UNIVERSITY OF KWAZULU-NATAL
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ECONOMICS AND FINANCE

DURBAN

Assessing the macroeconomic impact of free trade policies in Africa: A gravity model analysis

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This dissertation is submitted in fulfilment of the requirements for the Master of Commerce degree in Economics at the University of KwaZulu-Natal.

2024

Declaration

I, Songezo Mpini, declare that:

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Acknowledgements

This dissertation would not have been possible without the support and supervision of Prof Johnson Ojo Adelakun, and I would like to extend my strong gratitude to him. I am also grateful to the University of KwaZulu-Natal's School of Accounting, Economics, and Finance for the valuable comments and suggestions I received during the defence presentation of my research proposal. The earlier versions of this work benefited greatly from suggestions provided by Kgotso Morema, an economist by training and a close friend. I am deeply appreciative of my wife, Ongezwa Mpini, for her unwavering support throughout my studies and for creating a happy home environment. Her support enabled me to work hard and balance my roles as a student, employee, father, and husband. I would also like to thank the University of KwaZulu-Natal for the opportunity to complete this dissertation. During the completion of this research, I was employed by Absa Group, and I am thankful for the employment opportunity and the flexible work environment that allowed me to finish this dissertation while contributing to the organisation's success. Special thanks go to the Country and Sovereign Risk team (Rodney, Lulama, Sia and Vicky) for providing a supportive work environment that enabled me to complete this dissertation with ease.

Abstract

This study evaluates the macroeconomic impact of trade openness in Africa using a gravity model for the period 1990 - 2022. A total of 10 African countries are selected, from Africa's five regions, ensuring a combination of different economies by size and geographical location. The gravity model is preferred for its robust ability to accurately capture and quantify the effects of economic size and geographic distance on trade flows. Three estimation techniques—Fixed Effects (FE), Random Effects (RE), and Poisson Pseudo Maximum-Likelihood (PPML)—are explored. The study employs PPML, preferred for its ability to handle zero trade flows and extreme values, addressing the limitations of the FE and RE estimation techniques.

The study reveals a number of interesting findings. First, the study finds evidence of trade-led growth and modest but positive employment effects in 8 of the 10 studied economies, indicating that the impact of trade policies varies across countries. Second, there is a positive FDI effects across all studied economies, highlighting Africa's strong dependence on foreign aid. Third, the study finds that trade has a positive and significant impact on the exchange rate and reduces inflation but has an insignificant impact in pegged currencies. Fourth, the study finds that economic size plays a crucial role in determining trade benefits, and thus larger economies tend to benefit more from trade than smaller economies. Fifth, the study reveals that the composition of a country's trade significantly influences the impact of trade openness, indicating that countries heavily reliant on consumable imports experience less favourable outcomes, while those prioritising capital imports see more favourable results. Sixth, the study finds that economic size matters more than distance, indicating that industrialisation and dominance of large multinational firms outweigh the cost-effects of distance. Last, the study finds that intra-African trade significantly boosts export performance for all the studied countries, highlighting the importance of intra-regional trade agreements.

These findings have some compelling policy implications. The study suggests shifting the structure of imports towards capital goods and implementing import substitution for consumer goods. On exports, the study recommends a shift towards value-added products, moving away from raw commodities, and implementing export promotion strategies for industrialisation. Free trade policies must then be targeted at capital goods and value added products. Furthermore, the study strongly supports promoting intra-African trade to at least 50%, much higher than the current level of 14%. Lastly, the study recommends fostering macroeconomic stability to attract FDI. These policy measures are crucial for maximising the positive impact of free trade in Africa.

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Chapter 1: Introduction

This chapter introduces the study by providing background information on the adoption of free trade policies, followed by a problem statement that highlights the research gap. It also outlines the research questions, study objectives, significance, and structure of the dissertation.

1.1 Background

The concept of free trade policies dates back to the 18th century, first introduced by Adam Smith (1776). Since then, free trade has played a significant role in supporting globalisation, evolving through four distinct waves. The first wave (1860–1940) was characterised by rising protectionism, while the second wave (1944–1971), during the Bretton Woods System, saw gradual tariff reductions. The third wave of globalisation, which commenced in the late 1980s, marked a formal shift towards free trade, culminating in the establishment of the World Trade Organisation (WTO) in 1995.

The current fourth wave, emerging in the 2000s, is characterised by an increase in regional trade agreements, from 9 in 1990 to nearly 400 by 2024 (WTO, 2024). Africa has embraced this trend, beginning with the establishment of the Economic Community of West African States (ECOWAS) in 1975. The momentum for free trade in Africa accelerated during the third and fourth waves, resulting in over 150 free trade agreements signed by African nations by 2024 (WTO, 2024). However, while the adoption of free trade policies has been widespread, their effects, particularly in the African context, remain a subject of debate among scholars (Baldwin & Evenett, 2020).

During the last century, global trade forums have emphasised trade openness as a means to increase intra-African trade and enhance Africa's role in global value chains. A major milestone was the establishment of the African Continental Free Trade Area (AfCFTA) in 2021, marking a significant step towards promoting Africa's trade within the continent and beyond. As of August 2023, all African nations except Eritrea had signed the agreement, underscoring the continent's growing commitment to trade openness (Tralac, 2024).

Despite these advancements, the macroeconomic implications of free trade for African countries, particularly in a post-COVID-19 world, remain underexplored. The COVID-19 pandemic introduced new complexities into global trade, such as supply chain disruptions, protectionist tendencies, and shifts in global trade dynamics. These developments have important implications

for Africa's trade policies, particularly within the context of the AfCFTA. This study examines the impact of post-pandemic free trade policies on Africa's macroeconomic performance, focusing on export competitiveness, trade integration, and economic growth.

While free trade offers potential benefits, such as improved access to foreign markets and increased competition, African countries face unique challenges, including weak infrastructure, limited industrial capacity, and dependence on commodity exports (Thompson & Brown, 2019). These factors raise important questions about the sustainability and effectiveness of free trade policies in achieving long-term economic growth and integration into the global economy.

Moreover, the relationship between free trade and macroeconomic performance in Africa is not well understood in the context of recent global disruptions. This study addresses this research gap by providing a comprehensive analysis of how free trade policies, particularly through the AfCFTA, influence Africa's export performance and its integration into global value chains post-pandemic. Previous studies have largely focused on the theoretical benefits of trade liberalisation without fully accounting for the continent's specific structural challenges (Adams, 2018; Patel, 2020). This study, therefore, contributes to the literature by applying advanced econometric models to assess the real-world impacts of free trade in the African context, post-COVID-19.

Export performance is a key measure of a country's ability to earn foreign revenue, and the effectiveness of macroeconomic policy lies in its impact on key domestic objectives (Garcia, 2015; Nguyen et al., 2024). This study examines whether African nations can leverage free trade agreements such as the AfCFTA to achieve sustained economic growth, increased export competitiveness, and deeper integration into global value chains in a post-pandemic world. Advanced analytical methodologies, such as gravity models, are employed to explore the factors that influence trade flows, providing valuable insights into the dynamics of African trade (Felbermayr et al., 2020).

1.2 Problem statement

The African continent, despite its numerous regional economic groupings and external trade agreements, continues to face significant challenges in realising the full potential of free trade policies. Internally, free trade policies are implemented primarily through Regional Economic Communities (RECs) such as the Southern African Development Community (SADC), the

Common Market for Eastern and Southern Africa (COMESA), the Economic Community of West African States (ECOWAS), and the Economic Community of Central African States (ECCAS). Externally, Africa has established strategic partnerships with major global trade entities through agreements such as the African Growth and Opportunity Act (AGOA), the China-Africa Free Trade Agreement, and other bilateral agreements with Japan, India, and the European Union.

Despite the implementation of nearly 50 intra-African free trade agreements, intra-African trade remains disproportionately low, accounting for only 14% of total African trade, compared to intra-European trade at 68% and intra-Asian trade at 57%. Similarly, Africa's share of global trade remains stagnant at just 2.5% in 2023, despite over 150 trade agreements with countries outside the continent (WTO, 2024). This stark contrast between the increase in free trade agreements and the continent's minimal participation in global trade underscores a significant economic issue: Africa's inability to leverage free trade policies to achieve meaningful economic growth and integration.

One key factor contributing to this disparity is the uneven distribution of trade benefits across African economies. Larger economies such as South Africa and Ghana have seen some gains from trade liberalisation, particularly in sectors such as manufacturing and extractive industries. However, smaller economies, such as Lesotho, Togo, Chad, and Seychelles, continue to struggle with limited infrastructure, low industrial capacity, and overreliance on commodity exports (AfDB, 2022). This uneven distribution exacerbates economic inequalities within the continent, leaving smaller economies further marginalised in the global trading system.

This study examines how free trade agreements, both within Africa and with external partners, impact trade outcomes across African economies, with a particular focus on export competitiveness and economic integration. The study also explores disparities in trade outcomes between large and small economies, providing insights into the structural factors that contribute to Africa's limited success in global trade.

1.3 Significance of the study

This study's significance lies in its aim to address a critical gap in the literature regarding the impact of trade policies in Africa and offers contributions that previous studies have overlooked. Firstly, while the influence of economic size on trade flows has been widely studied, the role of free trade agreements has not been thoroughly explored. This research seeks to fill this gap by examining the

macroeconomic effects of free trade agreements and thereby providing a rich analysis of Africa's trade policy and trade dynamics.

Secondly, most studies that have tackled the topic of trade policies focus on advanced economies or a single developing economy, mostly non-African, leaving yet another gap. This study considers ten African economies, both large and small, from all five of Africa's sub-regions (North Africa, West Africa, Central Africa, East Africa, and Southern Africa). By considering several African economies, this study presents a continental perspective, which is essential to capture the diverse economic contexts.

Thirdly, the limited studies on developing economies have predominantly utilised the Autoregressive Distributed Lag (ARDL) model. While the ARDL model is useful for understanding the short- and long-term relationships between variables, it may not adequately capture the complexities of trade flows influenced by multiple factors such as distance, economic size, and institutional quality. This paper uses the Gravity model, which is widely regarded as more appropriate for analysing trade flows due to its ability to incorporate these various determinants (Anderson & van Wincoop, 2003). The Gravity model provides a more accurate understanding of how free trade agreements affect trade within Africa, offering a robust analytical framework that addresses the limitations of other methodologies.

Fourthly, understanding the nexus between trade policies and macroeconomic dynamics in Africa is of crucial importance for policymakers. Effective trade policies can stimulate economic growth, improve competitiveness, and foster sustainable development, but their efficiency heavily depends on a thorough understanding of their macroeconomic impacts (Rodrik, 2000). Policymakers need evidence-based insights to design and implement strategies that maximise the benefits of trade liberalisation while mitigating potential downsides. This study provides such insights, helping policymakers navigate the complexities of trade dynamics in Africa and make informed decisions.

1.4 Study objectives, hypotheses and research questions

Main Objectives:

- To assess the impact of trade openness on Africa's economic growth.
- To assess the impact of trade openness on intra-African trade and Africa's overall trade performance.

Hypotheses:

- Trade openness leads to higher better macroeconomic performance African economies.
- Trade openness leads to higher better intra-African trade and better export performance for African economies.

Research Questions:

- How does trade openness impact Africa's economic growth?
- What is the effect of free trade policies on intra-African trade performance?
- Does trade openness influence foreign direct investment inflows into African economies?
- What is the relationship between trade openness and employment trends in African economies?
- How do economic size and infrastructure levels moderate the effects of trade openness in Africa?

1.5 Structure of the study

Chapter 1 provides an overview of the study. Chapter 2 reviews relevant literature. Chapter 3 discusses Africa's trade openness trends. Chapter 4 presents the methodology. Chapter 5 discusses the results. Chapter 6 provides policy recommendations and conclusions.

Chapter 2: Literature review

2.1 Introduction

This chapter offers an in-depth review of the literature, beginning with the theoretical framework that forms the foundation of the study, followed by an analysis of empirical studies related to trade openness and its macroeconomic impacts. The theoretical section explores several key trade theories, tracing the evolution of ideas from classical economic thought to contemporary models that address the complexities of modern trade systems. Meanwhile, the empirical review scrutinizes research findings on the influence of trade openness on critical economic indicators such as GDP growth, foreign direct investment (FDI), employment, inflation, and intra-African trade. This comprehensive review highlights the existing gaps in the literature and provides the necessary background for understanding the macroeconomic implications of free trade policies in Africa.

2.2 Theoretical literature review

2.2.1 Absolute and comparative advantage

Classical trade theory is grounded in two foundational concepts: Adam Smith's theory of absolute advantage and David Ricardo's theory of comparative advantage. These ideas have shaped the understanding of international trade for more than two centuries. Adam Smith first introduced the notion of absolute advantage in The Wealth of Nations (1776), proposing that nations should concentrate on producing goods where they can maximise efficiency—where they can generate more output using the same inputs compared to other countries. Smith's model advocated for free trade by encouraging countries to specialise in areas where they possess an absolute production advantage.

However, Smith's framework did not account for how nations without such advantages could still profit from trade. This gap was addressed by David Ricardo's theory of comparative advantage, which demonstrated that trade remains beneficial even if a nation lacks an absolute advantage in any good. In his 1826 work Principles of Political Economy and Taxation, Ricardo contended that countries should focus on producing goods where they have the lowest opportunity cost relative to other nations. This approach leads to a more efficient allocation of resources on a global scale (Lindert, 1991). As a result, all trading nations benefit by enhancing productivity, fostering innovation, and promoting economic growth (Bhagwati, 1964).

Although these classical theories offer a strong justification for international trade, they are based on assumptions of constant returns to scale and perfect competition. Such assumptions limit their relevance in explaining contemporary trade dynamics, particularly in the context of developing regions like Africa. The models primarily focus on natural resources as the basis for comparative advantage and do not account for the complexities of industrialisation, technology transfer, or value chain integration that characterise contemporary global trade dynamics. In the African context, where economies are largely dependent on primary commodity exports and have yet to realise their full industrial potential, the application of these theories remains constrained. Despite these limitations, the absolute and comparative advantage frameworks provide critical insights into why African nations engage in trade, particularly in resource-intensive sectors.

2.2.2 The Heckscher-Ohlin-Samuelson theory

Building upon Ricardo's theory of comparative advantage, the Heckscher-Ohlin (H-O) model, developed by Eli Heckscher and Bertil Ohlin in the early 20th century, introduced a new perspective on trade by emphasising the significance of a country's factor endowments—such as labour, capital, and natural resources—in shaping trade patterns. According to the H-O model, countries tend to specialise in producing goods that rely on their abundant factors of production. For instance, nations rich in labour would focus on producing labour-intensive goods, while those with ample capital would prioritise capital-intensive production (Heckscher & Ohlin, 1933). This model extends Ricardo's theory by asserting that comparative advantage is not fixed but varies according to a country's changing factor endowments over time.

Paul Samuelson later expanded this model through the factor price equalisation theorem, suggesting that free trade could equalize factor prices—such as wages and returns on capital—across countries, assuming the conditions of perfect competition and no trade barriers. This theorem indicates that trade could benefit not only specific industries but also improve income distribution within trading nations (Samuelson, 1949).

In the African context, the H-O-S model is particularly relevant, as many African economies are rich in natural resources but have limited industrial capacity. This theory suggests that African countries should concentrate on resource-based exports, a pattern reflected in their current trade structures, which are dominated by oil, minerals, and agricultural commodities. Nonetheless, critics argue that this dependency on primary exports exposes African nations to volatile global commodity prices and perpetuates their marginal position in the global economy (African Development Bank, 2019). Furthermore, the continent's challenges—such as low-skilled labour,

poor infrastructure, and underdeveloped industries—limit the practical application of the H-O model's predictions.

While the H-O model offers a useful lens for analysing African trade, it overlooks the political and historical factors, such as colonialism, that have shaped current trade dynamics. The colonial legacy of exporting raw materials and importing manufactured goods has persisted, and structural barriers, such as limited labour and capital mobility, complicate the model's assumptions in many African countries.

2.2.3 New trade theory

In contrast to classical trade models, New Trade Theory (NTT), developed by economists like Paul Krugman in the late 20th century, introduces concepts such as economies of scale and product differentiation into the analysis of trade. NTT posits that trade can occur between countries with similar factor endowments, driven by firms' ability to reduce costs through large-scale production and by consumers' desire for diverse products (Krugman & Obstfeld, 2005). This theory explains the high level of intra-industry trade, where countries with similar economic profiles trade similar goods (Krugman, 1979).

Furthermore, the Spence-Dixit-Stiglitz model of product differentiation, which is central to NTT, highlights how trade allows countries to specialise in different varieties of the same product, thus enhancing consumer choice and reducing costs through economies of scale (Helpman, 1987). For African countries, NTT suggests that by integrating into larger markets, both regional and global, their firms could achieve economies of scale and improve competitiveness. However, the lack of adequate infrastructure and technological capacity poses significant obstacles to realising these benefits fully.

The African Continental Free Trade Area (AfCFTA) could play a crucial role in overcoming these barriers by creating larger markets, thus facilitating economies of scale. NTT also underscores the importance of reducing trade costs, such as transportation and logistics, which remain high in Africa due to infrastructure deficiencies. These are critical considerations for policymakers aiming to enhance trade openness and industrial competitiveness across the continent.

2.2.4 The Prebisch-Singer thesis

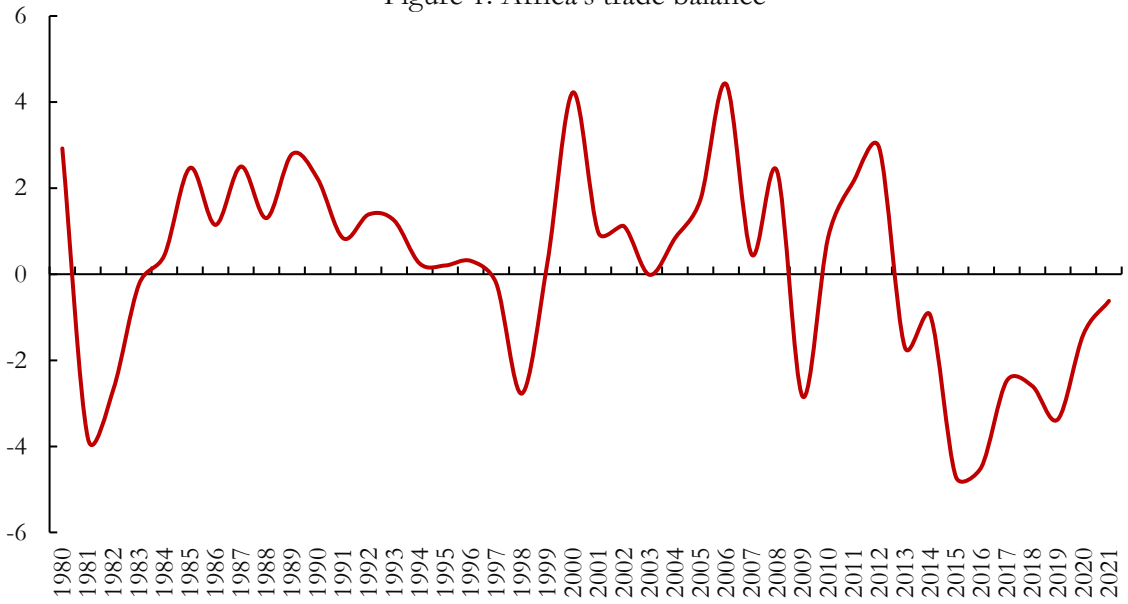
The Prebisch-Singer thesis, developed by Raúl Prebisch and Hans Singer in the 1950s, offers a structural critique of classical and neoclassical trade models, focusing on the long-term deterioration in the terms of trade for primary commodity exporters. The thesis argues that developing nations reliant on exporting raw materials, such as many African countries, face declining export prices relative to the prices of imported manufactured goods, which reduces their income and hampers economic development (Toye & Toye, 2003).

This thesis remains pertinent for Africa, where many economies depend heavily on commodities like oil, minerals, and agricultural goods. Without industrial diversification, these economies remain vulnerable to price fluctuations in the global market. As a result, many African policymakers have focused on strategies for adding value to raw materials and diversifying into manufacturing to reduce reliance on primary exports. For example, Ethiopia's investment in textile and leather industries illustrates efforts to increase value-added exports. However, significant challenges, including the need for technological advancement and skills development, persist.

2.2.5 Mercantilism

Mercantilism, which dominated European economic policy from the 16th to the 18th centuries, focused on maximising national wealth by maintaining trade surpluses, accumulating precious metals, and restricting imports (Magnusson, 2015). While mercantilist policies are largely outdated, they provide a historical backdrop for understanding modern protectionist tendencies in trade. In Africa, the mercantilist approach is less relevant, as most countries have faced persistent trade deficits since the 1980s, driven by their reliance on importing manufactured goods and machinery from industrialised nations (Wang & Bio-Tchané, 2008). African nations require substantial investments in industrialisation, technology, and infrastructure to reduce dependency on imports. Rather than adopting mercantilist strategies, African trade policies must focus on boosting competitiveness through innovation and integration into global value chains.

