CONTINENTAL INTEGRATION & THE NIGERIAN ECONOMY

The Effect of the African Continental Free Trade Area on Medium Small and Micro-scale Enterprises in Nigeria

September 2020

COALITION PARTNERS

FUNDED BY CIPE

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ACKNOWLEDGEMENTS

Profile of Coalition Members

NACCIMA: The Nigerian Association of Chambers of Commerce, Industry, Mines and Agriculture (NACCIMA) established in 1960, is the umbrella organization for all the various affiliate member- chambers within the country. The Association's membership is voluntary, and it encompasses City, State and Bilateral Chambers, Business/Professional Associations and Corporate Bodies. It champions the course of business through its advocacy role and influence public policies that promote free enterprise. The perspective of NACCIMA is in accordance with contemporary ideas of the Chamber of Commerce Movement in a relatively free enterprise economy the world over.

MAN: The Manufacturers' Association of Nigeria (MAN) was established in May 1971 as a company limited by guarantee. The establishment of the Association was motivated by the desire to have a focal point of communication and consultation between industry on the one hand, and the government and general public on the other. Hitherto, there was no institutional organ whose central focus was to give meaning to the interests, problems and aspirations of the manufacturing sector. The establishment of the Manufacturers Association of Nigeria was to provide a platform for the private sector to formulate and articulate policy suggestions that would be complementary to government's efforts at policy formulation.MAN is in the business to create a climate of opinion in Nigeria in which manufacturers can operate efficiently and profitably for the benefit of all. As the collective voice of its members, MAN was established to promote and protect manufacturers' collective interests.

NECA: Nigeria Employers' Consultative Association (NECA) is the umbrella organization of Employers in the Organized Private Sector of Nigeria. It was formed in 1957 to provide the forum for the Government to consult with private sector Employers on socio-economic and Labor policy issues. NECA provides a platform for private sector employers to interact with the government, labour, communities and other relevant institutions in and outside Nigeria for the purpose of promoting harmonious business environment that will engender productivity and prosperity for the benefit of all. NECA is not a trade union but a dynamic and highly respected professional body registered under the Company and Allied Matters Act 1990.

NASSI: The Nigerian Association of Small Scale Industrialists (NASSI) was founded in 1978 and registered under the Land Perpetual Succession Act as a non – profit making and non – governmental organization. It has branches in all the states of the Federation, the FCT Abuja and Local Government Areas. The mission statement of NASSI is 'to create wealth through the industry in an enabling environment for the benefit of all stakeholders.

NASME: The Nigerian Association of Small and Medium Enterprises (NASME) was registered in 1996 as a Business Membership Organization (BMO), to co-ordinate and foster the promotion of Micro, Small and Medium Enterprises (MSMEs) in Nigeria. The Association provides a forum for interaction, and adoption of concerted approach to issues of strategic importance to the development of MSMEs. The Association is committed to further advancing the NASME brand by providing high-quality and responsive services and building and strengthening partnerships nationwide in order to better serve her members.

NANTS: NANTS is the umbrella body of traders in raw materials, industrial and finished goods (both locally made and imported) as well as small and medium enterprises (SMEs) in Nigeria. However, in order to encourage/improve the interlink between production and (market access) distribution of goods, NANTS membership has recently been expanded to small scale manufacturers of items like shoes, garments, cosmetics, furniture, household goods and local material providers as well as small scale farmers in various agricultural produce. Women constitute about 65% of NANTS membership.

FACAN: The Federation of Agricultural Commodity Associations of Nigeria (FACAN), the apex and umbrella body for agricultural commodity associations was formed in line with Public Private Partnership Arrangement (PPPA) as a one-stop shop between the Government and the Organized Private Sector in Agriculture along the agricultural value chain. Its mission is to promote mutual understanding among the agricultural commodity associations and create enabling environment for a unified organization that is better positioned operationally and financially to deliver to itself and the general public, value added services in agriculture and allied business.

Association of Nigerian Women Business Network

ANWBN: The Association of Nigerian Women Business Network (ANWBN) is a coalition of 45 Women Business and Professional Associations in Nigeria with over4 million entrepreneurs with the common goal of encouraging and improving sustainable entrepreneurial development among women through research, advocacy and policy reform initiatives. ANWBN was established in 2013 with 18 founding member associations. ANWBN is widely spread across the six geopolitical zones and with presence across most states of the federation and the Federal Capital Territory (FCT). In its short history, the network has undertaken series of Policy reform initiatives targeted at improving the operating environment of women business operators. ANWBN in 2016, launched the 'Women National Business Agenda (WNBA)' which brought about high level policy engagements with both the executive and the legislature. In 2020, ANWBN launched the revised edition of the WNBA and is presently engaging public sector stakeholders on the thematic issues highlighted in the report. www.anwbn.org.ng

Center for International Private Enterprise (CIPE)

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A Note on CSEA

The Centre for the Study of the Economies of Africa (CSEA) is a non-profit think tank based in Abuja Nigeria, that produces independent, high quality and evidence-based research on economic development issues in Africa. CSEA's objective is to use its research findings to enhance development outcomes . Since its inception in 2008, CSEA has evolved into a highly effective and influential think tank dedicated to utilizing its research output to facilitate evidence-based policymaking in African countries. The Centre has been consistently ranked as one of the leading think tanks in Africa by the University of Pennsylvania's Global Go To Think Tank Index. In 2019, CSEA was awarded the 'Recognition as SDG Champion' honor by the International Network for Corporate Social Responsibility (In-CSR), in acknowledgement and commendation of the Centre's success in advancing the Sustainable Development Goals (SDGs). In addition, CSEA became a United Nations Commission for Trade and Development (UNCTAD) Regional Centre of Excellence in 2019 in recognition of its research in promoting trade and development in the global South.

EXECUTIVE SUMMARY

Africa is at a historical crossroads. The launching of the operational phase of the African Continental Free Trade Area (AfCFTA) Agreement during the 12th Extraordinary Session of the Assembly of the African Union (AU) in Niamey, Niger on 7 July 2019 marks the most significant event in the decades-long project of African integration. If managed efficiently, this newly formed market of 55 nations, 1.2 billion people, and an aggregate GDP of up to $6.7 trillion Purchasing Power Parity (PPP) has the potential to bring unprecedented stimulus to African economies by unlocking the historically low level of intra-continental trade and attracting long-term, stable investments from around the world.

While there is general optimism surrounding the promise of AfCFTA to support economic development, there must also be a recognition that, like all Free Trade Agreements (FTAs), the AfCFTA will inevitably create winners and losers. Whether for their own inefficiencies, or the sub-optimal business environments they may find themselves in, some businesses – or even entire sectors of national economies – will not be in a position to make the most from the expanded market opportunities and may be unable to compete with the influx of new competitors from other economies.

These were just some of the considerations that sparked considerable opposition to the deal in Nigeria prior to its signing. Unfortunately, there has previously been a general lack of data and information regarding how the national economy will react, leaving plenty of room for speculation. In this report, CSEA employs a two-pronged strategy to begin filling in the knowledge gap that exists about the possible effects of the AfCFTA on Nigeria's economy.

First, we zero in on Nigeria's Micro, Small, and Medium Enterprises (MSMEs). It is no overstatement to say MSMEs are the backbone of the Nigerian economy. In fact, more than 96 percent of all business – contributing to 75 percent of national employment – qualify for MSME status. No trade deal can be good for Nigeria without it benefiting at least the majority of MSMEs. Too little is known about how MSMEs will be affected by the introduction of continental free trade.

In the production of this report, we conducted a representative survey of more than 1,800 MSMEs in five Nigerian states that covered the country's various sociocultural zones to evaluate MSME awareness and preparedness to take advantage of the AfCFTA Agreement. We also gauged their most urgent needs to make the most of the opportunities presented by AfCFTA and to recover efficiently from the impacts of the COVID-19 pandemic.

Through this process, we found a worrying degree of unawareness about AfCFTA. Two-thirds of MSMEs surveyed declared not knowing of the deal's existence. This lack of knowledge is particularly acute among smaller businesses and can represent an enormous obstacle to the successful uptake of AfCFTA. The knowledge deficit is compounded by the reported under-utilization of previously-entered-into FTAs as a result of their complicated compliance requirements. We therefore recommend a targeted, context-specific knowledge dissemination strategy as a key requirement for MSME success in a post-AfCFTA economy.

Among respondents aware of the Agreement's existence, we found general optimism about businesses' ability to make the most of its opportunities. Nevertheless, many were somewhat worried by the prospects of more competition and reported a strong need for government investment in electrification and general transport infrastructure to enable them to compete effectively. These problems are, of course, not new in Nigeria. Nevertheless, our findings reinforce the need for a national concentrated effort to ameliorate the business environment to ensure Nigeria thrives in the newly integrated continent.

Finally, the majority of businesses surveyed declared that, in their view, the most effective government relief strategy in the wake of the pandemic would be making business loans more readily available. While we do not take a position on the matter, the findings can certainly be beneficial to national policymakers as they plan the recovery strategy.

The second prong of this study takes a more general look at macroeconomic reactions and trade creation/diversion in the Nigerian economy as a result of AfCFTA. Here, we employed a Computable General Equilibrium (CGE) Model to simulate the general movements of the Nigerian economy, as well as those of other economies across the continent.

Our result shows modest positive welfare gains to Nigeria with machinery, other transport, textile and metal products as well as textile industries accounting for most of the positive effects on real wage. Sectors with large tariff reductions recorded higher volume of trade. AfCFTA led to changes in pattern of trade flow across Africa. The African countries facing the possibility of the most gains from AfCFTA are Angola, Botswana, and Seychelles.

It is clear from both sections of this study that the mere signing of the AfCFTA Agreement will not guarantee increased economic prosperity in Nigeria on its own. There is therefore no room for complacency. In this report, we highlight some of the most salient issues that may arise from the implementation of the AfCFTA Agreement and contribute to the foundation and accessibility of knowledge required to effectively set this historic Agreement in motion.

CHAPTER 1

Introduction

The roadmap towards a regionally integrated Africa formally commenced with the signing of the African Economic Community (AEC), also known as Abuja Treaty, in June 1991. The Treaty established the building blocks towards the completion of the AEC by 2028. With the Treaty coming into force in 1994, African countries were expected to complete six consecutive regional integration steps which would lead to a fully integrated market at the continental level within a 34-year period.

These steps included (i) strengthening of intra-regional integration and the harmonization between the blocs; (ii) creation of regional blocs (that is, the Regional Economic Communities or RECs); (iii) establishment of free trade areas (FTAs) and customs unions in each the RECs; (iv) creation of a continental free trade area and customs union; (iv) creation of an African common market; and (vi) establishment of an African economic monetary union and a parliament.

However, the process of having a regionally integrated Africa has not been smooth and linear, both within and across all of the RECs (Mevel and Karingi, 2012). FTAs are established components of regional integration and have been known to promote commodity trade and investment flows by creating an improved enabling environment for cross-border transactions (Kawai & Wignajara, 2008). The processes may also prompt diversion of trade and investment away from countries with less favourable business conditions (Yunling, 2010). Thus, the impact of FTAs widely differs across countries on account of a multitude of factors that impact the business environment.

Intra-continental trade in Africa is the lowest among all other regions in the world. This poor trade performance is both a significant cause and an obvious effect of the poor social and economic development of the region. Another crucial factor that could explain the low intra-African trade are both trade and non-trade barriers to exchange of good and services. The recent progress with the establishment of AfCFTA as endorsed by 54 African countries in July 2019 is therefore reassuring, given its potential to reduce the presence of barriers to trade on the continent.

However, the economic impacts of an FTA are unlikely to be the same across participating countries. There will be winners, and there will be losers. To this point, an in-depth literature review by Stevens et al. (2015) concludes that FTAs have positive effects on trade growth in at least some cases; however, the picture is mixed, with a range of widely-varying estimated effects. Even for a country benefiting from the ratifying of an FTA, the gains will be unevenly spread across sectors. This implies that, while aggregate trade and development gains from AfCFTA are likely, little is known on inter- and intra-sectoral gains within individual countries as well as the disparate effects in different nations.

For Nigeria, the impact of AfCFTA, as with any other FTA, could vary on account of a number of market opportunities and constraints to production. For example, Babatunde (2006) applied the gravity model to examine the impact of trade policy reform and regional integration on the export performance of the

Economic Community of West African States (ECOWAS). The author finds that unilateral trade barrier reductions and participation in preferential trade agreements within the ECOWAS sub-region is beneficial and trade-facilitating for Nigeria. On the other hand, Nwafor (2005) finds that a reduction in import tariffs through FTAs will expose Nigerian firms to an increased vulnerability, as it makes domestic producers more susceptible to imported goods of lower prices and/or higher quality in the short term. This is just one example of contradictory evidence that creates uncertainty on the ultimate outcome of FTAs generally, and AfCFTA in particular.

Existing discussion by some analysts suggest that Nigeria stands to benefit from the AfCFTA in a number of ways including: (i) increased sources of raw materials from the African continent; (ii) a larger market for Nigerian goods and services; (iii) increased employment for Nigerian youth (that are able to provide cross-border services, especially in technology); and (iv) an increased market share for the Nigerian financial services sector (which is currently dominating the West African market). However, prior to the signing of the Agreement by the Nigerian government, there were counter debates on these potentials, especially concerning the likely harmful effects it poses to the nation's fragile manufacturing sector, given the existing challenges that it already faces. Some of these challenges include high cost of capital (lending rate of about 17 percent), a severe infrastructure deficit, and the high cost and inadequate access to production inputs (Deloitte, 2018).

Amidst this discourse, the potential impact of the AfCFTA on MSMEs is the least understood. MSMEs are critical constituents of the Nigerian economy, as they represent about 96 percent of Nigerian businesses and contribute 75 percent to the national employment (SMEDAN, 2019). One predominant concern is that deficient human and technological capacity of MSMEs in Nigeria predisposes them to the negative spill overs potentially associated with free trade and investment exchanges within the continent. However, MSMEs can benefit from greater access to new markets and the possible economic transformation that competition could promote. With the conversation on the recent ratification of the AfCFTA in Nigeria (11 November 2020) growing, it is therefore imperative to evaluate the extent to which the economic expectations and growth potential of the AfCFTA will benefit Nigerian MSMEs, and understand the potential costs of these economic opportunities.

This report aims to delve comprehensively into the costs and benefits arising from AfCFTA on Nigeria's economy at large, while simultaneously paying particular attention to the fate of MSMEs. The framing of this report reflects the importance of small businesses in the national economic picture. The wider macroeconomic focus, and the concurrent ground-level interest in MSMEs, are reflected in the choice of research strategy and the structure of this report.

The remainder of the report proceeds as follows. After this short introductory chapter, Chapter 2 details the literature on the history of African integration, and the general content of the AfCFTA Agreement. Chapter 3 is dedicated to our study of MSMEs. In it, we rely on survey and stakeholder engagement across key sectors to elicit how the experience of past FTA – specifically the Economic Community of West African States (ECOWAS) Trade Liberalization Scheme (ETLS) – and the current COVID-related uncertainty have affected MSME operations. Section 3.1 will situate our project within the wider context of the Nigerian economy and provides a summary of the literature surrounding MSME uptake of FTAs. This is followed by a brief methodological section highlighting some of the key features of our fieldwork. Section 3.3 presents the results of our survey, highlighting the general sentiments and beliefs held by small business owners across the country.

Chapter 4 is aimed at addressing our second area of interest, which is the forecasted impact of the AfCFTA Agreement on the Nigerian economy at a more macroeconomic level. After an introductory section focusing on the theoretical underpinnings and justifications of our Computable General Equilibrium (CGE) model, the following sections provide the specifics of the data used and outline the results.

Finally, Chapter 5 seeks to highlight some of the results coming out of the previous two chapters, and draw some concluding inferences on the AfCFTA's forecasted impact in Nigeria. In so doing, some policy suggestions will be elucidated and justified with reference to experiences of other FTAs around the developed and developing worlds.

CHAPTER 2

African Integration in the Literature

2.1 AFRICAN INTEGRATION: HISTORY & ECONOMIC RATIONALE

From Pan-Africanism to AfCFTA: A brief history of modern African Integration

The notion of integration among African countries dates back to even before the formal independence of African states – that is, to the final years of the colonial era. Even as African anti-colonial leaders were actively advocating autonomy and independence for their nations, there was often vociferous recognition of the limitations single African states could face in the global economy once liberated from colonial oppression. Kwame Nkrumah and Leopold Senghor for instance, famously employed the term "Balkanisation" to express their fears of post-colonial Africa turning into a disjoint conglomerate of states too small to be relevant in global politics and economics (see Neuberger (1976) for a review of 'Balkanisation' in post-colonial African politics).

While the grander visions of pan-African political unity of Senghor and Nkrumah may have quickly dissipated in the frenzy of the early independence period, fears of neo-colonial economic dependence, as well as the shared bond and aspirations for development instilled by the common colonial past, kept continental economic integration – "the process of creating a unified market for goods, services, and production factors across the borders" (Ottaviano, 2016) – high on the agenda. As early as 1963, while many African countries were still struggling for independence, African leaders convened to establish the Organization of African Union (OAU) and the African Development Bank (AfDB), simultaneously recognising their shared economic interests and crystallising the territorial and political separation of the member states.

Rather than heading towards pan-continental integration, political trajectories in the following decades veered in the direction of a more fragmented approach, thus instigating the rise to prominence of RECs. The Lagos Plan of Action of 1980, considered by many a cornerstone of African integration, made little mention of pan-continental economic integration, if not as a distant aspiration, favouring instead increased coverage of distinct REC agreements (UNECA, 2013).

In the case of Nigeria, the desire for regional integration led to the establishment of ECOWAS in 1975. While great optimism on the potential of regional integration for national development motivated the Nigerian government's prominent role in the establishment of ECOWAS (see Olatunde, 1980), the union has had mixed results (Maku & Adelowokan, 2013). Despite being by far the largest member of the union, Nigeria's economy has struggled to attain the productivity required to make significant use of facilitated regional trade. These underwhelming results are compounded by the continued paucity of physical infrastructure, which has severely curtailed ECOWAS' potential to stimulate cross-border trade.

The emphasis on regionalisation at a continental level led to a complicated web of overlapping agreements, which were often deleterious to members' international trade prospects owing to the over-complication of regulatory frameworks (Murray-Evans, 2019). In general, despite strong emphasis on regional integration, intra-African trade has remained significantly lower than on other continents, underlining the "not impressive" (Hartzenberg, 2011:8) record of Africa's regional integration, and providing a justification for a unified pan-continental approach.

The Abuja Treaty of 1991, and the conversion of the OAU into the AU in 2000, eventually created the foundations for the current Africa-wide economic integration agenda embodied by the AfCFTA Agreement. In Abuja, the path towards continental integration was outlined in six steps, each intended to bring the existence of the AEC closer to fruition (Amadou, 2014).

The first step envisioned the creation of new RECs to complement the strengthening of those pre-dating the Abuja Treaty, as was the case for ECOWAS. The target was to promote normalisation of trade practices as well as internal regulations within regional communities: a building block to continental standardisation. The following steps entailed the strengthening of intra-regional integration; the establishment of free trade areas and customs union at a regional bloc level; the creation of a continental customs union and free trade area (the current stage); and finally, the completion of the AEC.

Empirical literature evaluating the progress of integration reveals a mixed picture with varying degrees of success. While some of the RECs have achieved significant outcomes in key areas of integration, others are yet to achieve the basic objectives of the Abuja Treaty. Moreover, the overlapping membership and, at times, contrasting mandates of RECs are such that there has often been a lack of clarity on policy direction. Consequently, some RECs have not been very effective as building blocks for the AEC (Amadou, 2014; Mlenga, 2012; UNECA, 2006).

The current developments corresponding to Stage Four of the Abuja process – the creation of the continental customs union – have, like the entirety of the process, progressed in steps. This gradual progress has culminated in the recent agreement on the AfCFTA. To this end, a significant development was the establishment of a tripartite FTA (TFTA) among the Common Market for Eastern and Southern Africa (COMESA), the Southern African Development Community (SADC), and the East African Community (EAC) in 2008, which began the continental unification process.

Following the establishment of the TFTA, the heads of state and government of African countries met at the AU in January 2012, and reached an agreement to establish the AfCFTA by 2017. However, the deadline of 2017 was not met. Nevertheless, given that 54 out of the 55 AU member states had signed as of July 2019, the operational phase of the AfCFTA was launched during the 12th Extraordinary Session of the Assembly of the AU in Niamey, Niger on 7 July 2019 marking the latest, and perhaps most significant, event in the decades-long project of African integration.

The Economics of Integration

The rationale for economic integration at a continental level is multi-faceted and fairly well established. A Free Trade Agreement, like the AfCFTA, promises a number of benefits for diverse players in the economy. For instance, from a consumer's point of view, continental integration is likely to increase access to a wider variety of products as well as fostering deflationary competition among continental producers.

Beyond forecasted consumer benefits, there is no doubt the most important considerations motivating the AfCFTA stem from a desire to promote continental economic production. In this light, the primary justification for seeking greater continental integration is to increase market size for African producers. While the majority of African markets are individually relatively small, the AfCFTA will establish a market of 1.2 billion people with a combined GDP of $2.5 trillion and joint consumer and business spending of more than $4 trillion (Fofack, 2018). This is envisioned to foster demand for African products via both trade creation and diversion, thus engendering the productivity revolution needed for African economies to integrate into the global economy and sustain long-term development. AfCFTA will further enhance international competitiveness by facilitating access to cheaper intermediate goods from across the continent, making African producers more efficient in relation to international competitors.

Furthermore, the increased market access could make previously-too-small African economies more attractive to international producers who might now seek to place higher value-added, longer-term, and more stable operations on the continent in order to tap into the large continental market, thus aiding the diversification process. The hypothesis of increased and more stable FDI is further strengthened by Stollinger et al (2018) who find that despite the ubiquity of international outsourcing of production, most value chains tend to concentrate within continental borders. Continental integration therefore increases Africa's attractiveness as a destination for entire value chains with the consequent transfer of jobs, skills, and technology.

Finally, the AfCFTA is also considered a promising avenue to follow in addressing Africa's long-recognised issue relating to poor diversification. African countries predominantly export low-value products to the rest of the world (average 15 percent value-added) but tend to export higher value-added goods to one another (40 percent)[1]. By reducing friction amongst themselves, thus implicitly discriminating against outside competition, higher value-added producers on the continent are likely to receive a boost in demand. This would facilitate the expansion of the currently undersized manufacturing sector, helping to diversify economies that remain largely geared towards their primary sector.

The optimism surrounding the African economic integration approach, while often justified, must however not disguise the very real challenges that do exist. For starters, the Africa Regional Integration Index (2019) highlights how the continent remains particularly "poorly integrated in the infrastructural dimension." African transport costs remain a key barrier to intra-continental trade and will require substantive investment to be addressed. Moreover, the vast differences between African economies themselves place some countries in a better position to take advantage of continental integration and consequent competition for consumers than others. Countries with underdeveloped industrial sectors in relation to continental partners, or with higher labour and transport costs, may see some of their productive sectors not only fail to develop export capacity, but also struggle to maintain domestic markets (Akeyewale, 2018).

Underscoring the possibility of adverse impacts of the AfCFTA on some economic actors, prior to the signing of the Agreement by the Nigerian government, there were heated national debates surrounding harmful effects the Agreement could have on specific sectors such as manufacturing. These debates led to initial hesitance in signing the Agreement. After the signing, final ratification has been subjected to wider, multi-stakeholder debate to uncover its potential effect on various sectors and policy options to mitigate negative impacts. Nigeria ratified the AfCFTA on 11 November 2020.

Ultimately, the long-term benefits of integration depend on the balancing of trade creation and trade diversion (see Aremu, 2004 for clear explanation of concepts). Under the AfCFTA, part of the provisions include tariff concessions for trading activities among member countries, which are not accessible to non-members. These preferences are based on the concept of trade creation, which anticipates that the elimination of trade barriers would lead to a reduction in production costs and, in the long run, greater efficiencies from investing in research and development to enhance the quality of goods andservices distributed, ultimately inducing greater volumes of trade among African states. The provisions of the AfCFTA also go beyond just tariff concessions, and include other trade competition

[1] https://www.cnbcafrica.com/article/2019/07/12/afcfta-understanding-the-rules-of-origin/

policies in order to drive costs down. The objective behind trade creation is to positively influence improved economic growth and general welfare for AfCFTA members.

Where trade creation occurs among African countries, the effect would usually mean the redirection or substitution of trade previously concluded with non-member countries (which might initially be cheaper and better quality) to AfCFTA members. This is referred to as trade diversion. Since trade diversion occurs alongside trade creation, there are several related risks, including reduced access to global markets, non-member countries choosing to retaliate and impose discriminatory sanctions on AfCFTA members, consumption of lower quality products and services, and loss of tariff related revenues for AfCFTA members from non-members who refuse to trade with them. The attractiveness or success of the AfCFTA is therefore dependent on recording a positive net effect, such that the impact of trade creation outweighs trade diversion.

Now that Nigeria has signed the AfCFTA, with ratification and domestication of the various protocols, the next line of action is to map out strategies on how the country can benefit maximally from the deal. Having established the likely presence of both winners and losers, a well-defined and evidence-based knowledge-generating process about the specific impact of AfCFTA on Nigeria's private sector firms becomes vital, especially for MSMEs. Understanding the specific impact and the potential challenges and needs of MSMEs as agents for socio-economic transformation for the country is required so that they can be adequately addressed in the negotiation and dialogue process of the AfCFTA going forward.

2.2 INSIDE THE DEAL: THE AFCFTA IN BRIEF

The signing of the AfCFTA Agreement represents a landmark moment not just in the history African integration, but more generally, in international relations and South-South cooperation: no FTA in the world encompasses as many countries as the AfCFTA (World Bank, 2020). The reaching of an agreement between so many countries with such diverse interests is a remarkable achievement, all the more so given that the AfCFTA will be the broadest and deepest trade agreement into which most African countries have entered. While the integration will progress in two phases and thus will not be immediate, the number of topics intended to be covered in the final text goes far beyond even the most expansive of the current RECs. The rest of this section briefly summarises the key components of the Agreement.

Phase I of negotiations focused on three main areas: Goods, Services, and the Dispute Settlement Mechanism (DSM). These areas represent the building blocks for most FTAs and provide the agreement for the shallower form of integration necessary for deeper agreement in the still ongoing Phase II of the negotiations. That said, the AfCFTA breaks with past regional trade agreements in Africa in that it seeks to foster greater standardisation and integration than before, even in areas that were covered by previous regional treaties.

The main objective of AfCFTA in relation to trade in goods is the progressive elimination of tariff and nontariff barriers to trade. In this regard, the highlight protocol of the Agreement is the requirement for signatories to remove tariffs on 97 percent of tariff lines. It must be noted however that, as the World Bank (2020) points out, 74 percent of imports in the average African country are covered by just 1 percent of tariff lines, which might slow the pace of liberalisation in some sensitive sectors, despite broad commitment to tariff-removal. Beyond tariff measures, the Agreement also stipulates the parties' willingness to cooperate on issues of customs standardisation and efficiency, Technical Barriers to Trade (TBTs), Sanitary and Phytosanitary (SPS) measures, as well as the promotion of diversification of continental economies – all of which are currently significant nontariff barriers to intra-African trade.

