

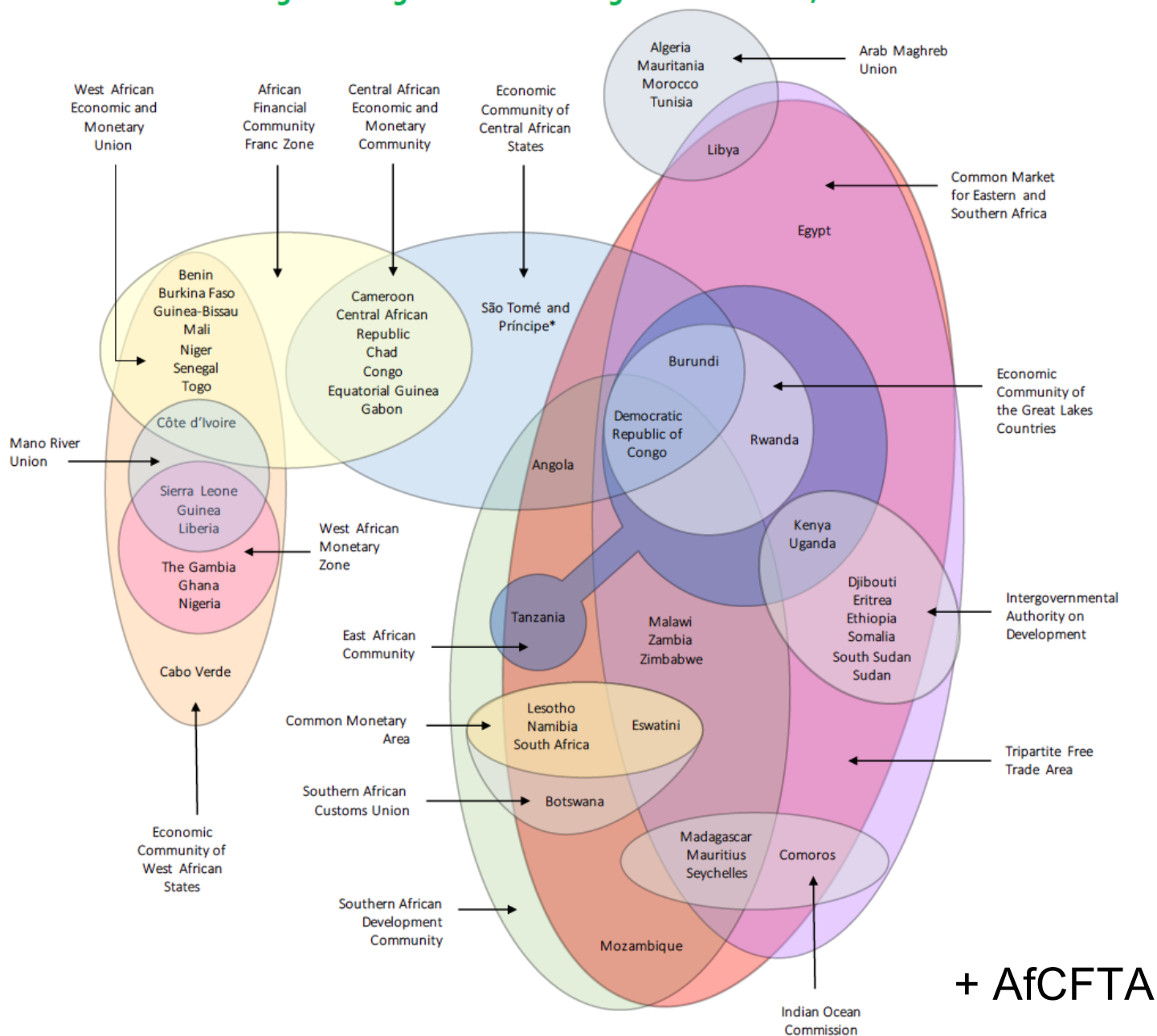
# Trade and Regional Flows:

What is the potential for more open trade,  
at the regional and continental level to  
strengthen and diversify economies?