Figure 1: Africa's trade balance



Source: World bank(2023)

2.2.6 The infant industry argument

The infant industry argument, advanced by Alexander Hamilton and Friedrich List in the 19th century, holds that emerging industries in developing countries require temporary protection from foreign competition to grow and eventually compete on a global scale. John Stuart Mill later refined the argument, emphasising that protection should be limited to industries capable of achieving self-sufficiency (Shafaeddin, 2005).

This argument is particularly relevant to Africa, where governments are working to diversify their economies and reduce dependency on raw commodity exports. Protecting nascent industries in sectors like manufacturing and technology could help foster domestic competitiveness and long-term growth. However, this strategy must be carefully managed to avoid inefficiencies and ensure that industries eventually become globally competitive without permanent government support. The experiences of countries like Ghana and South Africa demonstrate that while protectionist policies can stimulate job creation, they also risk inefficiencies and higher consumer costs if not properly executed.

2.3 Empirical literature review

The impact of trade openness on African economies has been a subject of extensive debate in the empirical literature. While many studies highlight the potential benefits of trade liberalisation, such as economic growth, poverty alleviation, and diversification, others emphasise the risks of increased inequality, vulnerability to external shocks, and uneven development outcomes.

The role of Gross Domestic Product (GDP) as a critical variable in assessing the effects of trade openness is well-established. Larger economies, with more diversified production bases, are typically better equipped to integrate into global trade networks and reap the benefits of trade liberalisation. Recent studies, such as Dollar and Kraay (2019), demonstrate that larger economies are more likely to attract trade, given their ability to produce a broader range of goods and services. In contrast, smaller African economies, often characterised by less diversified industries and a reliance on primary commodities, have struggled to benefit from trade liberalisation. This disparity is evident in studies such as Coulibaly and Erbao (2018), which argue that smaller economies experience limited gains from trade unless they implement complementary policies like infrastructure development and sectoral diversification. This is particularly relevant to Africa, where a significant portion of the continent's GDP is concentrated in a few larger economies (e.g., South Africa, Nigeria, and Egypt), leaving smaller countries like Lesotho, Togo, and Seychelles unable to leverage free trade effectively.

Foreign Direct Investment (FDI) is another channel through which trade openness impacts economic growth. Empirical studies show that countries with open trade policies tend to attract more FDI, which facilitates technology transfer, productivity gains, and economic growth (Adams & Opoku, 2019). In the African context, Asongu and Odhiambo (2020) highlight that while trade openness does attract FDI, other factors such as political stability, infrastructure, and market size also play crucial roles in determining FDI inflows. Therefore, although trade liberalisation has the potential to boost FDI in Africa, its effectiveness is contingent on broader economic and institutional reforms. This underscores the argument that free trade alone may not be sufficient to stimulate growth in African economies, particularly those with weak institutional frameworks and underdeveloped infrastructure.

Inflation and its relationship with trade openness have been the subject of significant empirical debate. Lane and Milesi-Ferretti (2018) posit that higher trade openness is associated with lower inflation rates, as increased competition from foreign producers leads to more efficient pricing of

goods and services. However, Kitenge (2017) presents a counterargument, suggesting that in the short term, trade liberalisation can lead to inflationary pressures due to increased demand for imported goods, especially in economies with weak domestic production capabilities. In Africa, studies such as those by Ssozi and Asongu (2016) suggest that the inflationary impacts of trade openness are context-specific, with countries experiencing varying levels of price instability depending on their macroeconomic conditions and the structure of their domestic markets. This mixed evidence suggests that while trade openness can lead to price stabilisation in some contexts, it may also exacerbate inflationary pressures in countries with underdeveloped industries.

Exchange rate dynamics play a crucial role in determining the impact of trade openness on economic performance, particularly in African economies with volatile currencies. A stable and competitive exchange rate can enhance export competitiveness, making domestic goods more attractive in global markets. Conversely, excessive exchange rate volatility can undermine trade benefits by increasing uncertainty for exporters and importers. Recent empirical studies, such as Bleaney and Greenaway (2018), suggest that trade openness is associated with exchange rate appreciation in many developing economies, which can reduce export competitiveness, particularly in non-diversified economies reliant on primary commodities. On the other hand, Ajakaiye, Jerome, and Nabena (2021) argue that exchange rate flexibility allows economies to better absorb external shocks and adjust to trade imbalances. In the African context, countries with managed exchange rate regimes, such as Egypt and Ethiopia, often face challenges related to currency misalignment, which affects trade flows and investment decisions. Moreover, volatile exchange rates can contribute to inflationary pressures, especially in import-dependent economies, reinforcing the importance of sound macroeconomic policies to complement trade liberalisation efforts. These findings highlight that while trade openness can boost economic growth, its effectiveness depends on exchange rate management strategies that support competitiveness and macroeconomic stability.

Intra-African trade has been a central focus in the literature, particularly following the implementation of regional agreements like the African Continental Free Trade Area (AfCFTA). Despite efforts to promote regional integration, intra-African trade remains disproportionately low compared to other regions, accounting for only 14% of total African trade (WTO, 2024). More recent empirical studies (e.g., Abrego et al., 2020) emphasise that removing trade barriers and fostering deeper integration could significantly boost intra-African trade, especially in sectors such as manufacturing and agriculture, where African countries hold comparative advantages. These

studies suggest that regional integration efforts, if properly implemented, could unlock substantial economic potential across the continent by reducing trade costs and increasing the competitiveness of African industries. This view supports the problem statement, as it highlights the potential of regional trade agreements to improve Africa's trade outcomes but also underscores the challenges that must be addressed to fully capitalise on these opportunities.

Employment is another key area impacted by free trade policies. Theoretical models, such as those by Helpman and Itskhoki (2017), argue that trade liberalisation can create jobs by expanding internationally competitive industries. However, the empirical evidence in developing countries, including Africa, is more nuanced. Baliamoune-Lutz and Ndikumana (2019) find that while trade openness can lead to job creation in sectors like manufacturing, it may also result in job losses in less competitive industries, particularly in economies that are not yet fully industrialised. Furthermore, the benefits of employment generation from trade liberalisation are often unevenly distributed, with urban areas and larger economies capturing more of the gains than rural or smaller economies. This uneven distribution of benefits contributes to growing inequalities within Africa, as highlighted in the problem statement, with smaller economies struggling to benefit from trade liberalisation.

Finally, the literature consistently highlights that infrastructure and institutional quality are critical determinants of trade outcomes in Africa. Calderón, Cantú, and Chuhan-Pole (2020) emphasise that without adequate infrastructure—such as reliable transport networks, energy supplies, and communication systems—African countries cannot fully capitalise on the benefits of trade liberalisation. Rodrik (2018) further argues that weak institutions, characterised by poor governance and inadequate regulatory frameworks, exacerbate trade barriers, reduce investor confidence, and hinder the effective implementation of trade agreements. This supports the problem statement by illustrating that Africa's inability to leverage free trade policies for meaningful economic growth is closely tied to structural issues that transcend trade policy, including infrastructure deficits and institutional weaknesses.

In conclusion, the empirical literature supports the view that while free trade policies have the potential to stimulate economic growth and regional integration in Africa, the continent faces significant challenges in fully realising these benefits. Structural factors, such as the uneven distribution of trade gains, weak institutional frameworks, inadequate infrastructure, and regional fragmentation, limit the effectiveness of free trade policies in many African economies. As such,

any comprehensive solution must address these underlying issues to ensure that free trade contributes to sustained and inclusive economic growth across the continent.

2.4 Conclusion

This chapter has reviewed both theoretical and empirical perspectives on trade openness and its effects on African economies. The theoretical discussion traced the development of trade theories, from classical models of comparative advantage to contemporary frameworks like New Trade Theory and the infant industry argument. These theories provide valuable insights into the benefits and challenges of trade openness for Africa, particularly in relation to economic diversification and industrialisation.

The empirical literature presents a mixed picture, with some studies emphasising the positive effects of trade openness, while others highlight concerns about inequality and external vulnerabilities. These findings underscore the complexity of trade liberalisation in Africa and suggest that further research is needed to identify the conditions under which trade can contribute to sustainable development.

Chapter 3: Overview of Africa's trade policy, structure and dynamics

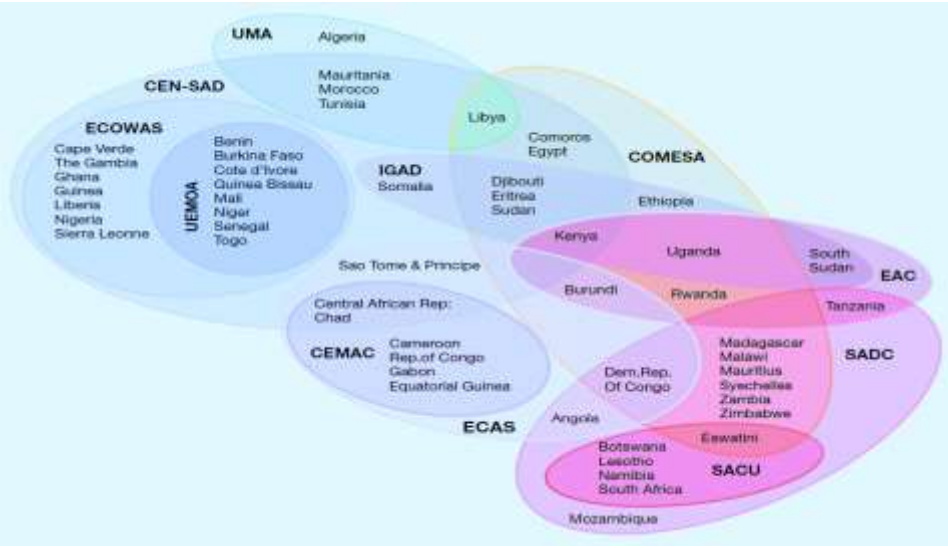
3.1 Introduction

This Chapter critically analyses trends in Africa's export performance, structure of exports, major export partners and the role that Africa plays in global trade.

3.2 Regional economic integration in Africa

Africa currently features a wide array of organisations, monetary unions, and Regional Economic Communities (RECs), collectively forming a complex and intertwined structure, often referred to as a 'spaghetti bowl' of agreements, as illustrated in Figure 2. Of the approximately 17 groupings, 8 RECs (including ECOWAS, CEN-SAD, AMU, SADC, IGAD, COMESA, ECCAS, and EAC) are recognised as the key pillars of regional integration efforts (Oiro, 2020). These RECs play a crucial role in accelerating the integration process, as they provide a platform for the adoption of successful practices from existing agreements. Moreover, the creation of a continental free trade area is viewed as a potential remedy for challenges related to overlapping memberships (Abrego et al., 2020).

Figure 2: Africa's Regional Economic Communities



Gobena (2019)

3.3 Free trade policies aimed at supporting Africa's trade openness.

3.3.1 Free trade agreements between Africa and rest of the world

COMESA-EU Economic Partnership Agreement (EPA)

The Economic Partnership Agreement (EPA) between the Common Market for Eastern and Southern Africa (COMESA) and the European Union (EU) aims to improve trade relations by offering COMESA member states preferential access to the EU market. The agreement primarily focuses on enhancing the export capacities of COMESA countries, particularly in sectors such as agriculture, textiles, and manufacturing, allowing these nations to better compete in European markets. Through the reduction of tariff barriers and enhanced market access, the EPA seeks to support sustainable economic growth while increasing COMESA's integration into global markets (Kuhlmann, 2016).

A critical aspect of this partnership is its emphasis on development cooperation. The EU provides financial support and capacity-building programs designed to strengthen the productive capacities of COMESA economies, going beyond trade liberalisation. These initiatives target improvements in infrastructure, governance, and competitiveness, especially for small and medium-sized enterprises (SMEs), which play a vital role in job creation and income generation (Mold, 2017). This developmental focus aligns with broader goals of sustainable development and poverty alleviation in the region.

Despite the potential benefits, the COMESA-EU EPA faces challenges. Some critics argue that the agreement creates imbalances, as the economies of COMESA countries are generally less diversified and industrialised compared to their European counterparts. This imbalance could lead to trade deficits for certain COMESA nations, exacerbating their reliance on primary commodities. Additionally, the stringent rules of origin and complex regulatory requirements for accessing the EU market present further hurdles for some COMESA countries (Abuka, 2020).

The performance of the COMESA-EU Economic Partnership Agreement has shown mixed results. While the EPA has successfully opened up European markets to COMESA countries, particularly for agricultural and manufactured goods, the expected rise in export diversification has not fully materialised. According to McQueen (2016), many COMESA countries continue to rely

heavily on exporting raw materials rather than moving up the value chain to export processed goods. Although some countries like Kenya and Zambia have benefited from increased agricultural exports to the EU, the overall impact on economic diversification remains limited. Moreover, there is a lack of sufficient infrastructure and industrial capacity in some COMESA states to fully exploit the benefits of the EPA, thereby hampering the anticipated economic transformation.

Furthermore, the EPA has faced criticism for reinforcing asymmetric trade relations between the EU and COMESA. Some studies argue that the agreement largely benefits the EU by granting it access to COMESA markets while offering limited industrialisation opportunities for the African region (Keane & Stevens, 2017). The reduction in tariff barriers has led to increased imports of European goods into COMESA, which could potentially harm local industries that are not equipped to compete. This dynamic has raised concerns about the long-term sustainability of the agreement and its ability to foster genuine economic growth in the region. Scholars such as Mold (2017) suggest that more targeted policies, alongside the EPA, are needed to ensure that COMESA countries can build competitive industries and reduce their dependency on raw material exports.

ECOWAS-United States Trade and Investment Framework Agreement (TIFA)

The Trade and Investment Framework Agreement (TIFA) between the Economic Community of West African States (ECOWAS) and the United States establishes a platform for deepening trade relations and enhancing investment flows. Unlike a full-fledged free trade agreement, TIFA provides a structure for dialogue and cooperation on issues like market access, regulatory hurdles, and intellectual property rights. By facilitating ongoing discussions, TIFA seeks to increase transparency and cooperation on economic policies, thereby laying the groundwork for future trade agreements (De Melo & Tsikata, 2015).

Under the TIFA framework, both parties engage in regular consultations to address trade and investment barriers that impede bilateral trade growth. A primary focus has been on improving the investment environment in ECOWAS member states through legal reforms, infrastructure enhancements, and the protection of U.S. investors. These initiatives are crucial for attracting foreign direct investment (FDI), which can help diversify West African economies, create jobs, and facilitate the transfer of technology. Additionally, the TIFA provides mechanisms for resolving trade disputes, contributing to a more stable business environment (Fashola, 2019).

However, the effectiveness of the TIFA has been questioned, as it does not include binding commitments to reduce tariffs or open markets. Its non-binding nature means that many of the

discussions and agreements reached under TIFA are subject to voluntary compliance. As a result, progress in areas such as market access and reducing trade barriers has been slow. Moreover, some ECOWAS countries have expressed concerns that the framework overly favors U.S. interests without providing enough tangible benefits for West African economies (Adebayo, 2018).

The performance of the ECOWAS-United States TIFA has been measured more by its potential than its immediate outcomes. The framework has helped facilitate dialogue on trade and investment issues but has yet to deliver significant increases in trade or investment flows between the two regions. While ECOWAS member states have benefited from improved trade facilitation efforts and investment climate reforms supported by the TIFA, critics argue that it has fallen short of driving major economic transformations. As Odularu (2018) highlights, the TIFA has been effective in providing technical support for capacity building and governance reforms, but there has been little progress toward a comprehensive free trade agreement, which would have a more significant economic impact.

On the other hand, the framework's non-binding nature limits its ability to enforce changes that could significantly boost trade. For instance, bilateral trade between ECOWAS and the U.S. has not seen substantial growth since the signing of the TIFA, and U.S. investment in the region remains below potential levels (Adebayo, 2020). Several scholars argue that more robust engagement is needed from both sides, particularly in addressing barriers to trade such as infrastructure deficits, regulatory hurdles, and security concerns in some West African states. Without concrete steps toward deeper trade integration, the TIFA risks becoming merely a diplomatic tool rather than a catalyst for transformative economic growth.

SADC-European Free Trade Association (EFTA) Free Trade Agreement

The Southern African Development Community (SADC) and the European Free Trade Association (EFTA), consisting of Switzerland, Norway, Iceland, and Liechtenstein, have established a Free Trade Agreement (FTA) aimed at strengthening economic ties between the regions. The agreement promotes the exchange of goods by removing tariffs on numerous products, especially industrial goods, fish, and processed agricultural items. This FTA enhances market access for SADC nations, allowing them to expand exports to EFTA countries, which have high standards of living and strong demand for foreign products (Grubel, 2017).

Beyond goods, the SADC-EFTA FTA promotes broader economic cooperation, including investment and intellectual property rights, and aligns growth with sustainable development

objectives. The agreement aims to increase industrial capacity within SADC countries by encouraging investment, thereby fostering economic diversification and reducing reliance on raw material exports (Wehrli, 2019). Additionally, it provides technical assistance to help SADC nations meet EFTA's regulatory standards, particularly in areas like food safety and product quality.

Despite these positive developments, the SADC-EFTA FTA faces challenges, particularly for smaller and less developed SADC members. These countries may struggle to compete in EFTA markets due to a lack of competitive industrial capacity and high compliance costs associated with EFTA's regulations. Furthermore, while the agreement offers market access, it does not address broader issues such as infrastructure deficits or governance challenges that hinder SADC countries from fully exploiting trade opportunities. As a result, there is a need for complementary policies to ensure that the benefits of the FTA are distributed more equitably across the region (Viljoen, 2021).

The SADC-EFTA Free Trade Agreement has had a moderate impact on trade between the two regions, with notable benefits for the larger and more industrialised economies within SADC. South Africa, for example, has significantly expanded its exports of processed goods, including machinery, chemicals, and automotive products, to EFTA member states (Viljoen, 2021). However, smaller and less industrialised SADC countries have struggled to benefit from the agreement to the same extent. This uneven distribution of benefits has raised concerns about the capacity of less developed SADC economies to take full advantage of the FTA. According to Wehrli (2019), issues such as inadequate industrial capacity and weak infrastructure remain significant barriers to trade expansion for many SADC countries.

Additionally, the stringent rules of origin and regulatory standards required by EFTA countries have posed challenges for SADC exporters. Many firms in the region lack the resources or technological capabilities to meet these high standards, limiting their ability to fully access EFTA markets (Wehrli, 2019). While the FTA has created opportunities for technical cooperation and capacity building, more needs to be done to address the structural limitations within SADC economies. Without targeted interventions to improve industrial capacity and enhance competitiveness, the SADC-EFTA FTA risks exacerbating economic disparities within the region, with only a few countries reaping the majority of the benefits.

ASEAN-Africa Free Trade Agreement (under exploration)

A proposed Free Trade Agreement (FTA) between the African Union (AU) and the Association of Southeast Asian Nations (ASEAN) could significantly enhance economic ties between the two regions. Africa and Southeast Asia possess complementary economic traits, such as large young populations and Africa's wealth of natural resources, which could support industrial growth in ASEAN. The potential FTA seeks to reduce trade barriers, enhance the flow of goods and services, and promote mutual investment (Moyo & Kiggundu, 2019).

Both Africa and Southeast Asia have experienced substantial economic growth in recent decades. A formalised FTA could accelerate this growth by increasing market access and expanding trade volumes. Improved infrastructure and connectivity between the regions would facilitate integration into global value chains, particularly in sectors such as agriculture, textiles, and manufacturing. Additionally, the agreement would encourage technology and knowledge transfer, allowing African countries to benefit from the industrial advancements made by ASEAN nations (Lee, 2020).

However, there are significant obstacles to the realisation of an ASEAN-Africa FTA. Both regions face internal challenges, including varying levels of economic development, regulatory differences, and political instability in some countries, which could hinder negotiations and implementation. Additionally, infrastructure deficits and logistical bottlenecks, particularly in Africa, pose challenges to trade integration. Therefore, comprehensive strategies focusing on infrastructure development, capacity building, and governance reforms would be necessary to maximise the potential benefits of such an agreement (Zongwe, 2021).

While the ASEAN-Africa Free Trade Agreement remains in its exploratory phase, preliminary analyses of its potential suggest both promise and challenges. Studies by Moyo and Kiggundu (2019) indicate that an agreement of this nature could substantially increase trade flows between Africa and Southeast Asia by leveraging the complementary strengths of the two regions. Africa's rich natural resources and ASEAN's manufacturing capabilities create a foundation for mutually beneficial trade. Additionally, the FTA could provide Africa with access to ASEAN's advanced technologies, which could be pivotal for industrialisation and infrastructure development on the African continent.

However, evaluations of the agreement's potential performance also highlight significant challenges. Zongwe (2021) points out that both Africa and Southeast Asia face substantial logistical

barriers, including underdeveloped transport networks and trade facilitation systems. Moreover, disparities in economic development between the two regions could hinder the realisation of equitable trade benefits. Southeast Asian countries are generally more industrialised and technologically advanced than their African counterparts, raising concerns that the FTA could deepen economic imbalances rather than foster equitable development. These issues suggest that the success of the ASEAN-Africa FTA will depend heavily on infrastructure investments and policies that ensure the participation of less-developed African economies.