A fundamental area in the Agreement on goods that is yet to be clarified is the stringency of Rules of Origin (RoO) requirements. RoOs define the level of transformation (usually in terms of value addition) a good must undergo in a signatory country in order to qualify for preferential treatment in accordance with AfCFTA. In negotiating, Nigeria has adopted a decisive stance in favour of tighter RoOs to limit the possibility for extra-regional products to enter the African market and unfairly compete with local producers by taking advantage of AfCFTA preferences. However, it is also important to note that excessively demanding requirements may increase the bureaucratic costs of compliance, thus putting off many small and medium businesses from seeking to expand their businesses using the provisions of AfCFTA. The final agreement on RoOs will be a crucial component for MSMEs across the continent and for Nigerian ones in particular.

The negotiation on services concurrently to that on goods is a novelty in African trade pacts, and highlights the paradigm shift in favour of deeper integration (Simo, 2020). In Phase I of the negotiations, member states have agreed on five priority services – financial services, communication, transport, tourism, and business services. Ultimately, the principal aims as stated in the Agreement are the enhancement of service competitiveness, the progressive liberalisation of services, and a commitment to fostering sustainable development through greater investment and focus on continental value chains (World Bank, 2020).

Similarly to the World Trade Organization's (WTO) DSM, the AfCFTA Agreement does not provide natural persons and corporate entities the right to recourse. The protocols of the Agreement establish instead a state-to-state DSM, meaning that only member states can bring claims to the AfCFTA DSM and that retaliations can only be enacted by and upon national entities. The impossibility of private recourse using the AfCFTA's DSM makes Phase II of the Agreement particularly important.

Phase II of the negotiations began in February of 2019 and encompass principally the areas of competition policy, intellectual property rights, and investments that have never been agreed upon at a continental level. While the outcomes of these negotiations are yet to emerge, the mere inclusion of such topics exemplifies the strong level of commitment to deeper integration at a continental level. The discussions surrounding these further chapters of the Agreement will require important decisions regarding the general direction of African integration, as well as how AfCFTA provisions will relate to the web of REC arrangements that exist at a sub-continental level (Signe & van der Ven, 2019). In this regard, Article 19(1) of the AfCFTA Agreement specifies that, unless otherwise stated, AfCFTA protocols will supersede regional agreements, while Article 19(2) makes reference to the continuation of "higher levels of regional integration" opening the door to the possibility of intra-African discrimination (World Bank, 2020). How these agreements will be implemented will be an important part of Phase II negotiations and is likely to have a large impact on the wider effects of the AfCFTA Agreement on MSMEs across the continent.

Table 1: *Comparison of ECOWAS and AfCFTA Coverage*

	ECOWAS	AfCFTA
Tariffs on Manufactured Goods	✓	✓
Tariffs on Agricultural Goods	✓	✓
Export Taxes	—	✓
Customs	✓	✓
Competition Policy	—	✓
State Aid	—	—
Antidumping	✓	✓
Countervailing Measures	—	✓
State Trading Enterprises	—	✓
Technical Barriers to Trade	—	✓
Trade in Service	✓	✓
SPS measures	—	✓
Movement of Capital	✓	✓
Public Procurement	—	—
Intellectual Property Rights	—	✓

	ECOWAS	AfCFTA
Investment	—	✓
Environmental Laws	✓	—
Labour Market Regulations	—	—

Source: *Based on Hofmann, Osnago & Ruta (2017), adapted from World Bank (2020)*

Between Phase I and Phase II issues, the AfCFTA will provide a regulatory framework that goes well beyond anything Nigeria has agreed upon before at a regional level. To emphasise this, Table 1 lists the eighteen most common topics covered in FTAs globally, and contrasts how many were included in ECOWAS treaties in comparison to those to be included in the AfCFTA. The difference is striking and points to the need for more knowledge generation around the impact of the unprecedented level of integration on various economic players, and particularly MSMEs, who may lack the internal technical knowledge to implement the provisions of the Agreement.

CHAPTER 3

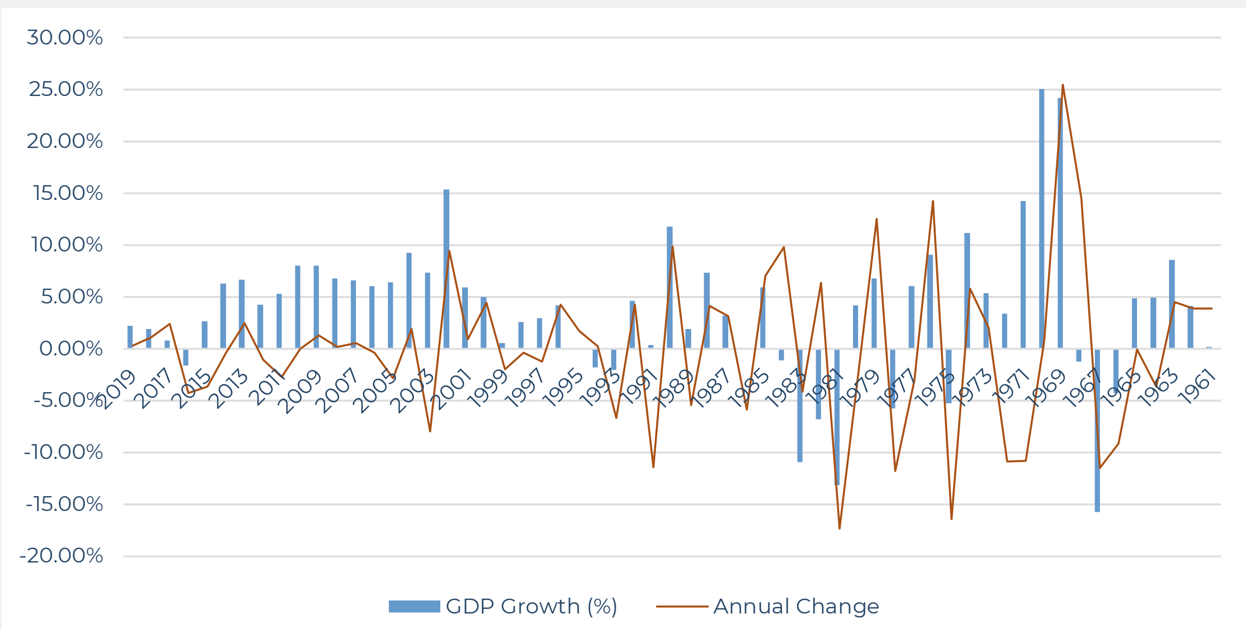
Surveying MSMEs

3.1 BACKGROUND

3.1.1 A Brief on the Nigerian Economy

Based on average national income, the Nigerian economy is classified under the lower middle-income category, and ranked as the twenty-sixth largest economy in the world by total GDP (World Bank, 2020). It is the most prominent economy on the African continent, contributing about 19 percent to the region's total production in 2019. Although the annual economic growth rate has fluctuated since independence in 1960, Figure 1 shows that there has been some level of stability in recent years. While it is still early, and definite long-term effects remain unclear, the current global COVID-19 pandemic poses a grave threat to these trends, and represents an important unknown variable in Nigerian's economic future.

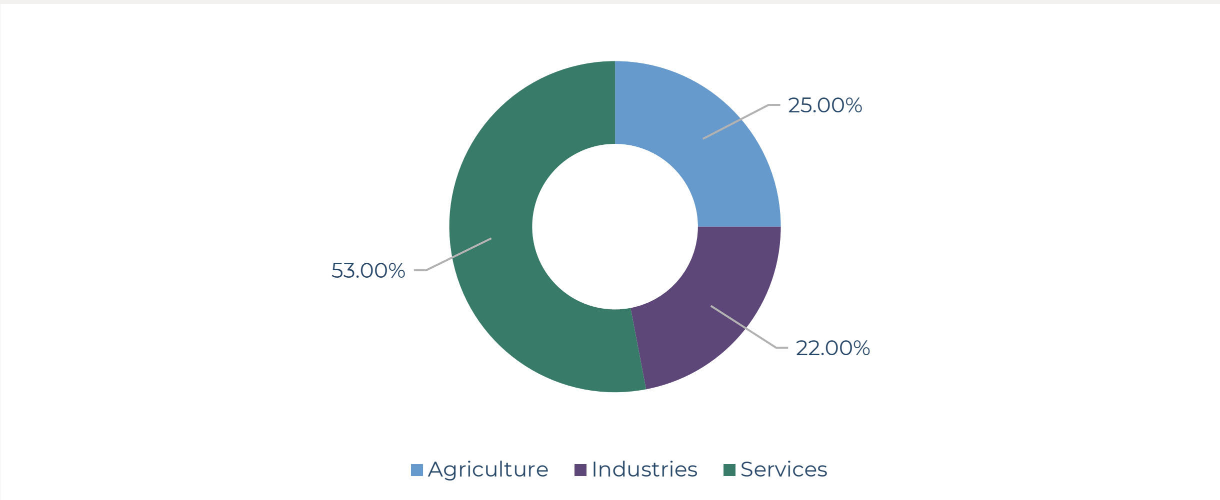
Figure 1: *Annual GDP growth rate from 1961 to 2019*



Source: *World Bank I Macrotrends (2020)*

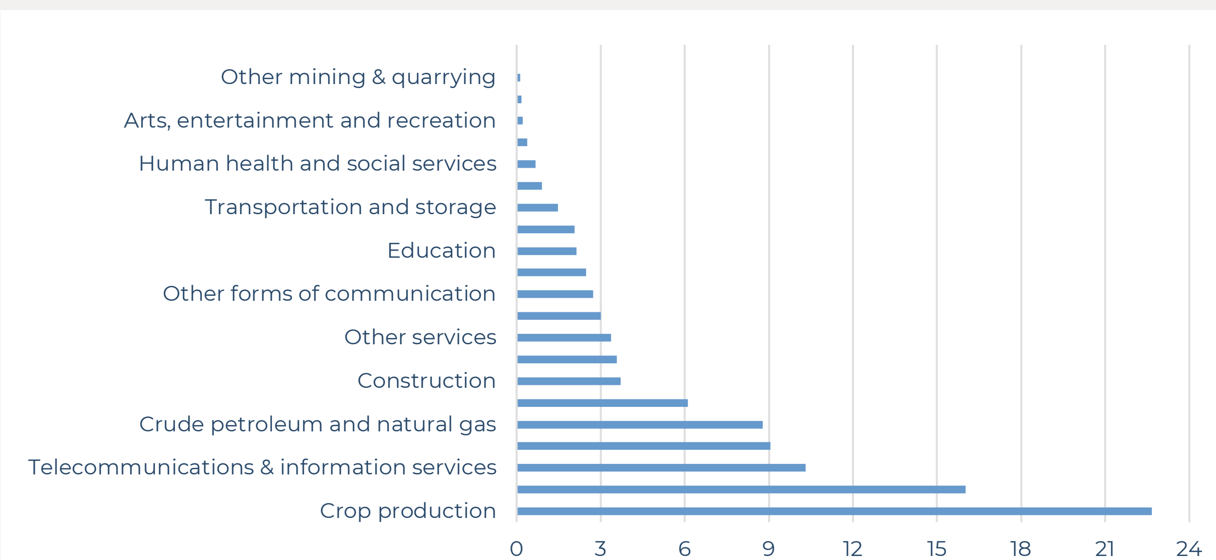
The services sector is currently the biggest segment of national output as highlighted in Figures 2 and 3, and comprises industries like telecommunications, wholesale and retail trade, real estate, and financial institutions, among others. Agriculture, especially crop production, has a significant share of the economy as well, although this is done mostly at subsistence level. Industries as a whole (such as manufacturing and mining) make up a smaller fraction of the economy.

Figure 2: *Sector contribution to annual GDP (2019)*



Source: *National Bureau of Statistics*

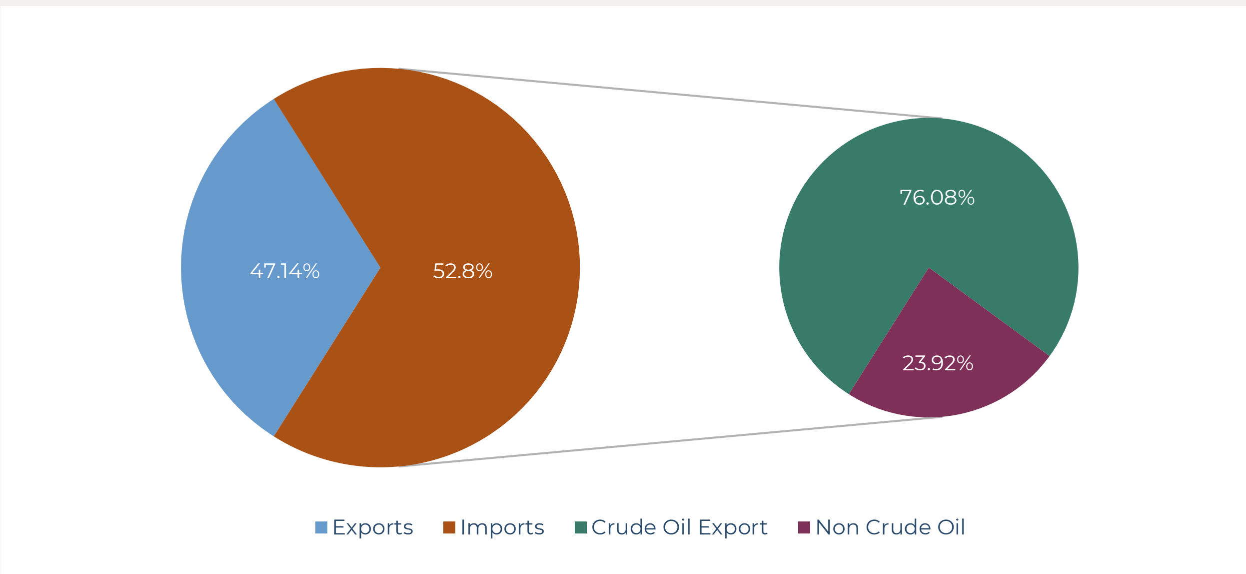
Figure 3: *Annual GDP % distribution per sub-sector (2019)*



Source: *National Bureau of Statistics*

Nonetheless, the economy remains strongly unidirectional due to over dependence on revenues from crude oil. Although crude oil and natural gas make up only 9 percent of the country's GDP (see Figure 3), this sub-sector continues to form the bulk of government revenue and total export earnings, a trend that has remained constant for several decades. This has made the economy susceptible to fluctuations in global prices, often resulting in trade deficits, especially during periods of global oil price shocks (Figure 4).

Figure 4: *Trade Composition Overview Q4, 2019*



The ripple effects of over-reliance on oil revenues have been enormous, particularly the negative impact on exchange rate and inflation. Other sectors of the economy have been neglected over time, leading to poor non-oil export results, attributable to the inability of domestic firms to scale-up and increase capacity in terms of efficiency, product quality, and quantity (Nwokoye, et al., 2019). Despite recording notable strides in improving the nation’s rankings on the global Ease of Doing Business index, Nigeria still ranks 131 out of 190 countries, implying an unconducive business environment, in sharp contrast to other African countries like Mauritius, Rwanda, and Kenya that have rankings similar to developed economies. Consequently, imports generally tend to be cheaper in Nigeria than locally produced goods and services, thereby increasing deindustrialization of the economy and failure of MSMEs, which in turn affects other areas of the economy, worsening unemployment and poverty rates.

Currently, Nigeria's top trading partners are non-African countries (NBS, 2020). More than half of the country's imports come in from Asia, followed by Europe. Examples of import items include machinery, manufactured goods, mineral fuels, food and beverages, among others. Export partners are mainly Europe and India, and some African countries like Ghana and South Africa.

In terms of the split between the formal and informal sectors the economy, approximately 59 percent of economic activities are linked to the informal sector, although measuring the real value of this sector can be challenging since most of the associated activities are not fully regulated (NBS, 2016). The government acknowledges the importance and growth potential of this sector, however there is insufficient information on the dynamics of the informal economy, making it difficult to initiate and implement economic policies to address their needs. To this end, the underlying objective of the existing national economic growth strategy is to diversify the economy, stimulate business expansion, include the informal sector into the formal ecosystem and increase non-oil exports (MBNP, 2017). These goals are expected to also form part of the subsequent long-term economic plan, which is due in 2021.

3.1.2 Overview of MSMEs in Nigeria & their Contribution to the Economy

The benchmark for defining MSMEs varies from country to country, mostly depending on the size of an economy (Okuma *et al.*, 2019). This implies that a business enterprise could be categorised as large in one country, whereas it may be considered small in another. In Nigeria, the basis for classification includes number of employees, asset base, and turnover as shown in Table 2.

Table 2: *Classification of MSMEs in Nigeria*

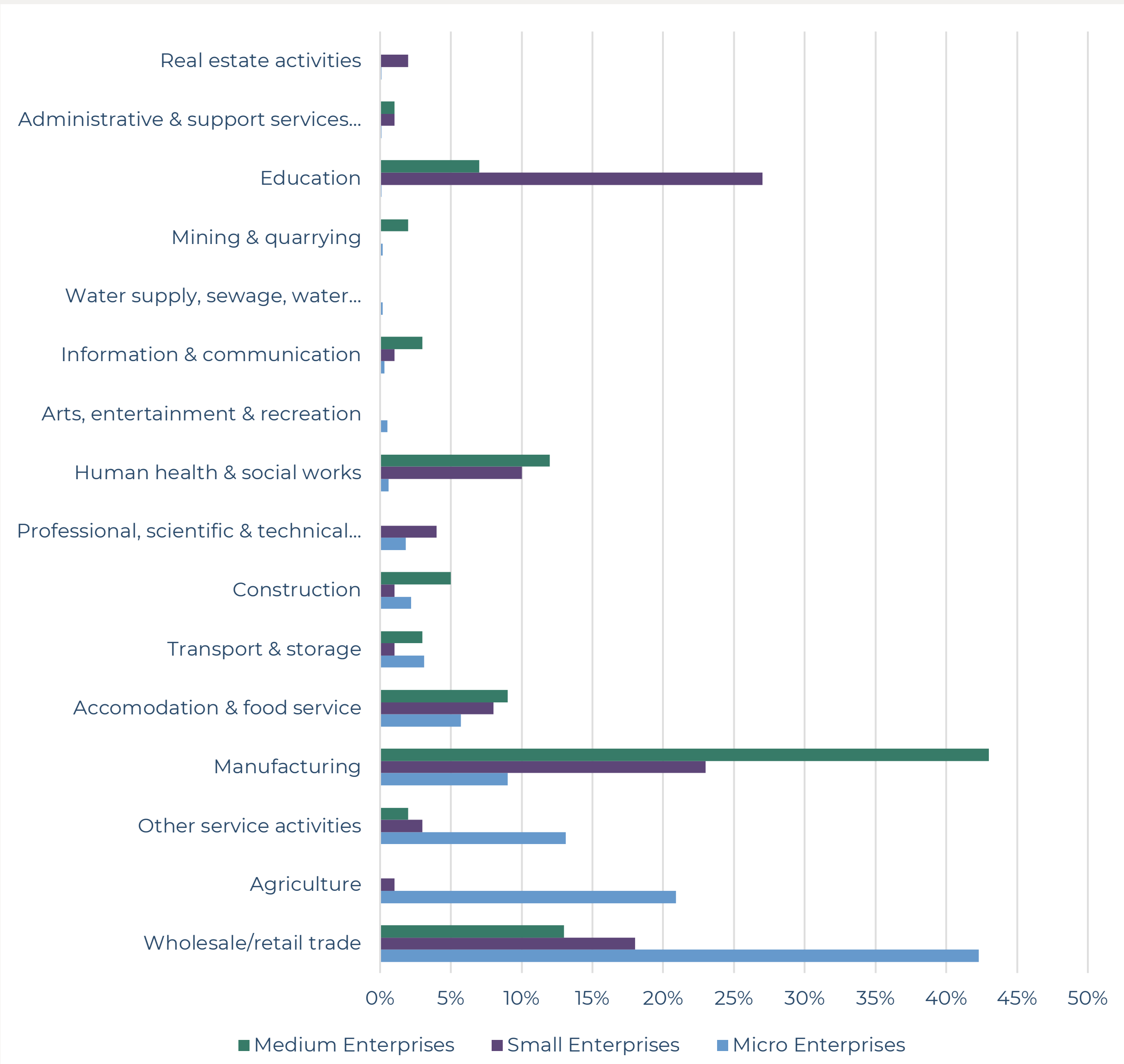
S/N	Type of enterprise	Staff strength	Asset base (N mil) (excluding land/buildings)	Annual revenue* (N mil)
1	Micro	≤ 10	≤ 5	≤ 20
2	Small	>11 ≤ 50	> 5 ≤ 50 (cap here is 100 for bank of industry)	≤ 100
3	Medium	> 50 ≤ 200	> 50 ≤ 500	≤ 100

Source: *National Policy on MSMEs I Bank of Industry (BOI)*

** Revenue is only included in the benchmark provided by BOI.*

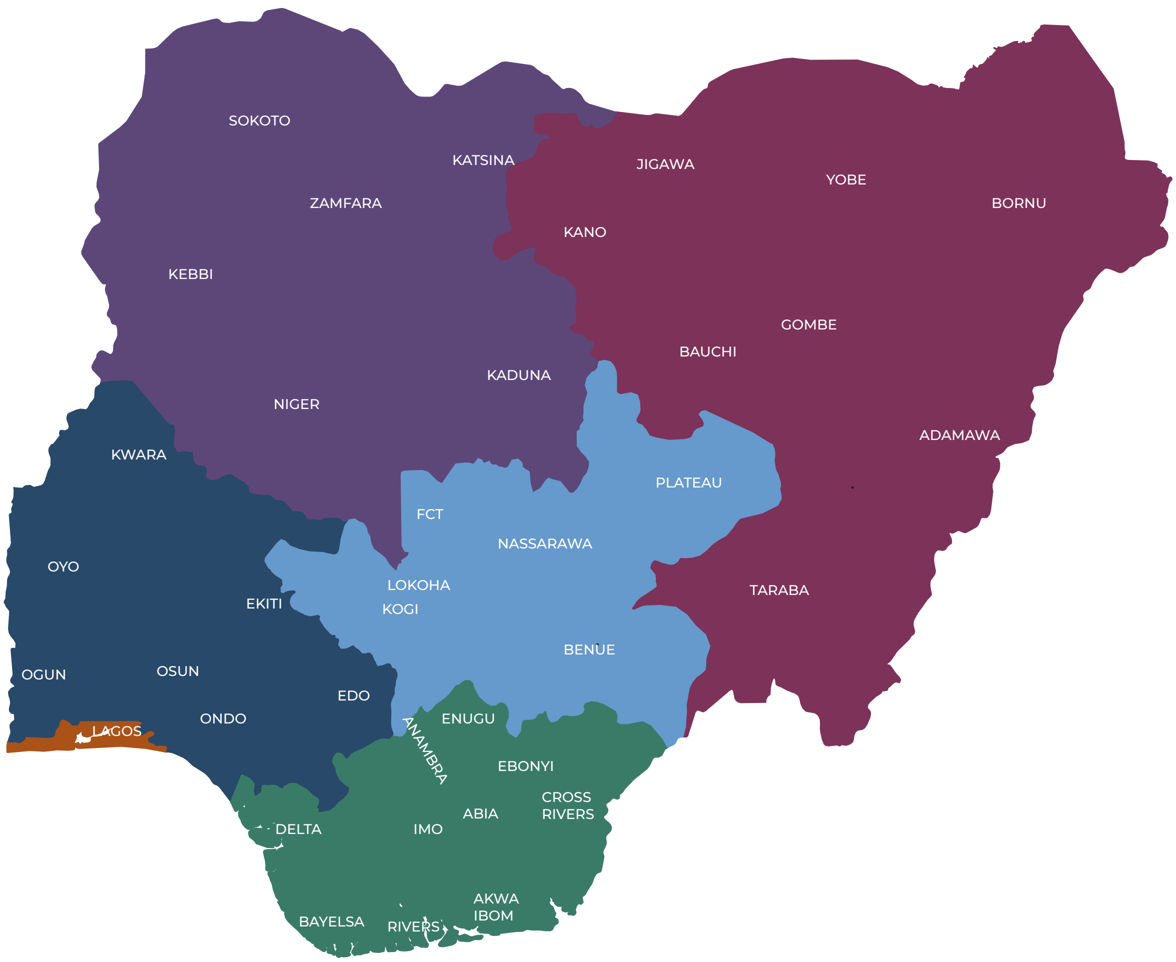
In Nigeria, most MSME business activities occur in the informal sector, and operational mechanisms for such enterprises differ significantly from the formal sector. These businesses often require less capital, minimal technical skills or expertise, utilise local resources, create jobs at relatively low cost by pooling together unskilled and semi-skilled workers, and improve market linkages especially in geographically remote locations. They operate in diverse sectors of the economy across the nation and provide a platform for generating income for poor households. Figures 5 and 6 highlight the sectorial and geographical spread of MSMEs in the country.

Figure 5: *Sectorial Distribution*



Source: *(NBS & SMEDAN, 2019)*

Figure 6: *SME clusters by geographical location*



Source: *(Oyeyinka, 2020)*

According to an NBS, 2019 survey, there are approximately 41.5 million MSMEs in Nigeria, with 99 percent operating at the micro level and largely as sole proprietors. The survey further highlights the importance of MSMEs in Nigeria in terms of employment potential, contribution to GDP, and export capacity, among other factors.

Table 3: *MSME Statistical Summary*

S/N	Statistical parameter	Summary
1	Total number of MSMEs	41,543,028
2	Contribution to employment	76.5 percent of total workforce (or 59,647,954 persons)
3	Contribution to GDP	49.78 percent
4	Contribution to exports	7.64 percent
5	Number of micro enterprises	41, 469,947
6	Number of small enterprises	71,288
7	Number of medium enterprises	1,793

Source: *NBS, 2019*

MSMEs have proven to play a huge role in stimulating the growth and development of many economies around the world (AfDB, 2012). The Nigerian government recognises the importance of this sector in achieving greater diversification, industrialization, and a more inclusive growth pattern for the country. Therefore, in a bid to better coordinate, monitor, and promote the government's MSME initiatives, the Small and Medium Enterprises Development Agency of Nigeria was established in 2004 to collaborate with other relevant stakeholders to strengthen the MSME sector and ensure MSMEs become a viable avenue for national economic development.

Despite the above progress, Nigerian MSMEs are yet to achieve their full potential. For example, MSMEs account for 40 to 60 percent of exports in China, in contrast with the mere 7.6 percent export contribution in Nigeria, and even less for manufactured exports (Oyeyinka, 2020). This underperformance is due to numerous and diverse challenges such as: macroeconomic policy inconsistencies; infrastructure deficit; poor power supply; inadequate technology; lack of access to credit facilities and inadequate financial literacy; weak competitive landscape; multiple taxation; poor linkage between policy actions and sectoral performance; deficient transport system; bureaucracy in obtaining licenses and permits; high prices and inflation, and more (Augusto et al, 2018; NBS & SMEDAN, 2019).

As a result of these challenges, MSMEs in Nigeria often become extinct or stagnant, and are scarcely able to scale up and sustainably transition to large enterprises (Fate Foundation, 2020). It is therefore imperative that the peculiarities of the informal economy and challenging business environment are urgently addressed to enable MSMEs to benefit from the planned regional integration in order to achieve full potential for national economic growth.

3.1.3 AfCFTA and Nigerian MSMEs: What We Know

It is no overstatement to say MSMEs are the lifeblood of the Nigerian economy. MSMEs constitute about 96 percent of all Nigerian businesses and contribute 75 percent of national employment (SMEDAN, 2019). Any shift in the national economic policy paradigm must therefore be evaluated in terms of its impact on MSMEs for the analysis to truly reflect the impact on Nigerian society.