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JRCPPF Conference, Princeton University  
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**Figure 1. Regional Trade Arrangements in Africa, 2019**



Source: IMF (2020)

Source: Adapted from *Economic Integration in Africa*, Figure 3.1,

[www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2019AEO/AEO\\_2019-EN-CHAP3.pdf](http://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/2019AEO/AEO_2019-EN-CHAP3.pdf)

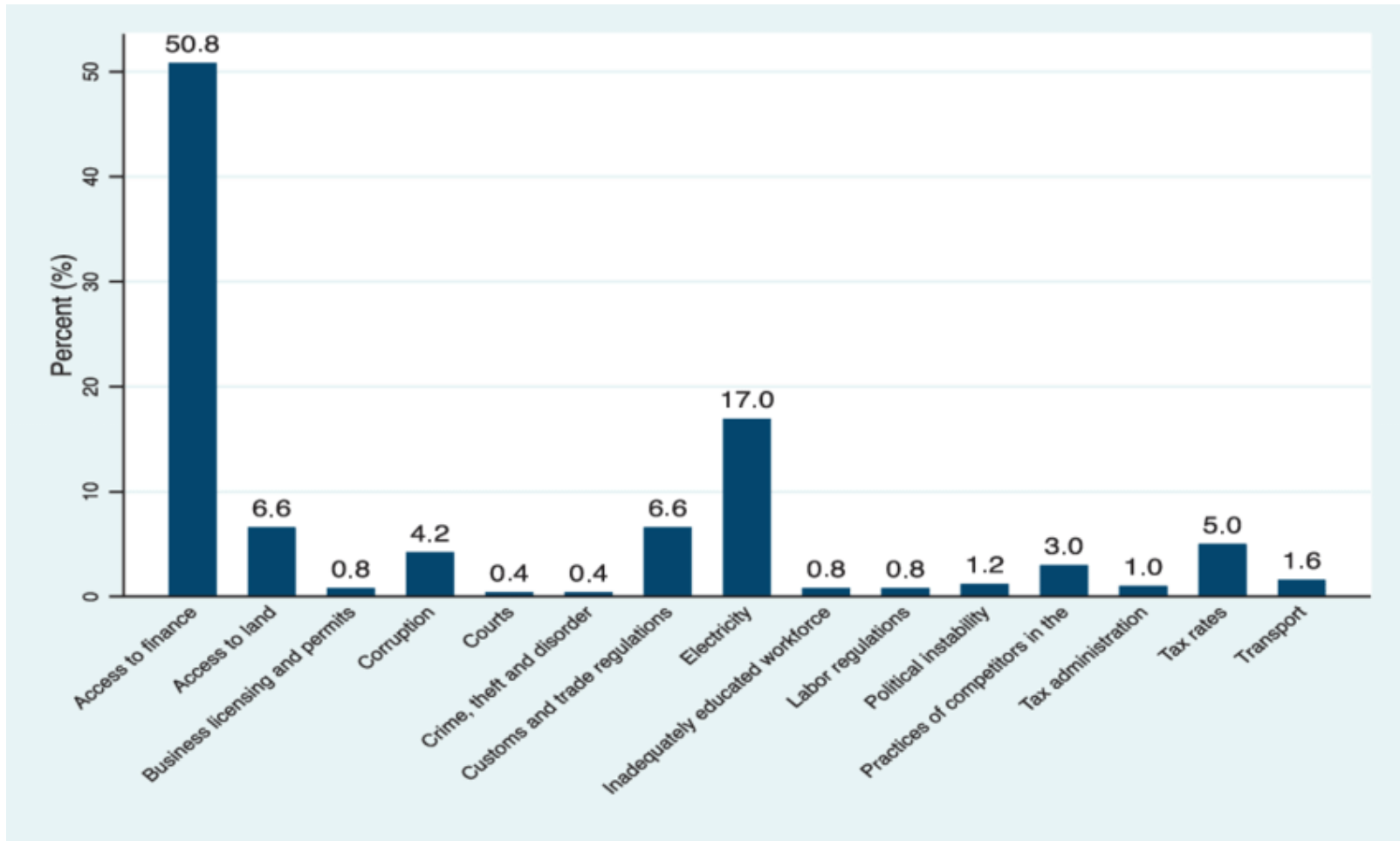
# Regional Integration and Economic Performance: Old Ideas

