

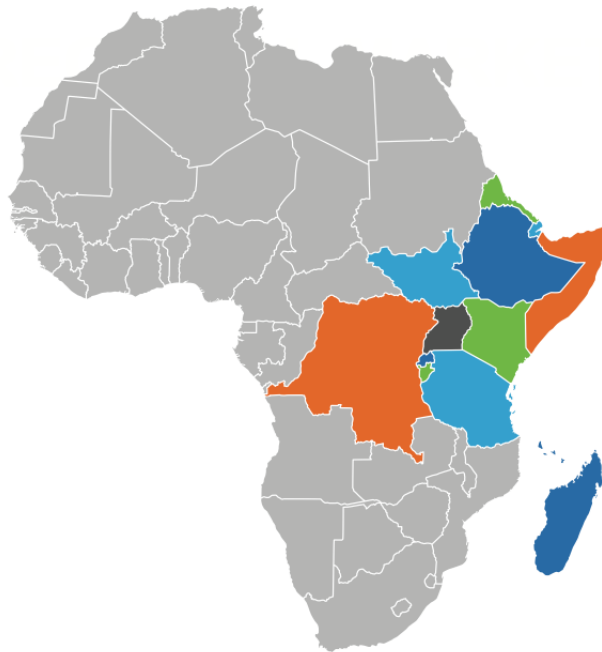


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The Economic and Social Impacts of the Covid-19 Crisis on Eastern Africa: Strategies for Building-Back-Better

The African Continental Free Trade Area: A Catalyst for Accelerating Services Trade in Eastern Africa

FULL REPORT

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United Nations
Economic Commission for Africa

THE AFRICAN CONTINENTAL FREE TRADE AREA: A Catalyst for Accelerating Services Trade in Eastern Africa

Abstract

This document reviews the evidence regarding the state of preparedness of Eastern Africa with regard to the implementation of the African Continental Free Trade Area (AfCFTA) in the area of services trade. The report highlights the opportunities, strengths and weaknesses of the regional economy in different services sectors, and discusses the areas for the attention of policymakers.

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Foreword

This report was written by staff of the Office for Eastern Africa of the Economic Commission for Africa. The lead author was Andrew Mold, and the main contributors were Raquel Federick and Samiha Chowdury (consultant). Inputs for an earlier draft were received from Rachael Nsubuga, Jessica Atsin and Geoffrey Manyara. The intention initially was to write a single report covering a thorough review of the services sector across Eastern Africa. However, given the wealth of materials, it was decided to publish this report in two parts – the first being this overview of the issues at stake, and the second to cover in more detail specific sectorial issues in the five AfCFTA priority service sectors – business services, tourism, transport, finance and ICT. The current version is a draft, and we would welcome comments from stakeholders regarding the text, with a view to publishing a revised version early in 2021. Finally, we would like to thank our colleagues Sizo Mhlanga and Bineswaree Bolaky at the Office for Southern Africa of UNECA for inviting us to present the preliminary findings at their Virtual Ad-hoc Expert Group Meeting (AGEM) on “*The African Continental Free Trade Area (AfCFTA) and Trade in Services: Opportunities and Strategies for Southern Africa*” on the 20th October 2020. That meeting was very helpful in terms of clarifying a lot of the service sector issues at stake in the crucial period of AfCFTA implementation. All errors in the report remain, of course, the responsibility of the authors.

Executive Summary

Despite its name, the African Continental Free Trade Area (AfCFTA) goes far beyond the establishment of a free trade area and includes provisions and Protocols on free movement, on investment, competition policy and intellectual property. One of the main areas flagged for intra-African liberalisation is Services. The AfCFTA identifies initially five service sub-sectors for liberalisation, on the basis that those five sub-sectors will have the greatest impact and synergies in increasing productivity and improving merchandise trade performance. But eventually the AfCFTA aspires to go beyond those five sectors and open up the whole range of services to intra-African competition. It is thus of crucial importance that policymakers in the region are aware of the implications and opportunities in these negotiations and have a more comprehensive understanding of the issues at stake.