Studies on the impact on various players of FTAs around the globe are abundant. For instance, FTAs have been noted to affect input prices, industrial outputs, competitiveness and firm productivity, among other things. The effects are typically heterogeneous across sector and industry, so costs and benefits of AfCFTA will play out differently across sectors. This uncertainty underscores how not much is yet known about the likely impacts of AfCFTA on Nigerian MSMEs, whose growth and competitiveness are hampered by a variety of internal and external factors.

In this regard, a historical perspective on the effect of national policymaking on MSME performance displays a mixed bag of results, as government and Central Bank policies have not always aided MSMEs.

One of the key challenges accounting for production gaps of Nigerian MSMEs is financing. Nigeria's lending rate is high (at about 17 percent) compared to other African countries due to a shortage of liquidity in the financial sector (Deloitte, 2018). This shortage is partly a result of the interventions of the Central Bank of Nigeria (CBN) in the currency market in order to stabilise the exchange rate. This results in high rates, which hamper long-term business prospects in the non-oil sector as MSMEs are discouraged from borrowing to grow their businesses.

Another key challenge for MSMEs is the infrastructure deficit that inevitably raises the cost of operation or production and hampers their competitiveness. The current infrastructure base in Nigeria is grossly inadequate in terms of capacity and quality and does not seem capable of catering to the anticipated industrial development. Despite government investments, Nigeria still has huge infrastructure deficits, particularly with regards to power generation, transportation, and potable water. For instance, the current power generation capacity is about 3000 Megawatts, which is just around 30 percent of the estimated national demand. To reap the benefits of trade, a key challenge for government and the private sector is to build a modern, efficient, and effective infrastructure network.

Access to production resources – such as physical space, public infrastructure, and information (a pivotal focus of this project) – is also a critical challenge to many Nigerian MSMEs. An example is provided by the agriculture sector, which holds tremendous opportunities for wealth creation in Nigeria. Despite its potential, the sector is faced by vast gaps in access to information, inadequate financing, and post-harvest losses that pose critical barriers for agricultural MSMEs. These barriers make many agricultural MSMEs less productive relative to comparable African countries. Accordingly, the Food & Agriculture Organisation (FAO) reports the yield on a staple like cereal is 1,444 kg per hectare in Nigeria, compared to 3,810 kg in South Africa and even 7,114 kg in Egypt.

Other challenges for MSMEs include fiscal and monetary policies related to trade and exchange rate; the complex, opaque, and over-bureaucratised regulatory and legal framework; and overall macroeconomic climate.

All of these challenges, some of which are direct results of a history of sub-optimal national policymaking from the point of view of MSMEs, constitute potential impediments to MSME growth and the socioeconomic benefits AfCFTA could bring to Nigeria.

That is not to say that the AfCFTA will follow the negative path of previous government policies and, in fact, there is a significant divide among scholars on the impact that economic integration has had, and will have, in Nigeria. While some opine that Nigeria, and its MSMEs, stand to benefit from trade liberalisation and economic integration, others point to some underwhelming effects of previous attempts at integration.

Looking at the impact of regional integration via ECOWAS on MSMEs in Nigeria for example, Faloye and Abasilim (2018) find that trade liberalisation is vital for the survival and innovative performance of Nigerian MSMEs. Oppositely, there is strong evidence that the majority of MSMEs, particularly those operating informally (who represent a significant share of intra-ECOWAS trade) lacked awareness of ECOWAS and its Economic Trade Liberalisation Scheme (ETLS) aiming to foster regional trade, pointing to the centrality of information dissemination for the full benefits of trade deals to be reaped (Karaki & Verhaeghe, 2017).

Turning to the forecasted effects of the AfCFTA Agreement, some existing studies suggest that the potential benefits of the Agreement are significant for several reasons. One, the target market for the AfCFTA is projected to rise from an estimated 1.27 billion to 1.7 billion by 2030, out of which about 600 million will be in the middle class (Bramdeo, 2018). Two, in terms of aggregate gross domestic product (GDP), this will range from $2.1 trillion to $3.4 trillion or $6.7 trillion at Purchasing Power Parity terms. Three, in terms of investments and consumer spending, the AfCFTA is expected to attract an estimated $4 trillion (Azikiwe, 2018).

For Nigerian MSMEs, some analysts suggest the category could stand to benefit from a number of opportunities AfCFTA could afford them. For instance, manufacturers should gain access to increased sources of cheaper and higher quality raw materials from the African continent. This will facilitate the production of cheaper and higher value products which in turn will gain access to a larger continental market. From a gender perspective, "AfCFTA will position women in such a way that they get to understand that trade is a force which, when properly harnessed, can help lift millions of professional and business women out of poverty and bring shared prosperity to them" (Chief (Mrs) Anita Nana Okuribido, National Coordinator, Association of Nigerian Women Business Network).

There are, however, some risks evident as well. For example, while the AfCFTA Agreement may prove beneficial for the already-dominant (in the West African context) Nigerian financial services sector by increasing its market share, Nigerian MSMEs may face an uncompetitive pressure on the currency from the increased demand, thus lowering their ability to export and increasing imports of cheaper continental products. This risk, coupled with the already challenging environment in which MSMEs operate in Nigeria detailed above, led various interest groups to argue that AfCFTA will have a harmful effect on specific sectors such as manufacturing. These debates led to initial hesitance in signing the Agreement.

3.2 SURVEY METHODOLOGY & DATA COLLECTION

The data collection procedure for this study focused on four key sectors within the Nigerian economy: wholesale and retail trade, the agricultural and food processing sector, the manufacturing sector, and the services sector. These sectors were selected given their high business potential and contributions to GDP, employment, and exports. The vast majority of MSMEs can also be categorized as operating within these four sectors. This section discusses the strategy used in data collection and analysis. It covers the research design, the systematic data management approach, and the validation and reliability of the survey instrument.

Key Research Questions

In providing empirical responses to questions concerning potential effects of the AfCFTA, the aim of the survey was to address the following key research questions:

1. What is the perception and level of awareness about the AfCFTA by firms?
2. What is the competitive capacity of MSMEs and their capacity to meet the AfCFTA process requirement?
3. What are the current international business operations of the firm?
4. What are the effects of the COVID-19 pandemic on the business activities of MSMEs?

Research Design and Sources of Data

In eliciting responses from firms (otherwise called enterprises), this study used a validated questionnaire as the primary survey instrument. Questions were structured to provide responses to the study's research questions and meet study objectives. In sampling firms, determinations on size were made via a rigorous sampling technique method based on the definition shown in Table 4, in accordance with standardized MSME definitions prevalent in Nigeria.

Table 4: *Definition of Enterprises*

S/N	Size Category	Employment	Assets (=₦= Million)
1	Micro	Less than 10	Less than 5
2	Small	10 to 49	5 to less than 50
3	Medium	50 to 199	50 to less than 500

Source: *(NBS, 2013)*

In line with the above definition of enterprises and their sizes, the sampling of Small and Medium enterprises was greatly informed by the selection of recorded extracts from feedback engagement with Business Membership Organizations (BMOs). Engaged BMOs include:

1. The Organized Private Sector of Nigeria (OPSN) – comprised of the Nigerian Association of Chambers of Commerce, Industry, Mines, and Agriculture (NACCIMA);
2. Nigeria Association of Small-Scale Industrialists (NASSI);
3. Manufacturers Association of Nigeria (MAN);
4. Nigerian Association of Small and Medium Enterprises (NASME);
5. Nigeria Employers Consultative Association (NECA);
6. Federation of Agricultural Commodity Association of Nigeria (FACAN); and
7. National Association of Nigerian Traders (NANTS).

Data collection personnel (otherwise known as enumerators) were trained specifically to administer the questionnaires in English in addition to the local languages (Igbo, Yoruba, and Hausa), in line with best data-collection practices in multi-ethnic contexts. Data was collected using smart phone technology, although enumerators were also provided with questionnaires in hardcopy. The softcopy was digitized and hosted by the SurveyCTO App. Several quality control measures were installed to allow quality data collection, including the coding of GPS locations and feedback reporting systems. The data collection process was monitored and closely supervised by personnel from the Centre for the Study of the Economies of Africa (CSEA).

Sampling of Enterprises Across States

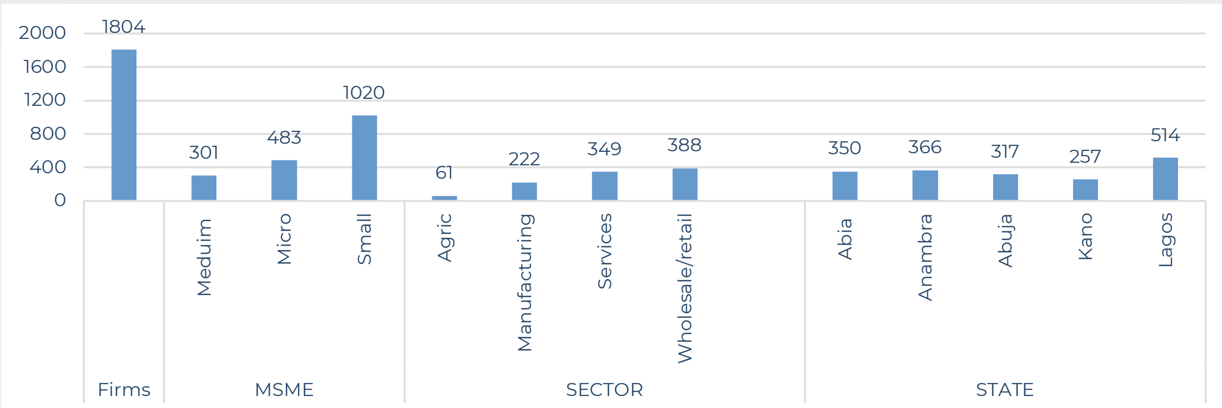
This study employed a multi-stage sampling procedure. In the first stage, Abia State, Anambra State, Kano State, Lagos State, and Abuja (FCT) were strategically selected because of the high presence of MSMEs and national representativeness. These five states are acknowledged as business hubs and cut across Nigeria's heterogeneous geopolitical zones with Kano representing the North, Abia and Anambra states the East, Lagos the West, and FCT covering the Central region of the country.

In the second stage, a proportionate sampling technique was used to determine the number of MSMEs to be sampled in each state. This is based on the sectoral MSME contribution to GDP, export, and employment as reflected in the National Survey of MSMEs by the National Bureau of Statistics (NBS, 2019). Thereafter, in the final stage, simple random sampling was used to select MSMEs for interview through the sectoral MSMEs register.

Out of the 19 standardized economic sectors modelled by NBS (2013), this study subdivided sectors into four core sectors – Agriculture, Manufacturing, Services, and Wholesale/Retail. In all, over 1,800 MSMEs were surveyed across the five states – Figure 7 shows the distribution of firms sampled in the study across sectors and business categories.

Across states, the scope of the study is set on samples of 61 Agricultural firms, 222 Manufacturing firms, 349 Services, and 388 Wholesale/Retail firms, which were distributed over 1,020 small, 483 micro, and 301 medium enterprises to capture the competitiveness of firms across sectors and business categories. A comprehensive selection matrix randomly allocated 350 firms in Abia, 366 firms in Anambra, 317 firms in FCT (Abuja), 257 firms in Kano, and 514 firms in Lagos being the commercial capital of Nigeria. Tables A-E in Appendix I shows the distribution of the sampled population across states.

Figure 7: *Distribution of Sampled Firms (by Sector and Size)*



The Research Instrument

The main research instrument for this study is a questionnaire. The six-sectioned questionnaires were administered in a softcopy format facilitated by the SurveyCTO App to ensure plausible quality data checks. Each of the sections were designed to focus on providing responses to the key research questions. A breakdown of the main features of the questionnaire is displayed in Table 5.

Table 5: *Main Features of Survey Questionnaire*

S/N	Section	Research Question	Remark
1.	A: International Business Operations	What are the current international business operations of the firm?	Captures firms' current disposition in business operations involving international activities
2.	B: Export and Import Operations	What are the current international business operations of the firm?	Capture firms market scope and experiences of FTA
3.	C: Awareness and Perception of the AfCFTA	What is the perception and level of awareness about the AfCFTA by firms?	Highlights the firm's perception and awareness level about prominent features of the AfCFTA
4.	D: Gauging MSMEs Competitive Capacity and Capacity to meet Process Requirements of the AfCFTA	What is the competitive capacity of MSMEs and capacity to meet the AfCFTA process requirement?	Gauges the potentials of firms to compete and meet AfCFTA policy requirements
5.	E. Effects of COVID-19 on MSMEs	What are the effects of COVID-19 pandemic situation on MSME business activities?	Understanding the impact of the COVID-19 pandemic on MSMEs business activities
6.	F: Demographic Activities	Nature of business activities MSMEs are involved in	

A Note on Validity and Reliability of Research Instrument

The final version of the survey underwent a series of reviews by experts from the Centre for the Study of the Economies of Africa (CSEA), the Center for International Private Enterprise (CIPE), and several BMOs. Information upon which questions were structured was garnered from the National Bureau of Statistics (NBS) and other national and international data sources. Additionally, a pilot study survey was carried out in Abuja beforehand to test the appropriateness of questions to the context of interest. Feedback from the pilot informed the restructuring of questions to meet study targets.

Focus Group Discussion

To strengthen the reliability of our results, and to enrich and triangulate findings from the field survey, structured interviews with key informants were conducted. The focus group discussions were held in three different sessions with participants grouped into the manufacturing, agricultural, and services sectors. The expert panel that participated in the opinion poll included BMO leaders such as Nigerian Association of Chambers of Commerce, Industry, Mines, and Agriculture (NACCIMA), Nigeria Association of Small Scale Industrialists (NASSI), Manufacturers Association of Nigeria (MAN), Nigerian Association of Small and Medium Enterprises (NASME), Nigeria Employers Consultative Association (NECA), Federation of Agricultural Commodity Association of Nigeria (FACAN), and National Association of Nigerian Traders (NANTS). Additionally, a telephone interview was conducted to elicit the perceptions of business leaders regarding the AfCFTA.

Selected extracts from these conversations emerge in the results section below.

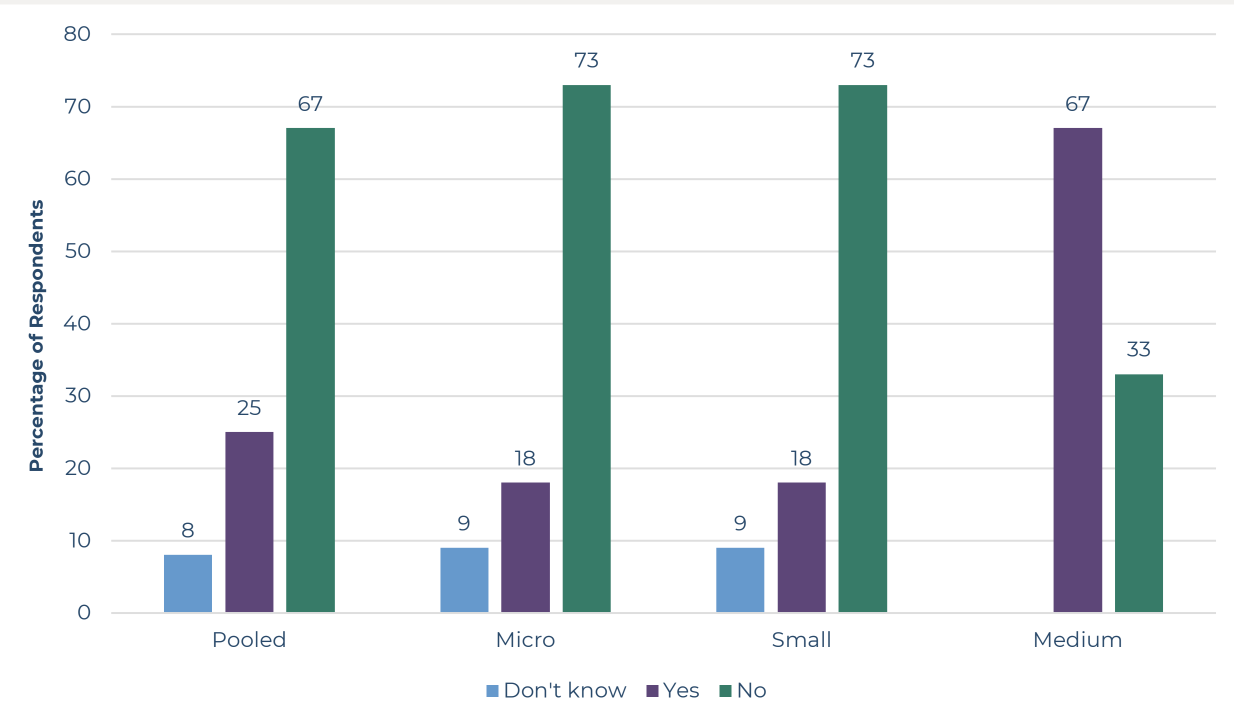
3.3 SURVEY RESULTS: MSME PERCEPTIONS OF AFCFTA

3.3.1 Knowledge of AfCFTA

It is clear that awareness is essential in both preparing for the potential threats and maximising the potential benefits of the AfCFTA for Nigerian MSMEs. In order to ascertain the level of awareness of MSMEs in Nigeria, the following question was posed – *"Are you aware of the African Continental Free Trade Area (AfCFTA) Agreement which Nigeria signed on July 7, 2019?"*

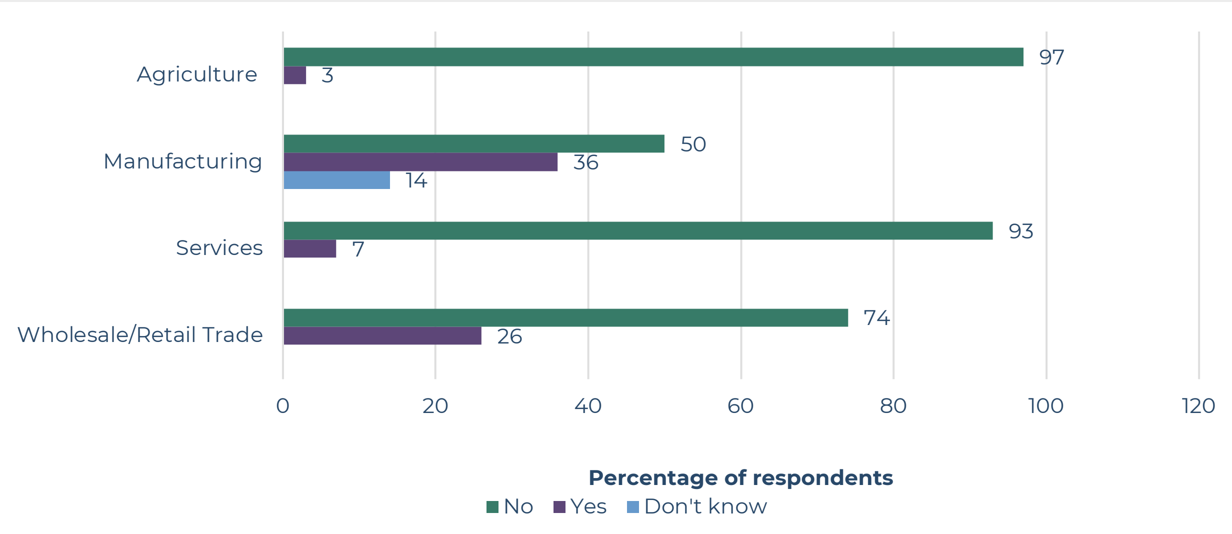
Figure 8 reveals that there is a low level of awareness regarding the existence of the Agreement among MSMEs, as demonstrated by the 67 percent of respondents answering "No" to the above question. Disaggregated analysis of the MSMEs' awareness by enterprise size shows that only about 18 percent of the micro and small enterprises were aware of the AfCFTA policy. Oppositely, a significantly more substantial portion (67 percent) of the medium-sized enterprises declared their awareness of the Agreement.

Figure 8: *Reported Awareness of AfCFTA by Enterprise Size*



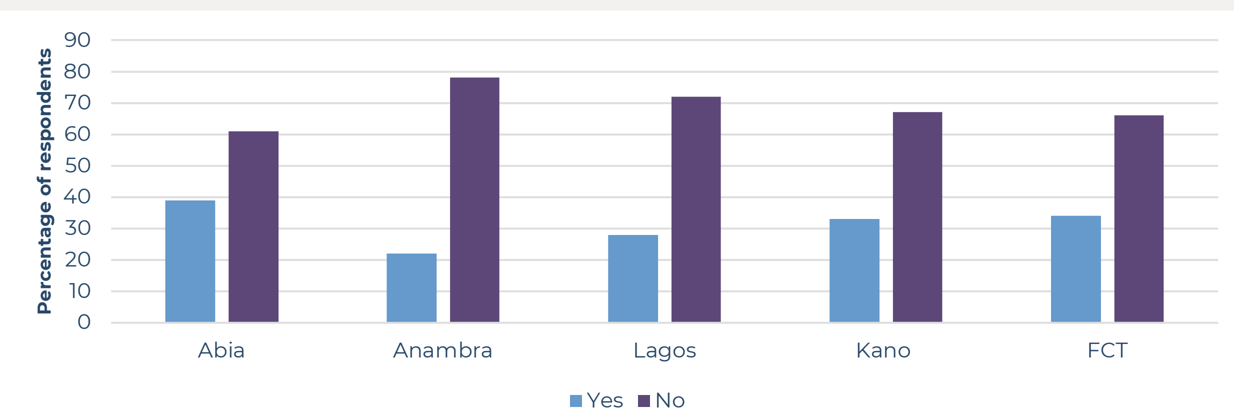
Further disaggregation by enterprise sectors shows that 97 percent of agricultural MSMEs were not aware of the Agreement, while 50 percent of manufacturing sector enterprises were also not aware of the Agreement (see Figure 9). Perhaps surprisingly given the increased awareness of the importance of services as both inputs to other exports, and as exports themselves throughout African economies (see Saez et al, 2015), some 92 percent of the MSMEs surveyed in the services sector said they were not aware of the AfCFTA policy. Finally, about 74 percent of the MSMEs in the wholesale and retail trade sectors did not know of the Agreement.

Figure 9: *Reported Awareness of AfCFTA by Enterprise Sectors*



A further disaggregation of respondents by geographic location highlights that unawareness is endemic throughout the country. The significant diference that exists in knowledge of the AfCFTA between the two Eastern states studied, Abia and Anambra, is striking. While 39 percent of Abia respondents were aware of the deal (the highest of the five locations surveyed), only 22 percent reported prior knowledge in Anambra state. Figure 10 breaks down the awareness figures of all states surveyed.

Figure 10: *Reported Awareness of AfCFTA by State*



Generally, this implies a vacuum in policy communications and a gap in knowledge of AfCFTA among MSMEs in the key sectors concerned in the implementation of the trade Agreement. This also underscores the low level of engagement of relevant stakeholders in the preparations for the kick-start of AfCFTA.

The need for awareness creation was also emphasised by participants in the focus group discussion that were held to zero in on some of the more specific issues currently facing the implementation of the deal. One participant, for instance outlined that...

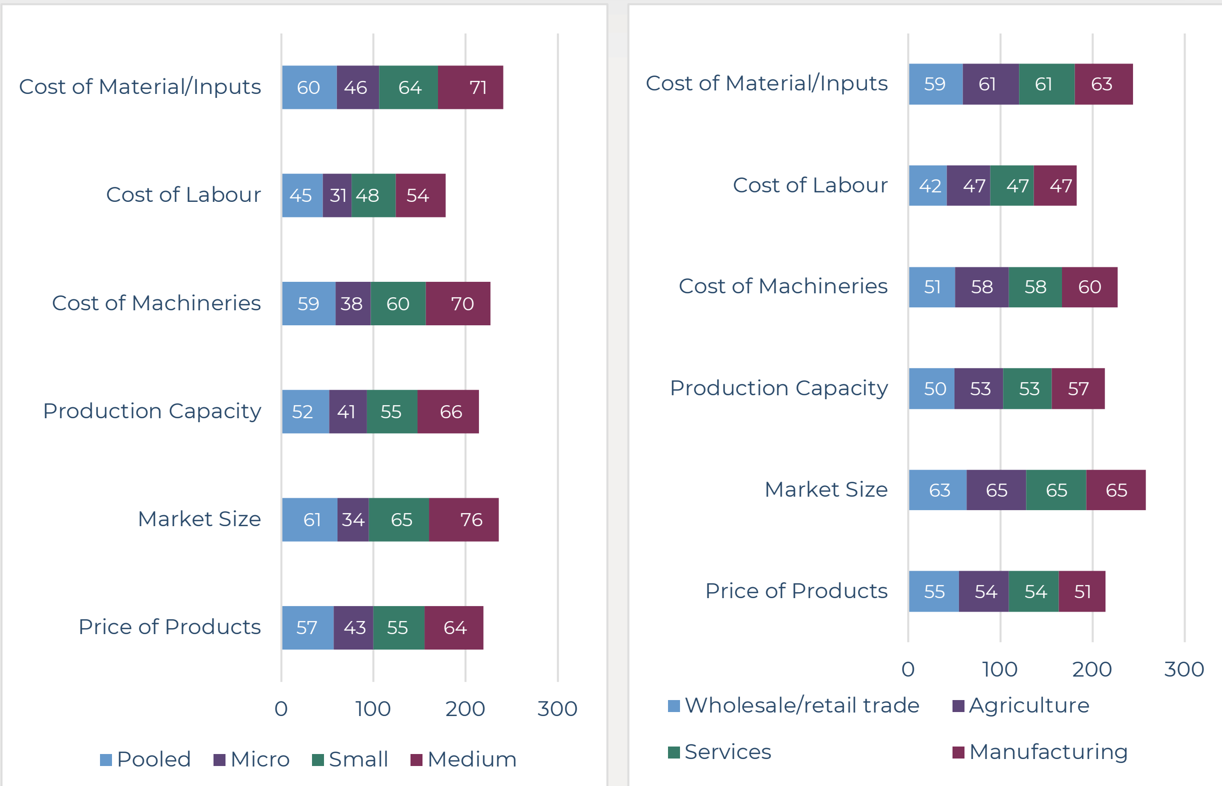
> ***"information is a big gap. You cannot plan for a market that you do not know or understand." (Mr. Opeyemi Oriniowo – Development Practitioner and Analyst, Principal Partner, Rindev Consulting Limited).***

3.3.2 The Potential Impact of AfCFTA

Among the minority of respondents aware of AfCFTA's existence, there is a general optimism surrounding the prospective effects of its implementation. Surveyed business owners and entrepreneurs expressed their forecasts on the potential impact of the AfCFTA, the results of which are reported in Figure 11. The pooled results show that 61 percent of this subsample are optimistic of a positive effect of the AfCFTA on their market size, while 60 and 59 percent are optimistic of positive effects on cost of materials and inputs and cost of machineries, respectively. Moreover, a majority of the medium enterprises surveyed opined that the AfCFTA will have positive effects in terms of cost of materials and inputs, cost of machineries, market size, and production capacity. A high proportion of the small enterprises perceive that the Agreement will have positive effects on their businesses in terms of cost of materials and inputs, costs of machinery, production capacity, market size, and price of products. Micro enterprises report a lower level of optimism across all categories, perhaps reflecting the smaller-scale, less internationally-minded scope of their operations.

Disaggregating the enterprises further by economic sectors, the manufacturing sector displays the most positive attitudes regarding the possible future effects of the AfCFTA on market size, cost of material and inputs, and cost of machinery.