- Economists have long predicted that regional integration could strengthen economic performance and productivity
  - If the effects of trade creation exceed trade diversion
  - Specialization according to comparative advantage
  - With larger market
    - Economies of scale
    - Access to cheaper and greater variety of goods and production inputs
    - Product and process innovation

# Positive welfare effects of AfCFTA

- Predicted welfare gains in SSA of 2.6% (IMF (2020))
- Most of the gains from eliminations of non-tariff barriers rather than tariffs
- Predicted expansion of trade in foods and manufactured goods
- These predictions are based on standard trade models that do not account for misallocation of resources nor domestic constraints/distortions
  - Not fully capture the environment in which firms in LMICs operate

# Main obstacles facing companies in Ghana



Source: Mohammed and Bunyaminu (2021) based on World Bank Enterprise Surveys

# Trade and Domestic Distortions

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## Distortions facing firms

- Small, informal firms
- Connected firms
- Access to Finance
- Energy/Land/Materials/Labor
- Imperfect competition
- Contracting Frictions
- Information frictions
- Externalities
- Weaker institutions

## Infrastructure

- Electricity
- Roads, ports
- Logistics

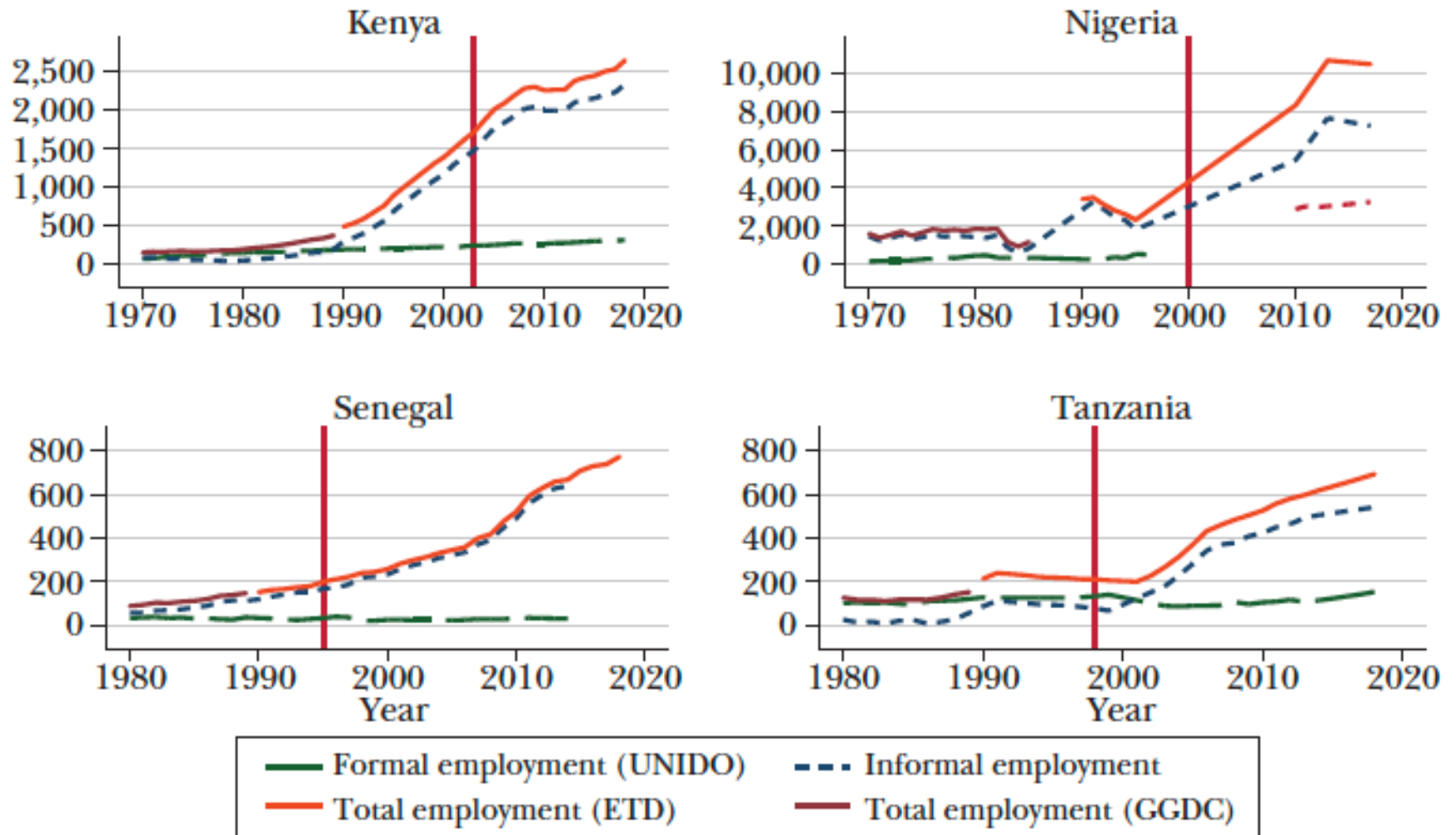
## Policies at the border

- Tariffs
- Non-tariff measures
- Customs
- Trade regulation
- Harmonization

# Can intra Africa trade strengthen economies?

- Important to consider how constraints facing companies and intermediaries/traders interact with trade
- International Trade VoxDevLit Survey (Atkin and Khandelwal (2022))

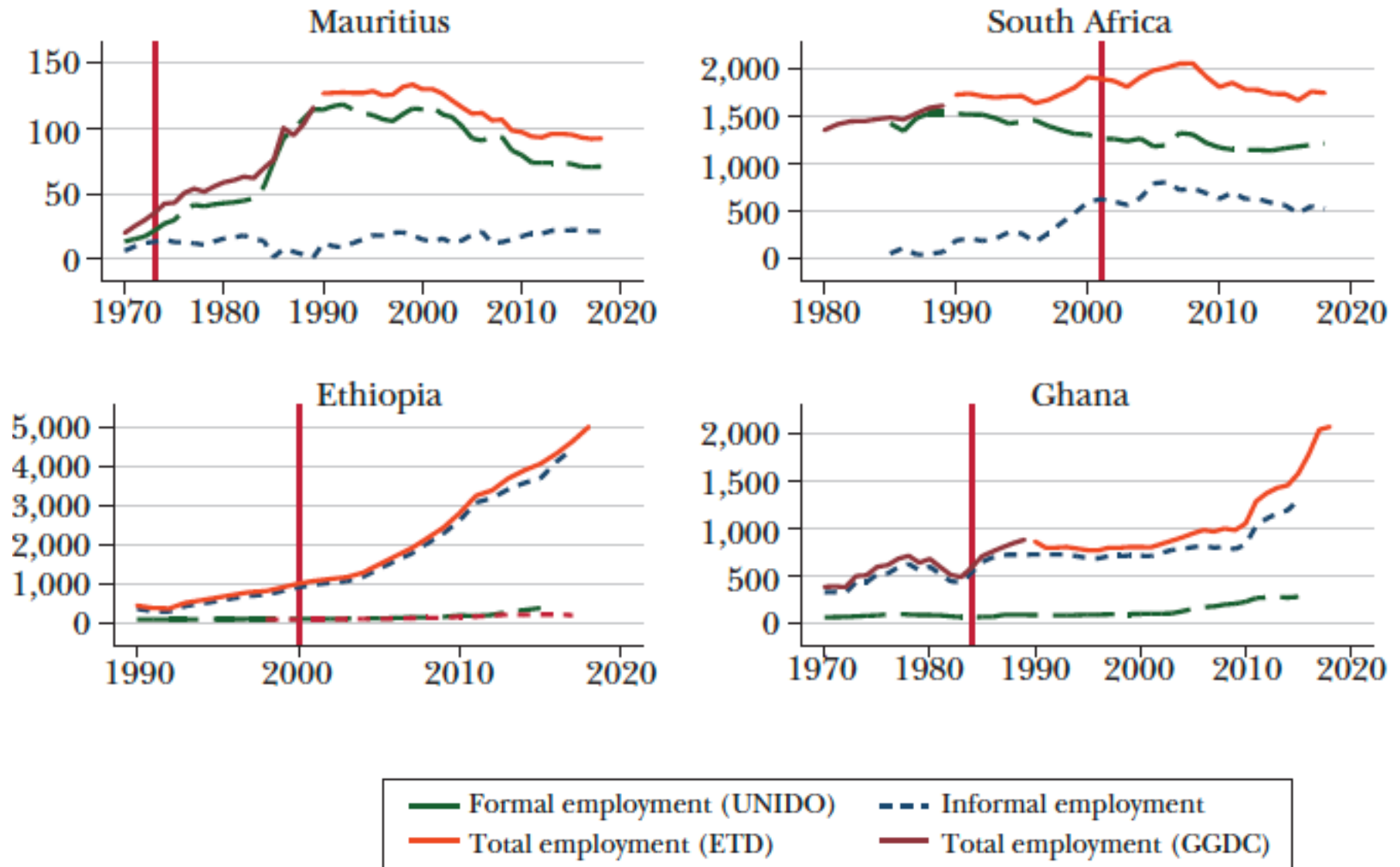
# #1: Manufacturing employment dominated by informality