This report argues that collectively the East African region stands to gain a lot from the establishment of a regional market in services trade, for a number of reasons:

1. Services have become the leading source of foreign exchange for around half of East Africa's member states. Moreover, at odds with most countries on the rest of the continent, the report reveals that the region has a revealed comparative advantage in services trade, of a fairly diverse nature (e.g. tourism, transport and financial services);
2. The report finds that the gains from intra-African merchandise trade liberalization (estimated in an earlier ECA (2020a) at around USD 1.8 billion) may be highly contingent on greater competition in associated services sectors, thus ensuring that the benefits from the reduction of tariffs on merchandise goods are passed on to consumers and firms.
3. The Report flags good examples (e.g. in telecommunications, finance) where a degree of liberalization has already benefited consumers and firms, through lower prices and/or improvements in quality/efficiency of service provision. The implementation of the AfCFTA could lead to more examples.
4. Finally, parts of the service sector in Eastern Africa are already highly profitable, signally both a lot of opportunities for intra-African investors and the scope for greater competition.

The report concedes that the starting point for East African member states is very different – the regulatory environment, the role of the state, the level of sophistication of the services sectors. Nevertheless, past precedent is encouraging. This report estimates econometrically that the establishment of the EAC Common Market led to an increase of 65 percent in bilateral services trade. The AfCFTA could contribute to compounding such gains across the region. Moreover, the econometric evidence shows that proximity matters as much for merchandise as for services trade. In principle, this puts regional firms in the services sector at an advantage in terms of being able to take up the opportunities from the AfCFTA.

As negotiations are still ongoing, knowledge about the state of the regional services sector is of prime importance. This document modestly sets forth some of the issues to be considered during the said negotiations, and points to areas of both strengths and weaknesses in the regional services market. The issues are not straightforward, with every service sub-sector having its own particular characteristics. Given their intangible nature and unique characteristics, negotiations are more challenging than that for goods. While we cover each of the service sub-sectors identified for priority liberalisation, the review is far from exhaustive. However, for policymakers wishing to see an overview of the issues at stake, we believe the current document should help gain a better understanding of what is at play.

1. Overview of the Issues at Stake

As a part of its goal to bolster intra-African trade, the AfCFTA committed itself to liberalizing services trade across the continent. Over recent decades, the services sector has become one of the key drivers of economic growth and structural transformation for many African countries (UNCTAD, 2016a:3). This is particularly apparent in Eastern Africa. In Kenya, for instance, the growth in the services trade has surpassed that of manufacturing and financial services; ICT, transport and tourism have been the main drivers (Khanna et al., 2016). In an effort to ‘leapfrog manufacturing’ (Berhuria and Goodfellow, 2018), Rwanda has expressly put services at the heart of its development strategy (Box 1).

In stark contrast to merchandise trade, where large deficits are recorded across the region, services have become a key contributor to export earnings, with six countries posting positive service trade balances in 2019 (Seychelles, Djibouti, Tanzania, Kenya, Madagascar and Ethiopia) and two countries (Rwanda and Uganda) not far from doing so. There is also an increasing recognition in the region that because many services act as inputs into manufacturing processes, an efficient service sector is also a key determinant of the competitiveness of manufacturing (Hoekman and Shepard, 2016; Newman et. al., 2016).

The economic import of the issue is therefore manifest. Negotiations under the AfCFTA are already well underway for service sector liberalisation, with currently ten countries across the continent having presented their preliminary offers. However, during the Covid-19 crisis, governments understandably focused on efforts to protect the citizens and limit the economic damage. In-person and virtual bilateral trade negotiations were delayed by logistic impediments (Fabricius, 2020) and the coming into force of the AfCFTA was postponed from July 2020 to January 2021. Global trade in services declined -30% in the 2nd Qtr of 2020, with some sub-sectors being hit particularly hard (WTO, 2020). The silver lining of the delays in AfCFTA implementation is that it has allowed some additional time to reflect on the long-term impacts of Covid-19 crisis on services trade.

The AfCFTA comes at a time when several member states in the region are reconsidering policy towards the strategic development of their services sectors.

As governments turn their attention to rebuilding their economies, there is a strong case for the AfCFTA to be a central part of national and regional strategies for economic recovery. It also comes at a time when several member states in the region are reconsidering policy towards the strategic development of their services sectors. In Ethiopia, for instance, 2019’s *Homegrown Economic Reform* policy envisages boosting the private

sector’s contribution to the service economy by opening up major public enterprises to private and foreign investment (Abitew, 2020)¹. Rwanda, for its part, is currently developing an explicit strategy for service sector exports. In sum, regardless of one’s position in the academic debate on the prevalent role of services in economic growth and development,² there is no gainsaying the centrality of the topic to the current developmental discourse.