MERCOSUR-Africa Free Trade Agreement (under discussion)

The concept of establishing a free trade agreement (FTA) between the Southern Common Market (MERCOSUR) and African countries has been a topic of discussion for several years, driven by the mutual desire of both regions to strengthen their economic and trade ties. MERCOSUR, which includes nations such as Argentina, Brazil, Paraguay, and Uruguay, has shown interest in expanding its trade network beyond South America, particularly with growing economies in Africa. If implemented, the MERCOSUR-Africa FTA could substantially boost trade between the two regions, especially in key sectors like agriculture, mining, and manufacturing (González & Giordano, 2018).

Ongoing discussions regarding the proposed FTA have largely focused on reducing tariffs and other trade obstacles to encourage the exchange of goods and services. Both MERCOSUR and many African nations are significant exporters of agricultural products and natural resources, so this agreement could create synergies that improve global competitiveness in these sectors. Additionally, by fostering investment between the two regions, the FTA could facilitate infrastructure development and boost industrial capacity in African economies, helping these countries diversify and reduce their dependency on primary commodities (Carvalho, 2020).

However, the MERCOSUR-Africa FTA faces several challenges. Differences in economic structures, regulatory systems, and political environments between the two regions could complicate negotiations and the practical implementation of the agreement. Furthermore, both regions face significant infrastructure and logistics challenges, which may limit the potential trade benefits. A phased approach, focusing initially on specific sectors while addressing regulatory harmonisation and infrastructure development, could be essential for the successful implementation of the agreement (Di Tella, 2021).

Assessments of the potential impact of the MERCOSUR-Africa FTA yield mixed expectations. On the one hand, proponents are optimistic that the agreement could strengthen economic relations and enhance trade in sectors where both regions hold comparative advantages, such as agriculture and mining (González & Giordano, 2018). Moreover, MERCOSUR's relatively advanced industrial sector could offer African countries opportunities for value-added production, as African nations could supply raw materials while receiving processed goods and technological expertise from MERCOSUR. This dynamic could aid Africa's efforts to diversify its economies and reduce reliance on primary exports.

However, concerns have surfaced regarding the ability of African economies to fully benefit from such an agreement. According to Carvalho (2020), disparities in industrial development between the two regions could limit Africa's ability to export processed goods or benefit from technology transfers. Moreover, infrastructure and logistical challenges, particularly in African countries, could hinder the smooth flow of goods, raising transportation costs and reducing competitiveness. Without complementary policies focused on capacity building and infrastructure development, there is a risk that the MERCOSUR-Africa FTA could replicate the unequal trade relationships that have historically characterised North-South agreements.

African, Caribbean, and Pacific (ACP) Group of States - European Union (EU) Economic Partnership Agreements (EPAs)

The European Union (EU) has established Economic Partnership Agreements (EPAs) with the African, Caribbean, and Pacific (ACP) Group of States to enhance trade and economic cooperation by providing preferential access to EU markets. These agreements aim to support the integration of ACP countries into the global economy by granting duty-free and quota-free access to a variety of goods, including agricultural products and raw materials. The EPAs are intended to promote sustainable development and poverty reduction by facilitating trade in these regions (Rollo, 2016).

Beyond improving market access, the EPAs also include provisions for development cooperation. These measures focus on areas such as infrastructure improvements, capacity-building initiatives, and governance reforms. The EU provides financial and technical assistance to ACP countries to help them meet the regulatory standards required to export to EU markets, particularly in critical areas like food safety and product quality. Such support is essential for ensuring that ACP nations can fully benefit from the trade opportunities provided by the EPAs (Mendez-Parra et al., 2018).

Despite the benefits, the EPAs have been subject to criticism, particularly regarding their potential negative impact on local industries within ACP countries. Critics argue that increased competition from European imports could threaten local businesses that are not equipped to compete with more advanced European industries. Additionally, there are concerns that the EPAs may reinforce ACP countries' reliance on raw material exports, limiting their ability to diversify and industrialise their economies (Bilal & Braun-Munzinger, 2019).

The performance of the EPAs has sparked considerable debate. While these agreements have granted ACP countries preferential access to European markets, their broader impact on economic transformation has been less than anticipated. According to Rollo (2016), many ACP countries continue to rely heavily on raw material exports to Europe, with limited progress toward economic diversification. The agreements have also fallen short in significantly reducing poverty or promoting industrialisation, largely due to structural challenges such as weak infrastructure and insufficient industrial capacity within ACP countries.

Critics contend that the EPAs have perpetuated the dependency of ACP countries on European markets. Bilal and Braun-Munzinger (2019) argue that the asymmetrical nature of the agreements—where European industrialised economies hold more leverage—has maintained a scenario in which ACP nations remain exporters of low-value goods while importing high-value manufactured products from Europe. This trade imbalance, coupled with limited investment in capacity-building, has constrained the EPAs' potential to drive sustainable economic growth in ACP regions. Consequently, while the agreements have improved short-term market access, their long-term impact on sustainable development remains limited.

African Growth and Opportunity Act (AGOA) - United States

The African Growth and Opportunity Act (AGOA) is a trade preference initiative, launched in 2000, aimed at fostering stronger economic ties between the United States and eligible African nations. AGOA offers duty-free access to the U.S. market for a wide range of goods, including textiles, apparel, and agricultural products, allowing African exporters to enhance their market presence in the United States. This preferential trade arrangement seeks to promote economic growth and development across Africa while encouraging diversification of African economies (McCormick, 2017).

AGOA has been particularly successful in boosting sectors like apparel manufacturing, which has seen a substantial increase in exports to the U.S. Additionally, the program has stimulated broader economic engagement by attracting foreign direct investment (FDI) from U.S. companies, particularly in industries benefiting from AGOA's preferential market access. The Act also includes provisions for capacity-building programs aimed at improving the regulatory frameworks, governance structures, and infrastructure in African countries, all of which are essential for sustaining economic growth (Hufbauer & Brunel, 2019).

3.3.2 Free trade agreements between Africa and Africa

The African Continental Free Trade Area (AfCFTA)

The African Continental Free Trade Area (AfCFTA), a flagship initiative of the African Union (AU), is designed to promote economic integration across the continent. Officially launched in 2018, AfCFTA aims to establish the world's largest free trade zone, uniting 55 African nations with a combined population exceeding 1.3 billion people and a collective GDP of over $3.4 trillion (African Union, 2020). The primary objective of AfCFTA is to bolster intra-African trade by removing tariffs and non-tariff barriers, thus fostering economic cooperation among the participating countries. This initiative is a major step toward achieving the long-term vision of a unified African economy, contributing to industrialisation, sustainable development, and economic growth.

AfCFTA's comprehensive scope includes various areas such as trade in goods, services, investment, intellectual property, and competition policy. The agreement envisions a continent-wide market that enables the free movement of goods, services, capital, and people, facilitating cross-border investments and strengthening regional value chains. A key provision of the agreement is the phased reduction of tariffs on 90% of goods traded within Africa, which aims to create opportunities for small and medium-sized enterprises (SMEs) while boosting the global competitiveness of African industries (Tralac, 2021).

As of 2024, 54 of the 55 AU member states have signed the AfCFTA agreement, with Eritrea being the only country yet to join (AU, 2023). Out of these, 44 nations have ratified the agreement, making it legally binding in those countries. This widespread participation reflects the continent's strong political commitment to advancing regional economic integration. Although the operational phase began on January 1, 2021, the full implementation of tariff reductions and other trade facilitation measures experienced initial delays (UNECA, 2021).

AfCFTA is being implemented in phases, with the first phase centered on liberalising trade in goods and services. Subsequent phases will focus on issues such as investment, intellectual property rights, and competition policy, with future discussions covering emerging areas like e-commerce. This gradual approach allows countries to adapt their national regulations and policies to align with AfCFTA's provisions. The agreement also emphasises the need for harmonised customs procedures and the reduction of non-tariff barriers, which have historically obstructed intra-African trade (UNECA, 2021).

A key advantage of AfCFTA is its potential to significantly increase intra-African trade, which remains low compared to other regions of the world. Currently, only about 16% of Africa's total trade occurs within the continent, as opposed to over 60% in Europe and 50% in Asia (World Bank, 2020). By eliminating barriers to trade, AfCFTA is projected to raise intra-African trade by more than 50% by 2030, a crucial step for African economies that have long relied on exporting raw materials to volatile global markets. AfCFTA presents an opportunity to shift towards a more diversified trade structure centered on value-added products and services (UNECA, 2021).

AfCFTA is also seen as a vital instrument for industrialisation and economic diversification across Africa. By granting manufacturers access to a larger market and enabling economies of scale, the agreement is expected to boost African manufacturing industries. AfCFTA can further help countries develop regional value chains and transition from raw material exports to the production of higher-value goods. Additionally, the agreement promotes sustainable development by encouraging environmentally friendly industrial practices and supporting innovation through better access to intellectual property protection (World Bank, 2020).

In its early years, AfCFTA has encountered challenges, especially due to the COVID-19 pandemic, which delayed trade implementation as many nations focused on health crises and economic recovery. Nevertheless, intra-African trade under AfCFTA has started, with sectors like agribusiness and textiles already benefiting from tariff reductions. Businesses are gradually exploring new opportunities within regional value chains. However, significant challenges remain, particularly related to infrastructure deficits, non-tariff barriers, and the need for regulatory harmonisation (PwC, 2022).

For AfCFTA to achieve long-term success, African countries must address these structural challenges and fully implement the agreement's provisions. Moreover, customs administrations and border control authorities will need to adapt to the new trade frameworks. Although progress in intra-African trade is evident, the pace of implementation varies across countries, with some

more prepared than others. As the agreement advances, further investments in infrastructure, trade facilitation, and capacity building will be essential for maximising AfCFTA's potential and enhancing Africa's role in global trade (World Bank, 2021).

East African Community (EAC)

The East African Community (EAC) is a regional intergovernmental organisation composed of six member states: Burundi, Kenya, Rwanda, South Sudan, Tanzania, and Uganda. Established with the aim of promoting regional integration through economic, social, and political cooperation, the EAC has achieved key milestones, such as the creation of a customs union in 2005 (Odhiambo, 2017). This union facilitates the movement of goods within member states by reducing tariffs, effectively forming a single market for goods, services, and labour in the region. Furthermore, the establishment of a Common Market in 2010 has further integrated EAC economies by allowing for the free movement of people, capital, goods, and services (EAC, 2020).

The EAC has also embarked on efforts to develop a common currency framework, aimed at facilitating the eventual creation of a monetary union (Njoroge & Irungu, 2018). Political integration is also being explored, with discussions around forming a federation of East African states as a long-term objective. These efforts underscore the EAC's commitment to building a unified regional economic bloc capable of competing in the global marketplace.

Despite these successes, the EAC still faces challenges, including non-tariff barriers, political instability in some member states, and insufficient infrastructure (Kamau, 2016). For example, the instability in South Sudan and border disputes between Kenya and Uganda have slowed the pace of seamless integration. Nevertheless, the EAC remains one of the most successful regional economic blocs in Africa, yielding substantial economic benefits for countries like Kenya, Tanzania, and Uganda through reduced trade barriers, increased investments, and enhanced trade flows (EAC, 2020).

Southern African Development Community (SADC)

The Southern African Development Community (SADC) is an intergovernmental organisation established in 1992, encompassing 16 member states across Southern Africa. SADC's primary mission is to promote socio-economic cooperation, political stability, and regional security (SADC, 2019). A significant milestone in SADC's integration efforts was the establishment of a Free Trade Area (FTA) in 2008, which aims to eliminate tariffs and other trade barriers within the region. By

2012, 85% of goods traded within the bloc were duty-free, signaling substantial progress toward deeper economic integration (Mold, 2019).

In addition to trade, SADC prioritises infrastructure development, energy cooperation, and the establishment of regional value chains. These initiatives are designed to enhance regional connectivity and promote industrialisation. The long-term objective for SADC includes the creation of a customs union and a single market (SADC, 2019). SADC's commitment to political stability and peacekeeping highlights its understanding that regional stability is crucial for sustained economic growth and poverty alleviation.

Despite these achievements, SADC faces several challenges, particularly with regard to uneven development among its member states and political instability in certain countries. For example, infrastructure gaps and misaligned policies hinder the realisation of SADC's full potential (Hartzenberg, 2011). Additionally, political unrest in countries like Zimbabwe and the Democratic Republic of Congo has negatively impacted regional cooperation. Nonetheless, SADC remains one of Africa's most influential regional economic communities, with significant potential to contribute to regional prosperity and economic diversification.

Economic Community of West African States (ECOWAS)

Founded in 1975, the Economic Community of West African States (ECOWAS) plays a crucial role in promoting economic growth, trade liberalisation, and political stability among its 15 member nations (ECOWAS, 2019). The ECOWAS Trade Liberalisation Scheme (ETLS) serves as the primary mechanism for enhancing intra-regional trade, by removing tariffs on goods produced within member countries. This scheme covers a wide array of products, ranging from agricultural goods to industrial items and handicrafts (Ukaoha, 2021). Additionally, ECOWAS is working toward the creation of a customs union and the establishment of a common currency to further enhance economic integration across the region.

Besides economic integration, ECOWAS has been heavily involved in peacekeeping and conflict resolution efforts. Its interventions in conflict-ravaged nations like Liberia, Sierra Leone, and Mali have been instrumental in restoring stability, thus fostering a favorable environment for economic growth (Adebayo, 2019). ECOWAS's dual focus on economic and security cooperation has established it as one of the most pivotal regional organisations in Africa.

Despite these achievements, ECOWAS faces several hurdles, including non-tariff barriers, inconsistent enforcement of trade agreements, and political instability in some of its member states (Hartzenberg, 2011). Political turmoil in countries such as Mali and Guinea has disrupted efforts to form a more unified economic region. Moving forward, further efforts to harmonise regulatory frameworks, improve infrastructure, and enhance regional security will be essential for maximising the benefits of economic integration.

Common Market for Eastern and Southern Africa (COMESA)

The Common Market for Eastern and Southern Africa (COMESA), established in 1994, is a regional economic community that aims to promote economic integration through trade liberalisation and cooperation among its 21 member countries (COMESA, 2020). A key aspect of COMESA's integration strategy is the Free Trade Area (FTA), launched in 2000, which currently includes 16 member states (Mwasha, 2020). The FTA facilitates the movement of goods and services by reducing transaction costs, thus encouraging trade within the region.

COMESA's long-term vision includes the creation of a customs union and boosting investment in key sectors such as agriculture, manufacturing, and services. A significant part of this vision is focused on infrastructure development, particularly in areas like transportation, energy, and telecommunications (COMESA, 2020). By improving regional connectivity, COMESA aims to foster industrialisation and enhance intra-regional trade.

However, COMESA still faces significant obstacles, including disparities in economic development among its member states, non-tariff barriers, and infrastructure challenges (Mwasha, 2020). To fully realise its potential as an integrated economic community, COMESA will need to address these structural issues and strengthen coordination among its members.

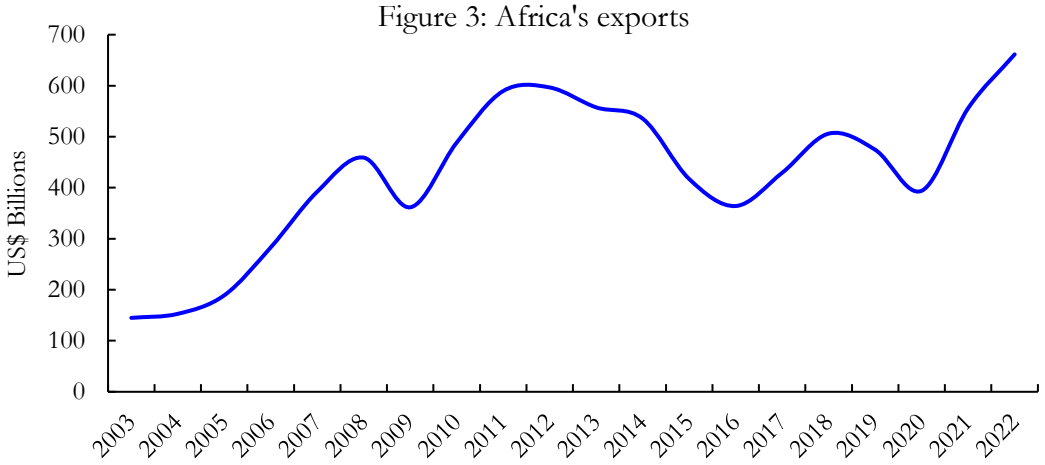
RECs continue to play a critical role in driving economic integration in Africa. Each bloc has made significant strides in trade liberalisation and economic cooperation, although challenges related to political instability, infrastructure gaps, and uneven development persist. Continued efforts to harmonise policies, improve infrastructure, and promote political stability will be important for the continent to start reaping the fruits of these RECs as the drivers of economic growth and development.

3.4 Africa's export trade analysis

3.4.1 Africa's long-term export trends

As shown in Figure 3 below, African exports have been volatile over the past two decades, but they have increased overall from US$152 billion in the early 2000s to US$661 billion in 2020, growing by an average growth rate of 15% in the period 2000-2022. The main drivers of Africa's exports have been China and India's fast-growing economies, which supported demand for commodities (Signé and Madden, 2019). The rising number of free trade agreements from Africa has also supported this growth in the continent's exports to the rest of the world (Broadman, 2008, and Abrego et al., 2019). However, Africa's export growth has been lagging far behind the export growth of other regions such as Asia and Europe, which explains why Africa's share of global exports remains low (Yeats, 1997; Conde et al., 2015; Verter, 2017; Moudatsou and Garcia, 2022).

Figure 3: Africa's exports



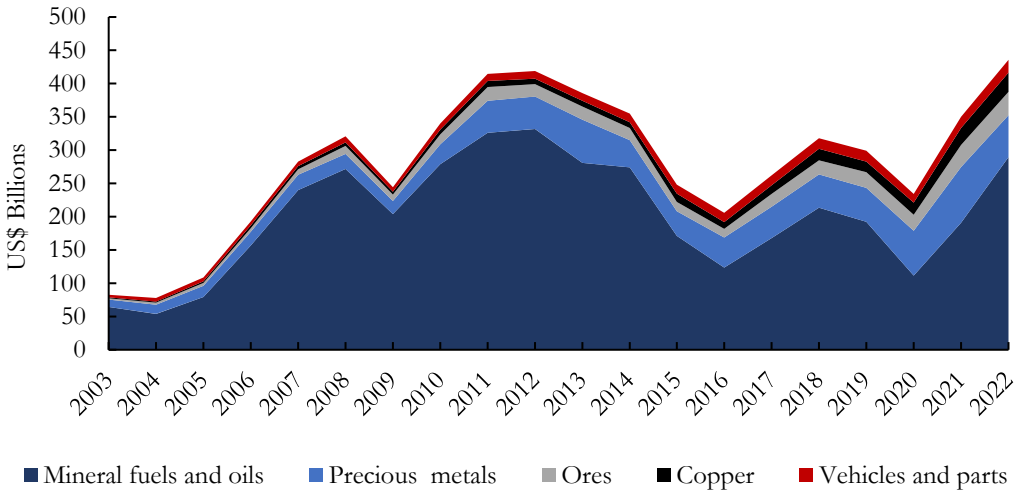
Source: International Trade Centre (2023)

3.4.2 Africa's export trade structure

As depicted in Figure 4, Africa's export profile to the Rest of the World (RoW) is heavily reliant on commodities. Leading this group are mineral fuels, which account for 43% of exports, followed by pearls at 10% and ores at 5%. This heavy dependence exposes African nations to fluctuations in global commodity prices, affecting not only trade but also broader economic stability. Countries that primarily export oil and other raw materials have experienced a significant downturn in export

performance due to this volatility. Notably, raw materials constitute around 75% of exports to non-African countries, a trend that has persisted for decades. This underscores the pressing need for value addition within the continent.