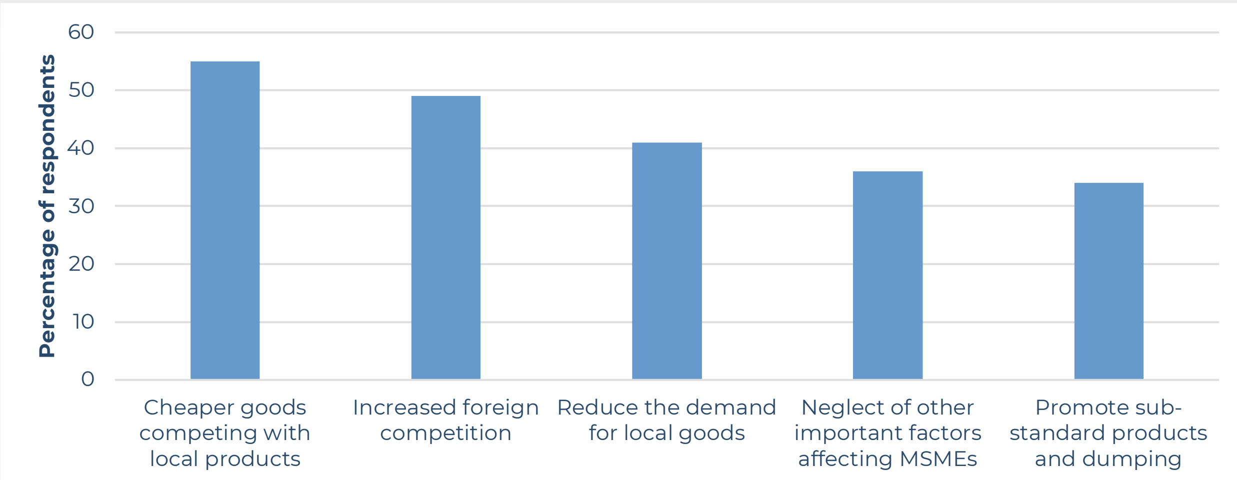
Figure 11: *Beliefs on Positive Potential Impacts of AfCFTA*



Perceived Threats of AfCFTA to MSMEs

While general optimism could be perceived among respondents (again, limited to the minority aware of the deal in the first place), Figure 12 reveals the share of respondents worried about five potential adverse effects of the AfCFTA to MSMEs in Nigeria. Most prominent among the threats is the fact that cheaper goods from other African countries will be competing with local goods in Nigeria. Other threats to MSMEs in Nigeria that could be associated with the AfCFTA include increase in foreign competition, reduction in the demand for local goods, and dumping of sub-standard products.

Figure 12: *Perceived threats of AfCFTA to MSMEs*



This point was further emphasized by participants in the focus group discussion. In the words of some key informants ...

> ***..... "Nigerians are not loyal to brand but loyal to products best suitable for 'pocket' and hence favour cheaper goods".***
>
> —(Olanrewaju Oniyitan – Founder & CEO of W-Holistic Business Solutions (W-HBS))

> ***"The ETLS gives us a pointer to how arrangement like this can be abused and how Nigeria could be a target for predatory practices..."***
>
> —(Member of the National Action Committee on AfCFTA)

3.3.3 Gauging MSMEs' Competitive Capacity and Capacity to Meet Process Requirements

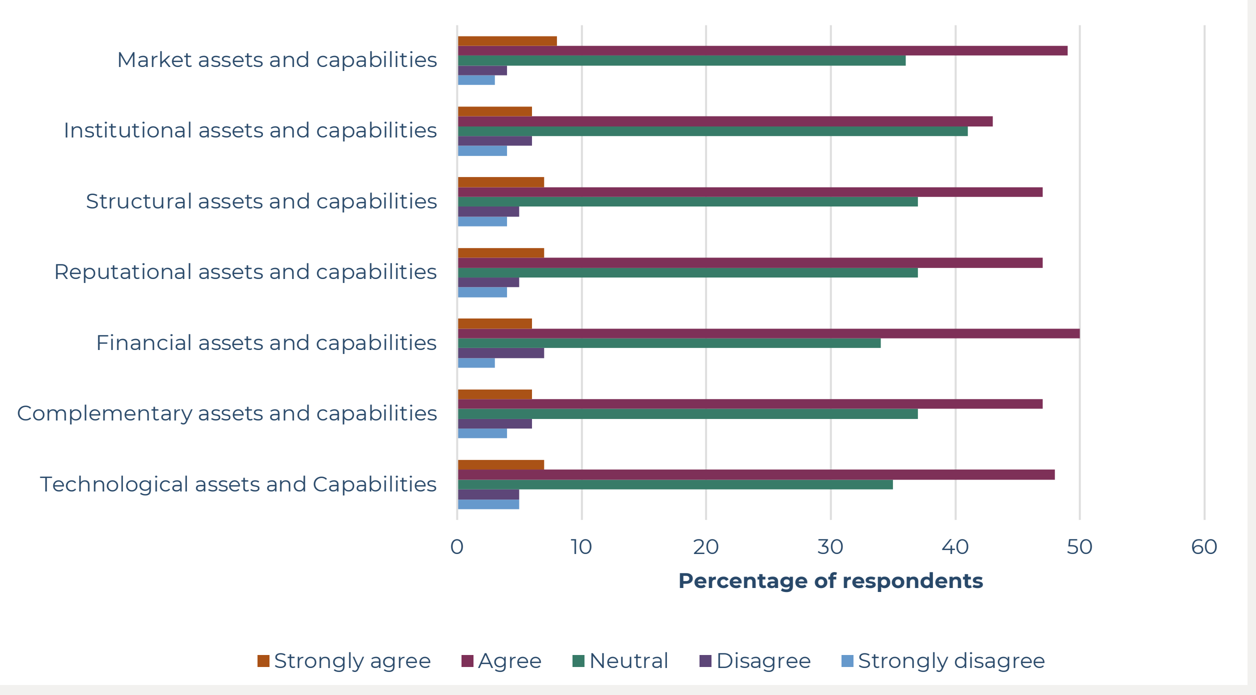
Reducing costs to a Highly Competitive Level

In order to gauge Nigerian MSMEs competitive capacity and potential to meet process requirements of the AfCFTA, business owners and entrepreneurs were asked to assess their own potential to combine their assets, resources, and capabilities in various realms in such a way to reduce firm costs to a highly competitive level in light of AfCFTA.

These capacities and assets include: technological and complementary assets, which refers to the ownership and utilization of technological assets to produce and deliver new products and services; financial assets, implying a firm's cash position, degree of leverage, and cash flow; reputational assets, referring to a firm's reputation; structural assets, denoting the formal and informal structure of organizations and their external linkages; and, institutional assets that refer to regulatory systems.

The generally high proportion that indicated 'agree' shows that most of these enterprises are optimistic about their capability to meet the process requirement for reducing costs to a highly competitive level.

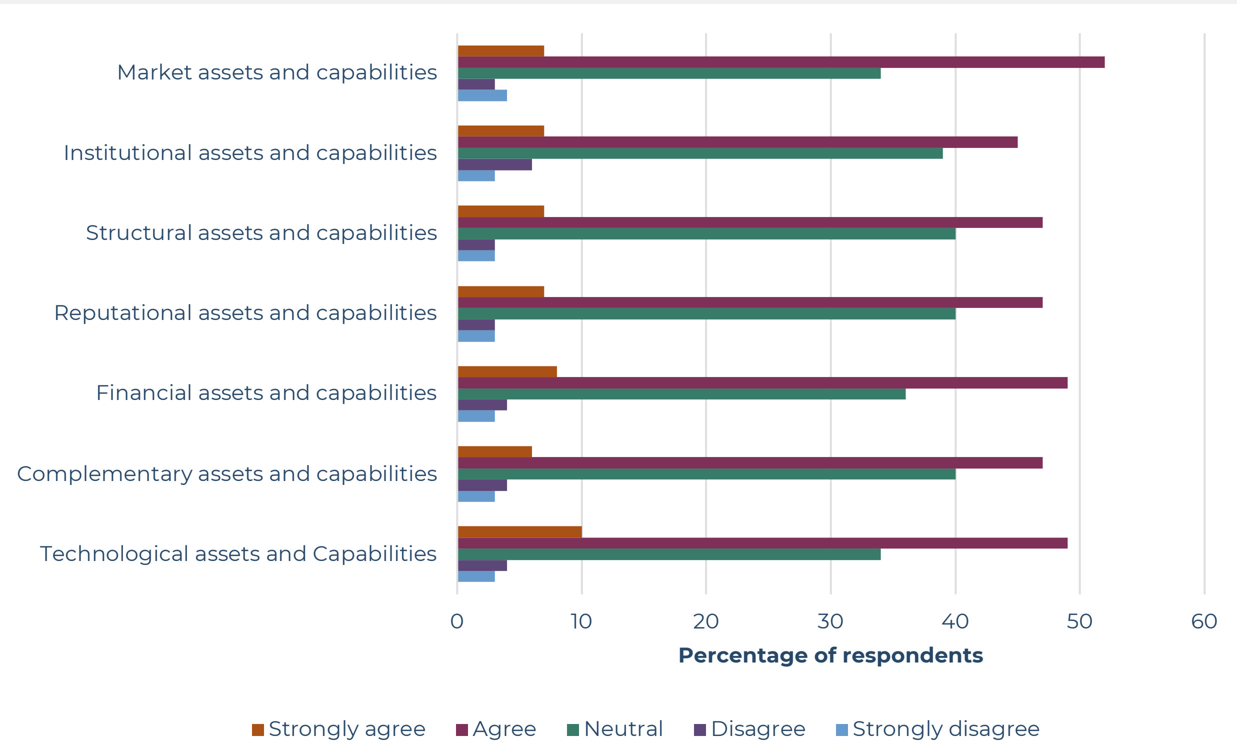
Figure 13: *Ability to Deploy Assets to Reduce Production Costs to a Highly Competitive Level*



Capabilities to Fully Benefit from All Market Opportunities of AfCFTA

In order to maximize the potential benefits associated with the AfCFTA, it is necessary that firms should be able to combine assets, resources, and capabilities to fully benefit from all market opportunities of the trade Agreement. Figure 14 shows that in terms of technological assets, most of the respondents agree that they will be able to acquire, protect, and utilize modern inputs and machineries to fully benefit from the trade Agreement. Additionally, the majority of the firms are optimistic and indicated that they will be able to combine complementary assets, financial assets, reputational assets, structural assets, institutional assets, market assets, and capabilities to maximize the potential benefits of AfCFTA. This implies that Nigerian MSMEs will strive to employ intangible organizational and managerial processes (such as the distinct skills, processes, procedures, decision rules, and innovations) in the execution of their day-to-day operations. It also suggests that these firms believe they will be able to seize and maximize the AfCFTA opportunity through enterprise structures, procedures, designs, and incentives.

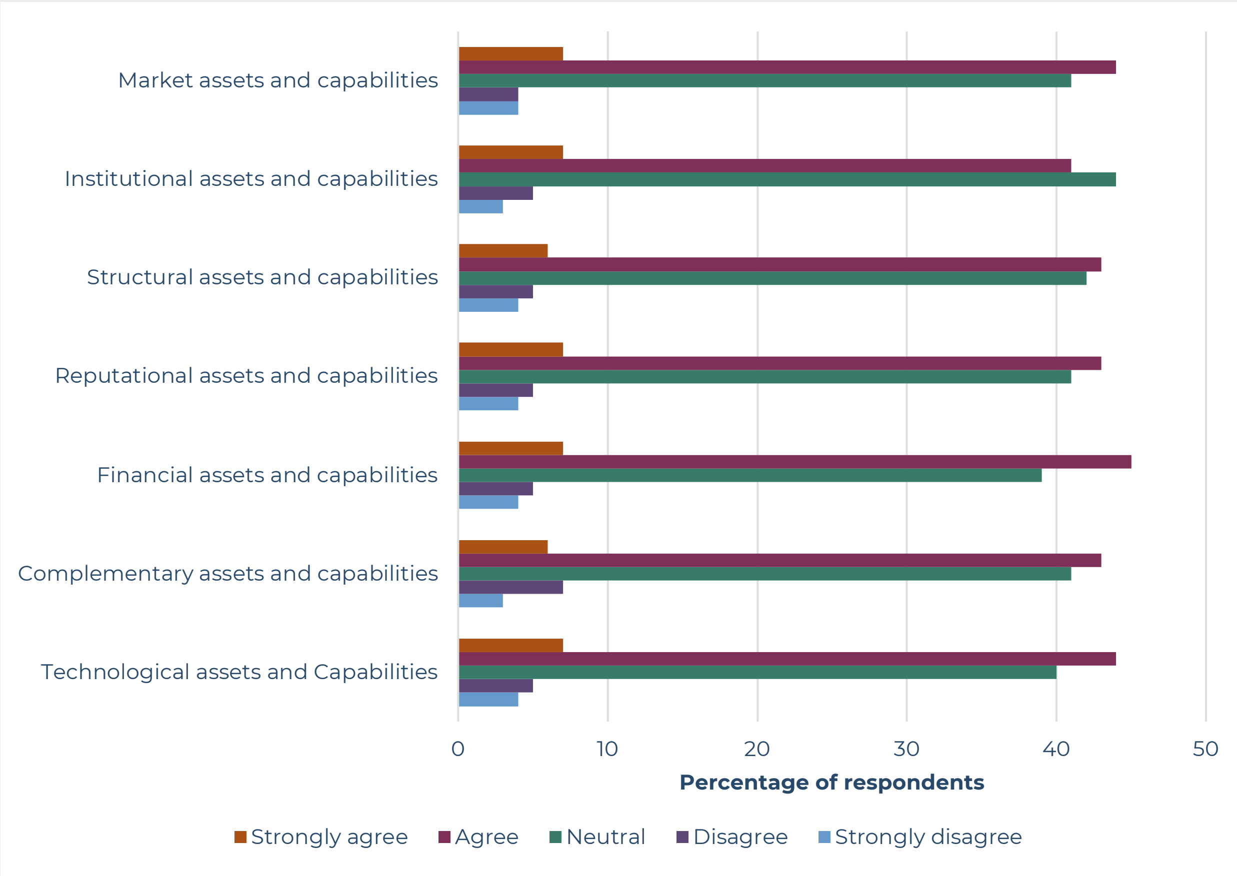
Figure 14: *Capacity to Deploy Assets to Fully Benefit from all Market Opportunities of AfCFTA*



Capabilities to Defend Against All Potential Competitive Threats of AfCFTA

Figure 15 shows that the sampled firms are optimistic that Nigerian MSMEs will be able to combine assets, resources, and capabilities to defend against all potential competitive threats of AfCFTA. This is revealed by the high proportion of respondents who chose 'agree'. However, about the same proportion choose a 'neutral' response.

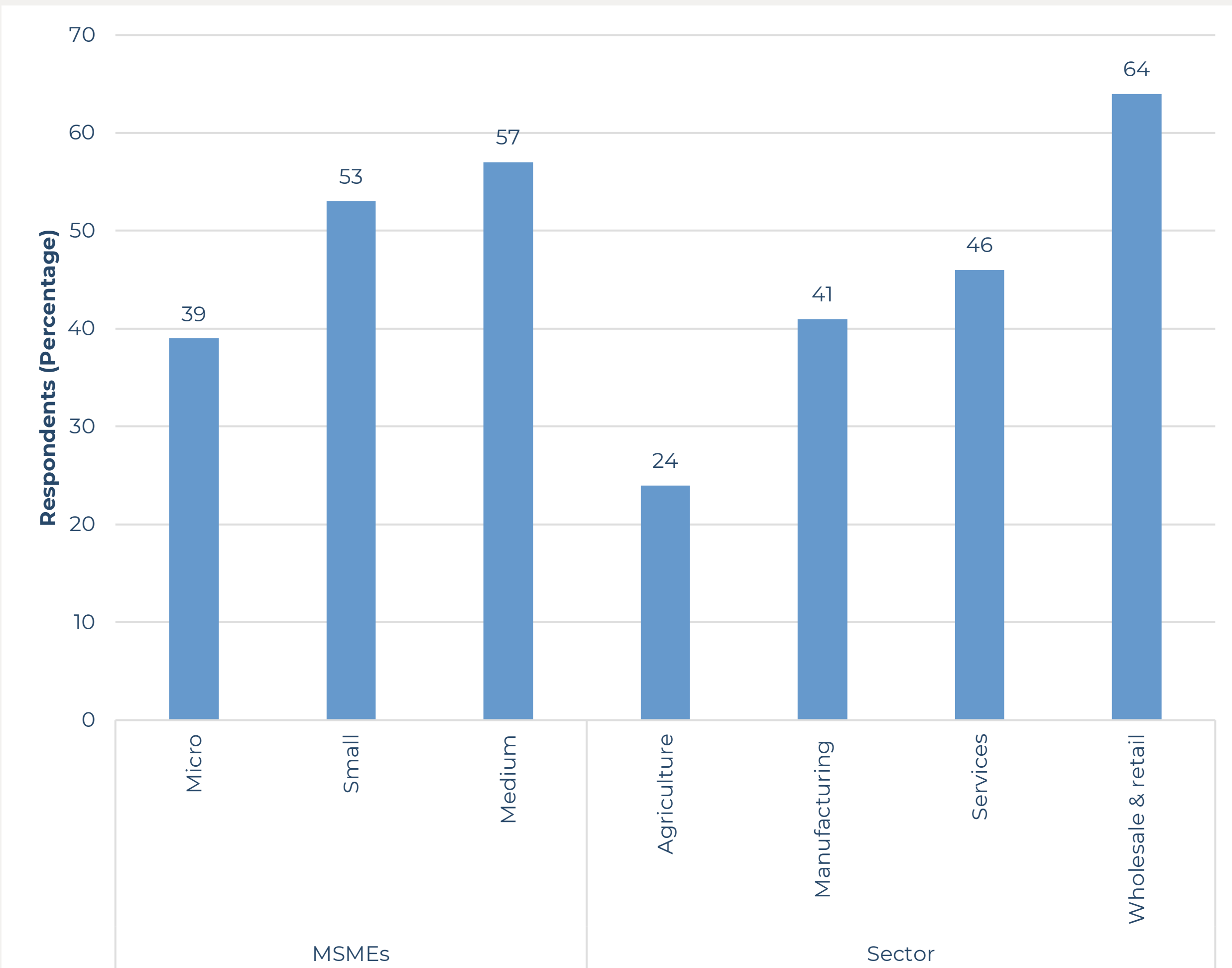
Figure 15: *Capabilities to Use Assets to Defend Against Potential Competitive Threats of AfCFTA*



3.3.4 MSMEs Prior Engagement in International Trade

Businesses with more international engagements, especially if export-oriented, are most likely to benefit from FTAs as they lower barriers to trade with other countries. Analysis of the engagement of the surveyed enterprises in international trade (Figure 16) shows that about 57 percent and 53 percent of the small and medium enterprises engage in international trade, while only 39 of Micro enterprises are involved in any form of international trade. A further analysis by sector shows about 64 percent of the wholesale and retail traders engage in international business activities. About 41 percent of the enterprises in the manufacturing sector engage in international business activities, while about 46 percent of the services sectors MSMEs and a modest 24 percent of agricultural businesses are engaged in international business activities. This connotes a low level of engagement in international trade by the MSMEs, except for those in wholesale and retail trade sector and medium scale enterprises.

Figure 16: *Engagement in International Business Operations by Firm Size and Sector*



Types of International Business Activities MSMEs are Engaged in

Among those involved in international trade, the majority of the MSMEs are involved in importation activities only. This entails a high proportion of the wholesale & retail trade (77.1 percent), services (62.9 percent), manufacturing (56.1 percent), and agriculture (64.9 percent).

Table 6: *International business activities by MSME enterprise sectors*

Variable	Agriculture		Manufacturing		Services		Wholesale/Retail Trade	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%
Commercial cooperation	5	13.5	12	8.1	28	12.2	35	8.5
Export only	-	-	4	2.7	1	.4	3	.7
Import only	24	64.9	83	56.1	144	62.9	316	77.1
Import and Export	4	10.8	37	25.0	13	5.7	43	10.5
Other	2	5.4	7	4.7	29	12.7	5	1.2
Sub-contracting	1	2.7	2	1.4	7	3.1	6	1.5
Technical cooperation	1	2.7	3	2.0	7	3.1	2	.5
Total	37	100.0	148	100.0	229	100.0	410	100.0

Engagement with Present Regional Integration Approaches

Our survey also sought to capture the level of usage of current (pre-AfCFTA) trade deals among Nigerian MSMEs. At present, these deals include the African Growth and Opportunity Act (AGOA), as well as the ECOWAS Trade Liberalization Scheme (ETLS). AGOA is a non-reciprocal trade preference programme that was signed into law by the United States of America in May 2000 to provide preferential market access and duty-free treatment to U.S. imports from eligible Sub-Saharan Africa (SSA) countries, including Nigeria. The ETLS, on the other hand, permits the free intra-ECOWAS movement of goods originating from member-states by eliminating tariff and non-tariff barriers. The Global System of Trade Preferences among Developing Countries (GSTP) is one more such integrationist trade deal that affects Nigeria's international trade.

Results of the survey as presented in Table 7 show that there is a low level of usage of present free trade instruments among MSMEs in Nigeria. Somewhat surprisingly, despite much higher reported levels of international trade engagement, only about 6.5 percent of the respondents declared they currently use any provision of the AGOA for their business activities, while just 11.2 percent reported utilizing the ETLS. An even smaller share of the surveyed businesses, just 4.6 percent, reported taking advantage of the GSTP in their import activities. While the contrast between these numbers and those relating to engagement in international business activities may raise some questions about respondents' awareness of FTA use, the low reported numbers imply that a bulk of the MSMEs do not take advantage of previous trade policies in international business activities.

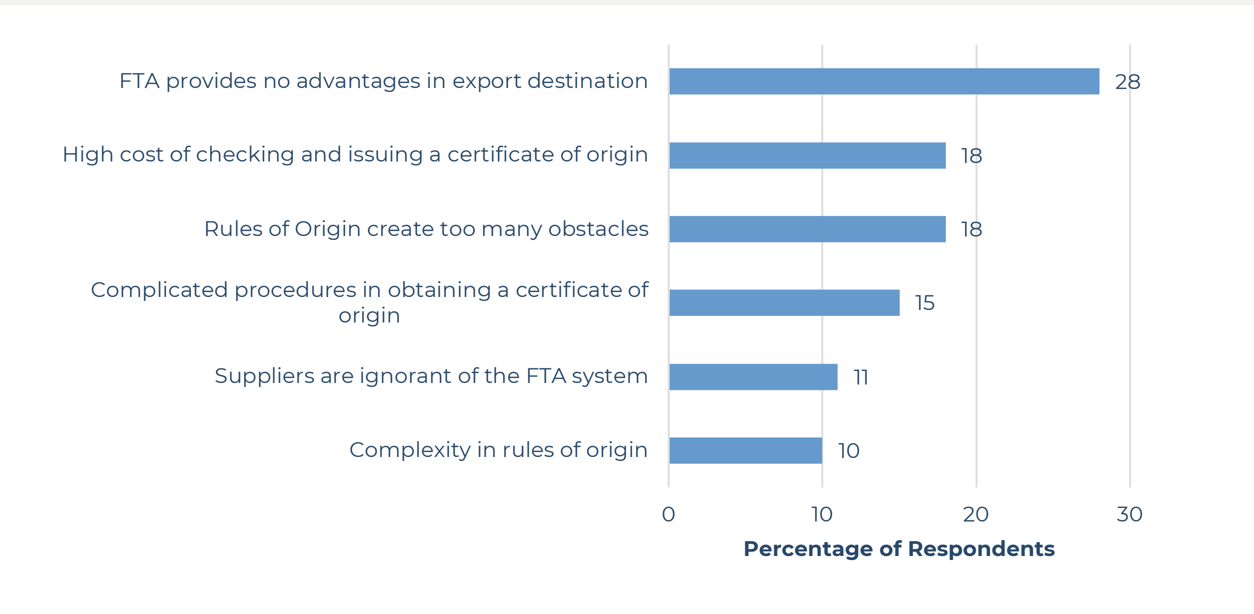
Table 7: *MSMEs use of existing trade policies (Imports and/or Exports)*

Multilateral Arrangement	AGOA No.	%	ETLS No.	%	GSTP No.	%
No plan to use	967	68.8	919	65.3	1,017	73.4
Considering	347	24.7	332	23.6	305	22.0
Currently	92	6.5	157	11.2	64	4.6
Total	**1,406**	**100.0**	**1,406**	**100.0**	**1,406**	**100.0**

Challenges Encountered with Present Regional Integration Approaches

The reasons for under-utilisation of the current trade provisions garnered from the survey were numerous and multi-faceted. The most common ones, along with their frequency, are presented in Figure 17. The most prominent among the reported obstacles to use is that FTAs provide no advantage in export destinations of interest. Other challenges attributed to previous FTAs include high cost of checking and issuing a certificate of origin and rules of origin (RoOs) create too many obstacles. These findings should underscore the importance of thoughtful rule design in the upcoming decisions regarding AfCFTA's RoOs negotiations.

Figure 17: *Reasons for Non-Utilisation of Existing FTAs*



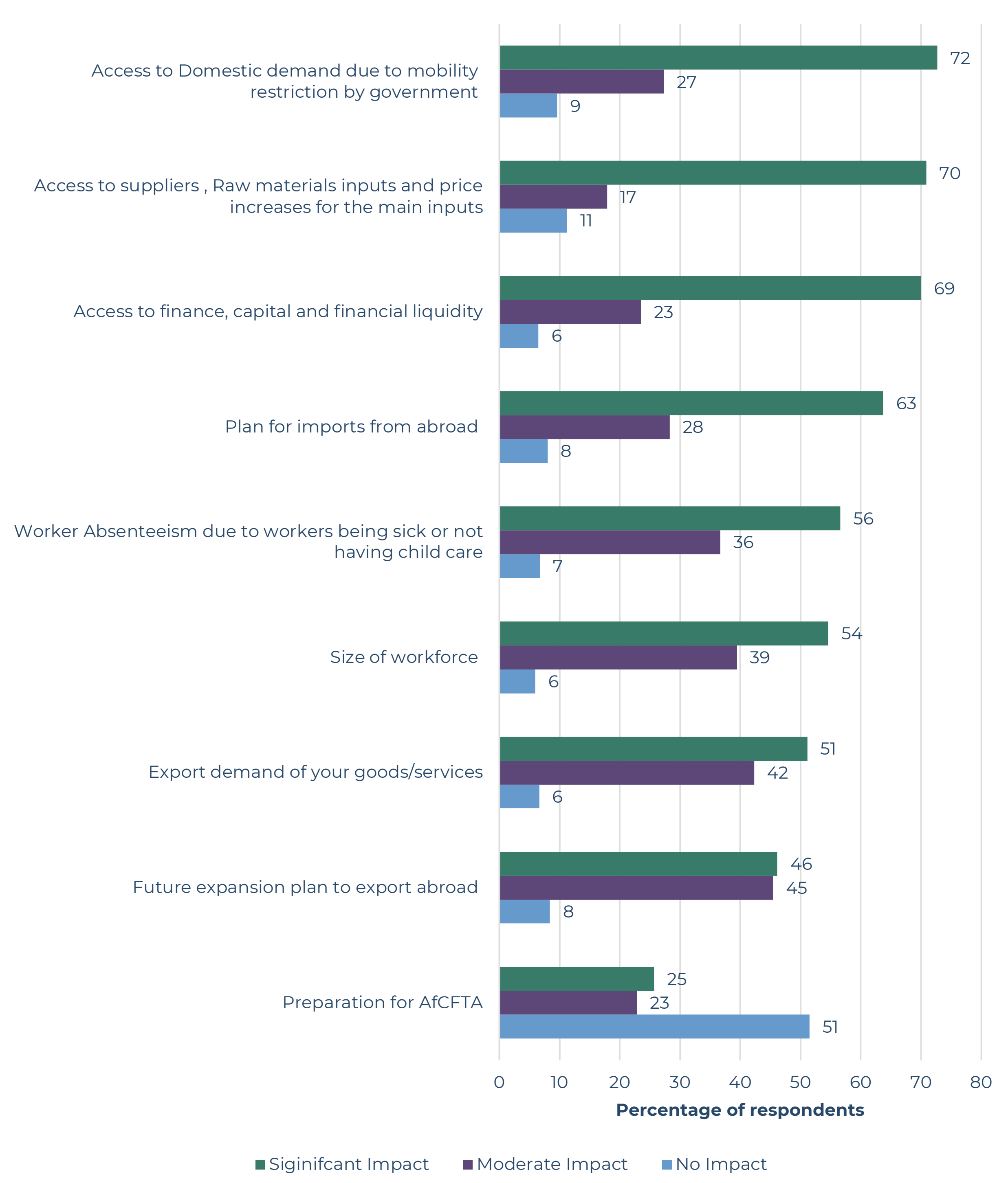
3.3.5 Perceptions on the Effects of the COVID-19 Pandemic

The survey period overlapped with the onset of the COVID-19 outbreak which, among other things, has also led to the postponement of the commencement period for the AfCFTA. The survey, therefore, sought to explore the likely impact of COVID-19 on MSMEs and draw implications to facilitate an expedited and efficient implementation of AfCFTA in Nigeria. There is no doubt that the COVID-19 outbreak is continuing to impact businesses in diverse ways. In relation to international trade, of respondents aware of AfCFTA (see section 2.3.1) Figure 18, shows that 25 percent experienced significant pandemic-related impact on their preparations for AfCFTA; about 46 percent experienced significant pandemic-related effects on their future expansion plans to export abroad; and 63 percent experienced significant pandemic-related effects on their plan for import from abroad.

