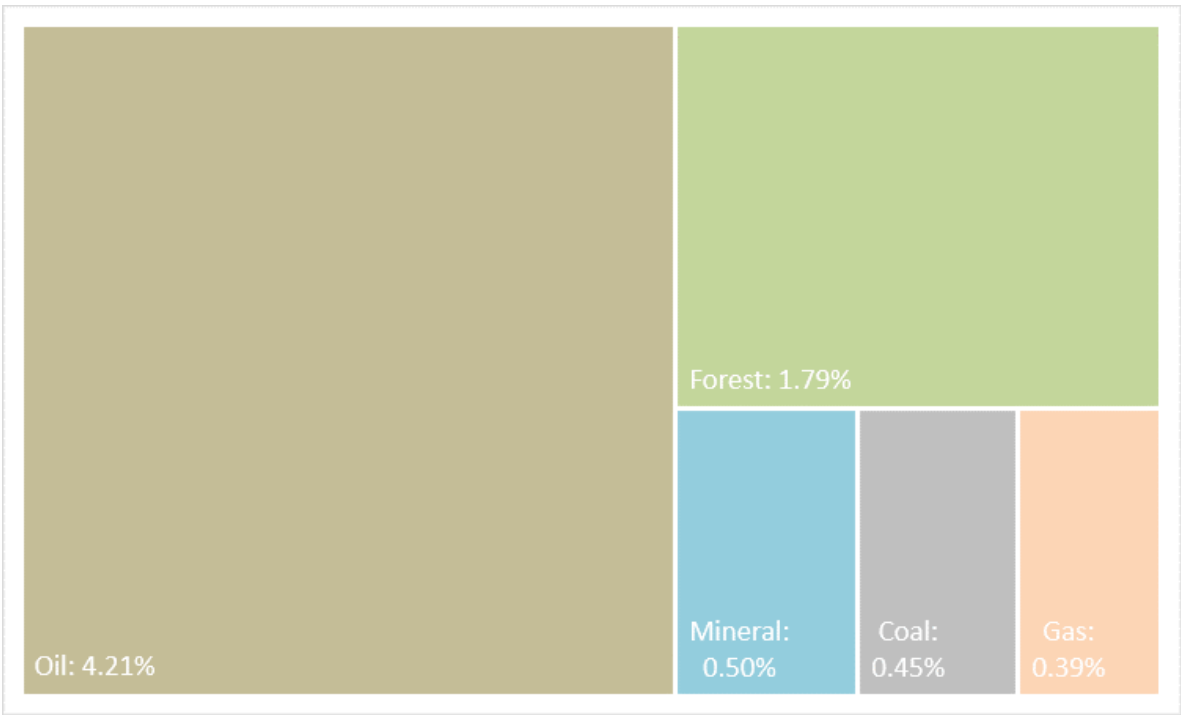
Figure 1. Natural Resource Rent (% GDP)



Source: ECA computed from World Bank WDI (2019)

Within Sub-Saharan Africa, natural resources rent are composed of 4.6% from Oil and Gas, 1.8% from Forest products, and 0.95% from Minerals and Coal. This dependency on natural resources highlights the need to diversify away from low-value added production and move up the value chain (increase value-added in primary sectors). Through investments in industrialization raw materials can be process into chemicals, pharmaceuticals, batteries, paper, furniture, and other goods with value-added. Further, economic diversification is an incubator structural transformation as the importance of manufacturing and supporting services in the economy increase over time.

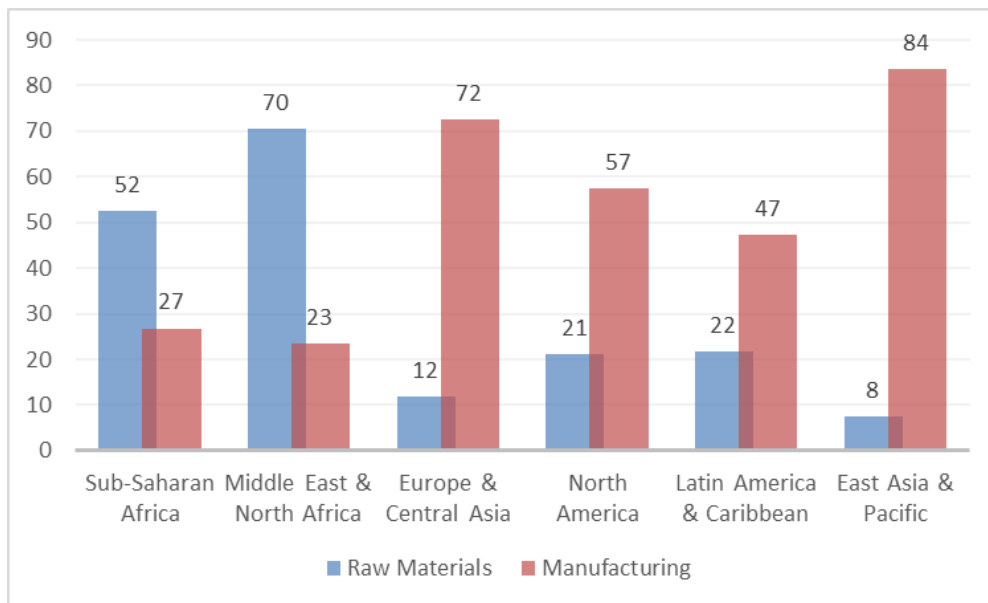
Figure 2. SSA Natural Resource Rent Composition (% GDP)