Source: McMillan and Zeufack (2022)



# Manufacturing employment dominated by informality



Source: McMillan and Zeufack (2022)

## #2: Information and contractual barriers to trade

- Traders face large costs to learn about products in distant markets
- Contracts are difficult to enforce internationally, especially among small-scale companies
- An Example: Nigerian importers who trade consumer goods such as clothing and electronics (Starz 2017)
  - Despite very costly travel, 2/3 of importers travel internationally to meet suppliers and purchase goods (rather than on a phone or online)
  - Product search and contracting problems reduce welfare by about 23% in trade of consumer goods (due to lack of varieties, lower profits)
  - This cost is over half the size of welfare losses due to traditional trade

# Reducing information and contractual barriers to trade

- Technology helps in markets with relatively homogeneous products (Aker and Mbiti 2010)
- Travel allows traders overcome large search and contract enforcement problems in more differentiated products (Starz 2017)

“travel regulations, the design of financial services, and information aggregation via trade fairs and credit bureaus.” (Starz 2017)

- Airlinks increase business links and the movement of people fosters investment (Campante and Yanagizawa-Drott 2018)
- Relational contracting (Macchiavello (2021))

## #3: Reforming Trade Institutions

- Why might distortions occur in protected markets?
  - Institutions such as customs are formed to manage trade barriers
  - They are subject to bureaucratic capture
  - Customs agents have lots of discretion to withhold goods in bonded warehouses, assess tariff duties, demand more paperwork, etc.
  - Institutions that manage trade barriers may favor firms that can navigate “the system” over firms that can produce efficiently
  - Misallocation of resources toward less efficient firms, reducing aggregate productivity

# Reforming trade institutions

- Customs reform can reduce such distortions
  - Improved aggregate productivity through reallocation of resources toward less connected, but potentially more productive firms (Khandelwal et al 2013 for China; Sequeria 2014 for Mozambique)
  - Improved tax revenue collection (Chalendard, et. al 2021 for Madagascar)
- If credible, AfCFTA might also reduce uncertainty about trade policy and regulatory environment
  - Improved incentives for firm entry and investment, including FDI (Handley and Limao 2015)

# Can intra Africa trade strengthen economies?

- Intraregional trade dominated by trade in food and manufactured goods
  - A lot of potential for gains from trade
  - Important to understand and address distortions/constraints that companies face and how they interact with trade integration
- If credible, AfCFTA could change trade institutions and reduce distortions & uncertainty that limit firm entry and growth
- Promising area for continued engagement of policy makers and researchers
  - Research on trade & development booming, broad range of methodological tools and increasingly rich data sources
  - Increasingly focused on how domestic distortions and trade interact
  - Check out VoxDevLit Wiki inspired Literature Surveys (International Trade)