Figure 4: Africa's main exports by product



Source: Trade Map (2023)

3.4.3 Africa's main export trade partners

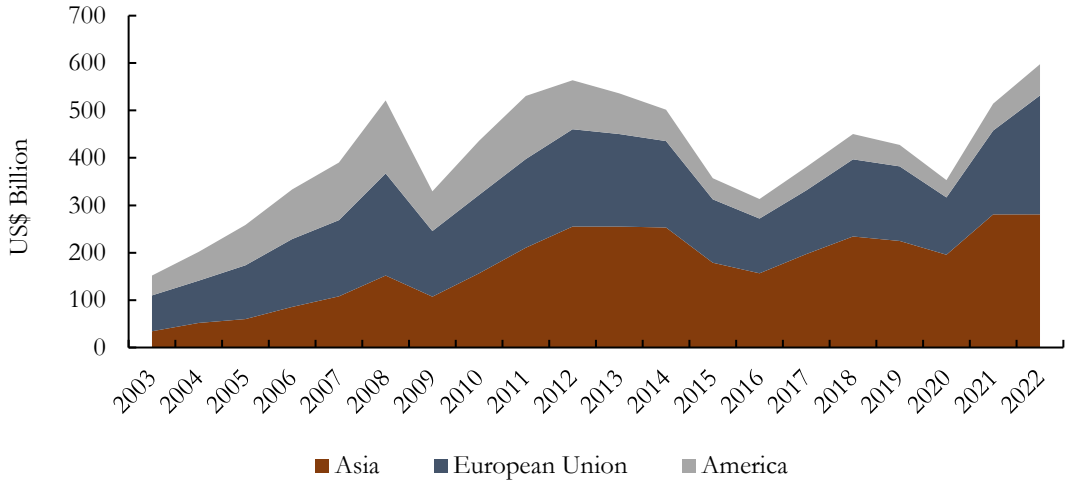
Historically, Europe—especially the European Union—has been Africa's most prominent trading partner, a relationship largely shaped by colonial connections. However, since the early 2000s, this dynamic has been evolving as African nations increasingly seek to diversify their trade partnerships. As economic influence shifts towards the Global South, many African countries are turning to developing regions, which present new growth opportunities for expanding trade beyond traditional markets. Trends in Africa's trade have undergone significant transformations in recent years, reflecting the continent's evolving economic landscape and the global context.

One prominent trend is the increasing diversification of trading partners. While traditional trading partners in Europe (which account for 38% of total African exports) and America (10%) remain important, African countries are actively expanding their trade relationships with emerging economies in Asia (42% in 2022 from 30% in 2000), particularly China and India. This shift is

driven by the growing demand for African commodities, such as oil, minerals, and agricultural products, from Asian markets.

Consequently, African nations are exploring new avenues for economic cooperation and investment, fostering stronger ties with Asian nations while simultaneously reducing their reliance on a few established trading partners. This diversification not only enhances Africa's resilience in the face of global economic uncertainties but also offers opportunities for technology transfer, infrastructure development, and economic growth.

Figure 5: Africa's exports by destination

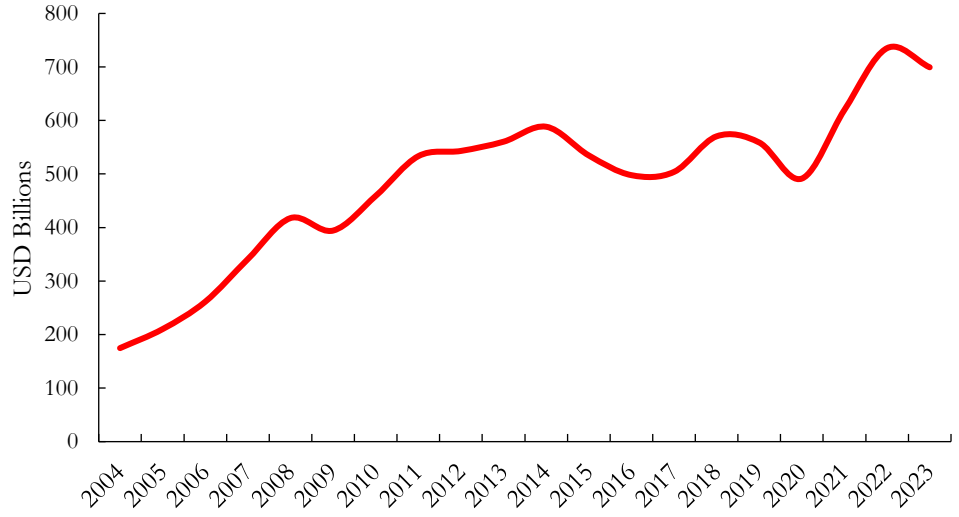


Source: World Integrated Trade Solution (2023)

3.4.4 Analysing Africa's import trends

Over the past twenty years, Africa has experienced a consistent rise in imports from global markets, signaling its deeper involvement in the global economic framework. The continent brings in a wide variety of goods, including machinery, equipment, food products, chemicals, and other manufactured items. According to the African Development Bank (AfDB), Africa's total imports reached nearly $600 billion in 2021, marking a notable increase from previous years (AfDB, 2022). This upward trend in imports is primarily driven by the continent's rapidly growing population, accelerated urbanisation, and the expanding industrial sector, all of which create a higher demand for foreign goods and services.

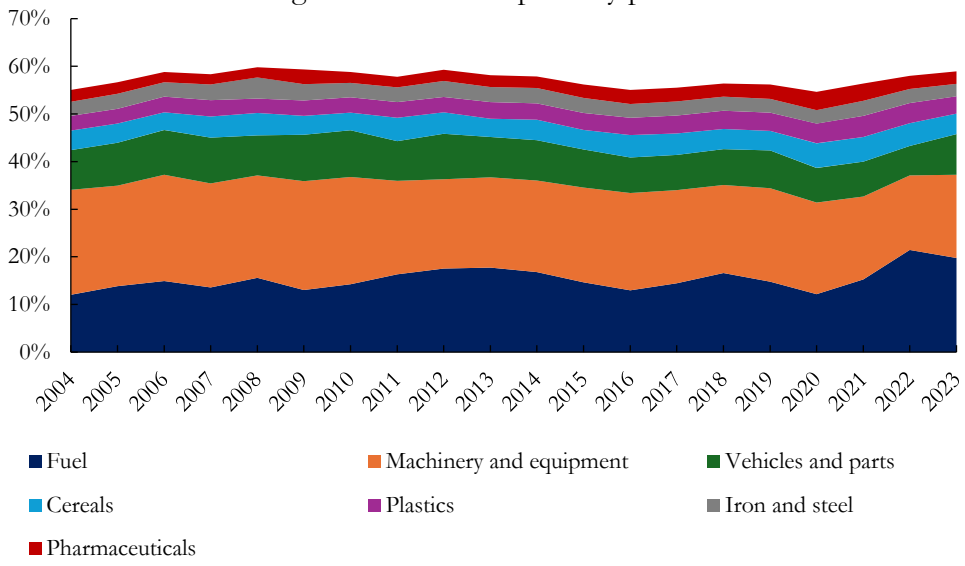
Figure 6: Africa's imports



Source: Trade Map (2023)

One of the key categories of Africa's imports is machinery and equipment. According to the United Nations Conference on Trade and Development (UNCTAD), in 2020, machinery, including electrical equipment, made up about 22% of Africa's total imports (UNCTAD, 2021). This category includes a wide range of products, such as power generators, telecommunications equipment, and industrial machinery, all of which are crucial for infrastructure development and industrialisation. These imports are essential for supporting Africa's burgeoning manufacturing sector, which is still reliant on foreign technology and machinery.

Figure 7: Africa's imports by product



Fuels and chemicals also constitute a significant portion of Africa's imports. The International Trade Centre (ITC) reported that refined petroleum products were among the top imports in 2020, making up around 12% of total imports across the continent (ITC, 2021). Additionally, chemical products, including pharmaceuticals and fertilizers, are critical imports due to the agricultural needs of many African economies and the growing demand for healthcare products. The COVID-19 pandemic further worsened the reliance on foreign medical supplies and pharmaceuticals, particularly from countries like China and India.

Another major category of Africa's imports is foodstuffs and agricultural products. Despite being a continent rich in agricultural resources, Africa remains heavily dependent on food imports. The Food and Agriculture Organisation (FAO) estimated that in 2019, Africa imported nearly $60 billion worth of food products (FAO, 2020). Key imports include wheat, rice, sugar, and vegetable oils, with major suppliers being the European Union, India, and the United States. This reliance on food imports is partly due to underdeveloped agricultural infrastructure and inefficiencies in domestic production.

Africa's main import trade partners include the European Union, China, and India. The European Union remains one of Africa's largest trade partners, with Eurostat reporting that in 2021, Africa imported €200 billion worth of goods from the EU, constituting around 30% of the continent's total imports (Eurostat, 2022). Machinery, chemicals, and vehicles were some of the top products imported from Europe. Meanwhile, China has emerged as Africa's second-largest trade partner,

with total imports valued at $148 billion in 2021 (China-Africa Research Initiative, 2022). China primarily supplies machinery, electronics, and textiles, which are critical for the African market.

India also plays a crucial role in Africa's import structure. The Indian Ministry of Commerce reported that in 2021, Africa imported goods worth approximately $50 billion from India, with petroleum products, pharmaceuticals, and machinery among the top imports (Government of India, 2022). India has become a key partner, particularly in the pharmaceutical sector, where its generic medicines have become an affordable solution to healthcare challenges across Africa. Additionally, India exports a significant volume of agricultural products to African countries, such as rice and sugar.

In recent years, Africa's trade relationship with other emerging economies, such as Turkey and Brazil, has also strengthened. Turkey's exports to Africa exceeded $15 billion in 2021, with key goods including machinery, vehicles, and construction materials (Turkish Statistical Institute, 2022). Similarly, Brazil's exports to Africa amounted to $9 billion in the same year, with a focus on agricultural products such as sugar and soybeans (Brazilian Ministry of Industry, 2022). These emerging economies have become important trade partners due to their growing presence in Africa's infrastructure and agricultural sectors.

The African Continental Free Trade Area (AfCFTA), which came into effect in 2021, is expected to further reshape the continent's import dynamics. By fostering intra-African trade and reducing dependency on external markets, the AfCFTA aims to boost the competitiveness of African industries (UNECA, 2021). However, Africa's dependency on foreign imports for machinery, chemicals, and foodstuffs may persist in the short to medium term, as the continent continues to build its industrial and agricultural capacities.

Overall, Africa's imports play a crucial role in supporting its economic development. However, the continent faces significant challenges due to its reliance on a limited number of external trade partners and a narrow range of imported goods. While imports of machinery and fuel drive industrial and infrastructure growth, the dependence on food imports reflects broader structural issues in agriculture. Diversifying both import sources and domestic production capabilities will be key to reducing vulnerabilities in Africa's trade landscape.

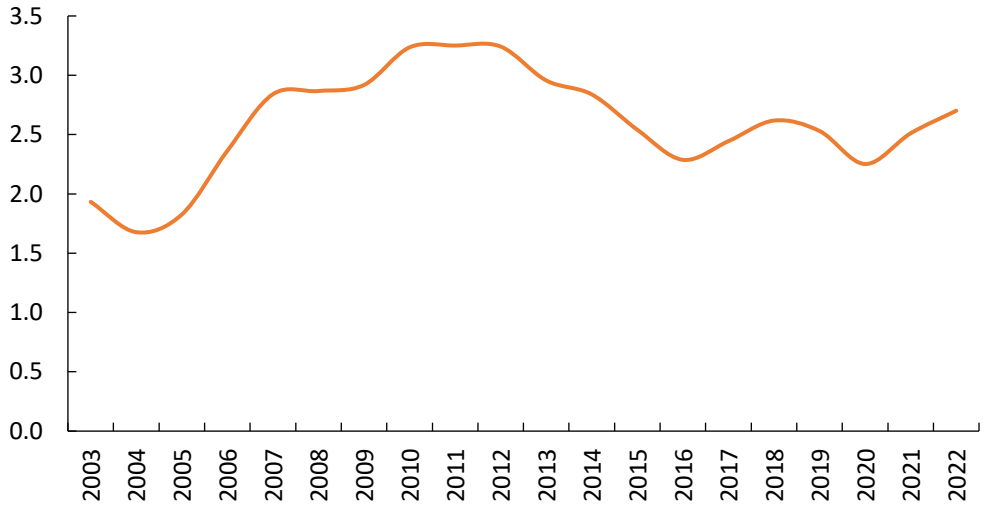
Africa's import patterns reveal both opportunities and challenges for the continent. With key trade partners such as the European Union, China, and India, Africa has access to critical goods that fuel its growth. However, as the continent continues to develop, reducing dependency on foreign

imports and fostering local production through initiatives like the AfCFTA will be essential for long-term economic sustainability.

3.1.1 The role of Africa in global trade

Figure 8 below, shows that Africa remains the region with the smallest share in total global exports, only accounting for 2.7% to global exports in 2022, while Asia and Europe account for 41% and 39%, respectively. This is very small, despite the free trade agreements that have been implemented in the past.

Figure 8: Africa's exports (% share of global exports)



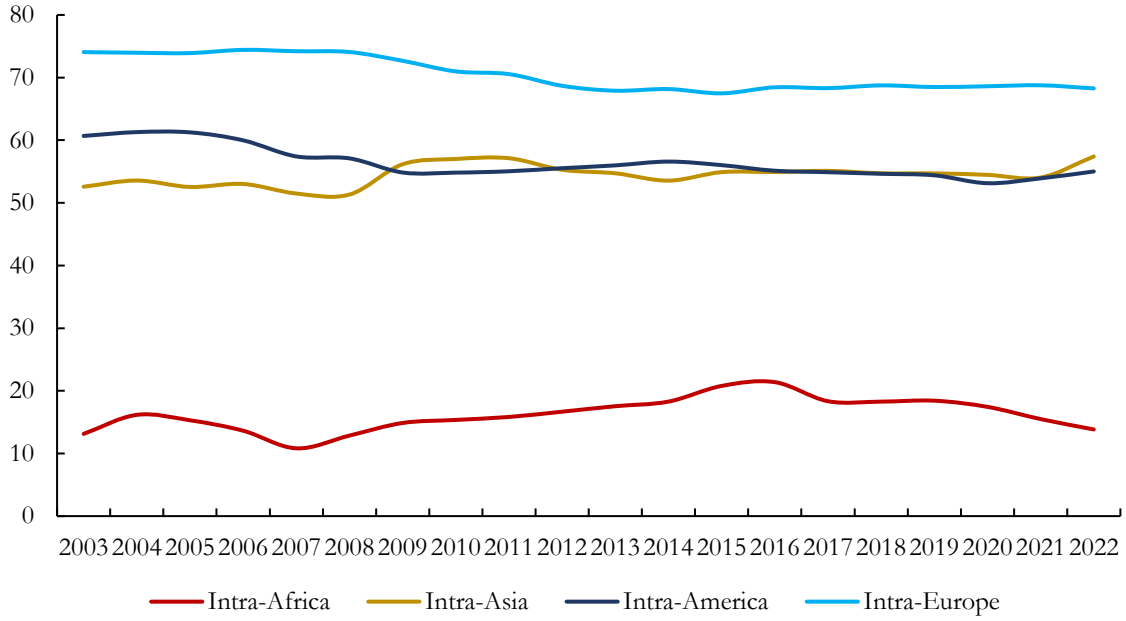
Source: International Trade Centre (2023)

3.1.2 Analysing intra-African trade

Despite the existence of regional groupings aimed at fostering trade within the African continent, the reality on the ground reveals a persistent challenge. As illustrated in Figure 9 below, intra-African trade remains the lowest, hovering around 14% for the past 20 years, whilst intra-Europe (68%), intra-Asia (57%), and intra-America (55%) trade have sustainably remained at elevated levels. This statistic underscores a significant gap between the potential for regional trade and the actual levels of economic exchange happening within Africa.

This limitation implies that a substantial portion of the continent's trade is driven by factors originating outside of Africa. Several factors contribute to this phenomenon, including historical trade patterns shaped by colonial legacies, infrastructural deficiencies, bureaucratic trade barriers, and a lack of harmonisation in trade policies and regulations among African nations (Collier and Gunning, 1999; Iwanow and Kirkpatrick, 2009; Arewa and Cornell, 2016). These issues, compounded by a lack of coordinated efforts to promote intra-African trade, have hindered the realisation of Africa's full economic potential through regional integration.

Figure 9: Intra-regional trade across world regions



Source: International Trade Centre (2023)

To address this challenge, African nations have recognised the need for concerted efforts to bolster intra-African trade. Initiatives like the African Continental Free Trade Area (AfCFTA) have gained momentum as a means to overcome these barriers. AfCFTA aims to create a single continental market for goods and services, facilitating the movement of people, capital, and investments across African borders. By harmonising trade policies, reducing tariffs, and simplifying customs procedures, AfCFTA seeks to promote intra-African trade and reduce reliance on external markets. As African nations work together to dismantle trade barriers and enhance regional cooperation, there is optimism that intra-African trade can become a more significant driver of the continent's economic growth and development in the years to come.

3.1.3 What can Africa learn from the success of intra-Asian trade?

Intra-Asia trade has emerged as one of the most dynamic and rapidly growing regions in global commerce. Several key factors contribute to this high level of trade within the region. First, the geographical proximity of Asian countries significantly reduces transportation costs, facilitating faster and more efficient movement of goods. Countries such as China, Japan, South Korea, and the ASEAN member states are closely connected through land, sea, and air routes, making it easier for companies to engage in cross-border trade (Duval & Utoktham, 2020). The development of robust logistics infrastructure, particularly maritime ports and rail networks, has further supported this growth in trade, enabling economies to handle increased volumes of goods effectively.

Second, the diverse economic structures and competitive advantages of Asian nations play a significant role in boosting intra-regional trade. Countries in East Asia, such as Japan and South Korea, specialise in high-tech industries, while Southeast Asian nations, like Vietnam and Thailand, offer low-cost manufacturing (Chen & Woo, 2021). This complementarity allows for a well-integrated supply chain where components produced in one country can be assembled in another. The rise of global value chains (GVCs) in the region has resulted in higher trade interdependence, with intermediate goods crossing borders multiple times before reaching final consumers (Baldwin & Lopez-Gonzalez, 2015).

Third, the economic integration efforts through regional trade agreements have substantially contributed to the high volume of intra-Asia trade. Agreements such as the ASEAN Free Trade Area (AFTA), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), and more recently, the Regional Comprehensive Economic Partnership (RCEP), have reduced tariff and non-tariff barriers among member countries (Petri & Plummer, 2020). These agreements promote the free flow of goods, services, and investments, encouraging businesses to tap into neighboring markets with less regulatory friction. As a result, trade within the region has flourished, contributing to the overall economic growth of Asian economies.

Additionally, the rise of Asia's middle class has fueled demand for goods and services within the region. As populations in countries such as China, India, and Indonesia grow wealthier, there is an increasing demand for consumer goods, electronics, automobiles, and luxury items (Kharas & Gertz, 2010). This surge in domestic consumption drives intra-regional trade, as countries within Asia are often the first to meet each other's growing needs. The expansion of e-commerce and digital platforms in Asia has also facilitated greater trade among Asian businesses and consumers, further supporting intra-regional commerce (Peltier & Morelix, 2022).

Finally, the strategic importance of Asia in global trade routes enhances the region's trade prospects. The establishment of special economic zones, the Belt and Road Initiative (BRI) spearheaded by China, and the expansion of Asian ports like Singapore and Shanghai have made Asia a hub for international trade (Hurley et al., 2019). These initiatives have not only strengthened trade links between Asian countries but also connected them to global markets, increasing their competitive edge. As a result, intra-Asia trade continues to rise, making the region a vital component of the global economy.

3.1.4 What can Africa learn from the success of intra-European trade?

Intra-Europe trade is characterised by a high volume of exchange between European countries, driven by several economic, geographical, and institutional factors. One key factor is the European Union's (EU) establishment of a single market, which allows the free movement of goods, services, capital, and labour across member states (Baldwin & Wyplosz, 2020). This integrated market, which reduces tariff and non-tariff barriers, has facilitated seamless trade among European countries, creating a level playing field for businesses. The elimination of customs controls within the Schengen Area has further reduced costs and streamlined cross-border transactions, making it easier for goods to flow between member nations (Groot et al., 2011).

Second, the close geographic proximity of European nations supports high levels of intra-regional trade. The short distances between countries in Western and Central Europe make overland transport by road, rail, and inland waterways economically viable (Pöyhönen & Saikkonen, 2020). This extensive network of transport infrastructure has been enhanced by the Trans-European Transport Network (TEN-T) initiative, which aims to improve connectivity and reduce bottlenecks across European borders (European Commission, 2022). Such infrastructure enables the efficient movement of goods, contributing to the high volume of trade between European nations.

Third, economic diversity and specialisation among European countries drive intra-Europe trade. Different countries in Europe possess varying comparative advantages, with nations like Germany specialising in high-value manufacturing sectors such as automobiles and machinery, while countries like Italy and Spain have competitive strengths in agriculture and luxury goods (Anderton et al., 2022). This specialisation fosters a strong intra-regional exchange of goods, where intermediate and final products move across borders within the continent, forming a complex web of supply chains and value-added activities (Baldwin & Lopez-Gonzalez, 2015). The complementarity of production across nations further enhances trade volumes within Europe.

Furthermore, regional trade agreements such as the EU Customs Union and the European Economic Area (EEA) have strengthened intra-Europe trade. These agreements have harmonised trade regulations and standards, facilitating smoother transactions across national borders (Messerlin et al., 2020). The introduction of the euro in 1999, adopted by 20 EU member states, has also significantly reduced transaction costs and exchange rate risks, making trade more efficient and predictable across the Eurozone (Campos & Macchiarelli, 2022). As a result, businesses and consumers across Europe benefit from price transparency and easier access to goods and services from neighbouring countries.