Source: ECA computed from World Bank WDI (2019)

Diversifying merchandise trade is key to enhancing economic resilience. Raw materials account for 52% of merchandise exports across Sub-Saharan Africa and 70% in MENA, compared with less than 25% in all other regions (Figure 3). Inversely, Manufacturing goods account for less than 30% of merchandise exports in Sub-Saharan Africa and Middle East & North Africa, compared with 47% and greater in all other regions.

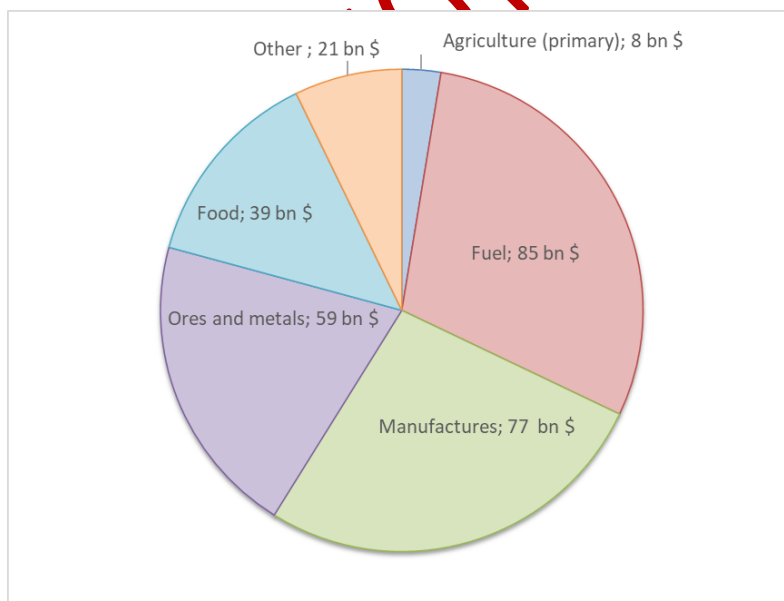
Figure 3. Merchandise exports (%)



Source: ECA computed from World Bank WDI (2020)

Within Sub-Saharan Africa, raw material exports include fuels (29%), ores and metals (20%), and primary agriculture (3%), for a total of 152 billion USD in 2020 (Figure 4). Increasing export diversification relies on countries aligning national trade strategies with national plans for industrialization and economic diversification. The AfCFTA presents itself as a key opportunity for countries to align national policies and implementation plans to diversify the economy and the export portfolio. Diversifying the export portfolio is crucial for hedging against international commodity price shocks and increasing overall economic resilience.

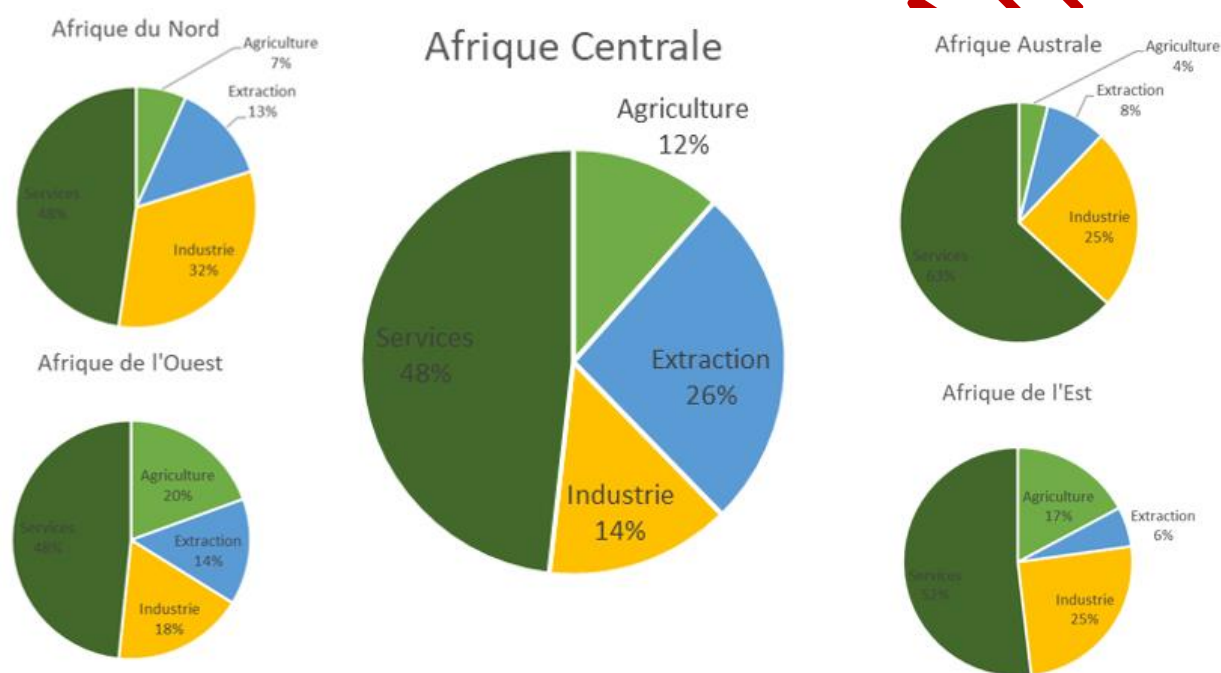
Figure 4. SSA Merchandise Export Composition