There is no doubt, therefore, that an effective strategy for the implementation of AfCFTA will not only have to incorporate a concerted effort to extend awareness of the deal's existence itself, but also account for the further challenges brought about by the pandemic, even among businesses that reported knowledge of AfCFTA's existence. An additional complication for businesses that may further lower uptake of AfCFTA's provisions is the effect of the pandemic on access to finance that may be necessary to expand operations internationally. A high proportion (69 percent) of the surveyed businesses said that the pandemic had a significant impact on their access to finance, capital, and financial liquidity, underscoring the multifaceted obstacle posed by COVID-19 to a successful implementation of the AfCFTA.

Moreover, the enterprises' access to suppliers, availability of raw material inputs, and prices of the main inputs were reported to have been significantly impacted by the COVID-19 pandemic. Additionally, about 72 percent of the sampled enterprises opined that the pandemic significantly impacted their businesses in terms of access to domestic demand due to mobility restriction by the government. This suggests that COVID-19 is changing the dynamics of MSME operations and could, therefore, have a non-negligible long-term impact on how the AfCFTA will affect MSMEs and the wider economy.

Figure 18: *Reported Effects of COVID-19 on MSMEs*



Expectations for Business Recovery

The surveyed firms are hopeful of recovery from the effects of the COVID-19 pandemic. The time projections for recovery varies among the firms as shown in Table 8. Our results show that, although a small share of businesses are optimistic about timely recoveries, more than half of respondents, irrespective of firm size, expect the adverse effects of COVID to persist for at least six months. Significant uncertainty exists, particularly among Micro enterprises.

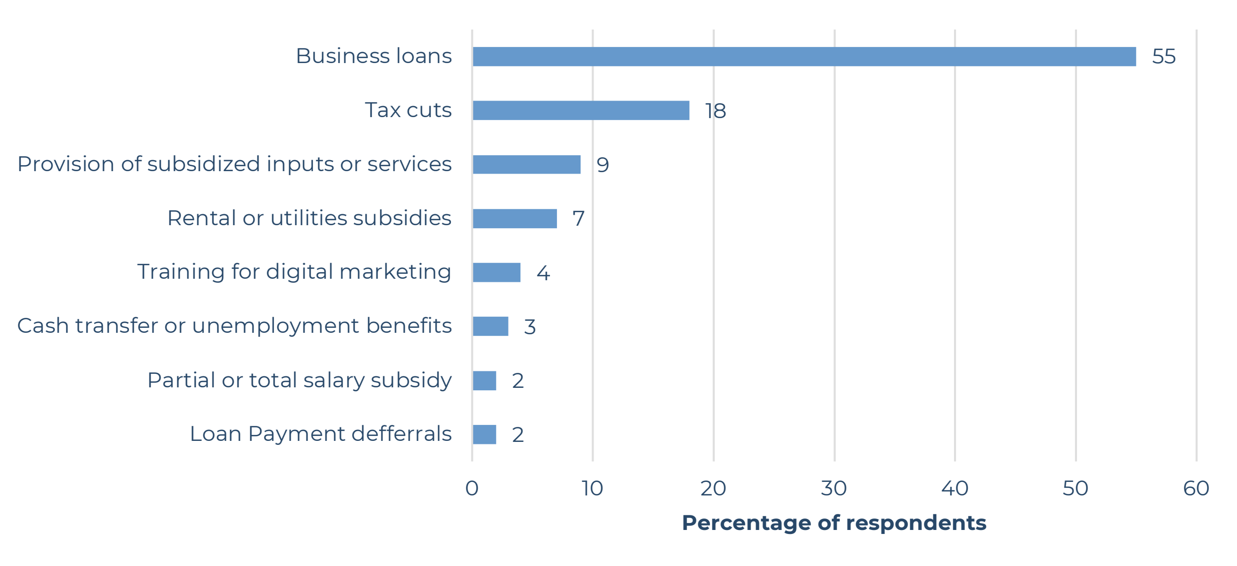
Table 8: *Expectations for business recovery by business categories*

Variable	Micro Enterprises (%)	Small Enterprises (%)	Medium Enterprises (%)
Less than a month	*3.4*	*4.4*	*7.8*
Between 1-3 months	*18.7*	*14.9*	*16.0*
Between 4-6 months	*17.5*	*19.5*	*19.2*
Between 7-9 months	*12.4*	*16.5*	*11.9*
Between 10-12 months	*13.8*	*16.8*	*13.2*
Over a year	*12.1*	*11.8*	*13.2*
Never	*0.5*	*0.1*	-
Don't Know	*21.6*	*16.0*	*18.7*

Recommended Policy Support

Respondents were further asked about their beliefs about what the most effective government policies would be to mitigate the adverse impact of COVID-19. Most prominent among the interventions believed to be important is increasing the availability of business loans as stated by about 55 percent of the enterprises. Implementing a tax cut was suggested by 18 percent of the enterprises. Provision of subsidized inputs or services, as well as rental or utilities subsidies, were suggested by 9 and 7 percent of the surveyed enterprises, respectively. Figure 19 displays the results. The data disaggregated by firm size can be found in Appendix II.

Figure 19: *Reported Beliefs on Most Needed COVID Mitigation Policies*



CHAPTER 4

CGE Model

4.1 CGE MODEL: INTRODUCTION AND GOALS

To promote political and economic integration across and within the African region, the African Continental Free Trade Area (AfCFTA) Agreement was enacted in March 2018 with 44 African countries and an additional 10 states, including Nigeria, in July 2019. AfCFTA represents the largest free trade area, covering 54 countries and over $3.4 trillion in GDP. Understanding and quantifying the impacts of trade liberalization across the African region on Nigeria is the central issue of this report. However, this is a difficult question to answer, as analysing the welfare effect of this Agreement faces three challenges: first, the Agreement has not yet been fully effected because of COVID-19; second, it is very new and the long term impacts are not evident; and third, this Agreement covers countries that already participate in other bilateral and multilateral trade agreements.

A change in trade costs impacts the distribution of economic activity in all locations through complex general equilibrium interactions. More trade with other African countries means reduction in market share of other top Nigerian trade partners. In 2000, before China's accession to the WTO, the share of Nigeria's imports from China was 6 percent and rose to 21.9 percent by 2014. As the second largest country in Africa, joining the AfCFTA means an increased market for exports and access to cheaper imported inputs. In 2014, Nigeria had high import penetration in agriculture, wood and paper, machinery, and metal products while the volume of exports was larger than imports in mining, textiles, petrochemicals, and other manufacturing industries.

In this report, we implement a general equilibrium framework that takes into account each of the aforementioned challenges, providing a tractable way of assessing the welfare impacts of AfCFTA on Nigeria and other Africa countries. Our model is based on the work of Caliendo and Parro (2015), which itself draws from the seminal work of Eaton and Kortum (2002). Each country has labour forces that are mobile across sectors but immobile across countries. There is a continuum of tradable goods and the distribution of productivity over the continuum belongs to the Frechet family; countries differ in average productivity but have common shape parameter within a sector. International trade is subject to barriers in the form of iceberg trade costs. All markets are competitive. The magnitude and direction of trade flow is determined by technologies and trade costs.

Specifically, this chapter contributes to four strands of discussion on FTAs in Africa. First, we employ a model that allow us to quantify the impacts of several scenarios including free trade among African countries while leaving the rest of the world at the higher tariff regime as at 2014. Second, by employing a static model, we are able to assess the immediate effect of AfCFTA, providing evidence of short-term effects of the trade Agreement. Third, as sectors are interrelated, a tariff reduction in one sector affects the prices on other sector through supply chain interactions. Rather than using a simple empirical model, the analytical framework we employ has implications for sectoral input-output relations and provides insights on the effects of AfCFTA on global trade patterns. Finally, we account for the contribution of each industry by decomposing the welfare effects into volume of trade and terms of trade effects. Although the model yields results for all of the countries in our sample, this report specifically covers the impacts on Nigeria.

Measuring potential welfare effects requires computing the change in real GDP per worker associated with moving from its current observed level to a new level in the frictionless world. We quantify our welfare effects by using data on trade share, value added, and gross output to calibrate a 54-country and 25-sector version of the model to year 2014. We then conduct several experiments, including a free trade agreement within the Africa region. AfCFTA comes at a time when the global economy is entering into an unprecedented health and economic crisis that continues to generate arguments against globalization. COVID-19 and the policies enforced to curtail the spread of the virus have disrupted business operations and impacted industry supply chains, making countries rely on domestic production for the supply of essential goods. Regional trade agreements could help offset the high costs associated with traveling and importing from outside the region.

Our key results suggest a 1.55 percent welfare gain to Nigeria. Growth in volume of trade accounts for 73 percent of gains in real consumption. Nigeria' real GDP per worker rises by 1.43 percent as a result of trade liberalization. AfCFTA changes Nigeria's share of expenditure on goods across countries; imports from Canada decline by 30 percent while imports from China – Nigeria's top trade partner – decline by 11.33 percent. Clearly, within this model, AfCFTA will lead to changes in Nigeria's trade patterns, but not all African countries receive a share of Nigeria's spending. Nigeria's imports from Botswana, Burkina Faso, Seychelles, and Zambia decline by more than 10 percent.

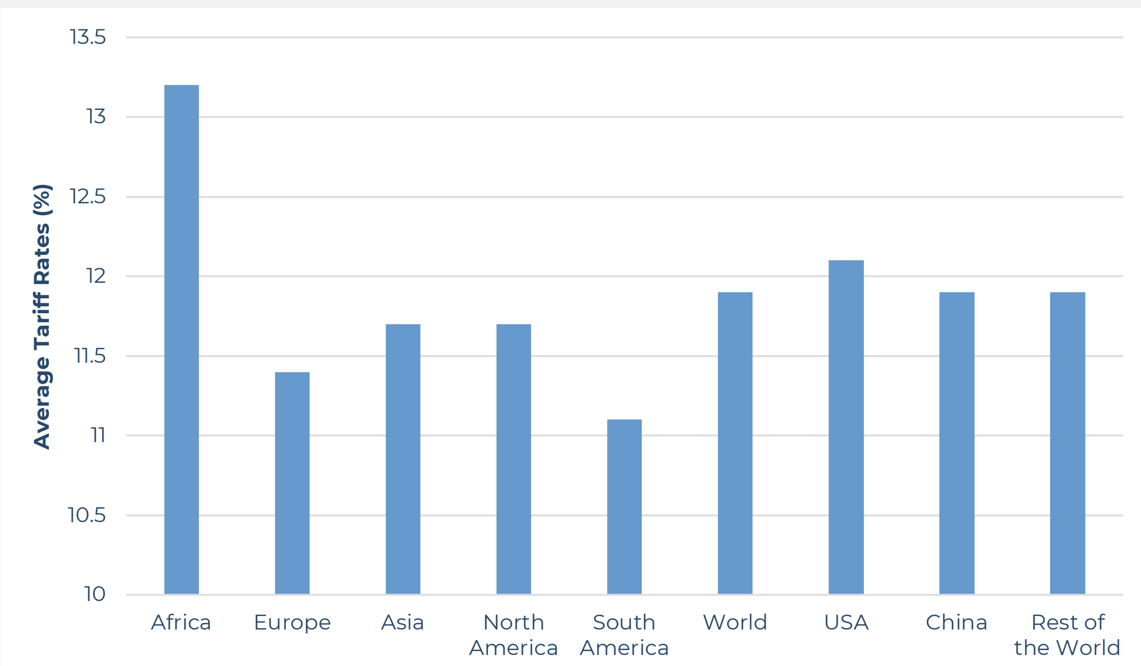
4.2 OVERVIEW OF TRADE, TARIFFS, & PRODUCTION PATTERNS

Reduction in tariff rates change countries' productivity draw; goods from some countries become relatively cheaper, changing trade patterns across countries and sectors. Effects of trade patterns further impact factor payment to labour and prices across countries and sectors, which also depend on one another. In this section, we provide an overview of Nigeria's tariff rates and trade patterns.

As of 2000, Nigeria's tariff rates on imports from the Africa region were 33 percent and declined to 13.2 by 2014. In Figure 20, we analyze Nigeria's imports on 7 regions/categories and two countries – the United States and China. Nigeria's tariff rates on goods from other African countries was higher compared to other trade partners. Average tariffs on imports from Europe and the United States was 11.4 and 12.1 percent, respectively. Nigeria imposed 11.9 percent tariffs on imports from China as well as articles from the rest of the world.

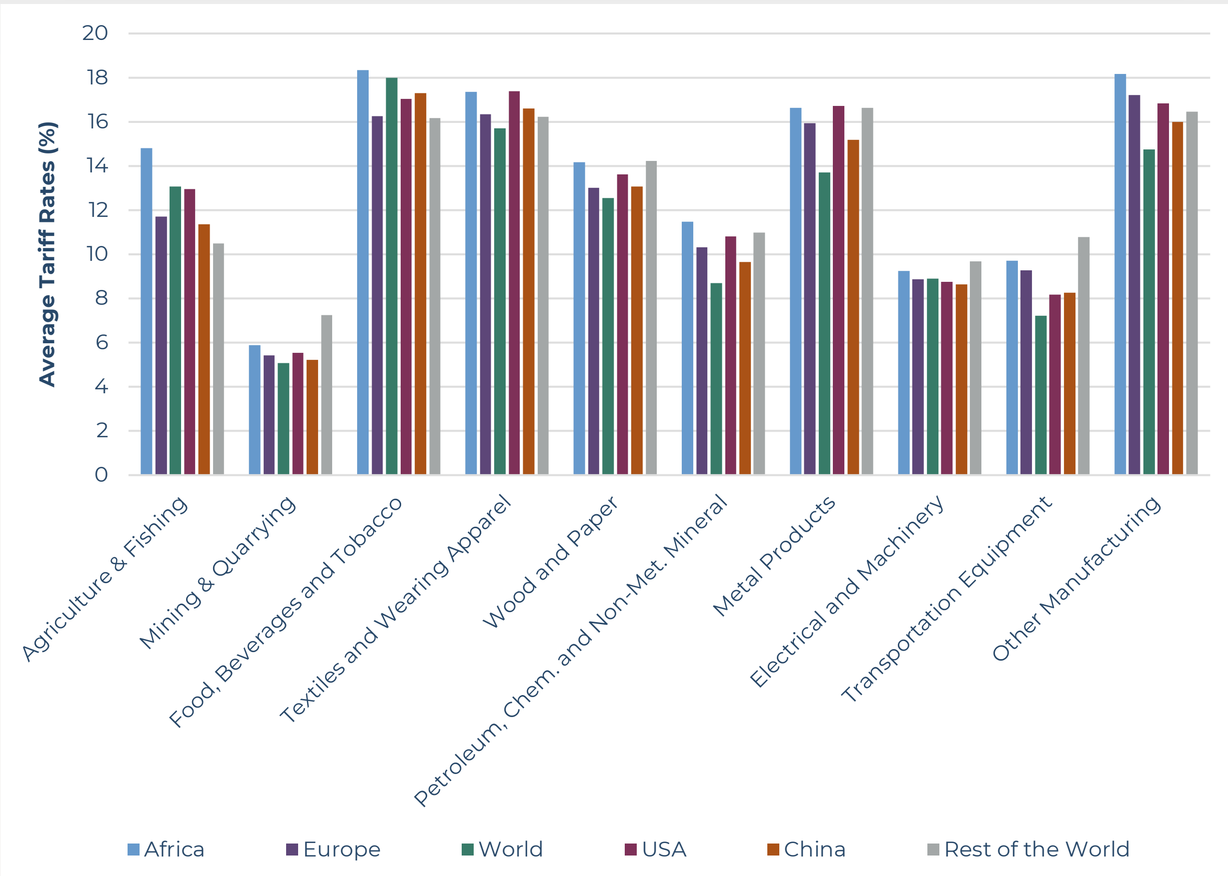
Nigeria's tariff rates differ across sectors and partners. Average tariff rates are lower in mining, petrochemicals, chemicals, and machinery sectors. Figure 21 shows that Nigeria's tariffs on imports from the African region are higher in most sectors compared to imports from Europe, China, the United States, and the rest of the world. With free trade in African countries, we expect prices of imports from other African countries to be relatively lower, leading to an increase in exports from other African countries to the Nigerian market.

Figure 20: *Average Effective Tariff Rates on Nigeria's Imports*



Source: *Simple average tariff rates in 2014 from UNCTAD TRAINS on HS6 dis-aggregated products.*

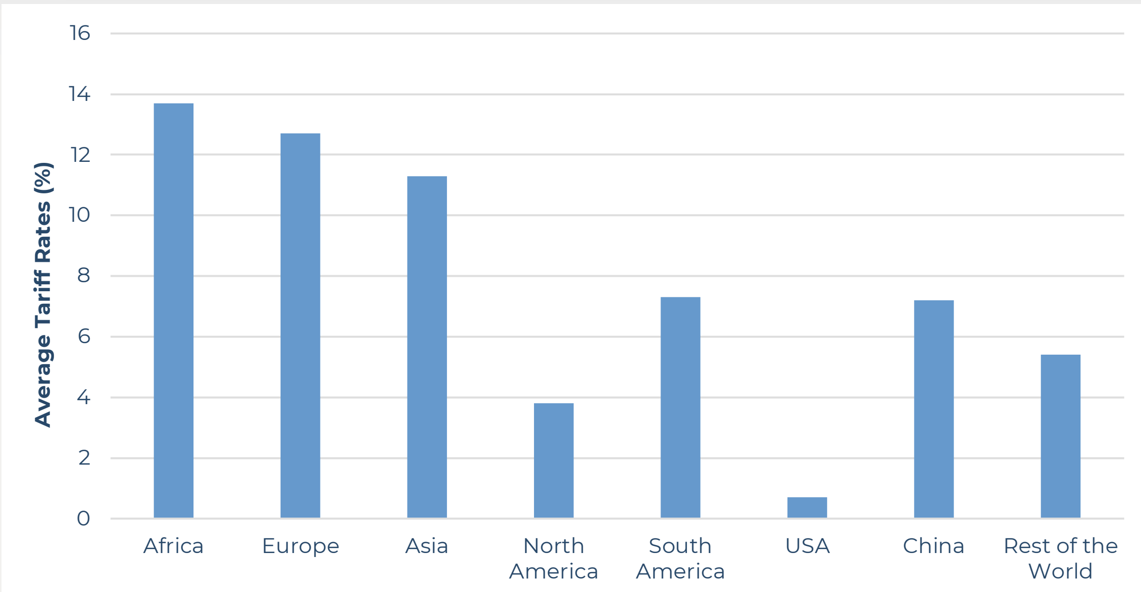
Figure 21: *Average Tariff Rates on Nigeria's Imports by Sector*



Source: *Simple average tariff rates in 2014 from UNCTAD TRAINS on HS6 dis-aggregated*

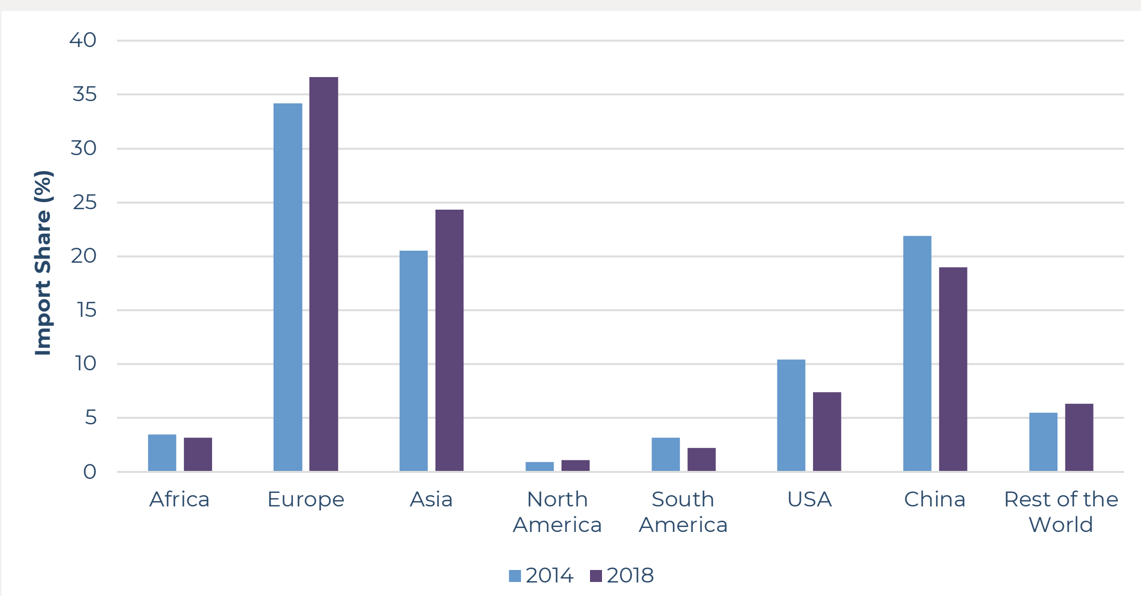
To analyze how AfCFTA and frictionless trade across Africa affects the prices of Nigeria's exports, in Figure 22, we analyze tariff rates imposed on Nigeria's exports to seven markets/regions. As shown in Figure 22, Nigeria faces 13.7 percent tariff rates on exports to other African markets, 3.8 percent on exports to Europe, 7.2 percent on exports to China, and 0.7 percent (lowest) on exports to the United States. Tariff rates on Nigeria's exports differ across sectors, however, in most sectors – other than food and beverages, where tariffs on Europe were as high as 45 percent, and auto for China, where tariffs were 14 percent – Nigeria faces a higher tariff from African countries compared to other partners. With AfCFTA and the subsequent zero tariff bound rates, Nigeria has a higher comparative advantage which possibly opens these markets up for Nigeria's exports. Tariff rates in 2014 forms our benchmark for the CGE modeling and is used to assess the impacts free trade in Africa.

Figure 22: *Average Tariff Rates on Nigeria's Exports*



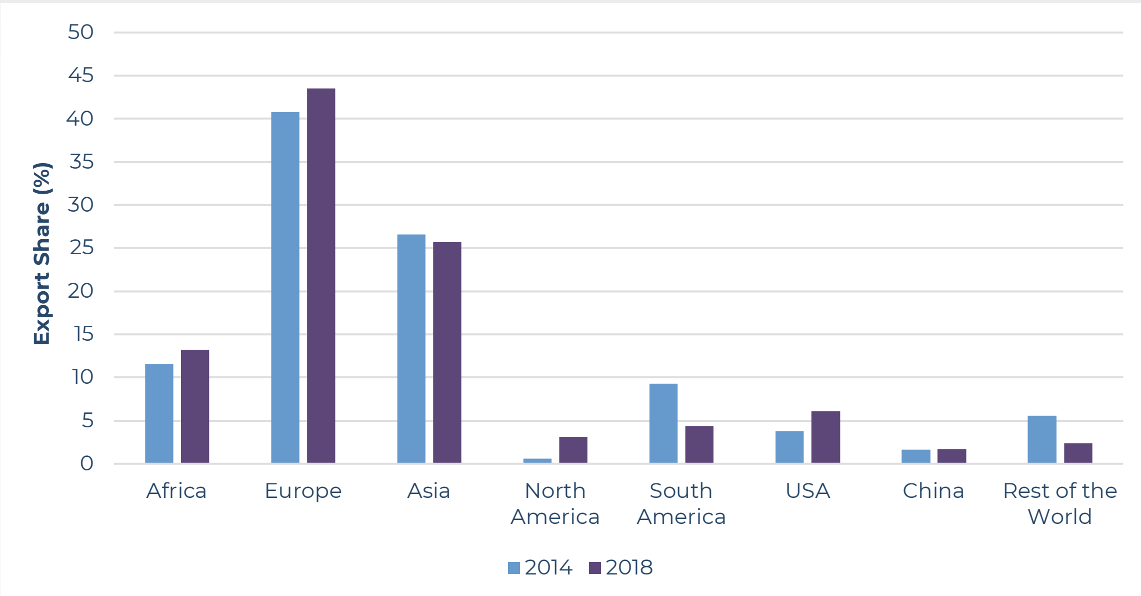
Source: *Simple average tariff rates in 2014 from UNCTAD TRAINS on HS6 dis-aggregated products.*

Figure 23: *Nigeria's Imports Share*



Source: *Bilateral trade data at HS6 level is from UN Commodity trade database.*

Figure 24: *Nigeria's Exports Share*



Source: *Bilateral trade data at HS6 level is from UN Commodity trade database.*

Based on the tariff rates, trade patterns follow the expected direction: countries with lower tariffs like China and Europe export more to Nigeria, while Nigeria's imports and exports from and to the Africa region is lower. As at 2014, 34.2 percent of Nigeria's total imports were from Europe, 21.9 percent from China, and 3.5 percent from the Africa region. As shown in Figure 23, Nigeria's import from Europe, Asia, North America, and the rest of the world rose between 2014 and 2018. Figure 24 presents Nigeria's export share; most of Nigeria's exports are to countries in Africa (11.6 percent), Europe (40.8 percent), Asia (26.5 percent), and South America (9.3). Although average tariff rates on Nigeria's exports to the United States were lowest at 0.7 percent (see Figure 22), the share of Nigeria's exports to the region remained low at 3.8 percent. Bilateral trade share in 2014 is used as a benchmark of economic activity and then used to conduct counterfactual analysis.