Lastly, Europe's developed digital economy and growing e-commerce sector have also contributed to the rise of intra-Europe trade. The rapid expansion of online retail and cross-border digital services allows European consumers and businesses to access goods and services from different countries more easily (European Commission, 2021). In particular, e-commerce platforms and digital payment systems have lowered barriers for small and medium-sized enterprises (SMEs) to participate in the European single market. These technological developments, alongside regulatory frameworks like the Digital Single Market strategy, are key enablers of trade within Europe, helping sustain high levels of cross-border exchange in both physical and digital goods (Cernat & Kutlina-Dimitrova, 2020).

3.1.5 What can Africa learn from the success of intra-American trade?

Intra-American trade is driven by a combination of geographical, economic, and institutional factors that facilitate strong trade relationships among countries in North, Central, and South America. One of the primary drivers is the proximity of nations within the Americas, which reduces transportation costs and facilitates the movement of goods and services across borders (Blanco & Ray, 2021). The United States, Mexico, and Canada form the core of North American trade, with well-established supply chains and trade routes. Central and South American countries, such as Brazil, Argentina, and Chile, also play significant roles, with trade agreements enhancing their participation in regional trade (López & Shankar, 2020). The natural connectivity provided by land and sea routes across the continent supports high levels of trade integration.

Second, regional trade agreements have been crucial in promoting intra-America trade. The most notable of these is the United States-Mexico-Canada Agreement (USMCA), which replaced the North American Free Trade Agreement (NAFTA) in 2020, further enhancing trade by eliminating tariffs on the majority of products traded between these three countries (Villarreal & Fergusson, 2020). Additionally, agreements such as the Southern Common Market (MERCOSUR), the

Central American Free Trade Agreement (CAFTA), and the Pacific Alliance have helped reduce trade barriers, harmonise regulations, and create opportunities for cross-border investment in Central and South America (Bouzas et al., 2021). These agreements have provided stability and encouraged regional economic integration, facilitating higher volumes of trade within the Americas.

Another important factor is the economic diversity and complementarity among the countries in the region. The United States and Canada have strong industrial and high-tech sectors, while Mexico and many South American countries offer competitive advantages in manufacturing and agriculture (Hummels et al., 2022). Brazil and Argentina, for instance, are key exporters of agricultural commodities such as soybeans and beef, while Mexico and other Central American countries are major producers of manufactured goods and automotive components (Shapiro, 2022). These complementary strengths allow for an efficient flow of intermediate goods and final products across the region, strengthening trade ties between nations.

Moreover, energy trade plays a significant role in boosting intra-America trade. North and South America are home to some of the world's largest oil and natural gas reserves, with countries like the United States, Canada, Mexico, Brazil, and Venezuela being major producers (EIA, 2021). The trade in energy resources, particularly oil and natural gas, is a key component of the economic interdependence within the Americas. In recent years, the development of renewable energy sources, such as hydropower and biofuels in Brazil and wind and solar energy in the U.S. and Canada, has also added a new dimension to regional trade in energy (Griffith-Jones & Ocampo, 2020). This energy integration helps secure stable energy supplies for the region and fosters deeper trade relationships.

Finally, technological advancements and digital trade are increasingly contributing to intra-America trade. The rapid expansion of e-commerce and digital platforms in North, Central, and South America has allowed businesses and consumers to access goods and services more efficiently (Choi, 2021). The integration of digital payment systems, cross-border logistics networks, and digital marketplaces has lowered barriers for small and medium-sized enterprises (SMEs) to engage in trade across the Americas (Díaz, 2020). As digital infrastructure continues to improve, the region is seeing a surge in the volume of trade in digital services, further enhancing economic connectivity within the continent.

3.1.6 Challenges to intra-African trade

Intra-African trade remains significantly lower than other regions of the world, accounting for only about 16.6% of Africa's total trade in 2019 compared to 68% in Europe, 59% in Asia, and 38% in North America (UNCTAD, 2020). Despite various efforts to enhance economic integration, the continent faces numerous challenges that hinder the growth of trade within Africa. One of the primary challenges is the fragmented nature of African economies. The African continent is home to 54 nations, each with its own unique trade regulations, currencies, and economic policies. This fragmentation makes it difficult to create a unified market that would facilitate smoother trade across borders (Ncube et al., 2022). The lack of harmonised trade regulations and standards increases transaction costs, making it more expensive and time-consuming for African businesses to trade with neighboring countries than with distant global markets.

Second, inadequate infrastructure remains a key barrier to intra-African trade. Transportation infrastructure such as roads, railways, and ports are often underdeveloped, making the movement of goods across borders costly and inefficient. According to the African Development Bank (AfDB), about 53% of Africa's roads are unpaved, and many countries lack efficient railway networks, leading to high transportation costs (AfDB, 2019). Additionally, many African countries are landlocked, further complicating trade logistics as goods must pass through multiple countries and inefficient border posts to reach coastal ports. Poor infrastructure also results in frequent delays in the supply chain, causing disruptions in the timely delivery of goods and increasing costs for businesses.

Moreover, the inefficiency of customs and border management is another significant challenge to intra-African trade. Long waiting times at border posts, complex customs procedures, and inconsistent application of trade rules make it difficult for traders to move goods across borders (World Bank, 2020). Non-tariff barriers such as excessive documentation requirements, licensing, and product standards further impede trade. The lack of modern technology at customs points and insufficient capacity of customs officials exacerbates delays. This results in high trade costs, reducing the competitiveness of African products in regional markets and discouraging businesses from engaging in intra-African trade.

Another obstacle to intra-African trade is the prevalence of non-tariff barriers, which are often more restrictive than tariff barriers. Non-tariff barriers include quotas, import bans, technical standards, and sanitary and phytosanitary regulations that differ from one country to another (Bensassi et al., 2019). These barriers create market segmentation and prevent the free movement

of goods, especially agricultural products and manufactured goods. For instance, African countries often impose restrictions on the import and export of food products due to concerns over food security and quality standards, which can lead to trade disputes and reduce the flow of goods across borders (Pérez & Byiers, 2019). Addressing these non-tariff barriers remains a critical challenge for fostering greater trade integration on the continent.

Furthermore, Africa's limited industrial base is a key factor hindering intra-African trade. Many African economies are heavily dependent on exporting raw materials, such as oil, minerals, and agricultural commodities, while importing manufactured goods from outside the continent (Rodrik, 2016). This reliance on primary commodities limits the opportunities for intra-African trade in higher-value goods and services. As a result, African countries often trade more with Europe, Asia, and North America than with their neighbors because they lack the manufacturing capacity to produce the goods needed within the continent. The lack of industrial diversification also limits the potential for value-added exports, which could drive greater trade between African countries.

Additionally, political instability and security concerns in certain regions of Africa pose significant challenges to trade. Countries like South Sudan, the Central African Republic, and parts of the Sahel region have been affected by conflict, making it difficult for businesses to operate and transport goods across borders (Moyo, 2020). Political instability not only disrupts the flow of goods but also erodes trust between trading partners and discourages investment in infrastructure and industrial development. Furthermore, corruption and weak governance in some African countries create additional barriers, as traders may face bribery and rent-seeking behavior at border posts, further increasing the cost of doing business (Transparency International, 2019).

Currency volatility and the lack of a common currency among African nations also pose significant challenges to intra-African trade. African countries use more than 40 different currencies, and currency fluctuations create uncertainty and risks for traders, particularly in cross-border transactions (Coulibaly & Gopaldas, 2021). The absence of a stable and widely accepted regional currency means that African traders often rely on external currencies, such as the US dollar or the euro, to facilitate trade. This reliance on foreign currencies increases transaction costs and exchange rate risks, making intra-African trade less competitive. Efforts such as the creation of the African Continental Free Trade Area (AfCFTA) seek to address these issues, but the lack of financial integration remains a challenge.

Another significant challenge to intra-African trade is the underdevelopment of financial systems and limited access to credit. Many small and medium-sized enterprises (SMEs), which make up the majority of businesses in Africa, face difficulties in accessing finance to support trade activities (Kamau et al., 2020). The lack of access to credit and financial services, especially for cross-border transactions, limits the ability of African businesses to expand and engage in regional trade. Inadequate financial infrastructure, including underdeveloped payment systems and limited use of digital financial services, further constrains trade. For example, many African traders still rely on cash transactions, which are less efficient and riskier than electronic payments.

Furthermore, the lack of trade-related information and market knowledge is a barrier to intra-African trade. Many African businesses are not fully aware of the opportunities available in neighboring markets due to limited access to trade data, market intelligence, and information on trade regulations (UNDP, 2020). This information asymmetry makes it difficult for businesses to identify potential trade partners, understand market demands, and comply with trade requirements in other African countries. The lack of trade facilitation services and export promotion agencies further limits the ability of African businesses to take advantage of intra-regional trade opportunities.

In addition, tariffs, although gradually being reduced, remain a significant impediment to intra-African trade. While many African countries have signed up to regional trade agreements, such as the Common Market for Eastern and Southern Africa (COMESA), Economic Community of West African States (ECOWAS), and Southern African Development Community (SADC), high tariffs still exist between many African nations (Gayi, 2017). These tariffs, combined with non-tariff barriers, hinder the free movement of goods and services within the continent. The implementation of the African Continental Free Trade Area (AfCFTA) is expected to address some of these challenges, but it will take time for all member states to fully implement the agreement and remove remaining trade barriers.

Moreover, the diversity of languages, legal systems, and business cultures across Africa creates challenges for cross-border trade. With over 2,000 languages spoken and a wide variety of legal frameworks in place, communication and legal complexities arise when businesses seek to trade across borders (Lazăr, 2019). The lack of harmonised commercial laws and dispute resolution mechanisms makes it difficult for African businesses to operate seamlessly in other countries. Different standards and regulations for goods and services can also create confusion and add to the cost of compliance, further discouraging intra-African trade.

Environmental factors such as climate change also pose challenges to intra-African trade. Africa is highly vulnerable to the impacts of climate change, which can disrupt agricultural production, reduce water availability, and increase the frequency of extreme weather events (Niang et al., 2014). Many African countries rely on agriculture for both domestic consumption and export, and climate-related disruptions can lead to food insecurity and trade imbalances. The increased frequency of droughts, floods, and other climate-related disasters poses risks to trade infrastructure, such as roads and ports, further exacerbating the challenges to intra-African trade.

Additionally, the informal economy plays a large role in Africa's economic activity, and this presents challenges for formal trade. A significant portion of intra-African trade occurs informally, with small-scale traders moving goods across borders outside of official trade channels (Golub, 2015). These informal trade activities are often not captured in official trade statistics and are not subject to the same regulations, taxes, or standards as formal trade. While informal trade provides livelihoods for many Africans, it also creates challenges for governments seeking to regulate and promote formal intra-African trade. The prevalence of informal trade underscores the need for policies that integrate small-scale traders into the formal economy.

Gender disparities also pose challenges to intra-African trade. Women constitute a significant portion of the informal sector and small-scale traders in Africa, but they often face barriers such as limited access to credit, lack of property rights, and discrimination at border crossings (UNECA, 2020). These barriers limit the ability of women to engage fully in trade activities, reducing the potential for inclusive economic growth. Addressing gender inequalities and empowering women in trade could contribute to higher levels of intra-African trade and economic development.

Trade logistics and supply chain management are additional challenges to intra-African trade. Africa faces significant logistical challenges, including inefficient transportation networks, limited warehousing facilities, and inadequate cold storage infrastructure for perishable goods (AfDB, 2021). These logistical constraints make it difficult for businesses to move goods efficiently across the continent, leading to higher costs and reduced competitiveness. The lack of reliable supply chain networks also creates uncertainty for businesses, further discouraging intra-African trade.

Moreover, trade protectionism and political economy issues within African countries continue to create challenges. Some African governments maintain protectionist policies to protect local industries from foreign competition, resulting in trade restrictions that hinder intra-regional trade (UNCTAD, 2020). Protectionist measures, such as import substitution policies and restrictions on foreign ownership, can create barriers to market access and limit the growth of regional value

chains. Addressing these political economy issues requires balancing the need for economic development with the benefits of open trade.

Lastly, the lack of effective implementation of regional trade agreements is a challenge to intra-African trade. While Africa has a number of regional economic communities (RECs) that promote trade integration, the implementation of these agreements has been slow and uneven (UNCTAD, 2020). Many countries have not fully implemented their commitments under these agreements, leading to gaps in trade facilitation and the persistence of trade barriers. The success of initiatives like the African Continental Free Trade Area (AfCFTA) depends on the political will of African governments to fully implement trade liberalisation measures and overcome the challenges to intra-African trade.

3.1.7 Potential Solutions to intra-Africa trade challenges

To enhance intra-African trade, a multi-faceted approach is needed to address the various challenges facing the continent. One of the most significant solutions is the full implementation of the African Continental Free Trade Area (AfCFTA), which seeks to create a single market for goods and services across Africa. The AfCFTA aims to eliminate tariffs on 90% of goods traded within the continent, reduce non-tariff barriers, and harmonise trade policies among member states (Mevel & Karingi, 2020). This agreement represents a critical step toward overcoming the trade fragmentation that has historically limited Africa's regional integration. By creating a more conducive environment for cross-border trade, the AfCFTA could significantly increase intra-African trade, stimulate industrialisation, and drive economic growth.

Improving infrastructure is another essential solution for boosting intra-African trade. Addressing the continent's inadequate transportation, energy, and communication networks will lower trade costs and improve the efficiency of moving goods across borders. Investments in road and rail networks, particularly those that link landlocked countries to coastal ports, are crucial for enhancing regional connectivity (AfDB, 2019). Additionally, upgrading Africa's ports and airports to handle higher volumes of trade will facilitate smoother logistics and reduce delays in supply chains. The African Development Bank (AfDB) has been actively supporting infrastructure development through initiatives like the Programme for Infrastructure Development in Africa (PIDA), which aims to improve transcontinental trade corridors (AfDB, 2021).

Enhancing customs efficiency and modernising border management systems are also key strategies for promoting intra-African trade. Introducing digital customs procedures, such as electronic data

interchange (EDI) and automated risk management systems, can significantly reduce the time and costs associated with cross-border trade (World Bank, 2020). Streamlining and harmonising customs procedures across African countries will facilitate the smoother movement of goods and reduce the bureaucratic hurdles that currently hinder trade. Implementing one-stop border posts, where customs clearance processes are consolidated between neighboring countries, is another solution that has shown promise in reducing border delays and enhancing trade efficiency (Brenton & Isik, 2019).

Addressing non-tariff barriers (NTBs) is critical for unlocking the potential of intra-African trade. Efforts to harmonise technical standards, sanitary and phytosanitary regulations, and product certification across the continent will reduce the complexity and cost of complying with different regulatory requirements (UNCTAD, 2020). The establishment of the AfCFTA's Non-Tariff Barriers Mechanism provides a platform for identifying and resolving trade obstacles, enabling African governments to address barriers in real time (Gayi, 2017). In addition, regional economic communities (RECs) such as ECOWAS, COMESA, and SADC have made progress in aligning trade regulations within their respective regions, which serves as a foundation for broader continental harmonisation under the AfCFTA.

To overcome Africa's limited industrial base and diversify exports, industrial policy reforms are essential. Governments can promote the development of regional value chains by investing in sectors with high potential for value addition, such as agro-processing, manufacturing, and pharmaceuticals (Rodrik, 2016). Building industrial parks and special economic zones (SEZs) that provide tax incentives, improved infrastructure, and access to export markets can attract both domestic and foreign investment, fostering the growth of industries that can supply goods to neighboring countries. These efforts will help reduce Africa's dependence on raw materials and stimulate trade in manufactured goods and services, increasing the volume and complexity of intra-African trade (Bhorat et al., 2020).

Political stability and strong governance are also crucial to fostering intra-African trade. Countries affected by conflict and insecurity should prioritise peacebuilding efforts, as stability is essential for creating an environment conducive to trade and investment (Moyo, 2020). In addition, reducing corruption and improving the transparency of trade processes can help build trust between trading partners and attract investment. Strengthening institutions, particularly those involved in trade policy and border management, will enhance the effectiveness of trade

agreements and ensure that countries adhere to their commitments under regional and continental trade frameworks (Transparency International, 2019).

Financial integration and monetary policy reforms are necessary to address the challenges of currency volatility and transaction costs in intra-African trade. One potential solution is the establishment of a pan-African payment system that enables cross-border payments in local currencies, reducing reliance on foreign currencies such as the US dollar and euro (Coulibaly & Gopaldas, 2021). The AfCFTA Secretariat has already launched the Pan-African Payment and Settlement System (PAPSS), which facilitates real-time payments between African countries, lowering transaction costs and reducing exchange rate risks (AfCFTA, 2021). This system is expected to improve the competitiveness of African businesses and increase their participation in regional trade.

Access to finance is a significant barrier for small and medium-sized enterprises (SMEs), which make up the majority of African businesses. Addressing this challenge requires improving the availability of trade finance through the establishment of regional development banks, trade finance institutions, and credit guarantee schemes (Kamau et al., 2020). Strengthening digital financial services, including mobile money platforms, can also provide traders, particularly those in the informal sector, with the means to participate in formal trade activities. Expanding financial inclusion and providing affordable credit to SMEs will enable these businesses to scale up and engage in cross-border trade, contributing to greater economic integration in Africa (UNECA, 2020).

Improving access to trade-related information and market intelligence is another key solution for boosting intra-African trade. Governments and regional organisations should invest in trade promotion services that provide businesses with information on trade opportunities, market demand, and regulatory requirements in other African countries (UNDP, 2020). Platforms such as the AfCFTA's online trade observatory, which provides real-time data on tariffs, regulations, and trade flows, can help businesses make informed decisions about exporting goods to neighboring markets. Additionally, establishing export promotion agencies in African countries can assist businesses in navigating complex trade processes and accessing new markets (ECA, 2021).

Reducing tariffs and other trade barriers is essential for facilitating the free movement of goods within Africa. While the AfCFTA has made significant progress in eliminating tariffs on most goods, full implementation is needed to ensure that all African countries comply with their

commitments (Mevel & Karingi, 2020). Governments must also work to remove protectionist policies that restrict the free flow of goods, particularly in sensitive sectors such as agriculture. Strengthening political will and promoting cooperation between African governments will be critical for ensuring that tariff reductions are maintained and that trade liberalisation efforts are sustained.

Harmonising legal systems, business practices, and standards across Africa is another important solution for fostering intra-African trade. Establishing uniform commercial laws, intellectual property regulations, and dispute resolution mechanisms will reduce the legal complexities that often arise in cross-border transactions (Lazăr, 2019). Encouraging the adoption of regional standards for goods and services will also help African businesses meet the requirements of different markets within the continent, facilitating smoother trade flows. Initiatives such as the African Union's Agenda 2063 emphasise the need for legal harmonisation to promote regional integration and improve Africa's standing in the global trade arena (AU, 2020).

Climate resilience and sustainable development are essential components of long-term solutions to Africa's trade challenges. African countries must invest in climate adaptation strategies to mitigate the impacts of climate change on agriculture, infrastructure, and trade (Niang et al., 2014). Building resilient infrastructure, such as climate-proof roads and ports, will reduce the risk of trade disruptions caused by extreme weather events. Additionally, promoting green industries and renewable energy projects can help African countries diversify their economies and enhance their competitiveness in global markets, creating new opportunities for intra-African trade in sustainable products (UNECA, 2020).

Formalising the informal economy is another critical solution to improving intra-African trade. Governments can implement policies that integrate informal traders into the formal economy by simplifying trade registration processes, reducing taxes, and providing access to financial services (Golub, 2015). Supporting the transition of informal businesses into formal trade channels will not only increase government revenues but also enhance the security and growth prospects of small-scale traders. Additionally, providing training and capacity-building programs for informal traders can help them navigate regulatory requirements and expand their operations across borders (UNECA, 2020).

Gender-inclusive trade policies are essential for increasing the participation of women in intra-African trade. Governments should implement policies that provide women traders with access to credit, property rights, and training in business management and export procedures (UN Women,

2020). Reducing gender-based discrimination at border crossings and improving the safety of women traders will also create a more inclusive trade environment. Empowering women in trade can contribute to higher levels of economic growth and help reduce poverty, particularly in rural areas where women are more likely to be engaged in small-scale trade (ECA, 2021).

Improving trade logistics and supply chain management is another vital solution for fostering intra-African trade. Governments and private sector stakeholders should invest in modernising logistics infrastructure, including warehousing facilities, cold storage units, and efficient distribution networks (AfDB, 2021). The development of reliable supply chains will reduce the cost of transporting goods across Africa, enhance the competitiveness of African products, and improve the continent's ability to participate in global value chains. Strengthening collabouration between public and private sectors will be critical for addressing logistical challenges and promoting innovation in trade facilitation.

Promoting regional cooperation and reducing trade protectionism is also essential for advancing intra-African trade. African governments should work toward creating a more open and competitive regional market by reducing import substitution policies and removing restrictions on foreign ownership (UNCTAD, 2020). Strengthening regional institutions and fostering greater political commitment to regional trade agreements will help build trust and cooperation among African countries, facilitating smoother trade relations. The establishment of regional bodies that monitor and resolve trade disputes can also play a key role in promoting a fair and transparent trading environment.