Source: ECA computed from World Bank WDI (2020)

Within the African continent, the level of dependance on natural resources and, inversely, the level of economic diversification is variable across regions. Measuring output across subregions from the GTAP Database (Aguiar et al., 2019), Central Africa is the subregion with the highest production dependence on extraction, accounting for 26% of total output, compared with an average of 10% across the rest of the continent. Further, manufacturing output is the lowest amongst subregions, accounting for 14% of total output, in contrast to an average of 25% across all other subregions (Figure 5).

Figure 5. Production Structure in the GTAP Database



On 29 September 2017, Central African member states adopted the Douala Consensus, committing to spurring economic diversification through industrialization and trade, with the aim to increase subregional production of higher-value products. In parallel, all Central African member states ratified the African Continental Free Trade Area (AfCFTA), under which free trade began on 1 January 2021. The AfCFTA is a key opportunity for Central African governments to build upon regional integration strategies, aligning their national trade strategies as well as industrial strategies, to enhance intra-regional trade as well as trade with continental partners. However, only by achieving the objectives of the Douala Consensus will Central African states be able to unlock the full potential of the AfCFTA.

In this paper, we assess the impact of economic diversification and industrialization in combination with the implementation of the AfCFTA for Central Africa. Several CGE studies have analyzed

the AfCFTA, at the continental level, with certain reporting results for select members of Central Africa, from institutions including the European Commission (Simola et al., 2021), the World Bank (The World Bank, 2020), the IMF (Abrego et al., 2019), UNCTAD (Vanzetti et al., 2018; Saygili et al., 2018), and UNECA (UNECA, 2021). Ekobena et al. (2021) specifically analyze the effects of the AfCFTA on Central Africa, presenting macro-level findings at the country level for Cameroon, the Central African Republic, the Democratic Republic of Congo, Gabon and Chad. The present paper expands upon these studies through its focus on Central African countries and importantly through linking trade policy to industrialization plans at the sectoral level.

## 2. Methods

We begin with a Computable General Equilibrium (CGE) simulation of the AfCFTA, implementing a preliminary version of the GTAP Database with increased coverage for Economic Community of Central African States (ECCAS) members, featuring updated data for Cameroon as well as newly included data for Chad, the Congo, Gabon, Equatorial Guinea, and the Central African Republic<sup>1</sup>. We use the standard GTAP model (Corong et al., 2017) to implement sequential simulations of the AfCFTA through (1) tariff removal, (2) non-tariff barrier reduction, as well as economic diversification and industrialization through (3) manufacturing growth, and (4) services growth. Simulations (3) and (4) are linked to exogenous structural change, for which we explore adaptations of mechanisms as outlined by Château et al. (2020) in which primary efficiency and the intensification of intermediate demand are calibrated. We additionally consider preference twists, as per mechanism described in Carrico et al. (2020).

## 3. Results

Preliminary results from the AfCFTA simulation demonstrate overall increases in trade among ECCAS member countries across all products, with the exception of extraction products which decrease. Trade between ECCAS members and the rest of the continent increases across all products. Extra-continental trade decreases. The most important increases in trade for ECCAS as a subregion occur for heavy and light manufacturing as well as processed food. While the largest current increases in trade for the ECCAS subregion are in fact import substitution (Rest of World imports replaced by Rest of Africa imports), structural change simulations are anticipated to increase trade within the ECCAS subregion as well as boost exports to the rest of the continent.

- a. Macro-economic results
- b. Production results
- c. Trade results

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<sup>1</sup> Data for Rwanda is already in the standard release of the GTAP Database version 10. Data collection for Burundi has been completed. A data collection project for the Democratic Republic of Congo, Angola, and São Tomé and Príncipe is underway.

## 4. Discussion

## 5. Conclusion

## 6. References

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