4.3 GAINS FROM TRADE MODEL

To quantify how much trade liberalization in the Africa region impacts wages and consumption across all countries, we employ a static general equilibrium model of trade developed by Caliendo and Parro (2015) which in itself draws from the Eaton and Kortum (2002) theoretical framework. Since the model is based on comparative advantage, relative differences in technological efficiency drive the direction and magnitude of international trade flow. This section provides a summary of the model.

4.3.1 Household

Consider a world with N countries indexed by *n* (importer) and *i* (exporter). Each country has J sectors indexed by *j* (user) and *k* (source). In each country, there are a measure of Ln representative households that maximize utility by consuming final goods *Cjn* and supplies a unit of labor. Labour is mobile across sectors and immobile across countries. Each consumer supplying one unit of labour inelastically, earns a wage *w* and receives lump sum transfers from the government (coming from the tariff revenues). Furthermore, each consumer maximizes preferences over the sectoral final good, which is non-traded. There is perfect competition in all markets, therefore all market clears.

4.3.2 Intermediate Goods Producers

As in Dornbusch et al. (1977), in each sector *j*, there is a continuum of goods □ ϵ [0, 1]. Producers in each sector combine labour (*ljn*) and composite intermediates (*mk,jn*) from all countries and sectors to produce other tradable intermediate goods and non-tradable final goods used for domestic consumption.

The Cobb Douglas production function is given by:

$$q_n^j(w^j) = z_n^j(w^j)[l_n^j(w^j)]^{y_n^j} \prod_{k=1}^{J}[m_n^{k,j}(w^j)]^{y_n^{k,j}}$$

where *ϒkjn* captures the sectoral input-output linkages and denotes the share of materials from sector k used in the production of intermediate goods in sector j, with PJ*k* =1 *k,j n* = 1–*jn*. *Kj n* captures the heterogeneity in bilateral tariff reductions. *Jn* is the value-added share. The representative firm's problem is to minimize cost of supplying by choosing labour and the aggregate tradable goods, given factor prices *wn* and *pk n*.

Producers purchase inputs from the lowest cost suppliers. There are three factors that determine which country has the lowest cost: (i) factor prices and inputs cost (w, p) which are determined in equilibrium, (ii) exogenous trade costs between countries and (iii) level of productivity *zjn* (□). In particular, efficiency of producing good □ is a random draw from Frechet distribution with a location parameter □*jn* that governs a country's average productivity by sector, and _*j* is the sectoral trade elasticity estimate and represents the dispersion in productivity parameter. The fraction of goods for which the efficiency is lower than z is expressed as:

$$F_n^j(z) = \exp\left(-\lambda_n^j z^{-\theta^j}\right)$$

Trade in goods across countries is costly. There are two types of trade costs: observed ad valorem tariffs _ *jni* and unobserved iceberg trade costs *djni*. ˜ _*jni* = 1 + _ *jni*/100. Iceberg costs are defined in physical units according to Samuelson (1969) where by one unit of a tradable intermediates good in sector j from country i requires producing *djni* _ 1 units in i with *djnn* = 1. Non-tradable goods are assumed to attract infinite tariffs. Combining both trade costs yields:

$$K_{ni}^j = \bar{\tau}_{ni}^j d_{ni}^j$$

Therefore, a change in ad valorem tariff rates _ *jni* is perceived as a shock to productivity efficiency which changes the distribution of prices and wages, which in turn impacts suppliers' cost. Together, changes in the distribution of prices causes changes in world trade patterns and consumption across countries. From the first order condition, we can solve for the equilibrium price, trade share, total expenditure, and trade balance which are described in detail in Appendix III.

4.3.3 Gains from Trade and Welfare Effects Decomposition

Welfare gain is calculated from the equilibrium real wage per capita and the tariff revenues. Since the real wage equation provides more intuition, the following section focuses on that. There are three sources of gains from trade: (i) Final goods consumers who are paying lower relative prices and consuming more varieties, (ii) Intermediate users who are purchasing materials at a lower price, and (iii) Inter-sectoral linkages effect. Both the final goods consumers and intermediate goods users leads to increase in volume of trade while sectoral linkages capture trade diversion, a situation whereby domestic exporters are hedged out in a market because relative prices are higher in the third country. The change in real wage is defined as:

$$In\ \frac{\widehat{w}_n}{\widehat{P}_n} = \underbrace{-\sum_{j-1}^{J} \frac{\vartheta_n^j}{\theta^j} ln\ \hat{\pi}_{nn}^j}_{Final\ goods} \underbrace{-\sum_{j-1}^{J} \frac{\vartheta_n^j}{\theta^j} \frac{1 - y_n^j}{y_n^j} ln\ \pi_{nn}^{\hat{j}}}_{Intermediate\ goods} \underbrace{-\sum_{j-1}^{J} \frac{\vartheta_n^j}{y_n^j} ln \prod_{k-1}^{J} \left(\frac{\hat{P}_n^k}{\hat{P}_n^j}\right)^{y_n^{k,j}}}_{Sectoral\ linkages}$$

Where a variable *x*ˆ denotes the changes in x. This equation shows that all the general equilibrium effect on real wages can be identified from the change in the share of own spending on domestic goods produced in sector j, $\pi\hat{}j$, the changes in aggregate consumption prices $P\hat{}k/P\hat{}j$ and they all depend on the consumption expenditure share, α^j and the estimated trade elasticity, θ^j.

Welfare effects are measured by changes in real wage and consumption associated with moving from higher tariffs before AfCFTA and the counterfactual and can further be decomposed into sectoral terms of trade (ToT) effects and volume of trade (VoT) effects. Total differentiation of *Wn* and the equilibrium conditions of the model yields:

$$d\ in\ W_n = \frac{1}{l_n}\sum_{j=1}^{J}\sum_{i=1}^{N}\underbrace{(E_{ni}^{j} d\ ln\ c_n^{j} - M_{ni}^{j} d\ ln\ c_i^{j})}_{Terms\ of\ Trade} + \frac{1}{I_n}\sum_{j=1}^{J}\sum_{i=1}^{N}\underbrace{\tau_{ni}^{j} M_{ni}^{j}(d\ ln\ M_{ni}^{j} - d\ ln\ c_i^{j})}_{Volume\ of\ Trade}$$

4.4 DATA

The quantitative general equilibrium model has 27 African countries, 3 North American countries (including the United States), 5 South American countries, 9 Asian countries (including China), 5 European countries, and constructed the rest of Africa, Asia, Europe, South America, North America, and the rest of the world, making 54 countries in the sample. We calibrate a 54-county, 25-sector (tradable and services) version of the model to the year 2014. These countries together account for over 95 percent of trade in goods and services across countries. Data used for calibration are bilateral trade flows, bilateral tariff rates, sectoral outputs, sectoral value added, and input-output (IO) tables.

Bilateral trade data was obtained from the United Nations Commodity Trade Database (UNCOMTRADE), which reports exchange of goods and services at HS6 and HS4 aggregation level across 194 countries. The UNCOMTRADE has both traded goods for use as intermediate and traded goods for final consumption. The sectoral bilateral trade flows between the 54 countries and 10 sectors were constructed by first aggregating these HS6 products to ISIC rev 3.1 using the World Integrated Trade System (WITS) HS6 to ISIC rev 3.1 concordance. The bilateral trade data covers 2000, 2014, and 2018.

Effective tariff rates data were obtained from the United Nations Trade Analysis and information System (TRAINS) database. The simple average tariff rates were used to aggregate to 15 tradable sectors in a similar manner as the trade data. For example, the tariff rates of the food sector shown in Figure 20 are derived from the weighted average of the tariff rates of all commodities aggregated to the food sector.

Value added, gross output, and input-output tables are from the World Input-Output Database (WIOD) for OECD countries and from the EORA multi region input-output (MRIO) database for non-OECD countries.

4.5 QUANTITATIVE RESULTS

The model is calibrated to data in 2018 for 60 countries and 20 tradable and non-tradable sectors. We then introduce free trade for all African countries while leaving tariffs on non-African countries to be at 2018 level. While this report has implications for all countries in the sample, this report focuses on the effect of AfCFTA on Nigeria. Welfare effects are decomposed into volume of trade and term of trade at the sectoral level.

Table 9 reports change in wage and the aggregate welfare effects of free trade across African countries. Welfare effects are decomposed into terms of trade (ToT), effects of change in relative prices; and volume of trade (VoT), effect of growth in imports. As Table 9 shows, the welfare effect of AfCFTA is positive (1.55 percent); growth in volume of trade accounts for over 73 percent and Nigeria records a 1.43 percent increase in real GDP. Since Nigeria is a relatively small country in terms of GDP and global trade, tariff reductions on imports lower the price of imports while an increase in the supply of exports does not change the world price, therefore reduction in price of imports account positively to changes in welfare.

Surprisingly, Nigeria and South Africa, the top two economies in Africa in terms of GDP, record modest welfare effects compared to other African countries. AfCFTA raises real wage by 24 percent for Benin, 16.6 percent for Botswana, 8.89 percent in Burundi, and 14.3 percent for Tanzania. South Africa records an insignificant growth in real wage as a result of AfCFTA while Ethiopia records 10.6 percent decrease in welfare.

Decomposing the welfare effects by sector shows the sectoral contribution to the aggregate effects. Figure 21 reports the sectoral contribution from volume of trade and terms of trade effect. Our simulation result indicates that agriculture, mining, food, and machinery n.e.c. dilutes the overall gains from terms of trade as the price of export for these commodities decline relative to the price of their imports. Although there is growth in export of agricultural products, as shown in Figure 25, the term of trade deterioration in this sector dilutes the overall gains from trade and changes in real wage from the agricultural sector. Together, the agriculture, mining, food, and textile industries contribute about 37 percent to the deterioration in Nigeria's term of trade. Other manufacturing, wood, paper, and metal products account for over 90 percent of Nigeria's total gain from term of trade improvements and volume of trade.

Table 9: *Welfare Effects of AfCFTA*

Countries	Welfare	ToT	VoT	Change in Real Wage
Algeria	1.89%	0.926%	0.961%	2.83%
Angola	10.2%	7.37%	2.81%	12.5%
Benin	-1.05%	-7.71%	6.66%	24.2%
Botswana	7.28%	4.79%	2.49%	16.6%
Burkina Faso	3.9%	1.04%	2.86%	8.89%
Burundi	0.686%	-0.581%	1.27%	5.48%
Cote d'Ivoire	-0.00683%	-0.531%	0.524%	2.84%
Egypt	1.5%	0.336%	1.17%	2.99%
Ethiopia	8.11%	-10.9%	19%	-10.6%
Gambia	4.39%	-1.03%	5.41%	2.74%
Ghana	4.03%	1.72%	2.31%	6.54%
Kenya	1.08%	0.659%	0.419%	5.92%
Madagascar	2.34%	0.00965%	2.33%	14.1%
Mauritius	2.33%	1.41%	0.925%	5.98%
Morocco	2.59%	1.54%	1.05%	4.28%
Mozambique	2.19%	1.16%	1.03%	7.41%
Namibia	10.5%	4.36%	6.12%	33.1%
Netherlands	0.162%	-0.0838%	0.245%	0.541%
Nigeria	1.55%	0.416%	1.14%	1.43%
Qatar	0.653%	0.39%	0.263%	3.17%
Rep. of Korea	0.445%	0.0225%	0.422%	0.725%
Rest of Africa	2.38%	0.75%	1.63%	4.4%
Rest of Asia	0.0584%	-0.118%	0.177%	0.197%
Rest of Europe	-0.103%	-0.0906%	-0.012%	0.136%
Rest of North Am.	-1.24%	-1.55%	0.316%	2%
Rest of South Am.	0.278%	0.136%	0.143%	0.432%
ROW	0.181%	0.326%	-0.145%	0.734%
Rwanda	1.53%	0.925%	0.608%	6.64%
Sao Tome Principe	-0.308%	-12.3%	12%	4.89%

Countries	Welfare	ToT	VoT	Change in Real Wage
Senegal	1.7%	1.27%	0.428%	3.7%
Seychelles	6.17%	3.94%	2.23%	9.04%
South Africa	0.45%	0.222%	0.228%	0.876%
Uganda	-1.01%	-5.14%	4.13%	3.28%
Tanzania	5.85%	1.99%	3.86%	14.3%
Zambia	-0.328%	1.79%	-2.12%	9.5%
Zimbabwe	10.3%	-5.32%	15.7%	5.51

As shown in Figure 27, there is significant reduction in export prices of tradable goods. Changes range from 0.8 percent in electrical and machinery and 8.0 percent decline in prices of metal products, a sector that accounts for 13.3 percent in gains from term of trade. Tariff reductions on imports not only affect prices in that sector but, interestingly, impacts prices of non-tradable sectors, highlighting the importance of supply chains. Construction uses about 20 percent metal products in production, hence the drop in price of consumption as seen in Figure 27.

Table 10: *Changes in Imports from AfCFTA Tariff Reductions*

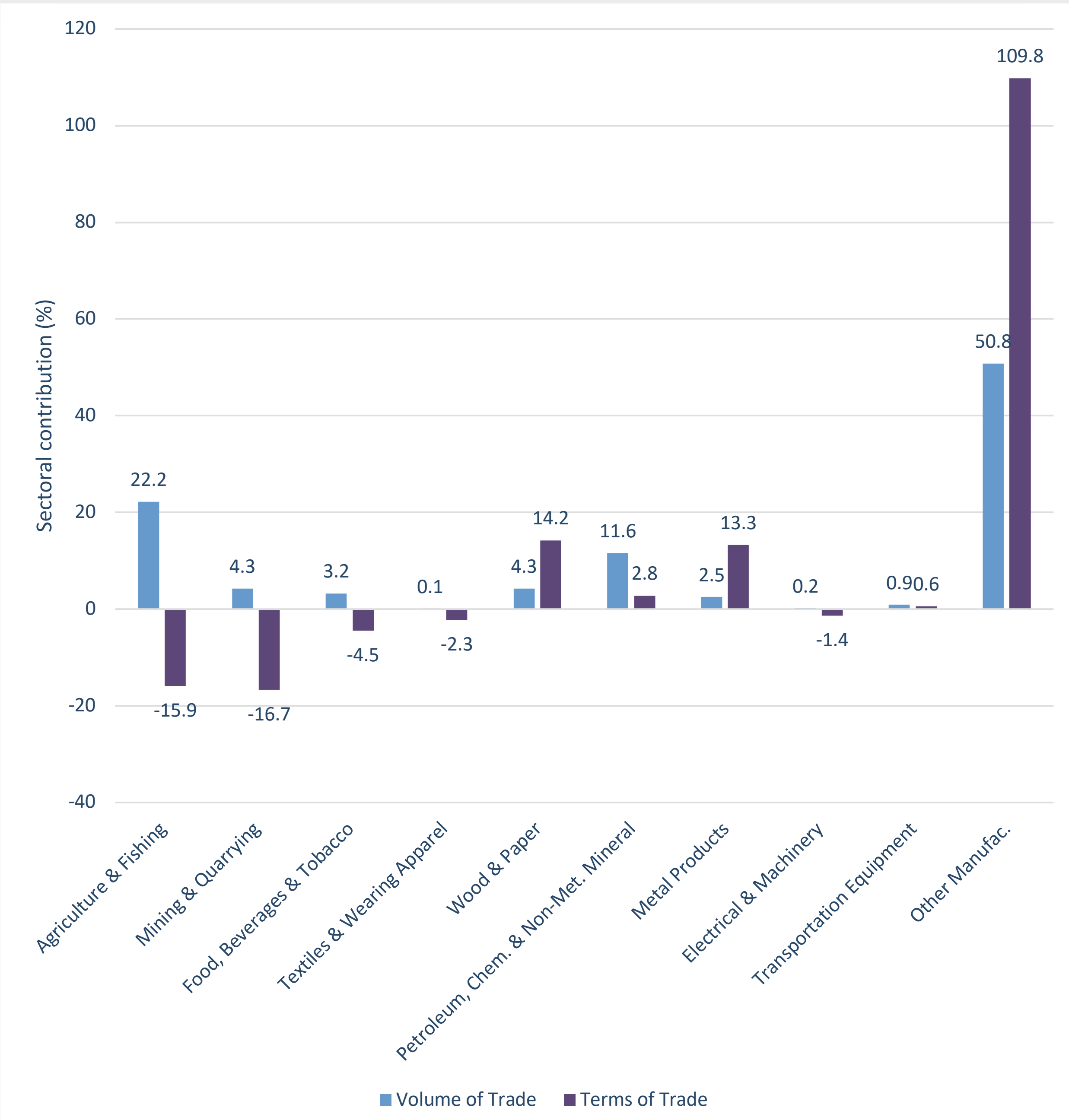
Country	Growth in Imports	Country	Growth in Imports
Algeria	16.80	Netherlands	92.73
Angola	-10.44	Nigeria	NaN
Argentina	28.04	Peru	6.44
Belgium	-0.09	Portugal	1.07
Benin	9.69	Qatar	-1.03
Botswana	-14.22	Rep. of Korea	-9.75
Brazil	35.28	Rest of Africa	-0.99
Burkina Faso	-26.27	Rest of Asia	17.65
Burundi	-28.08	Rest of Europe	70.56
Canada	-29.53	Rest of North Amer.	-22.26
Chile	-8.52	Rest of South Amer.	-5.70
China	-11.33	Rest of the World	2.08
Cote d'Ivoire	45.30	Russian Federation	16.37
Egypt	38.84	Rwanda	38.18

Country	Growth in Imports	Country	Growth in Imports
Ethiopia	183.95	Sao Tome and Principe	93.75
France	3.09	Senegal	15.39
Gambia	8.37	Seychelles	-19.50
Germany	22.38	South Africa	41.94
Ghana	-8.54	Spain	-9.82
India	47.82	Sweden	45.28
Indonesia	1.94	Switzerland	1.42
Italy	108.83	Thailand	60.32
Japan	100.96	Turkey	40.04
Kenya	48.52	USA	59.15
Madagascar	-5.0	Uganda	12.95
Mauritius	42.01	United Arab Emirates	9.01
Mexico	94.13	United Kingdom	-3.72
Morocco	58.32	United Rep. of Tanzania	-3.07
Mozambique	32.52	Zambia	-15.86
Namibia	-19.18	Zimbabwe	105.60

Further, we report the changes in Nigeria's import as a result of AfCFTA. Based on model predictions, Nigeria's imports from several African countries, including Botswana, Burundi, Ghana, and Namibia decline by more than 10 percent as well as imports from China and Canada by 29.5 and 11.3 percent, respectively. Nigeria's imports from Ethiopia triple, while imports from Italy (108.8 percent), Japan (100.96 percent), and Zimbabwe double. Imports from OECD and North America rise. Nigeria's imports from Italy, Japan, Netherlands, and the rest of Europe rise by 108.83 percent, 100.96 percent, 92.73, and 70.83, respectively.

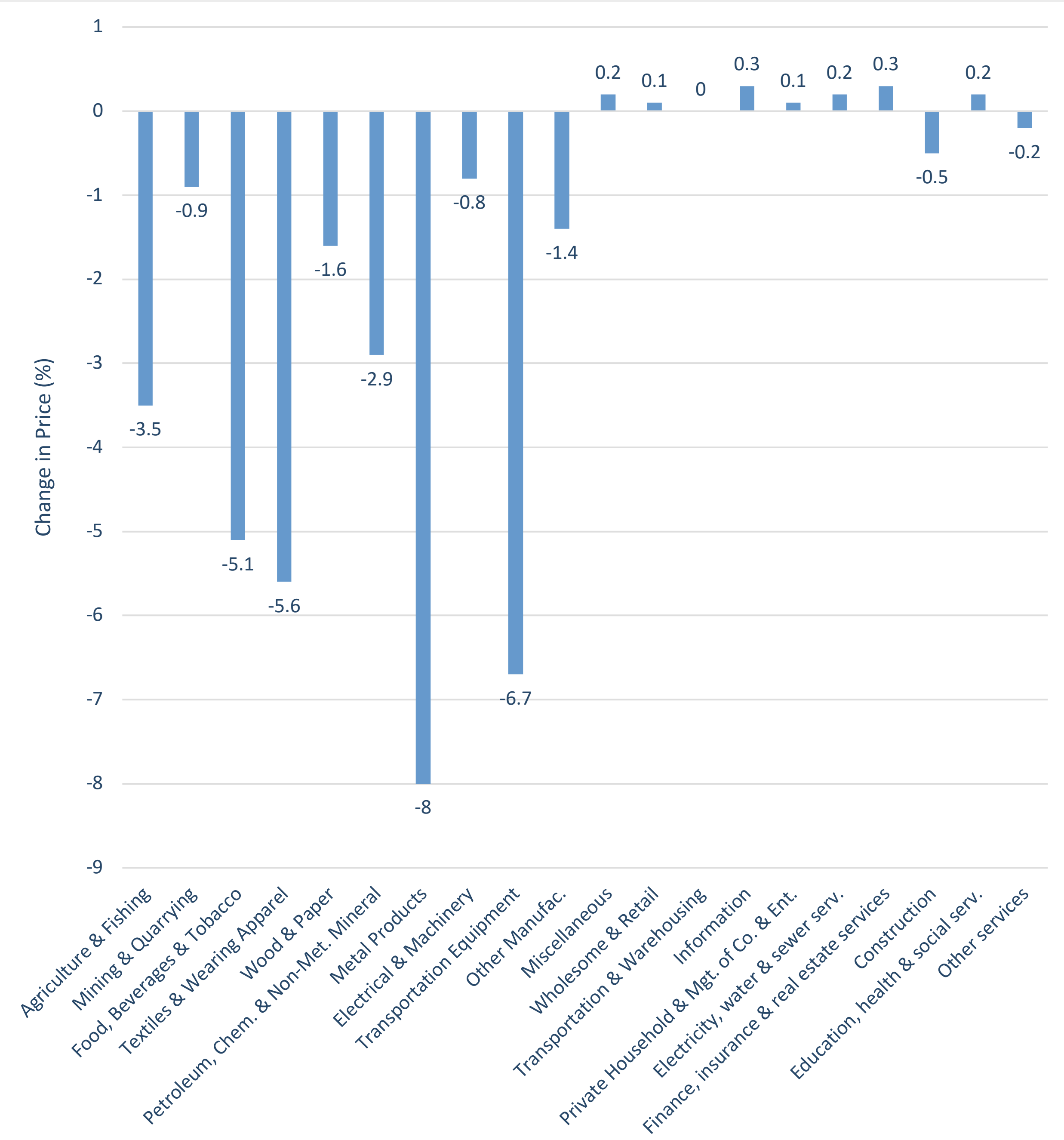
On export, Nigeria records growth in exports of agricultural products, food, electrical, and machinery products while exports decline significantly in the wood and paper industry.

Figure 25: *Sectoral Contribution*



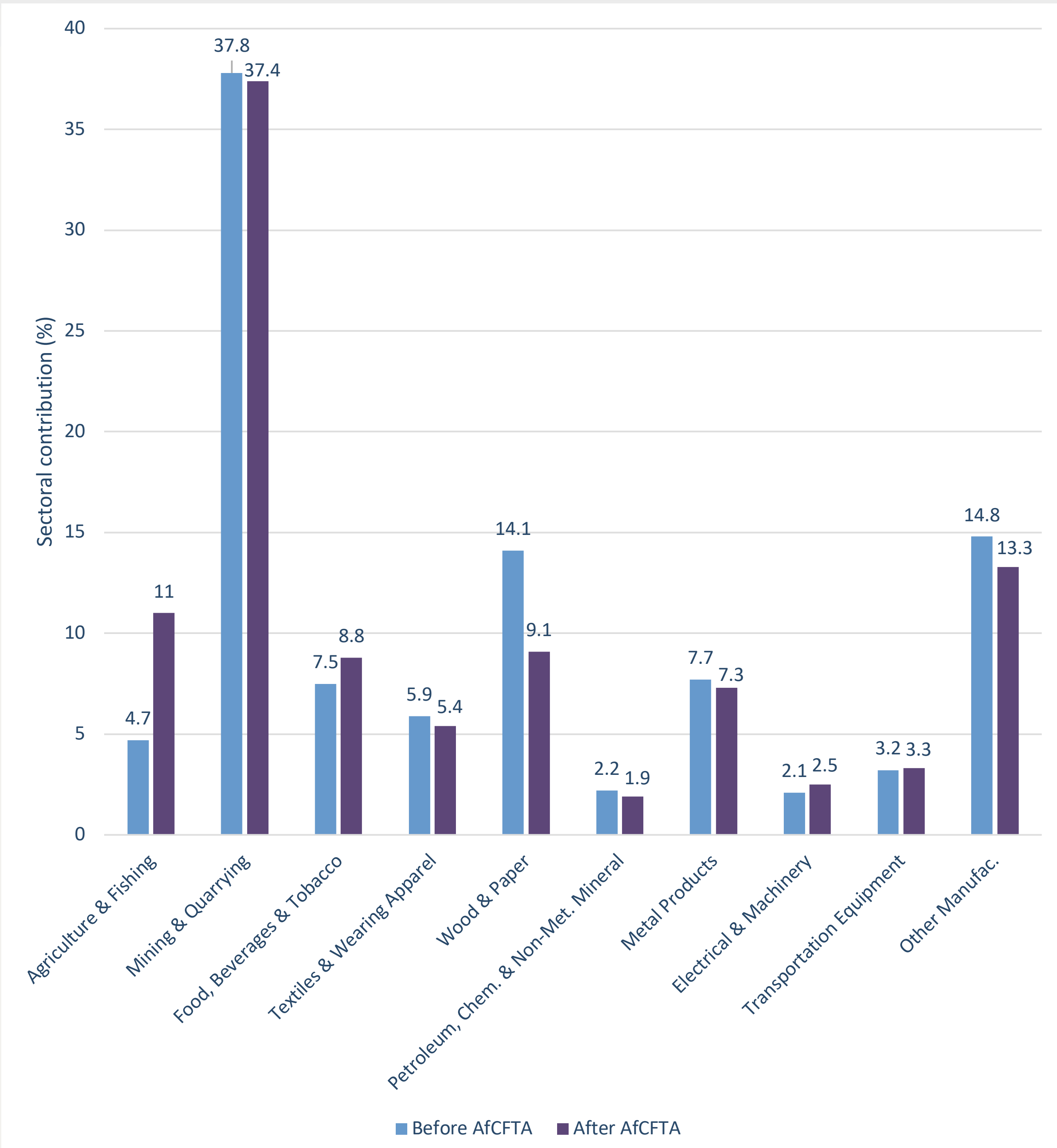
Source: *Based on simulation results, volume of trade contribution is calculated by dividing sectoral trade by total trade in all sectors. Terms of trade is calculated as difference in price of export and price of imports as a share of total price difference in all sectors. Each bar represents the share of changes relative to total. VOT and TOT bars should add up to 100.*

***Figure 26**: Change in Sectoral Prices*



***Source:** Based on simulation results, volume of trade contribution is calculated by dividing sectoral trade by total trade in all sectors. Terms of trade is calculated as difference in price of export and price of imports as a share of total price difference in all sectors. Each bar represents the share of changes relative to total. VOT and TOT bars should add up to 100.*

Figure 27: *Change in Sectoral Export Shares*



Source: *Based on simulation results, volume of trade contribution is calculated by dividing sectoral trade by total trade in all sectors. Terms of trade is calculated as difference in price of export and price of imports as a share of total price difference in all sectors. Each bar represents the share of changes relative to total. VOT and TOT bars should add up to 100.*

4.6 CGE MODEL CONCLUSION

This report quantitatively solves for the effects of free trade across the African region on Nigeria's economic performance and household welfare using a tractable analytical model of trade that is based on comparative advantage. Before AfCFTA, Nigeria faced higher bilateral tariffs on imports and exports from and to the Africa region. The model is calibrated to the year before trade policy. With tariff reductions, several forces are engaged: first, households pay a lower price on final demand, raising their welfare; firms and businesses pay lower prices on inputs, raising their productivity and possibly promoting exports. However, tariff reduction on countries in the same region accentuates the advantage of agile transportation infrastructure, leading markets and businesses to move to countries with lower cost of doing business and higher productivity.