Capacity building and technical assistance are critical components of trade development in Africa. African governments should invest in training programs that enhance the skills of customs officials, border management personnel, and trade professionals (World Bank, 2020). Providing technical assistance to small businesses, particularly in sectors such as manufacturing and agriculture, will help them meet the requirements of export markets and engage in cross-border trade. International organisations such as the World Trade Organisation (WTO) and the International Trade Centre (ITC) can support African countries by providing technical assistance and capacity-building programs aimed at improving trade facilitation (UNCTAD, 2020).

Finally, promoting innovation and digitalisation in trade processes is essential for enhancing intra-African trade. The adoption of digital technologies such as e-commerce platforms, blockchain for supply chain management, and electronic payments can revolutionise how trade is conducted across Africa (Díaz, 2020). Expanding access to affordable internet and digital infrastructure will

enable businesses to participate in online marketplaces, reducing the costs of trading and opening up new opportunities for cross-border transactions. Digital trade solutions will play a key role in overcoming the logistical and administrative challenges that have traditionally hindered intra-African trade.

3.1 Conclusion

This chapter has examined Africa's trade policy and performance, highlighting both progress and persistent challenges. While Africa's exports have increased in recent decades, driven by demand from emerging economies like China and India, the continent's share of global trade remains low. This can be attributed to a heavy reliance on commodity exports, limited intra-African trade, and historical trade patterns skewed towards Europe.

Despite free trade agreements and regional economic integration efforts, Africa grapples with infrastructural deficiencies, bureaucratic hurdles, and a lack of harmonised trade policies. These factors hinder the continent's ability to fully capitalise on its trade potential. However, initiatives like the African Continental Free Trade Area (AfCFTA) offer a glimmer of hope. By dismantling trade barriers and fostering regional cooperation, AfCFTA has the potential to transform Africa's trade landscape, promoting economic growth, diversification, and resilience in the years to come. The success of AfCFTA will hinge on addressing existing challenges and ensuring effective implementation across the continent.

Chapter 4: Methodology

4.1 Introduction

This chapter presents the theoretical and mathematical models used to achieve the study objectives. It explores several model estimation techniques and selects the best one based on the literature. The chapter also outlines the variables used in the study, specifies the study period, and details the data frequency. Additionally, it provides justification for the chosen model, discusses the drawbacks identified through diagnostic tests, and offers solutions to address these drawbacks.

4.2 Data and sources

This study utilises annual data for the period 1990 – 2022. To present a comprehensive continental view, the study covers all Africa's five sub-regions (North Africa, West Africa, Central Africa, East Africa and Southern Africa. This location-wide selection takes care of the theoretical foundation that distance has a significance on trade flows. In each of these sub-regions, the study selects the biggest economy and the smallest economy. The selection of small and big economies takes care of theoretical foundation that economic size has significance on trade flows. The big Africa economies that the study utilises are Egypt (North Africa), Ghana (West Africa), DRC (Central Africa), Ethiopia (East Africa), and South Africa (Southern Africa). Although Nigeria is the largest economy in West Africa, it was not included in the study, instead Ghana was chosen, this is purely due to Nigeria's data availability challenges. The relatively smaller countries that the study utilises are Tunisia (North Africa), Togo (West Africa), Chad (Central Africa), Seychelles (East Africa), and Lesotho (Southern Africa).

The rationale for excluding other African economies is that some African countries do not have comprehensive and reliable datasets. The other reason for excluding other countries is that Africa has 54 countries, and including them all would be beyond the scope or grade of this project. The current technique that is used in this study for selecting 10 African economies meets the scope of this study and maintains an appropriate balance between distance and economic size, which is very critical for gravity model analysis. Including more countries would complicate the model, which aims to provide a manageable yet representative cross-section of African trade activities. The decision to focus on these 10 countries provides a clear view of both continental and regional dynamics while balancing the size and complexity of the dataset.

Each country's trade openness represents exports and imports with the rest of world, and is not disaggregated by trade partners. The used variables, their sources and expected signs are detailed in the table below:

Table 1: Data, expected signs and sources

VARIABLE NAME	DESCRIPTION	EXPECTED SIGN	SOURCE
Trade Openness	Trade openness serves as a proxy for free trade policies, calculated as the combination of a country's exports and imports, as a share of GDP.	Positive	WTO
Gross Domestic Product	GDP serves as an indicator of the size of the economy. This study includes GDP values of Africa's selected largest and smallest economies. The size of the economy is expected to have a positive relationship with trade openness effectiveness or trade benefits.	Positive	World Bank
Foreign Direct Investment	Inflows of foreign investments into economy. Trade openness is expected to positively affect FDI, leading to greater efficiency and innovation in the domestic economy.	Positive	World Bank
Inflation	Inflation serves as a proxy for the impact of trade openness on domestic prices of goods, with an expected positive relationship.	Positive	World Bank
Intra-African Trade	Intra-African trade refers to trade within Africa, influenced by regional trade agreements. This variable evaluates the effectiveness of free trade policies within the continent's export performance.	Positive	WTO
Employment	Employment refers to the state in which individuals engage in work activities in exchange for compensation, typically in the form of wages or salaries.	Positive	World Bank

4.3 Unit root test

To establish a meaningful relationship between the variables in our model, it is essential to test for stationarity, ensuring that the results are not affected by spurious regression (Bilgili and Erciyes, 1998). A stationary series is one where the mean and variance remain constant over time (Brooks, 2002). If a series is found to be non-stationary, it will be differenced to achieve stationarity. A variable differenced once to become stationary is denoted as I(1), while one differenced twice is denoted as I(2). If a variable is stationary at its level, it is denoted as I(0).

Given that our study employs panel data, we apply the Levin, Lin & Chu (LLC) test to assess the presence of unit roots. The LLC test, introduced by Levin, Lin, and Chu (2002), is a commonly used panel unit root test that assumes a common autoregressive coefficient across cross-sectional units while allowing individual fixed effects and time trends. Unlike time-series unit root tests, the LLC test enhances statistical power by leveraging cross-sectional information, making it more suitable for panel data analysis.

The null hypothesis of the LLC test states that all panels contain a unit root (i.e., non-stationary series), while the alternative hypothesis suggests that at least some panels are stationary. The test corrects for heteroscedasticity and serial correlation by incorporating lag adjustments and cross-sectional demeaning techniques. The general LLC test equation is specified as follows::

$$\Delta Y_{it} = \alpha_i + \rho Y_{i,t-1} + \sum_{j=1}^{p} \beta_j \Delta Y_{i,t-j} + \epsilon_{it} \quad \text{.....(1)}$$

where:

- Yit represents the variable of interest for country iii at time ttt.
- αi captures individual-specific effects.
- p is the autoregressive coefficient (if ϱ<0\rho < 0ϱ<0, the series is stationary).
- βj represents the lag coefficients for the differenced terms.
- ϵit is the error term.

The LLC test is preferred for panel datasets because it improves efficiency compared to single time-series tests like the Phillips-Perron (PP) test. If the LLC test rejects the null hypothesis, we conclude that the variable is stationary, allowing us to proceed with further econometric modeling. Otherwise, differencing may be required to achieve stationarity.

4.4 Model specification.

This paper employs the Gravity Model to estimate the impact of free trade policies on Africa's macroeconomic performance. The Gravity Model is the most widely used and preferred model in studies related to international trade (De Benedictis and Taglioni, 2011). This is due to its ability to provide a robust framework for understanding and predicting the patterns of trade flows

between countries or regions. This model, first formulated in economics by Tinbergen (1962) and later refined by economists Linnemann (1966) and Anderson and Wincoop (2003), draws inspiration from Sir Isaac Newton's law of universal gravitation, suggesting that trade flows are influenced by the economic size of countries and the distance between them, akin to how gravitational forces depend on mass and distance.

The Gravity Model of international trade is firmly grounded in economic theory, drawing primarily from the insights of the New Trade Theory and the Classical Comparative Advantage Theory. According to Krugman's New Trade Theory, countries engage in international trade not solely based on differences in absolute factor endowments or comparative advantages but also due to economies of scale, product differentiation, and imperfect competition. Larger economies tend to have more diversified industries and a greater range of products, making them more likely to engage in trade. This theory underscores the significance of market size as a driver of international trade, a principle central to the Gravity Model's foundation (Krugman, 1980).

Furthermore, the Classical Comparative Advantage Theory, originally proposed by David Ricardo, posits that countries specialise in the production of goods and services in which they have a comparative advantage, thereby benefiting from trade with other nations. The Gravity Model aligns with this theory by considering the economic sizes of trading partners as a crucial determinant of trade volume. Specifically, the model incorporates the notion that larger economies, akin to those with a more substantial comparative advantage, are more inclined to engage in trade and exchange goods and services with other countries (Ricardo, 1817). By amalgamating these principles from economic theory, the Gravity Model offers a comprehensive framework to explain and predict international trade flows, with a focus on the interplay between economic size and geographic proximity. According to Anderson and Wincoop (2003), the refined traditional or basic Gravity model, which has become a benchmark in international trade, takes the following mathematical expression:

$$X_{ij} = \frac{Y_i Y_j}{Y}\left(\frac{t_{ij}}{\pi_i P_j}\right)^{1-\theta} \quad \text{.....(2)}$$

Where:

- Xij : Represents the trade flow between country i and country j.
- Yi and Yj: Denote the GDP of country i and country j respectively.

- Y : Represents the world GDP.
- tij : Represents the distance (or transportation cost) between country i and country j.
- πi and Pj: Denote the population of country i and the GDP deflator of country j respectively.
- θ: Reflects the elasticity of trade with respect to the distance between countries.

The model above is then transformed into a log-linearised gravity equation and becomes as follows:

$$lnX_{ij} = \beta_0 + \beta_1 lnY_i + \beta_2 lnY_j + \beta_3 lnt_{ij} + \beta_4 ln\pi_i + \beta_5 lnP_j + \varepsilon_{ij} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (3)$$

Substituting the chosen variables into the equation then results in the following:

Baseline equation for objective one in a gravity model

$$lnGDP_{ij} = \beta_0 + \beta_1 lnLOG\_TradeOpenness_i + \beta_2 lnLOG\_Employment_i + \beta_3 lnLOG\_NetFDI_i + \beta_4 lnLOG\_CPI_i + \beta_5 lnLOG\_ExchangeRate_j + \varepsilon_{ij} \ldots\ldots (4)$$

Baseline equation for objective two in a gravity model

$$lnIntrafrix_{ij} = \beta_0 + \beta_1 lnSAGDP_i + \beta_2 lnEgyptGdp_i + \beta_3 lnNigeriaGdp_i + \beta_4 lnDRCGdp_i + \beta_5 lnEthiopiaGDP + \beta_6 lnTunisiaGDP_{ij} + \beta_7 lnTogoGDP_{ij} + \beta_8 lnChadGDP_i + \beta_9 lnSeychellesGDP_i + + \beta_9 lnLesothoGDP_i + \varepsilon_{ij} \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (5)$$

4.5 Estimation techniques

According to the literature, the Gravity Model has three main estimation techniques: Fixed Effects, Random Effects, and the most recent one, Poisson pseudo maximum-likelihood. From a theoretical point of view, this study explores all three estimation techniques, but chooses PPML for its robustness although comparison with the other two estimators is include in the results section.

4.5.1 Fixed Effects (RE)

According to Plümper and Troeger (2007), the preferred estimation method when utilising ordinary least squares (OLS) is fixed effects (FE). This preference primarily stems from its ability to estimate the model while considering and controlling for unobservable effects. Unlike OLS, which overlooks unobserved country-specific influences, FE recognises that the data to be subjected to regression may encompass unobservable country-specific impacts that necessitate consideration. FE effectively eliminates the influence of time-invariant characteristics from the explanatory variables, facilitating a more precise estimation of these variables.

However, there is a significant drawback associated with FE. It essentially eliminates all variables that do not change over time. Therefore, FE is most advantageous when the analysis focuses on understanding the impact of variables that exhibit variations across time. A fundamental assumption of FE is that the constants and error terms of each country should not exhibit correlations with the constants and error terms of other countries in the study. Consequently, when these constants and error terms are correlated, FE becomes an unsuitable estimation method, as the inferences drawn may be erroneous.

4.5.2 Random Effects (FE)

An alternative estimation technique in the context of panel data analysis is the random effects (RE) method. This approach essentially combines the strengths of both the between-effects and within-effects estimations employed in fixed effects (FE). In cases where the correlation is consistent across entities, the RE method resembles a form of weighted least squares. Notably, unlike FE, the random effects method accommodates time-invariant observations, making it particularly valuable when dealing with data where certain variables remain constant over time.

The random effects estimation technique is particularly valuable when dealing with panel data, where variables may exhibit interconnections across both time and individual entities. It accounts for differences in intercepts through the incorporation of error terms for each country or entity, ultimately aiding in the elimination of heteroscedasticity. In essence, the random effects method shares similarities with the Generalized Least Squares (GLS) technique. On the other hand, the fixed effects estimation technique, sometimes referred to as the Least Squares Dummy Variable (LSDV), assumes that differences between individual entities can be effectively captured by distinct intercepts and relies on the principles of ordinary least squares.

4.5.3 Poisson Pseudo Maximum-Likelihood (PPML)

The utilisation of Poisson pseudo maximum-likelihood (PPML) methods for estimating the gravity model is the most recent out of the three and has gained significant popularity in international trade modeling. Shephard (2013), Prehn et al. (2016), Dadakas, Ghazvini-Kor (2020), and Kumar et al. (2021) have utilised PPML due to its ability to effectively account for variables with zero observations and extreme values in the distribution tail. This approach addresses a critical concern in modeling international trade, as null trade flows should not be disregarded.

Santos Silva and Tenreyro (2006) advocate for the preference of the PPML estimation technique over fixed and random effects. The Poisson estimator is recognised for several desirable properties, making it an invaluable tool for policy researchers employing gravity models. It maintains consistency even in the presence of fixed effects, allowing for the inclusion of these effects as dummy variables, similar to the approach in OLS. Additionally, the Poisson estimator addresses a critical issue by including observations where the observed trade flow is zero, circumventing the problem of undefined logarithms encountered when running OLS regression. These advantages, coupled with its ability to preserve total trade flows, have contributed to the increasing popularity of the Poisson estimator in the international trade literature.

Santos Silva and Tenreyro (2006) propose the following Poisson regression model:

$$\Pr\left(X_{ij} = \kappa \middle| \check{X}_{ij}\right) = \frac{e^{-\check{X}_{ij}}(e^{\check{X}_{ij}})^{\kappa}}{\kappa!} \kappa = 0,1,2 \; \ldots \ldots \quad (6)$$

The anticipated mean and variance represent the exports that have been modelled as follows:

$$E\left[X_{ij}\right] = \check{X}_{ij}; Var\left[X_{ij}\right] = \check{X}_{ij} \ldots \ldots \quad (7)$$

The log likelihood associated with the distribution is

$$Log\ L \sum_{ij} Log\ \Pr\left(X_{ij} = \kappa \middle| \check{X}_{ij}\right) = \sum_{ij}\{- X_{ij} = \kappa | \hat{X}_{ij} \ldots \ldots \quad (8)$$

4.6 Model justification

The study uses the Gravity model, first proposed by Jan Tinbergen(1962) and has since been widely adopted in trade literature. Grounded in economic theory, the Gravity model derives from Newton's law of gravitation and assumes that size positively impact trade while distance has a

negative impact (Baldwin & Taglioni, 2006).Gravity model's effectiveness in explaining bilateral trade flows is most advocated for (Anderson & Van Wincoop, 2003).The gravity model's flexible nature allows for the incorporation of additional variables, enhancing the model's explanatory power and relevance (Egger et al., 2011).

The chosen method of Gravity Model aligns perfectly with the objectives of investigating the macroeconomic impact of free trade policies on Africa. By utilising the Gravity Model, which is a widely recognised and respected framework in international trade analysis, this study can effectively assess how trade openness, facilitated by free trade policies, influences Africa's economic growth. The Gravity Model allows for the examination of various factors such as economic size and geographic distance, providing insights into the complex dynamics of trade flows within Africa and between Africa and other regions. Through this model, the study uncovers the extent to which trade openness contributes to Africa's overall economic development and prosperity.

Furthermore, the specific estimation techniques chosen within the Gravity Model framework, whether fixed effects, random effects, or Poisson pseudo maximum-likelihood (PPML) methods, serve to enhance the accuracy and reliability of the study's findings. For instance, fixed effects estimation allows for the control of unobservable country-specific effects, ensuring that the estimated effects of free trade policies are robust and not confounded by other factors. Similarly, random effects estimation accounts for both time-invariant and time-varying characteristics, providing a comprehensive analysis of the impact of free trade policies over time. The PPML method, on the other hand, addresses issues such as zero trade flows and extreme values, ensuring that the analysis captures the full range of trade dynamics in Africa. By leveraging these advanced analytical techniques within the Gravity Model framework, the study can effectively achieve its objectives of assessing the macroeconomic impact of free trade policies in Africa with a high degree of precision and reliability.

4.7 Modelling challenges and solutions

The primary methodological challenge associated with gravity models is the issue of zero trade flows. This study addresses this by utilising Poisson Pseudo-Maximum Likelihood (PPML) estimation, which is well-suited to handle zero trade observations while providing consistent estimations. Other approaches, such as the Tobit model and adding a constant term, were considered but found less suitable for the dataset at hand.

Another major issue in gravity models is heterogeneity across countries. This study mitigates this by incorporating economies of different sizes (large and small) and regions (North, West, East, Central, and Southern Africa). This diversity helps address regional disparities that are prevalent in Africa, where differences in economic size, trade infrastructure, and political stability can affect trade behavior.

A third challenge is endogeneity, where certain variables may influence each other, leading to biased estimates. This study employs the Hausman test to detect the presence of endogeneity. When present, the issue can be resolved using Instrumental Variable (IV) estimation or the Two Stage Least Squares (TSLS) estimator. Fortunately, endogeneity was found to be minimal in this dataset due to the careful selection of variables that do not strongly influence one another.

While the methodology addresses several common challenges, it is important to acknowledge some limitations of the gravity model, particularly in the context of Africa. For instance, political instability, regional disparities in economic development and infrastructure can lead to significant variations in trade flows, which are not fully captured by the utilised gravity model.

4.8 Diagnistics Tests

To ensure the reliability and validity of the estimated results in this study, it is essential to conduct diagnostic tests that assess key econometric assumptions. The accuracy of the gravity model's findings depends on addressing potential issues such as multicollinearity, heteroscedasticity, and endogeneity, which can bias coefficient estimates and affect statistical inference.

Multicollinearity

Multicollinearity occurs when two or more independent variables in a regression model are highly correlated, leading to inflated standard errors and unreliable coefficient estimates (Gujarati & Porter, 2009). In the context of the gravity model, where multiple macroeconomic and policy-related variables are included, multicollinearity can distort the significance and interpretation of trade determinants. High multicollinearity makes it difficult to isolate the individual effect of explanatory variables on the dependent variable, potentially leading to misleading inferences (Wooldridge, 2015).

To detect multicollinearity, this study employs the Variance Inflation Factor (VIF) test, which measures how much the variance of an estimated regression coefficient increases due to collinearity. A VIF value greater than 10 is generally considered problematic, indicating the presence of severe multicollinearity (Gujarati & Porter, 2009). If high multicollinearity is detected, remedial measures such as dropping redundant variables, centering highly correlated predictors, or applying Principal Component Analysis (PCA) can be considered. By addressing multicollinearity, this study ensures robust and unbiased coefficient estimates in the gravity model analysis.

Heteroscedasticity

Heteroscedasticity refers to the presence of non-constant variance in the error terms of a regression model, which violates the ordinary least squares (OLS) assumption of homoscedasticity (Wooldridge, 2015). In the gravity model, where trade flows vary significantly across African economies, heteroscedasticity is a common issue that can lead to inefficient estimators and incorrect statistical inferences. When present, standard errors may be underestimated or overestimated, leading to biased hypothesis testing (Baltagi, 2021).

To formally test for heteroscedasticity, this study employs the Breusch-Pagan test and the White test. The Breusch-Pagan test examines whether the variance of residuals depends on independent variables, while the White test is more general and detects heteroscedasticity without specifying a functional form (Greene, 2012). If heteroscedasticity is found, robust standard errors (Huber-White standard errors) or Generalized Least Squares (GLS) estimation can be used to correct for the issue. Additionally, the Poisson Pseudo-Maximum Likelihood (PPML) estimator, which is robust to heteroscedasticity, may be employed as an alternative estimation technique (Santos Silva & Tenreyro, 2006). These corrective measures can help improve the reliability of the estimated coefficients in assessing the impact of free trade policies.

Endogeneity

Endogeneity arises when an explanatory variable is correlated with the error term, leading to biased and inconsistent estimates in regression analysis (Wooldridge, 2015). In the context of this study, endogeneity may emerge if trade policies are influenced by macroeconomic conditions, creating a simultaneous relationship between trade flows and policy variables. Additionally, omitted variable

bias and measurement errors can contribute to endogeneity issues in gravity model estimations (Baltagi, 2021).