Our result shows modest positive welfare gains to Nigeria with machinery, other transport, textile, and metal products as well as textile industries accounting for most of the positive effects on real wage. Sectors with large tariff reductions record a higher volume of trade. AfCFTA led to changes in pattern of trade flows across the African region. Among African countries with most gains from AfCFTA are Angola, Botswana, and Seychelles.

While the effects on labour market implications and household saving and consumption behavior are not captured in this report, this exercise provides useful insight on the sectoral impacts of this trade agreement. A dynamic general equilibrium model that has implications for housing saving and investment decisions provides an interesting follow-up as the role of multinational investment, foreign direct inflow, and firm productivity growth play important roles on the impacts of trade policy.

CHAPTER 5

Tying it All Together

5.1 DISCUSSION & POLICY IMPLICATIONS

Trade experts and development practitioners alike are overwhelmingly bullish about the potential of the AfCFTA Agreement to bring unprecedented prosperity to African economies. Indeed, there is a lot to be confident about. From increased consumer choice to greater availability of affordable productive inputs from across the continent, an effective implementation of the Agreement is likely to spur widespread development at a pan-continental level.

In this regard, the CGE model outlined in Chapter 3 quantitatively solves for the effects of free trade across the African region on Nigeria's economic performance and household welfare using a tractable analytical model of trade that is based on comparative advantage. Before AfCFTA, Nigeria faced higher bilateral tariffs on imports and exports from and to the African region. We calibrate the model to the year before trade policy.

Our result show positive, albeit modest, welfare gains to Nigeria with machinery, other transport, textile, and metal products as well as textile industries accounting for most of the positive effects on real wage. Predictably, sectors with large tariff reductions record higher volume of trade. In our model, the introduction of AfCFTA led to changes in pattern of trade flows across the African region. Among African countries with most gains from AfCFTA are Angola, Botswana, and Seychelles. Nigeria's absence from the highest expected beneficiaries helps explain the widespread skepticism emerging from different stakeholders in the economy in anticipation of the signing of the Agreement.

While the effects on labour market implications and household saving and consumption behavior are not captured in this report, we believe our CGE simulation provides useful insight on the sectoral impacts of this trade agreement. A dynamic general equilibrium model that has implications for housing saving and investment decisions provides an interesting follow-up as the role of multinationals investment, foreign direct inflow, and firm productivity growth play important roles on the impacts of trade policy.

The cautiously optimistic note highlighted in our macroeconomic CGE model is perhaps exceeded by the general buoyancy relayed by respondents to our on-the-ground survey of MSMEs. Particularly in larger firms – generally keener on engaging in international business operations – the data suggests that the benefits associated with market size expansion and the availability of lower input costs make Nigerian MSMEs confident of their chances to take advantage of the deal's implementation. Figures 13-15 denote this confidence by demonstrating business owners' general belief that they possess the necessary assets and capabilities to make the best of the opportunities created by the trade deal.

We must not, however, neglect the very real concerns that exist and may prevent Nigerian MSMEs from positioning themselves to take full (or any) advantage of the AfCFTA Agreement. As this report seeks to emphasise, MSMEs are the lifeblood of the Nigerian economy. It is, therefore, hard to imagine a scenario where the signing of the AfCFTA results in beneficial trends in the national economy without an active engagement with, and betterment of, MSMEs' ability to take advantage of the deal's provisions. As our survey results highlight, a majority of Nigerian MSMEs are not currently in a position to expand their business operations via the AfCFTA Agreement, thus severely curtailing its foreseeable upsides.

Perhaps the most salient – and worrying – finding in our survey is the strong evidence of a multi-pronged information deficit, which places an artificially low ceiling on the expected uptake of the deal among MSMEs. The first, and most concerning, feature of the information deficit is a striking lack of awareness about the deal itself: some two-thirds of business owners reported they were not aware of the existence of the AfCFTA. In line with previous international studies (for ex. Arudchelvan & Wignaraja, 2015), business size and access to information are shown in our results to be positively correlated. While micro and small enterprises reported unusually similar rates of unawareness, medium-sized enterprises were significantly more likely to know of the deal's existence – a necessary first step to ensure its use. The unfamiliarity with the AfCFTA's existence that micro and small enterprises reported, however, remains particularly worrying given that within the set of MSMEs, micro and small businesses represent an overwhelming majority across the country (see Table 2).

The information gap that exists between smaller firms and larger ones (even within the "MSME" categorization) points to an ineffective policy communication strategy that has been unable to overcome the structural obstacles that MSMEs face in acquiring knowledge. This extends to other information deficits highlighted in our survey results concerning usage of previously signed preferential trade agreements, and the reasons for the lack thereof. The fact that only 11.2 percent of respondents reported trading via the ETLS provisions of ECOWAS, underscores the insufficient care given to information dissemination efforts in the implementation strategy of free trade agreements in Nigeria. While low MSME-uptake of FTAs is overwhelmingly common globally, the proportions uncovered by our survey data are remarkably small, even in comparison to results from other countries at a similar stage of development. For instance, a 2011 survey conducted by the Asian Development Bank reported that some 28 percent of Thai and Filipino MSMEs used FTA preferences in their operations (Kawai & Wignaraja, 2011).

Technical knowledge is another key component of the information deficit, and is known in the literature to be a fundamental obstacle to MSME-uptake of FTA provisions – an axiom supported in our data. We find that insufficient understanding of market opportunities, difficulties in compliance, low comprehension of rules of origin, and general procedural complexity all contribute to low uptake of previously-agreed FTAs, and are among the principle concerns existing surrounding respondents' own ability to effectively expand their businesses through the AfCFTA Agreement. This is even the case among the minority of MSMEs surveyed that declared knowledge of the deal (and therefore had an opinion on its potential challenges) in the first place.

Information deficiencies are endemic to MSMEs by their very nature (WTO, 2016). Due to their small scale, the majority of MSMEs are devoid of a formal institutional structure that would allow them to invest labour hours into the acquisition of knowledge. In contrast, large firms are more likely to have dedicated resources for advertising, market research, and developing/enhancing distribution networks, which generate the requisite knowledge of market opportunities that permit the utilization of FTAs.

In addition to MSME's unconducive organizational structures, our survey, in line with the literature, also provides evidence on the cost of information acting as a significant trade barrier (for ex. Anderson & Wincoop, 2004). Since information costs are independent of the value and volume of trade, the costs are proportionately high for MSMEs due to their inherently low volumes. Market research and the acquiring of technical knowledge on matters of regulatory compliance thus entail sunk costs prohibiting MSME's export participation.

Our survey finds, therefore, that policy interventions to minimize these deficits are crucial for a successful implementation of the Agreement – in line with the literature's findings in other contexts (see, for ex. Vonk et al, 2015). There is a strong need for programmes enhancing information access for MSMEs that otherwise risk remaining incapable of navigating a multitude of procedural issues, such as standards and labelling requirements, and RoOs – not to mention the risk of them remaining in the dark about the very existence of the deal itself.

Here, tailoring the knowledge dissemination strategy to the Nigerian context is essential. In the developed countries, access to trade-related information is often considered easily acquired through digital sources. In that regard, the implementation of some North-North FTAs (ex. EU-Japan), as well as those involving developing signatories at a later stage of development than Nigeria (ex. CPTPP[2]), have demonstrated general success in setting up effective platforms via public websites collating information on these agreements, such as chapter summaries, in an accessible manner (UK Trade Policy Observatory, 2020).

[2] The mega block CPTPP has a dedicated chapter for SMEs stating that each member shall self-establish or self-maintain a website with the information on agreement, including information designed for SMEs. The agreement has a provision for instituting a 'Committee on SMEs' to apprise the benefits of the agreement, facilitate programs for their development and integration into global supply chains, and provide information for monitoring the relevant implementation of the agreement. (Tandon, 2020)

In this regard, the African Import-Export Bank (Afreximbank) has already teamed up with the International Trade Centre (ITC) to launch a training programme that will run on ITC's SME Trade Academy online platform. The scheme will be piloted in Nigeria, Rwanda, and Côte d'Ivoire and launched in close collaboration with trade promotion organizations from the three selected pilot countries. While this is encouraging and demonstrates understanding of the knowledge gap that exists, its exclusive focus on internet-based training is potentially problematic.

Nigeria has a relatively high digital penetration in comparison to regional neighbours. Nevertheless, internet use among Nigerians stood at just 26 percent in 2016, highlighting the insufficiency of a purely digital knowledge dissemination strategy (World Bank, 2019). MSMEs must be assisted through specialized export coaching programmes (ECPs) that have demonstrated success at an international level, and go beyond the mere facilitation of access to information online (CBI, 2015). Industry-specific training in regulatory compliance, in addition to support in generating real-time market assessments to uncover international demand for MSME products, must also be considered in order to fill the information gap MSMEs report. Moreover, generating enthusiasm for trade among MSMEs themselves via, for instance, the promulgation of success stories demonstrating the potential upsides of the initial investment into knowledge acquisition, can serve as a powerful stimulant to business owners and generate greater MSME engagement with the AfCFTA.

In addition to highlighting a profound, multi-dimensional information deficit as the foremost obstacle to MSME engagement with international markets via the AfCFTA Agreement, respondents noted a number of other challenges relating to Nigeria's general business environment that pose a threat to their ability to effectively make use of the AfCFTA Agreement. These challenges are familiar ones. Nigeria came in at number 131 in the World Bank (2020) Ease of Doing Business rankings – a ranking weighed down by even lower scores in sub-components such as "access to electricity" (169th) and, of particular salience to this report, the "ease of trading across borders" where Nigeria ranks 179th globally.

Considerations regarding the general quality of business infrastructure ranging from electrification to road and rail transport emerge in both chapters 2 and 3 of this report. Along these lines, our CGE model clarifies that tariff reductions on countries in the same region accentuate the advantage of agile transportation infrastructure such that markets and businesses move to countries with lower cost of doing business and higher productivity. The decadence of Nigeria's infrastructure, therefore, poses a threat to the potential of AfCFTA to benefit the Nigerian economy at large.

These concerning difficulties for businesses are strongly reflected in our survey results. For instance, all four sectors surveyed report policy to enhance access to electricity as being among the most required to ensure their businesses' ability to engage in international trade (see Appendix II, Figures A-E). This is mirrored by the results in the data disaggregated by firm size, although larger firms declared being more in need of reliable electrification than did smaller ones. Concerns about electricity in Nigeria are widespread and have been raised in numerous contexts not just specific to MSMEs. Nevertheless, our findings make it worth reiterating that investing heavily in guaranteeing a stable power supply is paramount for the competitiveness of Nigerian producers – even more so now that they could face increased regional competition from the reduction of protections implied by the AfCFTA's implementation.

A similar story can be told about Nigeria's severe infrastructure deficit. The national transport network has, over many years, fallen into disrepair in large part due to decades of under-investment in critical infrastructure. While the road network spans nearly 200 thousand kilometers, the majority is unpaved and in dire need of maintenance, exacerbating crippling urban congestion and cross-country cargo travel times. The country's 3,500km rail network has also deteriorated, with cargo volumes falling to all-time lows in the early 2000s, exacerbating highway maintenance challenges, and weighing on trade and economic growth (OBG, 2018). It is no surprise, therefore, that our survey found infrastructural investment to be among the top perceived priorities for MSMEs (see Appendix II). Like with electricity, this result underscores the need for high levels of investment to generate business environments suited to highly competitive international trade.

Affordable access to finance, particularly in light of the current COVID-19 pandemic and the revenue shortage resulting from falls in demand, also landed high on the priority list (and perceived obstacles to AfCFTA use list) among respondents. When asked about preferences on the form of government support during the pandemic, a majority of MSMEs across all sectors suggested accessible government loans would be most useful (See Figure 19, and Appendix II). This reflects pre-pandemic limitations as well: a 2016 NBS survey found that 73 percent of respondents listed finance as their top priority for assistance (Tom et al, 2016). Policy to accommodate these perceptions, we believe, would not only be optimal in helping businesses confront short-term COVID-related loss of sales, but would also put these enterprises in a position to better equip themselves to achieve long-term sustainability through a diversified and expanded international market, providing them with the minimum necessary capital to acquire knowledge and technical knowhow.

Finally, while total reliance on digitalisation and e-solutions is not sufficient in a Nigerian context, the realities of COVID-induced social distancing and diminished footfall requires creative approaches to deal with the low levels of digitalization. In this regard, policymakers and donors alike should seek to complement access to finance and AfCFTA-specific knowledge dissemination with initiatives to promote e-market linkages for MSMEs in the post-COVID period. This could take forms inspired by current policies being unrolled in other developing contexts with similarly low levels of digital penetration like India, where the government has proposed using e-market linkages as replacements to trade fairs and exhibitions (GOI, 2020).

Actionable Plans for Government

The implementation of AfCFTA will require targeted, intelligent government intervention strategies. The findings in our report suggest the following priorities:

1. Develop a context-specific awareness dissemination strategy
    - This report's findings suggest a high level of unfamiliarity with the AfCFTA's existence. MSMEs will not be able to prepare effectively, let alone take full advantage of, AfCFTA without prior awareness.
    - Special attention should be paid to non-digital dissemination strategies to ensure full reach of Nigerian businesses irrespective of their technological participation levels.
    - Partnerships should be developed with local BMOs and business group representatives to better assess how best to engage entrepreneurs.
2. Develop a context-specific training programme
    - Many MSMEs are often disenfranchised from international trade as a result of the complications associated with compliance to FTAs.
    - Ensuring localised training programmes through partnerships with the private sector and international donors can help fill the technical skills gap that will hamper MSME uptake of AfCFTA.
3. Investment in the creation of a more competitive business environment
    - Electrification and transport infrastructure deficiencies are particularly problematic in Nigeria and risk putting Nigerian businesses at a significant disadvantage in relation to continental competitors.
    - A targeted, strategic investment plan should therefore be a priority.
4. Facilitate access to finance for businesses
    - A strong re-emergence from the COVID-19 crisis is a necessary condition for successful uptake of the AfCFTA Agreement.
    - A vast majority of MSMEs declare that easier-to-access business loans are the key policy requirement to ensure post-COVID enterprise sustainability.

5. Evaluate the progress on AfCFTA
    - The creation of a platform for regular monitoring and evaluation of progress on AfCFTA is required at national and sub-regional levels.

Actionable Recommendations for Business Representatives

1. Active participation and partnership with government
    - Given the weakness in information sharing and awareness about AfCFTA, more direct engagement of BMOs will be crucial. This can include within the design and medium of messaging as well as direct engagement of BMOs in advocacy and public awareness campaigns.
    - BMOs can shape the direction and structure of the trade agreement in a way that supports their members and engenders Nigerian economic development. This is dependent on their active engagement in deliberation and discussion on key issues arising from the negotiation.
    - BMOs unifying around common causes and factors that limit the benefits annexed from AfCFTA will be crucial.
2. Establish channel of support for members
    - BMOs need to work with their members on an individual basis to understand the benefits that they can tap into with AfCFTA, while at the same time empowering them with knowledge on mitigating the likely threats.
    - A dedicated line of support to communicate with and educate BMO members needs to be set up.
3. Partnership to mitigate threats:
    - There are many steps that firms on their own can take to address threats. For instance, upscaling business management skills and tapping into human resources made available by AfCFTA are things that depend on firms' decision or indecision.
    - An experience-sharing platform to highlight what works and why will be vital. Both formal and informal partnerships can help support fragile firms to withstand the increased competition that AfCFTA will create.
    - Interestingly, the recent Companies and Allied Matters Act (2020) has set the condition for ease of vertical and horizontal business integration in Nigeria. Exploring all available avenues to improve resilience and competitiveness of local businesses is a crucial area that will

require support from BMOs.

- A platform to track progress of AfCFTA in terms of awareness and economic impact on BMOs should be set up. Firms that are negatively impacted should be reintegrated and supported to compete favourably.
- Given that low comprehension of rules of origin contribute to low uptake of previously agreed FTAs, BMOs need to participate actively on the discussion on how to streamline this issue. This will be key in removing obstacles that apparently impacted other FTAs.

4. Partnership for standardization:
   - BMOs need to partner with specific agencies such as SON and NAFDAC to ensure adherence to standards. This will boost the capacity of Nigerian businesses to compete in AfCFTA.
5. Partnership with donors:
   - BMOs need to partner with donors to develop a context-specific information dissemination strategy to allow MSMEs to overcome their current knowledge deficit.
   - Donors can also support BMOs in terms of standadization and meeting the process requirements of AfCFTA.
   - Targeted funding to support the government and BMOs in trade facilitation and other modalities for aid to trade.

5.2 CONCLUSION

Africa is on the verge of its biggest integrationist step in its post-colonial history. When the AfCFTA Agreement is set in motion, it will be the largest FTA in the world by number of signatories, and will establish a market of 1.2 billion people, forecasted to grow rapidly in the coming decades. While the possibilities emerging from the Agreement abound, certainty about its effects on various facets of African economies is inevitably lacking and caution is needed.

This report has sought to generate knowledge about how the forthcoming AfCFTA will impact the Nigerian economy, both at a macroeconomic scale and at a more localised level through the lens of Micro, Small, and Medium enterprises across Nigeria. The focus on MSMEs is especially important as they represent the very core of the Nigerian economy, contributing to the employment, and hence sustenance, of some 75 percent of the Nigerian workforce. Ensuring an optimal outcome for MSMEs therefore must be a paramount target in policymakers' efforts to implement the AfCFTA nationally.

To do so, we approached the AfCFTA's effects on Nigeria from tw complementary angles. We first sought to gauge MSME preparedness and perceptions about the deal. This was done through a comprehensive survey of MSMEs covering Nigeria's diverse demographic and socioeconomic regions. To supplement the subjective findings garnered from MSMEs themselves, we carried out a higher level Computable General Equilibrium simulation to estimate how Nigeria's macroeconomy, in terms of changes in wage and the aggregate welfare effects, and origins of imports will be affected by the triggering of AfCFTA.

This report found that, generally, optimism about the deal's effect on the economy is justified. Aggregate welfare is predicted to moderately increase, an effect mirrored by the moderately optimistic subjective results of our survey.

However, a number of challenges still remain that may stifle the unlocking of AfCFTA's full potential for the Nigerian economy. To begin with, Nigerian MSMEs are overwhelmingly impaired by information deficits. Moreover, the knowledge challenge endemic among small businesses is compounded by difficulties faced by all businesses in the Nigerian environment – unreliable electricity and high transportation costs chief among them.

Without an active strategy to ensure MSMEs are put in a position to increase their international operations via the Agreement, it is likely that the promises and aspirations attached to AfCFTA will remain just that. We therefore argue that the Federal Government, as well as like-minded donors, should endeavour to develop a context-specific information dissemination strategy to allow MSMEs to overcome their inherent knowledge deficit. This should be compounded with easier access to finance to allow MSMEs to invest in gathering information, particularly now when business savings will be especially depleted as a result of the COVID-19 pandemic's hit on consumer demand. Finally, a general plan to improve the business environment is central to ensuring the competitiveness of Nigerian enterprises in the future. Exposing Nigerian MSMEs to strong regional competition without putting them in a condition to engage in a fair competitive battle hardly seems like a winning strategy.

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APPENDIX I: FIRM SAMPLING BREAKDOWN BY STATE

Table A: *Distribution of Aggregate Sample Size Across Abia State*

Sectors	Micro Enterprises Sample	Small Enterprises Sample	Medium Enterprises Sample	Total Sample Size
Wholesale/Retail Trade	36 respondents	62	11	109
Agriculture	4 respondents	7	8	19
Manufacturing	29 respondents	45	9	83
Services	25 respondents	86	28	139
Total	**94**	**200**	**56**	**350**

Table A shows the disintegration of firms across economic sectors and business categories in Abia state. The sample randomly selected 109 firms from wholesale/retail, 19 firms from the agriculture sector and 83 from the manufacturing sector, and 139 from the services sector. Across the business category, 94 enterprises were categorized under Micro, 200 under small, and 56 under medium enterprises.

Table B: *Distribution of Aggregate Sample Size Across Anambra State*

Sectors	Micro Enterprises Sample	Small Enterprises Sample	Medium Enterprises Sample	Total Sample Size
Wholesale/Retail Trade	40 respondents	75	12	127
Agriculture	13 respondents	17	7	37
Manufacturing	26 respondents	53	13	92
Services	28 respondents	73	9	110
Total	**107**	**218**	**41**	**366**

Table B shows the disintegration of firms across economic sectors and business categories in Anambra state. The sample randomly selected 127 firms from wholesale/retail, 37 firms from the agriculture sector, 92 from the manufacturing sector, and 110 from the services sector. Across the business category, 107 enterprises were categorized under Micro, 218 firms under small, and 41 firms under medium enterprises.

Table C: *Distribution of Aggregate Sample Size Across Abuja*

Sectors	Micro Enterprises Sample	Small Enterprises Sample	Medium Enterprises Sample	Total Sample Size
Wholesale/Retail Trade	48 respondents	102	17	167
Agriculture	10 respondents	14	2	26
Manufacturing	10 respondents	21	3	34
Services	25 respondents	56	99	90
Total	**93**	**193**	**31**	**317**

Table C shows the disintegration of firms across economic sectors and business categories in the FCT, Abuja. The sample randomly selected 167 firms from wholesale/retail, 26 firms from the agriculture sector, 34 from the manufacturing sector, and 90 from the services sector. Across the business category, 93 enterprises were categorized under Micro, 193 firms under small, and 31 firms under medium enterprises.

Table D: *Distribution of Aggregate Sample Size Across Kano State*

Sectors	Micro Enterprises Sample	Small Enterprises Sample	Medium Enterprises Sample	Total Sample Size
Wholesale/Retail Trade	23	51	10	84
Agriculture	8	7	6	21
Manufacturing	22	43	8	73
Services	23	51	10	79
Total	**76**	**147**	**34**	**257**

Table D shows the disintegration of firms across economic sectors and business categories in the Kano state. The sample randomly selected 84 firms from wholesale/retail, 21 firms from the agriculture sector, 73 from the manufacturing sector, and 79 from the services sector. Across the business category, 76 enterprises were categorized under Micro, 147 firms under small, and 34 firms under medium enterprises.

Table E: *Distribution of Aggregate Sample Size Across Lagos State*

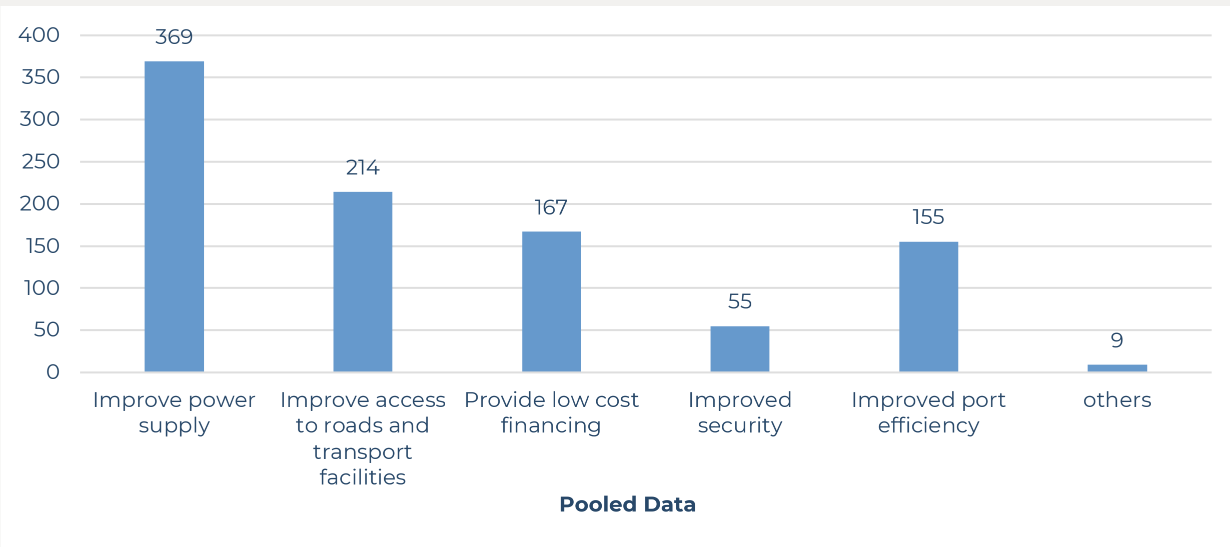
Sectors	Micro Enterprises Sample	Small Enterprises Sample	Medium Enterprises Sample	Total Sample Size
Wholesale/Retail Trade	39	98	43	180
Agriculture	17	16	12	45
Manufacturing	31	60	26	117
Services	26	88	58	172
Total	**113**	**262**	**139**	**514**

Table E shows the disintegration of firms across economic sectors and business categories in the Lagos state. The sample randomly selected 180 firms from wholesale/retail, 45 firms from the agriculture sector, 117 from the manufacturing sector, and 172 from the services sector. Across the business category, 113 enterprises were categorized under Micro, 262 firms under small, and 139 firms under medium enterprises.

APPENDIX II: NATIONAL MEASURES TO MITIGATE THREATS & MAXIMIZE AFCFTA BEMEFITS

Results of the analysis of the surveyed data as presented below shows that MSMEs have high expectations from the Nigerian government in preparations for the AfCFTA. In order to reposition the nation and businesses to maximize the benefits of AfCFTA and mitigate potential negative effects of the policy, infrastructural decadence must be addressed. Other measures suggested by the sampled firms include improved power supply, improved access roads and transportation, low cost financing, improved security, and improved port efficiency.

Figure A: *Beliefs about Nigerian Government's responsibilities to mitigate the potential threats and maximize the potential benefits AfCFTA*



The respondents were further disaggregated into enterprise sectors to better understand their expectations. A higher proportion of the respondents from the agricultural sector, manufacturing sector, services sector, as well as the wholesale and retail trade sector emphasized that the power supply must be improved by the government. This implies that the current state of business infrastructure, especially power supply, is detrimental to the productivity of MSMEs in Nigeria and could jeopardize their effective participation in AfCFTA.