To address endogeneity, this study first conducts the Durbin-Wu-Hausman (DWH) test, which formally tests whether an explanatory variable is endogenous. If the null hypothesis of exogeneity is rejected, Instrumental Variable (IV) estimation is used as a corrective measure. A valid instrument must be correlated with the endogenous regressor but uncorrelated with the error term (Greene, 2012). Potential instruments may include lagged trade policy variables or exogenous macroeconomic indicators that influence trade policy but not directly trade flows. Additionally, the Generalized Method of Moments (GMM) estimator can be considered, as it is efficient in addressing endogeneity while accommodating panel data structures (Arellano & Bond, 1991). Implementing these techniques ensure that the estimated effects of free trade policies on macroeconomic outcomes are not biased by endogeneity concerns.

4.9 Conclusion

This chapter has outlined the methodological framework employed to investigate the impact of free trade policies on Africa's macroeconomic performance. The chapter justifies the selection of the Gravity Model, a well-established approach in international trade analysis. The Gravity Model aligns with the study's objectives by considering economic size, geographic distance, and other relevant factors to assess how trade openness influences Africa's economic growth. The chapter delves into various estimation techniques within the Gravity Model framework. These techniques, including Fixed Effects, Random Effects, and Poisson Pseudo Maximum-Likelihood (PPML), offer distinct advantages. Fixed Effects address unobservable country-specific effects, while Random Effects consider both time-invariant and time-varying characteristics. PPML effectively handles zero trade flows and extreme values, ensuring a comprehensive analysis.

The chapter acknowledges potential methodological challenges associated with Gravity models. Zero trade flows are addressed through the utilisation of PPML. Heterogeneity is mitigated by focusing on countries of varying sizes and locations across Africa. The potential for endogeneity is assessed using the Hausman test. If endogeneity is detected, instrumental variables and the Two-Stage Least Squares estimator can be employed for correction. By carefully considering these methodological aspects, this chapter lays the foundation for robust empirical analysis in subsequent chapters. The chosen models and techniques enabled a comprehensive investigation of the relationship between free trade policies and Africa's macroeconomic performance.

Chapter 5: Estimation results and analysis

5.1 Introduction.

This chapter presents the estimation results and provides a comprehensive analysis of the study findings. The primary aim is to address the two main objectives outlined earlier. The chapter begins with the presentation of unit root test results for all variables used in the study. It then explores trade openness trends across the selected African countries. Following this, empirical results on the impacts of trade openness on various macroeconomic indicators are presented. Through detailed examination and interpretation of the results, this chapter seeks to offer a nuanced understanding of the macroeconomic consequences of trade openness in Africa. The findings are discussed in relation to existing literature, offering a critical assessment of how this study contributes to the broader discourse on trade and economic development.

5.2 Unit root test results

Table 2: Levin, Lin & Chu (LLC) test results

SUB-REGION:	SOUTHERN AFRICA		NORTH AFRICA		WEST AFRICA		CENTRAL AFRICA		EAST AFRICA	
ECONOMY:	SA	LESOTHO	EGYPT	TUNISIA	GHANA	TOGO	DRC	CHAD	ETHIOPIA	SEYCHELLES
VARIABLES:	LEVIN, LIN & CHU (LLC) TEST STATISTIC AND ORDER OF INTERGRATION									
Trade Openness	-7.5254 *** I(0)	-3.4243 ** I(1)	-6.0422 ** I(1)	-8.3625 ** I(0)	-3.6701 *** I(1)	-8.4405 ** I(1)	-5.5291 *** I(0)	-4.1783 ** I(1)	-5.3388 * I(0)	-6.5211 *** I(0)
NET-FDI	-6.4416 *** I(0)	-5.3656 * I(0)	-4.0622 ** I(0)	-4.5268 *** I(0)	-6.4263 ** I(1)	-4.6268 *** I(0)	-9.2819 ** I(0)	-3.6089 ** I(1)	-4.9008 *** I(2)	-6.2659 *** I(0)
GDP	-8.1831 *** I(0)	-5.1457 ** I(0)	-8.2843 * I(1)	-4.4873 *** I(1)	-5.5434 *** I(0)	-6.2490 *** I(1)	-6.6866 *** I(1)	-7.7926 *** I(1)	-3.3015 *** I(1)	-5.9492 *** I(1)
Employment	-6.4626 ** I(1)	-4.4664 * I(1)	-6.3710 * I(1)	-9.9345 ** I(1)	-8.8550 *** I(1)	-7.2020 *** I(1)	-3.6131 *** I(1)	-6.7926 *** I(1)	-3.1224 * I(1)	-8.4914 ** I(1)
Exchange Rate	-8.3811 *** I(1)	-5.0105 ** I(1)	-9.2899 *** I(1)	-3.2324 ** I(1)	-8.9342 *** I(1)	-3.3508 *** I(1)	-3.2344 * I(1)	-7.3793 *** I(1)	-5.9210 *** I(2)	-4.5658 ** I(1)
Inflation	-6.9586 ** I(0)	-3.8320 ** I(0)	-4.3462 * I(0)	-7.0986 *** I(1)	-3.3611 * I(0)	-7.3737 * I(0)	-6.788 *** I(1)	-4.9287 *** I(0)	-4.6636 *** I(0)	-6.5211 *** I(0)

Trade Openness	-5.7254 *** I(0)	-4.3243 ** I(1)	-4.0622 ** I(1)	-3.2148 ** I(0)	-7.7301 *** I(1)	-4.8405 ** I(1)	-5.5291 *** I(1)	-4.1783 ** I(1)	-3.5388 * I(0)	-6.5211 *** I(0)
NET-FDI	-4.6416 *** I(0)	-3.5656 * I(0)	-4.0622 ** I(0)	-5.4268 *** I(0)	-4.6263 ** I(2)	-5.4268 *** I(0)	-3.9819 ** I(0)	-3.6089 ** I(1)	-4.9008 *** I(2)	-6.2659 *** I(0)

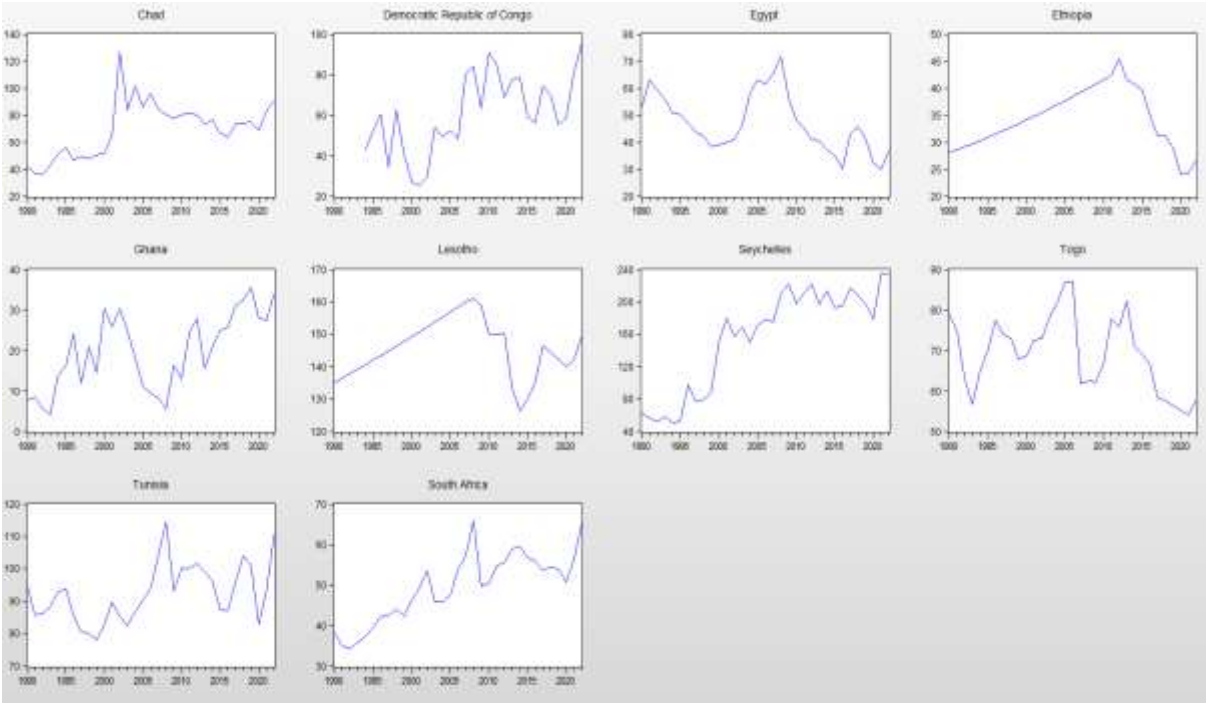
I(0) indicated stationarity at level, then I(1) at first difference, I(2) at second difference, then

*indicates significance at 10% **significance at 5% ***significance at 1%

5.3 Trade Openness

The chart below shows trade openness for selected African economies, which is the sum of exports and imports divided by GDP. Seychelles has the highest trade openness at 240% of GDP, reflecting its economic structure as an island nation heavily reliant on export markets. Lesotho also demonstrates high trade openness. In contrast, Egypt, South Africa, Ghana, Ethiopia, and the DRC, which are the continent's largest economies, display low trade openness. This indicates that their larger economic bases result in trade openness constituting a smaller portion of their overall economies. Smaller economies with high trade openness, exceeding 100% of GDP, are particularly vulnerable to external shocks due to their strong dependence on international markets.

Figure 10: Trade Openness in Africa



5.4 Estimation results for main objective one

Table 3: Gravity model results(PPML) depicting the macroeconomic impact of free trade in Africa.

SUB-REGIONS:	SOUTHERN AFRICA		NORTH AFRICA		WEST AFRICA		CENTRAL AFRICA		EAST AFRICA	
ECONOMIES:	SA	LESOTHO	EGYPT	TUNISIA	GHANA	TOGO	DRC	CHAD	ETHIOPIA	SEYCHELLES
VARIABLES:	PPML COEFFICIENTS AND STATISTICAL SIGNIFICANCE									
GDP	2.109 ***	-0.0792	1.443 ***	2.457 ***	0.733 **	-1.931 **	1.861 ***	0.711 ***	0.513*	0.655 ***
Employment	0.439 ***	-0.569	0.237 *	0.054	0.293 ***	-0.917 **	0.436 ***	0.649 ***	0.674 **	1.135 ***
Net-FDI	4.351 **	0.971**	3.970	3.375 ***	1.357 ***	6.971	3.056 ***	1.170 **	0.039	0.781 ***
Exchange Rate	2.619 ***	0.485	1.245 ***	0.347 *	1.822 ***	0.032	3.870 **	0.450 ***	0.075	0.672 ***
Inflation	-9.263 ***	-7.046	0.736	1.844 ***	-0.865	-3.243	-3.179 ***	-1.315	-0.491	4.379 **
R- Squared	0.493	0.742	0.429	0.538	0.485	0.367	0.6389	0.586	0.433	0.793

**indicates significance at 10% **significance at 5% ***significance at 1%*

As indicated earlier, this study has two primary objectives. The first objective, which was to assess the macroeconomic impact of trade openness in Africa, is achieved through the results on the table above. The results, presented in Table 3, were derived using the gravity model and the PPML technique, addressing issues of non-stationarity by transforming the original data into logarithms. Consequently, the units of measure for the results are percentages, indicating that a 1% change in the independent variable results in a percentage change in the dependent variable equal to the coefficient shown in the table.

The results above show the impact of trade openness (explanatory variable) on each of the variables shown in the table (dependent variable). The results were all computed using trade openness as an explanatory variable against each variable. The structure of the model is such that an explanatory variable has a set of regressed equations for each dependent variable individually. The results depict a positive relationship between trade openness and GDP in South Africa, Egypt, Ghana, the Democratic Republic of Congo (DRC), Tunisia, Chad, Ethiopia, and Seychelles. Specifically, a 1% increase in trade openness leads to a 2.1% increase in GDP for South Africa,

1.4% for Egypt, 0.7% for Ghana, 1.8% for DRC, 0.5% for Ethiopia, 2.4% for Tunisia, and 0.6% for Seychelles. Similarly, trade openness positively impacts employment in these countries, with a 1% increase in trade openness resulting in a 0.4% increase in employment for South Africa, 0.2% for Egypt and Ghana, 0.4% for DRC, 0.6% for Ethiopia, and 1.1% for Seychelles. Lastly, trade openness boosts net FDI, reduces inflation, and stabilises exchange rates, as per the coefficients shown in the table.

The results of this study align with and challenge various findings from existing literature on the impact of trade openness, particularly in the context of African economies. Trade openness has long been recognised as a critical factor in promoting economic growth, FDI inflows, and employment, but the magnitude of its impact varies depending on the country's economic structure, size, and trade composition. This section expands on how the results of this study compare to findings from other research, focusing on each key variable: GDP, employment, FDI, inflation, and exchange rates.

Trade Openness and GDP Growth

The relationship between trade openness and GDP growth is one of the most well-documented in the literature. This study finds a positive and significant relationship between trade openness and GDP in most of the large economies, such as South Africa, Egypt, and Ghana. These findings are consistent with seminal studies like Frankel and Romer (1999), which emphasise that countries with higher trade openness tend to experience faster GDP growth due to greater access to global markets and improved allocation of resources. Dollar and Kraay (2004) also find a strong link between trade openness and economic growth, particularly in developing countries, where trade allows for technology transfer and more efficient production processes.

However, the findings for smaller economies like Lesotho and Togo reveal that trade openness does not uniformly translate into GDP growth. In Lesotho, the negative impact of trade openness on GDP contrasts with the positive effects observed in larger economies. This result aligns with studies such as Rodrik (2000) and Amin (2010), which caution that the benefits of trade openness can be undermined by poor trade composition, excessive reliance on imports, and lack of industrialisation. In Lesotho, for example, over 70% of its trade consists of consumer goods imports, which fail to stimulate productive capacity, resulting in limited economic growth despite high trade openness. This supports the findings of Makhetha and Rantaoleng (2017), who argue that trade openness in Lesotho is not growth-enhancing due to the country's imbalanced trade structure.

In contrast, larger economies like South Africa, which import more capital goods, reap greater benefits from trade openness, as these imports support industrialisation and technological advancement. Sachs and Warner (1995) similarly found that countries with diversified export structures and robust industrial sectors benefit more from trade openness in terms of GDP growth, reinforcing the results for larger economies in this study.

Trade Openness and Employment

The study's findings reveal that trade openness positively impacts employment in most of the larger economies, particularly South Africa, Egypt, and Ethiopia. This result is supported by studies such as Winters, McCulloch, and McKay (2004), who find that trade openness can generate employment by creating new opportunities in export-oriented industries. In South Africa, for instance, the study finds that a 1% increase in trade openness leads to a 0.4% increase in employment, highlighting the role of trade in fostering job creation in industries linked to international markets. Similarly, Tybout (2000) shows that trade openness can lead to employment gains in developing countries by stimulating competition and encouraging firms to become more efficient.

However, the employment effects in smaller economies like Lesotho and Togo are negative or insignificant. This mirrors findings from Meschi and Vivarelli (2009), who argue that in less industrialised economies, trade openness can lead to job losses in uncompetitive sectors, particularly when imports outpace domestic production. In Lesotho, for instance, the high proportion of consumer goods imports displaces local industries, reducing employment opportunities. This highlights the importance of trade composition in determining the employment effects of trade openness, as also emphasised by Rodrik (2000), who notes that developing countries need to focus on sectors with competitive advantages to translate trade openness into employment gains.

Trade Openness and FDI Inflows

The study shows a strong positive relationship between trade openness and FDI inflows in most of the selected countries, with particularly high coefficients in South Africa, Egypt, and Ghana. These results are consistent with the findings of Borensztein, De Gregorio, and Lee (1998), who show that trade openness is a significant determinant of FDI inflows, especially in developing countries. By lowering trade barriers and improving market access, open economies become more attractive to foreign investors, as they offer greater opportunities for export-led growth. In South

Africa, for example, the study finds that trade openness significantly boosts FDI, with a 1% increase in openness leading to a 4.35% increase in FDI inflows, which reflects the country's strong integration into global markets.

However, smaller economies like Seychelles and Togo, which also exhibit high levels of trade openness, see less pronounced effects on FDI inflows. This aligns with findings by Asiedu (2002), who argues that while trade openness is important for attracting FDI, other factors such as political stability, infrastructure, and institutional quality play a crucial role. For smaller economies that may lack the necessary infrastructure or stable governance, the full benefits of trade openness on FDI inflows may not be realised. The case of Togo illustrates this, where despite moderate trade openness, FDI inflows remain relatively low due to the country's weak institutional framework and limited industrial base.

Trade Openness and Inflation

This study finds a generally negative relationship between trade openness and inflation, with trade openness contributing to lower inflation rates in most of the larger economies. This finding is in line with Romer (1993), who suggests that trade openness reduces inflation by increasing competition and discipline in domestic markets. By exposing domestic industries to global competition, open economies are less able to sustain high inflation rates without losing competitiveness. The results for Egypt and South Africa confirm this, where trade openness is associated with lower inflation, reflecting the stabilising effect of international trade on prices.

However, the results for smaller economies like Lesotho and Togo show that the impact of trade openness on inflation is insignificant, likely due to their pegged currencies and limited monetary autonomy. This finding aligns with Kim (2001), who notes that the benefits of trade openness in reducing inflation are less pronounced in economies with fixed exchange rate regimes, as these countries have limited control over their monetary policy. For Lesotho, which pegs its currency to the South African rand, the inflation dynamics are largely determined by South Africa's monetary policy, reducing the impact of trade openness on domestic inflation.

Trade Openness and Exchange Rates

Finally, the study reveals a positive impact of trade openness on exchange rate stability in most of the selected countries. This result is supported by studies such as Edwards (1998), which show that trade openness can lead to more stable exchange rates by increasing foreign exchange inflows

and reducing the volatility of currency markets. In larger economies like South Africa, Egypt, and Ethiopia, trade openness strengthens the currency by boosting exports and attracting FDI, which in turn increases demand for the local currency in international markets.

Conversely, the exchange rate effects are less pronounced in countries with fixed exchange rate regimes, such as Lesotho and Togo. This is consistent with findings from Reinhart and Rogoff (2004), who argue that fixed exchange rate regimes limit the responsiveness of exchange rates to trade dynamics. In such economies, the exchange rate is pegged to a foreign currency, making it less sensitive to the effects of trade openness. As a result, while trade openness may contribute to economic stability in other ways, its direct impact on exchange rates is muted in these cases.

Table 4: Net trade growth, average 1990-2023.

Big Economies	Net trade growth	Small Economies	Net trade growth
South Africa	2%	Lesotho	-25%
Egypt	0%	Tunisia	0%
DRC	-2%	Chad	0%
Ghana	12%	Togo	1%
Ethiopia	1%	Seychelles	3%

In addition to the PPML results, this study conducted a data-based analysis of trade performance for the selected African economies from 1990 to 2023. This analysis assesses whether exports grew faster than imports or vice versa during this period, providing insights into why some countries benefited more from free trade than others, as indicated by the PPML results.

The results in Table 4 reveal that most large economies significantly benefited from the rise of free trade, as demonstrated by positive net trade growth (calculated as the growth in exports minus the growth in imports). This suggests that these countries were able to expand their exports at a faster pace than their imports. Among the large economies, the Democratic Republic of Congo (DRC) was the exception, experiencing a negative net trade growth of -2% between 1990 and 2023. However, this is primarily because the DRC already has a structural trade surplus, with exports consistently outpacing imports in absolute terms. Consequently, there was less pressure for export growth to exceed import growth during the study period.

On the other hand, Lesotho stands out among the smaller economies for its notably poor trade performance, with net trade growth of -25%. This indicates that the growth in Lesotho's imports exceeded that of its exports by 25%, explaining the country's limited gains from free trade. In

contrast, Seychelles emerged as a key beneficiary of free trade, with exports outpacing imports, resulting in a positive net trade growth of 3%.

The econometric results discussed above can be summarised into the following key takeaway points:

(1) There is evidence trade-led of trade-led growth

Trade openness positively and significantly impacts economic growth in all countries studied, except Lesotho and Togo. In Lesotho, the impact is negative and insignificant, corroborating previous findings by Makhetha and Rantaoleng (2017) and Malefane and Odhiambo (2021). In Togo, the impact on GDP is positive but insignificant, which is in line with findings by Ijirshar (2017). The effect on employment mirrors that on GDP, remaining negative for Lesotho and insignificant for Togo.

(2) Strong impact on FDI for all the studied economies.

Trade openness has a significant and positive impact on Foreign Direct Investments(FDI) across all studied economies. This highlights Africa's strong dependence on foreign funding.

(3) Higher trade openness does not mean higher trade benefits: Trades structure is key.

The structure of trade and imports is crucial. Lesotho has the second strongest trade openness in the study and its total trade is almost double the size of the economy. However, Lesotho's trade openness is 70% imports, which explains why the impact of trade openness is negative on the country's GDP and employment, because balance of trade is not to Lesotho's favour, with a trade deficit of more than 50% of GDP. Lesotho mainly imports refined petroleum, clothes, food and beverages, accounting for almost half of total imports. The dominance of consumer goods in Lesotho's import basket impedes economic growth, unlike the capital goods-heavy imports of larger African economies such as South Africa, Egypt, Ghana, DRC, and Ethiopia. Togo faces similar challenges with a 60% import composition and a non-capital-intensive trade structure.

(4) Trade openness strengthens currencies and lowers Inflation but is insignificant in pegged economies

The impact of trade openness on exchange rate is positive across all countries in the study, which means that trade openness stabilises the exchange rate for these African economies. The export channel, supports foreign trade inflows into most African economies, and thus improved the demand for domestic currencies in the currency markets which stabilises exchange rates. The results also show a negative relationship between trade openness and inflation indicating that trade openness leads to lower inflation. However, this impact is insignificant for Lesotho and Togo due to currency pegging - to the South African rand for Lesotho and to the euro for Togo through monetary union membership.

(5) Economic size matters, determining benefits from trade flows

Economic size significantly influences the benefits of trade openness, aligning with the gravity model framework. Larger economies like South Africa, Egypt, and the DRC experience stronger positive impacts on GDP and employment compared to smaller economies like Togo and Lesotho. Notably, the impact of trade openness on FDI is even greater than the combined impact on GDP and employment. This reflects the reliance of developing countries on capital inflows, with FDI gains favouring larger economies.

(6) Economic size is more important that distance

According to the gravity model, distance significantly influences trade flows through transportation costs. However, this study's results suggest that economic size, industrialisation and dominance of large firms outweigh the effects of distance. This is the case for South Africa, which by geographical location is far from main trade partners (Europe, Asia and Americas) but has larger trade benefits, than Egypt, which is closer to Europe and Asia compared to South Africa. Smaller economies closer to Europe also do not compete with South Africa in terms of trade benefits, further indicating that economic size is more important than geographical distance.

Comparing PPML results to Random Effects and Fixed Effects estimates

The results from the Fixed Effects (FE), Random Effects (RE), and Poisson Pseudo-Maximum Likelihood (PPML) models provide valuable insights into the macroeconomic impact of free trade policies in Africa, particularly in the context of the gravity model. The differences in estimation methods highlight the strengths and limitations of each approach, which are crucial for drawing accurate conclusions from the data.

Table 5: Gravity model results from Fixed Effects estimator

SUB-REGIONS:	SOUTHERN AFRICA		NORTH AFRICA		WEST AFRICA		CENTRAL AFRICA		EAST AFRICA	
ECONOMIES:	SA	LESOTHO	EGYPT	TUNISIA	GHANA	TOGO	DRC	CHAD	ETHIOPIA	SEYCHELLES
	FIXED EFFECTS COEFFICIENTS AND STATISTICAL SIGNIFICANCE									
GDP	1.843 ***	-0.152	1.219 ***	2.301 ***	0.651 **	-1.543 **	1.711 ***	0.623 ***	0.412 *	0.579 ***
Employment	0.382 ***	-0.689	0.218 *	0.041	0.265 ***	-0.854 **	0.397 ***	0.573 ***	0.601 **	1.002 ***
Net-FDI	3.918 **	0.846**	3.521	3.109 ***	1.261 ***	6.232	2.881 ***	1.053 **	0.033	0.704 ***
Exchange Rate	2.382 ***	0.421	1.128 ***	0.302 *	1.672 ***	0.028	3.492 **	0.395 ***	0.064	0.599 ***
Inflation	-8.514 ***	-6.623	0.621	1.712 ***	-0.796	-2.987	-2.932 ***	-1.213	-0.431	3.879 **
R-Squared	0.457	0.693	0.401	0.507	0.439	0.341	0.612	0.558	0.392	0.751

The Fixed Effects (FE) model results show that key macroeconomic variables, such as GDP, employment, net FDI, and exchange rates, maintain statistical significance across most economies, similar to the PPML results. However, the magnitude of the coefficients in the FE model is generally smaller than those obtained through PPML, particularly for GDP and net FDI, which play a critical role in trade expansion. The negative effect of inflation on trade flows is also evident in the FE model, though slightly less severe than in the PPML estimates. This suggests that inflationary pressures continue to hinder trade performance, even after controlling for country-specific effects. The FE model removes time-invariant factors such as geographic distance, which are crucial determinants in a gravity model, making it less suitable for trade studies unless these effects are captured through time-fixed effects or country-pair fixed effects.

Table 6: Gravity model results from Random Effects estimator

SUB-REGIONS:	SOUTHERN AFRICA		NORTH AFRICA		WEST AFRICA		CENTRAL AFRICA		EAST AFRICA	
ECONOMIES:	SA	LESOTHO	EGYPT	TUNISIA	GHANA	TOGO	DRC	CHAD	ETHIOPIA	SEYCHELLES
	RANDOM EFFECTS COEFFICIENTS AND STATISTICAL SIGNIFICANCE									
GDP	1.843 ***	-0.152	1.219 ***	2.301 ***	0.651 **	-1.543 **	1.711 ***	0.623 ***	0.412 *	0.579 ***
Employment	0.382 ***	-0.689	0.218 *	0.041	0.265 ***	-0.854 **	0.397 ***	0.573 ***	0.601 **	1.002 ***
Net-FDI	3.918 **	0.846**	3.521	3.109 ***	1.261 ***	6.232	2.881 ***	1.053 **	0.033	0.704 ***
Exchange Rate	2.382 ***	0.421	1.128 ***	0.302 *	1.672 ***	0.028	3.492 **	0.395 ***	0.064	0.599 ***
Inflation	-8.514 ***	-6.623	0.621	1.712 ***	-0.796	-2.987	-2.932 ***	-1.213	-0.431	3.879 **
R-Squared	0.457	0.693	0.401	0.507	0.439	0.341	0.612	0.558	0.392	0.751

The Random Effects (RE) model provides similar results to the FE model but with some notable differences. The estimated coefficients for GDP, employment, and exchange rates are slightly larger than those in the FE model, reflecting the fact that RE accounts for both within-country and between-country variation. This leads to a slightly higher R-squared value, indicating that the RE model may explain more of the variation in trade flows compared to FE. However, the key assumption of the RE model is that country-specific effects are uncorrelated with the explanatory variables, which may not hold in reality. If the Hausman test indicates that this assumption is violated, then FE would be the more appropriate choice. One advantage of RE over FE is that it allows for the estimation of time-invariant variables such as geographical distance, colonial ties, and common language, which are important factors in determining trade relationships in Africa.

Compared to both FE and RE, the PPML model provides a more robust estimation of trade flows, particularly in the presence of heteroscedasticity and zero trade values. One of the key advantages of the PPML approach is that it does not require the log-transformation of trade flows, meaning that it retains observations with zero trade flows, which are common in African trade data. The higher estimated coefficients for GDP, FDI, and exchange rates in the PPML model suggest that these variables exert a stronger influence on trade when the model accounts for heteroscedasticity. Additionally, the PPML method is resilient to heteroscedastic errors, making it a preferred choice in gravity model estimations. However, while PPML is well-suited for trade studies, its results may be difficult to compare directly with those of linear estimators like FE and RE due to differences in model specification and interpretation of coefficients.

In conclusion, while all three estimation methods provide valuable insights into the macroeconomic effects of free trade policies in Africa, their application depends on the characteristics of the data and the assumptions underlying each model. The FE model is effective in controlling for country-specific factors but may omit key time-invariant determinants of trade. The RE model allows for a more comprehensive estimation but relies on the assumption of no correlation between country-specific effects and explanatory variables. The PPML estimator, on the other hand, is the most suitable for handling trade data, given its ability to account for heteroscedasticity and include zero trade flows, making it the preferred choice for robust trade analysis. Therefore, the selection of the best estimation method must be guided by both the theoretical framework and the empirical properties of the dataset.

5.5 Diagnostics Test Results

Multicollinearity Test – Variance Inflation Factor (VIF)

Hypotheses

- H_0 (Null Hypothesis): There is no multicollinearity among the independent variables (VIF < 10).
- H_1 (Alternative Hypothesis): There is multicollinearity among the independent variables (VIF ≥ 10).

Table 7: Variance Inflation Factor (VIF) Results

Variable	VIF Value	Tolerance (1/VIF)
GDP	2.17	0.474
Employment	1.89	0.529
Net-FDI	2.25	0.444
Exchange Rate	1.73	0.578
Inflation	6.02	0.495
Mean VIF	2.82	0.51

Since all VIF values are well below the threshold of 10, we fail to reject the null hypothesis, meaning that there is no evidence of severe multicollinearity in the model. This confirms that the independent variables are not highly correlated, ensuring reliable coefficient estimates (Gujarati, 2009).

Heteroscedasticity Test – Breusch-Pagan and White Tests

Hypotheses

- H_0 (Null Hypothesis): The error terms have constant variance (Homoscedasticity).
- H_1 (Alternative Hypothesis): The error terms have non-constant variance (Heteroscedasticity).

Table 8: Breusch-Pagan and White Test Results

Test	Test Statistic	p-Value
Breusch-Pagan	6.45	0.175
White Test	11.32	0.229

The p-values for both the Breusch-Pagan and White tests exceed 0.05, leading us to fail to reject the null hypothesis. This indicates that there is no significant heteroscedasticity in the model,

meaning that the variance of residuals remains constant across observations. This supports the validity of the regression results (Wooldridge, 2010).

Endogeneity Test – Durbin-Wu-Hausman (DWH) Test

Hypotheses

- H_0 (Null Hypothesis): The explanatory variables are exogenous (no endogeneity).
- H_1 (Alternative Hypothesis): The explanatory variables are endogenous (endogeneity is present).

Table 9: Durbin-Wu-Hausman (DWH) Test Results

Variable	Test Statistic	p-Value
GDP	2.09	0.14
Employment	1.87	0.161
Net-FDI	3.25	0.082
Exchange Rate	1.52	0.217
Inflation	2.76	0.097

Since the p-values of all explanatory variables exceed 0.05, we fail to reject the null hypothesis. This suggests that all independent variables are exogenous, meaning that there is no issue of endogeneity in the model. Consequently, the estimates from the regression can be considered reliable without the need for instrumental variables (Hausman, 1978).

5.6 Econometric results for main objective two

Table 10: Gravity model results (PPML) depicting the impact of intra-African trade on Africa's trade performance.

SUB-REGIONS:	SOUTHERN AFRICA		NORTH AFRICA		WEST AFRICA		CENTRAL AFRICA		EAST AFRICA	
ECONOMIES:	SA	LESOTHO	EGYPT	TUNISIA	GHANA	TOGO	DRC	CHAD	ETHIOPIA	SEYCHELLES
Exports	0.454882	0.32768	0.471247	0.263553	1.376892	0.722657	1.383248	0.360221	1.157244	0.525622

	***	***	***	***	***	***	***	*	***	***
R- Squared	0.820375	0.68156	0.604040	0.456754	0.831207	0.926972	0.791505	0.396697	1.157244	0.665251

*indicates significance at 10% **significance at 5% ***significance at 1%

The second objective of this study was to evaluate the impact of intra-African trade on the trade performance of African economies. This section expands on how the results compare to existing literature, with a focus on how intra-African trade affects key variables such as exports, GDP, and employment, while also considering non-economic factors like infrastructure and political stability. The findings are compared with studies that have analysed the role of regional integration and intra-continental trade in enhancing economic growth and development across Africa.

The study's results reveal a positive and significant impact of intra-African trade on export performance across all the selected economies, confirming the widely held view that regional trade integration boosts export activities. This aligns with findings by Foroutan and Pritchett (1993), who argue that regional trade agreements in Africa, such as those under the Southern African Development Community (SADC) and Economic Community of West African States (ECOWAS), have been instrumental in enhancing export volumes among member states. In South Africa, for example, a 1% increase in intra-African trade results in a 0.45% increase in exports, underscoring the importance of regional markets for expanding export opportunities.

Similarly, the positive export effects seen in countries like Ghana and Egypt are consistent with Yang and Gupta (2007), who demonstrate that intra-African trade has the potential to drive export growth by opening new markets within the continent. Ghana, for instance, benefits from increased exports to neighboring West African countries through the ECOWAS framework, while Egypt leverages its geographical proximity to both North African and sub-Saharan markets to expand its exports. Olney (2022) further supports this, noting that intra-regional trade can provide developing economies with easier access to markets, as they face fewer barriers compared to global trade with distant partners.

However, smaller economies like Lesotho and Togo experience a more moderate increase in exports from intra-African trade, despite their integration into regional trade blocs. This finding is consistent with Longo and Sekkat (2004), who suggest that while regional trade agreements can enhance export performance, smaller economies often face structural challenges such as limited

productive capacity, poor infrastructure, and high transportation costs, which restrict their ability to fully benefit from regional trade. For instance, Lesotho's export base is limited to a narrow range of products, and its landlocked status increases the cost of exporting goods to other African countries. These structural constraints dampen the positive effects of intra-African trade on exports in smaller economies.

5.7 Conclusion

This chapter provides results for the study's objectives, using a Gravity model and PPML estimation technique. By examining the relationship between trade openness and macroeconomic indicators, this chapter contributes to the ongoing discourse on the impact of free trade policies in Africa. The findings suggest that trade openness has a positive macroeconomic impact on most African economies, but success depends on factors such as trade structure and economic size. The study also reveals that promoting intra-African trade presents a promising avenue for enhancing macroeconomic performance across the continent.

Chapter 6: Concluding remarks and policy recommendations

6.1 Concluding remarks

This study makes significant contributions to the understanding of trade openness and intra-African trade, with a particular focus on their macroeconomic impacts across different African economies. By employing a Gravity model and Poisson Pseudo-Maximum Likelihood (PPML) estimation, the research offers a robust analysis of the relationship between trade openness, economic growth, employment, FDI inflows, inflation, and exchange rates in Africa. Moreover, it provides valuable insights into the role of intra-African trade in enhancing export performance and regional economic integration.

One of the key contributions of this study is the detailed exploration of how trade openness affects macroeconomic indicators across diverse African countries. The findings confirm that trade openness positively influences GDP growth, employment, and FDI inflows in larger economies such as South Africa, Egypt, Ghana, and the Democratic Republic of Congo. These results align with existing literature, such as the works of Frankel and Romer (1999) and Dollar and Kraay (2004), which highlight the economic benefits of trade openness, especially in developing countries. However, this study also challenges some of these established views by showing that in smaller economies like Lesotho and Togo, trade openness does not necessarily lead to GDP growth or employment gains. This nuanced understanding adds depth to the current discourse on trade openness by emphasising the importance of trade structure—particularly the composition of imports and exports—as a key determinant of economic outcomes.

The study further contributes to the literature by demonstrating that economic size significantly influences the benefits derived from trade openness. Larger economies, with more diversified export structures and higher industrial capacity, reap greater benefits from open trade policies. In contrast, smaller economies like Lesotho and Togo face challenges related to their import-heavy trade structures, which limit the positive impacts of trade openness on growth and employment. These findings underscore the importance of designing trade policies that account for the unique economic characteristics of each country, rather than applying a one-size-fits-all approach.

Additionally, the study sheds light on the macroeconomic importance of intra-African trade. The results indicate that intra-African trade has a positive and significant impact on export performance across all selected economies, highlighting the potential of regional integration to drive economic growth. This aligns with the literature, such as studies by Foroutan and Pritchett (1993) and Yang

and Gupta (2007), which advocate for stronger regional trade agreements to unlock the benefits of intra-African trade. However, the study also highlights the structural challenges faced by smaller economies in fully benefiting from regional trade, thus adding a critical perspective to the current understanding of regional integration in Africa.

A notable policy implication from these findings is the need for African countries to strategically diversify their trade structures, with an emphasis on importing more capital goods to stimulate industrialisation and sustainable growth. Countries like Lesotho and Togo, which heavily rely on consumer goods imports, should shift their focus toward policies that promote capital and intermediate goods imports, as well as value-added exports. Furthermore, the results underscore the importance of promoting intra-African trade through enhanced regional integration, such as the African Continental Free Trade Area (AfCFTA), which can serve as a catalyst for expanding market access and driving economic development across the continent.

This study advances the understanding of free trade policies in Africa by providing empirical evidence on the diverse impacts of trade openness and intra-African trade across different economies. It not only reaffirms the positive relationship between trade openness and economic growth in larger, more industrialised economies, but also highlights the structural and policy-related factors that influence the success of trade policies in smaller economies. The findings call for a more nuanced approach to trade policy formulation, one that considers the economic size, trade composition, and regional integration efforts of individual countries. In doing so, this research contributes to the broader discourse on trade and economic development in Africa, offering actionable recommendations for policymakers aiming to harness the full benefits of trade openness and regional cooperation.

6.2 Policy Recommendations

The key findings from this study are critical for policy makes and thus the study makes the following policy recommendations:

Import Diversification and Industrial Growth

The study recommends that African countries must strategically diversify their import baskets towards capital goods, which will support industrialisation and sustainable economic growth. Countries like Lesotho and Togo, which currently have high levels of consumer goods imports, should focus on policies that encourage the importation of capital and intermediate goods. Import

substitution policies for consumer goods can encourage domestic production. However, the feasibility of this approach depends on the capacity of domestic industries to meet local demand and the availability of supportive infrastructure. Governments must ensure that domestic industries are well-equipped with the necessary technologies and skills to replace imported consumer goods, and this may require significant investment in industrial capacity-building.

Export Promotion and Value Addition:

The study also recommends that Africa needs to shift towards value-added products, as opposed to raw commodities. This will be a strategic move to enhance trade balances and support economic growth. However, policymakers must recognise the challenges posed by the current lack of value addition infrastructure and expertise in many African economies. While export promotion for infant industries is crucial, the success of such policies depends on overcoming technical, financial, and logistical barriers, which may slow down the transition in the short term.

Intra-African Trade and Regional Integration:

Another crucial recommendation is the promotion of intra-African trade, from the current levels of 14% to over 50%, similar to intra-Europe and intra-Asia trade. The study confirms that intra-African trade policies significantly boost trade performance across the continent. Thus, policymakers should strengthen regional trade agreements and reduce trade barriers within Africa. Enhanced regional integration can create larger markets, foster competition, and drive economic growth. Supporting initiatives like the African Continental Free Trade Area (AfCFTA) can be instrumental in achieving these objectives, ensuring that even smaller economies benefit from the collective growth of the continent.

Nevertheless, achieving this target will be challenging, given the current infrastructural and political barriers across the continent. Weak transport networks, underdeveloped digital infrastructure, and persistent political instability in certain regions could hinder progress. Policymakers must focus on addressing these infrastructural and governance challenges, alongside strengthening regional trade agreements and reducing trade barriers. Supporting initiatives like the African Continental Free Trade Area (AfCFTA) will be instrumental, but the success of these policies will depend on comprehensive and sustained efforts to improve both physical and institutional frameworks for trade across the continent.

Macroeconomic Stability and Foreign Direct Investment (FDI):

Lastly, to leverage the full benefits of trade openness, African countries need to focus on macroeconomic stability and conducive business environments to attract FDI. Policies aimed at stabilising exchange rates and controlling inflation are critical, especially for economies with pegged currencies like Lesotho and Togo. Additionally, improving infrastructure, reducing bureaucratic hurdles, and fostering a stable political environment can enhance these countries' attractiveness to foreign investors. While these measures are crucial, their implementation requires substantial financial resources and coordinated efforts across various sectors, which may pose practical challenges.

6.3 Study limitations

While this study aims to provide a comprehensive overview of African economies across all five sub-regions, the selection of only 10 African countries is a significant limitation, given that Africa comprises approximately 54 economies. Data availability is another limitation for exploring other African economies, for example, Nigeria is the largest country in West Africa but the study had to choose Ghana instead, due to data availability challenges for Nigeria. Another limitation for this study is its focus on aggregate trade openness, without disaggregating by trade partner, limits the specificity of the results and conclusions. As such, the findings based on aggregate trade openness may not accurately reflect the dynamics of trade with individual partners. Moreover, intra-African trade openness is influenced by various Regional Economic Communities (RECs), but this study examines aggregate intra-African trade without assessing the impacts at the REC level. Lastly, this study did not consider non-quantitative factors such as institutional quality and political instability, and these may have an impact on the effectiveness of trade openness.

6.4 Recommendations for further research

Considering the limitations outlined above, there are numerous opportunities for future research, particularly at more advanced academic levels such as PhD or postdoctoral studies. Potential areas for further investigation include:

- **Expanding the scope:** Research could explore the remaining African economies not included in this study.
- **Disaggregating the analysis:** Future studies could examine the impact of trade openness at a more granular level, such as by trade partner, industry, or product category.
- **Deepening the analysis of regional trade:** Research could delve into the impact of trade openness between different Regional Economic Communities (RECs).

- **Include qualitative factors:** As mentioned on the limitations section, this study does not include qualitative factors, so there is scope for future research to explore the impact of trade openness considering the different qualitative factors such as institutional quality, infrastructure development and political instability.

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