Figure B: *Agricultural Sector Beliefs about Nigerian Government's responsibilities to mitigate the potential threats and maximize the potential benefits AfCFTA*

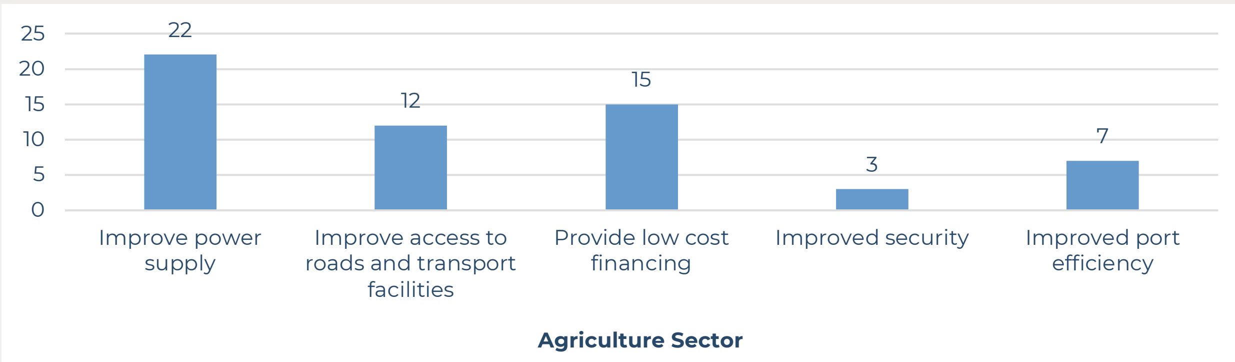


Figure C: *Manufacturing Sector Beliefs about Nigerian Government's responsibilities to mitigate the potential threats and maximize the potential benefits AfCFTA*

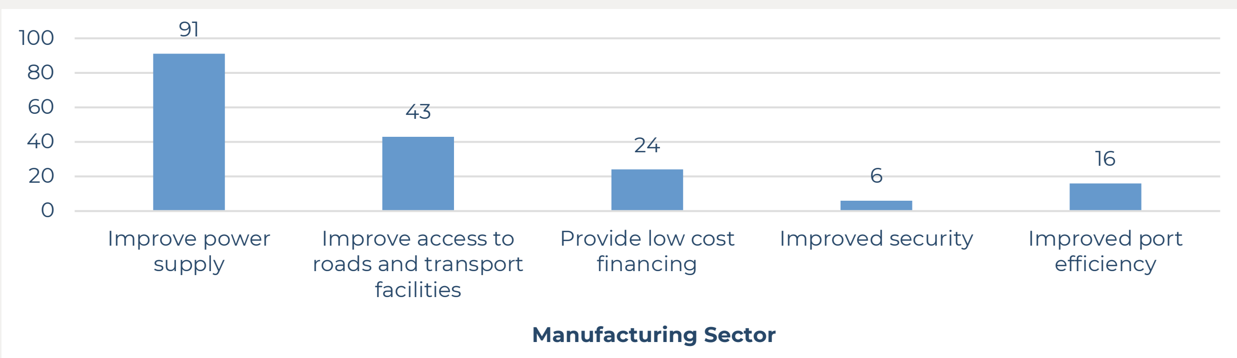


Figure D: *Services Sector Beliefs about Nigerian Government's responsibilities to mitigate the potential threats and maximize the potential benefits AfCFTA*

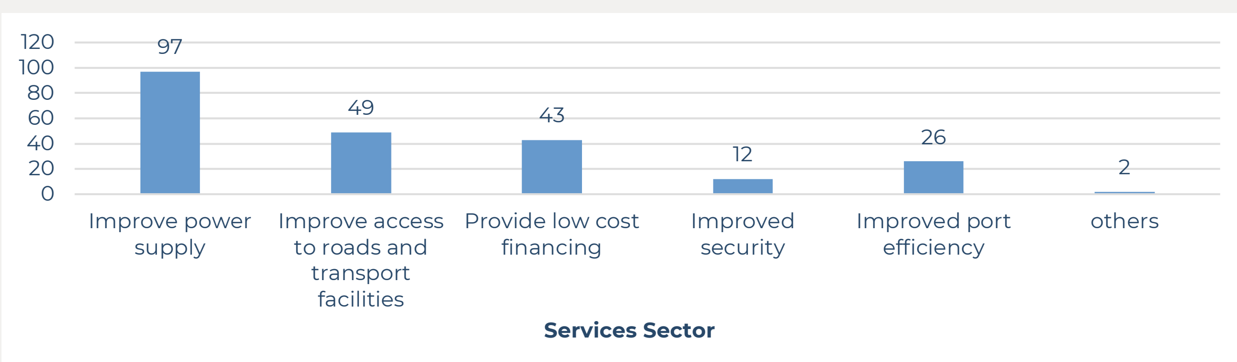


Figure E: *Wholesale/retail Sector Beliefs about Nigerian Government's responsibilities to mitigate the potential threats and maximize the potential benefits AfCFTA*

MSME views on government support to COVID-19 pandemic relief

Finally, MSMEs were also asked about the most relevant government relief strategies to address the adverse effects of the pandemic on their business. The disaggregated results by enterprise size are displayed in Figures F-H below.

Figure F: *Micro Enterprises' Desired COVID Relief*

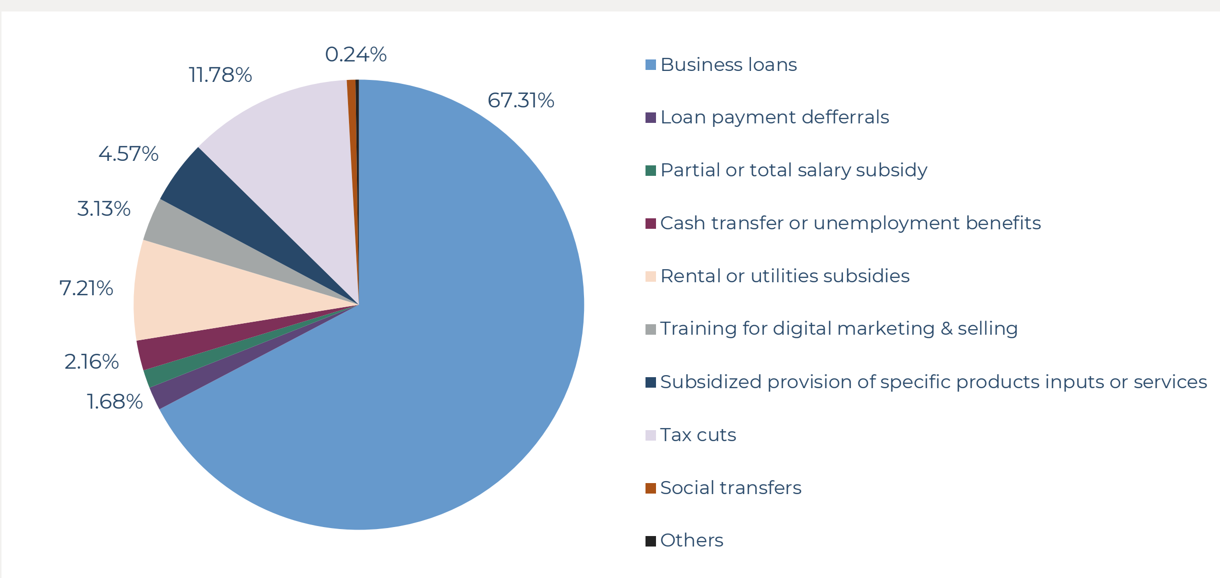


Figure G: *Small Enterprises' Desired COVID Relief*

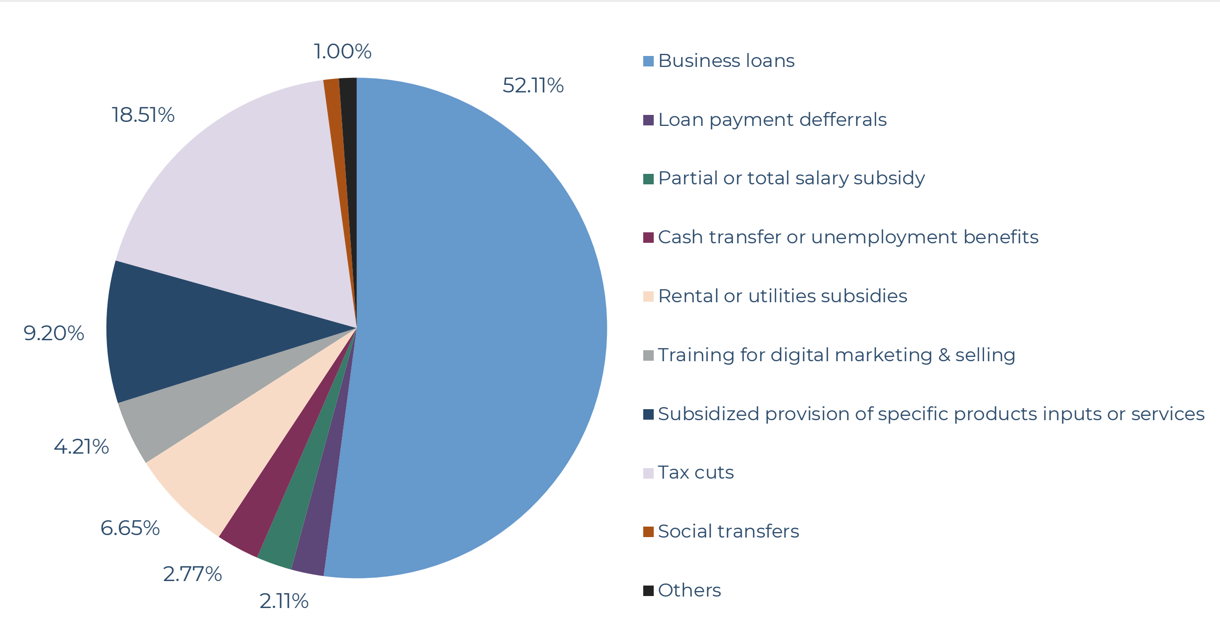
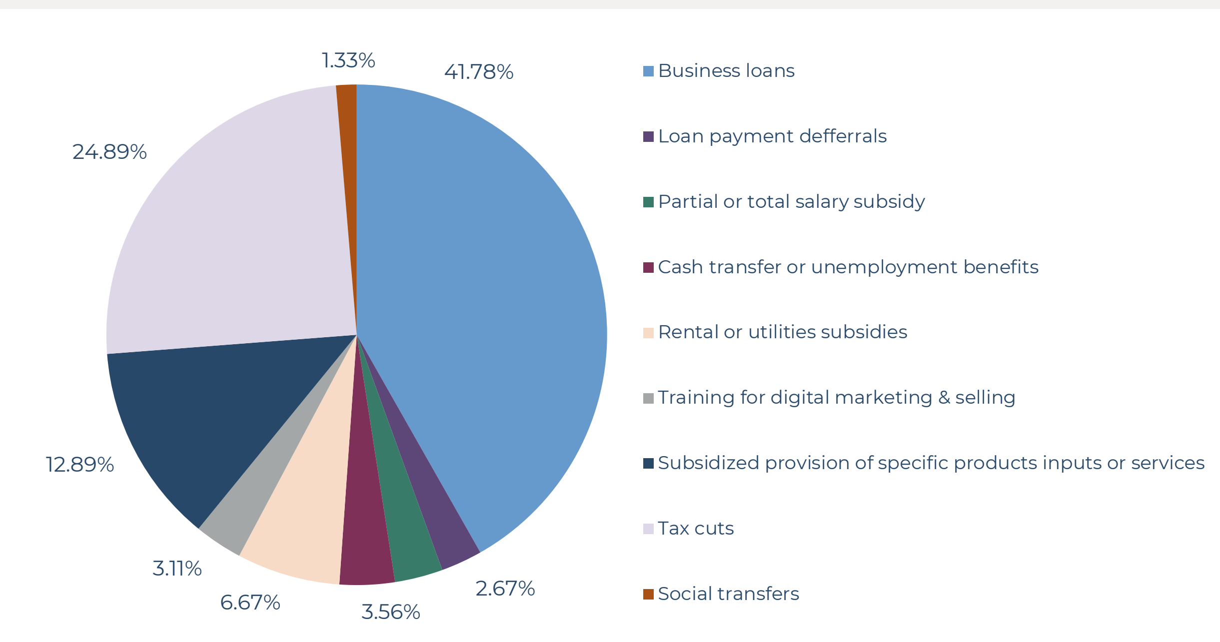


Figure H: *Medium Enterprises' Desired COVID Relief*



APPENDIX III

Solving the Model in Relative Changes

Following Dekle et al. (2008), the policy evaluation comes from comparing the equilibrium in 2014 before AfCFTA (under policy τ') with the equilibrium after the AfCFTA Agreement. One key advantage for using this model is that we do not need to calibrate the initial average productivity and trade costs. Rather, we use the actual data from 2014 and compare it with the counterfactual equilibrium. Re-writing the key equations of the model in 'hat' form where a $\hat{x}$ denotes X'/X, and X' is the new counterfactual variable, and X is the existing variable from the data, yields the equilibrium conditions. Together, we solve for N wage equation in N unknown; the trade share across countries; and price are J × N × N equations in J × N × N unknown. Using cost of inputs equations together with equations 5, 6, 7, and 8, the equilibrium conditions in relative changes are:

Cost of Input Bundles:

$$c_n^{\hat{j}} = w_n^{\hat{\gamma}_n^j} \prod_{k=1}^{J} \hat{P}_n^{k^{\gamma_n^{k,j}}}$$

Price Index:

$$\hat{P}_n^j = A^j \left[\sum_{i=1}^{N} \gamma_i^j \left(\hat{c}_i^j \hat{K}_{ni}^j \right)^{-\theta^j} \right]^{-\frac{1}{\theta^j}}$$

Bilateral Trade Shares:

$$\hat{\pi}_n^{j\prime} = \sum_{k=1}^{J} \gamma_n^{j,k} \sum_{i=1}^{N} X_i^{k\prime} \frac{\pi_{in}^{k\prime}}{1 + \tau_{in}^{k\prime}} + \vartheta_n^j I_n'$$

Trade Balance:

$$\sum_{j=1}^{J} \sum_{i=1}^{N} X_n^j \frac{\pi_{ni}^{j\prime}}{1 + \tau_{ni}^{j\prime}} - D_n = \sum_{j=1}^{J} \sum_{i=1}^{N} X_i^{j\prime} \frac{\pi_{in}^{j\prime}}{1 + \pi_{in}^{j\prime}}$$

Taking the Model to Data

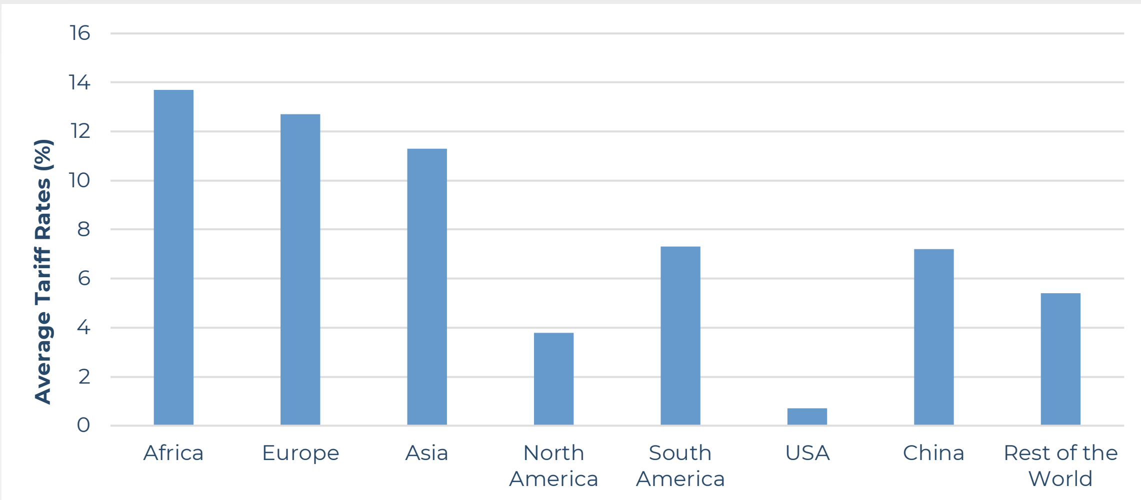
Solving the model in relative changes reduces the data required to calibrate the model. The data needed to quantify the effect of China joining the WTO are two sets of tariffs (τ and τ'), bilateral trade shares (π_{ni}^{j}), value added ($w_n L_n$), share of intermediate consumption ($\Upsilon_n^{k,j}$), and sectoral dispersion of productivity (θ^{j}) – otherwise called trade elasticity. The estimation method for the trade elasticity (θ^{j}) and result is shown in section 3.5. With this data, we calibrate the values forπ_{ni}^{j}, Υ_n^{j} , $\Upsilon_n^{k,j}$and α_n^{j} to year 2000. For tractability and analytical convenience, we aggregate the model to 25 countries – including a constructed rest of the world (ROW) – and 29 major industries.

Before we compute the bilateral trade share, first we calculate the domestic consumption of own goods in each country, M_{nn}^{j}. Domestic sales is computed as the difference between sectoral gross production and sectoral total exports: $M_{nn}^{j} = \Upsilon_n^{j} - \sum_{i=1, i\neq n}^{N} M_{in}^{j}$. Expenditure by country n on sector j goods imported from country i is X_{ni}^{j}. X_{ni}^{j} can be calculated by multiplying trade value with tariffs: $X_{ni}^{j} = M_{in}^{j}$ $(1 + \tau_{ni}^{j})$. The trade share π_{ni}^{j} for each sector j and country pair n, i are obtained as follows $\pi_{ni}^{j} = X_{ni}^{j} / \sum_{i=1}^{N} X_{ni}^{j}$.

The share of sector j's spending on sector k's goods $\Upsilon_n^{k,j}$ is calculated from the IO matrix as the share of intermediate goods from sector k used in producing one unit of sector j's goods. From a typical IO table, the sum of the column items is the total input used in production while the sum of the row items is the total output for that given sector. The $\Upsilon_n^{k,j}$ is obtained by dividing the value of sector k goods used in producing one unit of sector j goods by the total input used in producing one unit of sector j's goods.

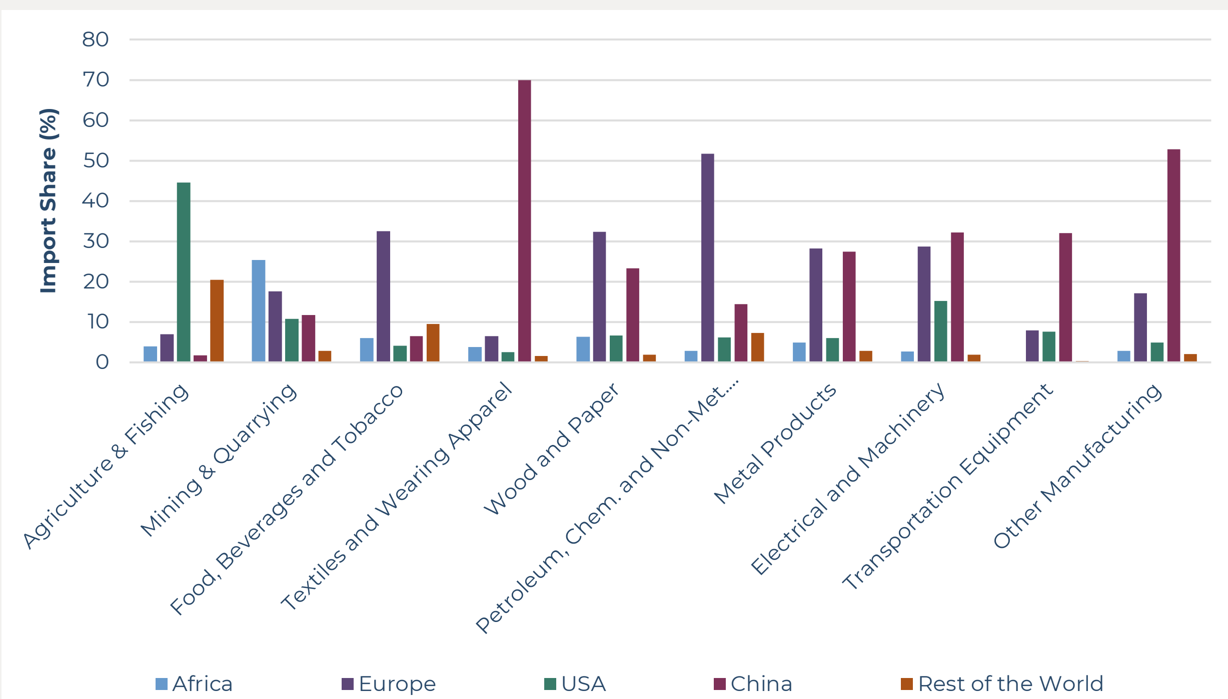
The share of value added is given as $\Upsilon_n^{j} = V_n^{j} / Y_n^{j}$. To calculate the final consumption expenditure share α_n^{j}, we take the sectoral total expenditure after subtracting intermediate goods expenditure purchased from both domestic and foreign consumers, and then divide it by total final absorption (Income). Specifically, $\alpha_n^{j} = (Y_n^{j} + D_n^{j} - \sum_{k=1} \Upsilon_n^{j,k}\ Y_n^{k}) / I_n$. Sectoral trade deficit in each country is given by $D_n^{j} = \sum_{i=1}^{N} M_{ni}^{j} - \sum_{i=1}^{N} M_{in}^{j}$. The only remaining parameter is the sectoral dispersion of productivity θ^{j}.

Figure I: *Average Tariff Rates on Nigeria's Exports*



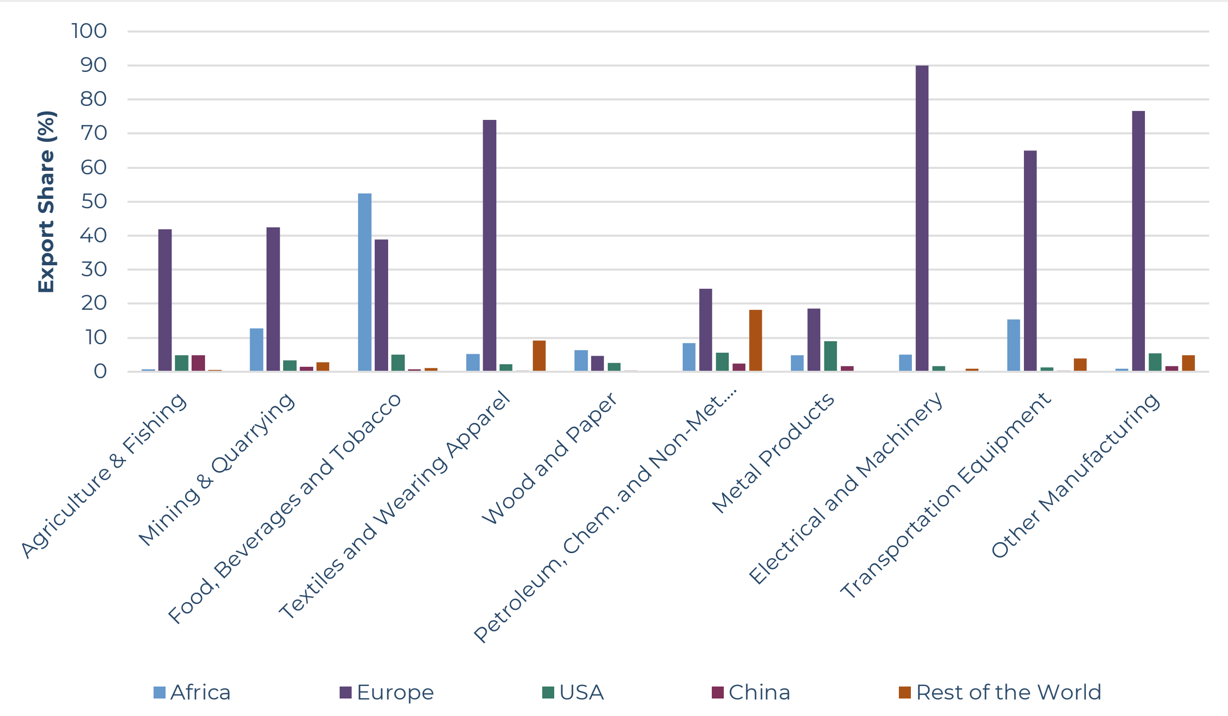
Source: *Simple average tariff rates in 2014 from UNCTAD TRAINS on HS6 dis-aggregated products.*

Figure J: *Nigeria's Import Share by Sector*

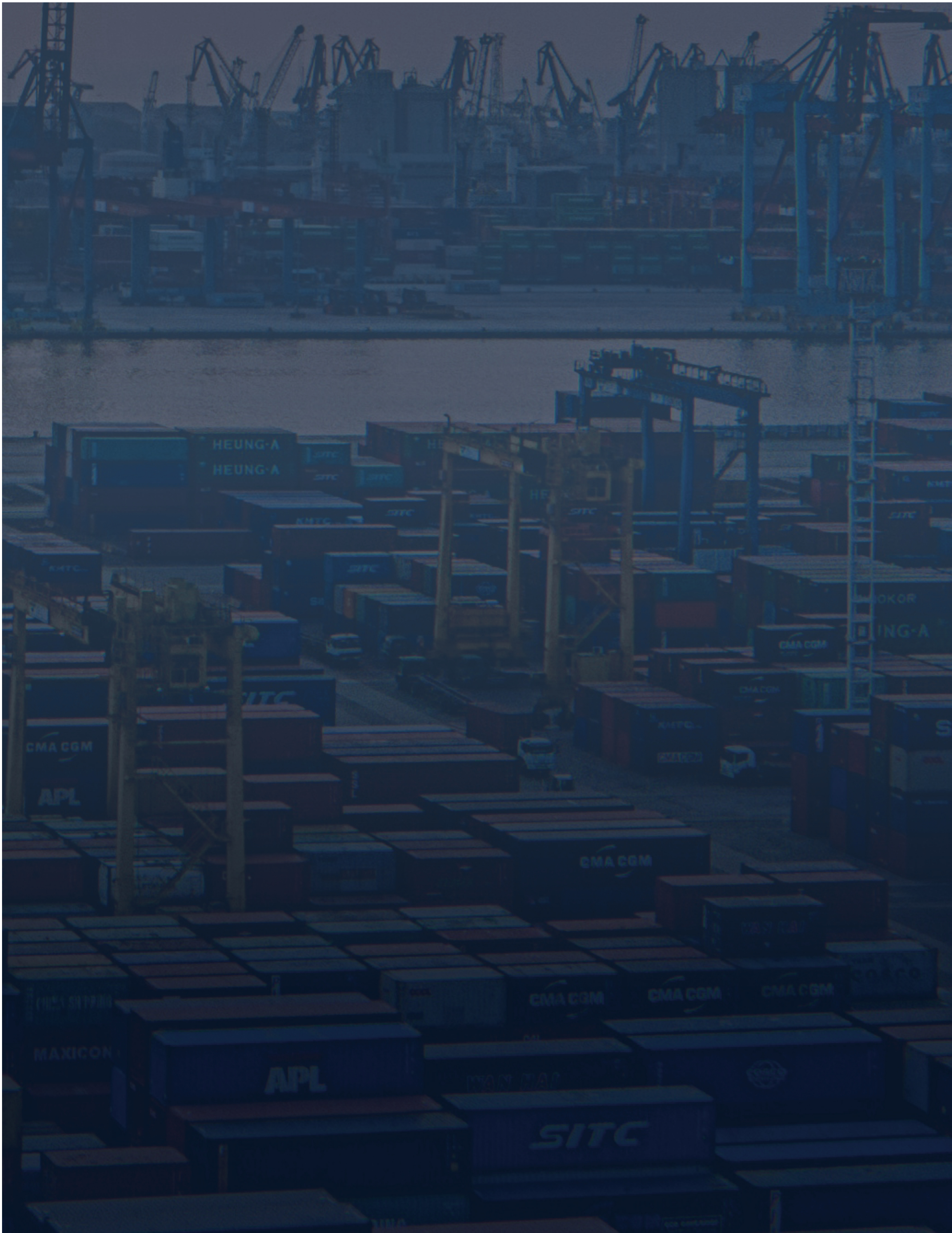


Source: *Bilateral trade data at HS6 level is from UN Commodity trade database.*

Figure K: *Nigeria's Export Share by Sector*



Source: *Bilateral trade data at HS6 level is from UN Commodity trade database.*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