¹ These include Ethiopian Airlines, Ethio Telecom, Ethiopian Electric Power Corporation, and Ethiopian Shipping & Logistics Services Enterprises. The country is also still considering liberalising its banking sector (Schipani, 2020).

² See Berhuria and Goodfellow (2019) for a summary of the different academic positions on the matter of ‘services vs. manufacturing-led development’.

Box 1: 'Leapfrogging Manufacturing'? Rwanda's strategy of service-led growth

Being landlocked, Rwanda faces the challenges of lack of proximity to ports, raising transportation costs for raw material imports and finished good exports, causing the country to lose competitiveness vis-à-vis low wage manufacturing economies. However, Rwanda has developed a solution by focusing on service-led growth to 'leapfrog manufacturing'. Tourism is a priority sector and additionally two main strategies of Meetings, Incentives, Conferences and Events (MICE) and Finance, Insurance and Real Estate (FIRE) are being implemented with the goal to be a hub for Eastern and Central Africa. The construction of Kigali Convention Centre and the 30 million USD sponsorship of Visit Rwanda on Arsenal's jerseys were key initiatives to back up these strategies. Over the years Rwanda has seen a surge in the number of visitors for professional and personal reasons courtesy to the impressive levels of safety and security it maintains and the niche tourism experience that it offers. The national airline RwandAir is an intrinsic part of this strategy, beginning its operations in 2002, rapidly expanding its fleet and currently flying to 24 destinations. The results have been encouraging - services exports have grown at an average annual rate of 11.4% and the share of services exports in total exports reached around half by 2019 (UNCTADstat, 2020).

The goal of the service-led strategy is twofold: economic growth and job creation to be able to absorb the growing size of the working age population forecast to increase from 6.7 million in 2014 to 16 million in 2050 (World, Bank, 2016). However, the service sectors inherently necessitate labour with the requisite technical knowledge. In an attempt to fill the skills gap in the tourism sector, for instance, the government has established both the Rwanda Tourism University College and Akhilah Institute for Women. Skills gaps still persist, however, and the Rwandan government takes the gradualist approach of simultaneously importing capacity and developing local capacity by promoting skill transfer (Behuria and Goodfellow, 2018). As an EAC member state, through the *Movement of Natural Persons Protocol*, Rwanda has been able to hire professionals from other EAC countries to help fill capacity gaps in the local labour market. This temporary solution of hiring workers from the regional community is preferable to hiring people from outside the continent, as it causes greater spill-overs in the regional block through rising in incomes, consumption and multiplier effect (Behuria and Goodfellow, 2018). In future, the implementation of AfCFTA may enhance the scope for regional labour market integration for Rwanda and help strengthen its skill transfer networks all over the continent. If more investment in the service sector can be attracted from firms originating in Africa through the AfCFTA, there could be greater scope of skills' spillovers to the local population and thus more job creation for Rwandan nationals. Finally, African-wide integration will open a multitude of opportunities for Rwanda to collaborate on appropriate initiatives to overcome the bottlenecks in its service sector.

Against this backdrop, this report makes the case for **the AfCFTA as a timely catalyst for the expansion of services trade in Eastern Africa**. The AfCFTA was signed in March, 2018, at an African Union Summit held in Kigali, Rwanda. Of 55 total African Union member states, 54 countries have signed up and the process of ratifications is well underway. As of October 2020, 33 countries have ratified – 5 of them Eastern African member states.³ For those countries who have deposited their ratifications, the AfCFTA will become operational on 1 January 2021. It

The AfCFTA is a timely catalyst for the expansion of services trade in Eastern Africa

³ Those countries are Djibouti, Ethiopia, Kenya, Uganda and Rwanda.

aims to remove tariff and non-tariff barriers on substantially all trade in goods and services, liberalising the movement of people and investments.

Under the free trade area, trade in services will be governed by the Protocol on Trade in Services whose aim is to create “open, rules-based, transparent, inclusive and integrated single services market.” The first phase of negotiations focuses on five priority sectors: business, communication, financial, transport and tourism services. Negotiations of the remaining seven sectors will follow thereafter (African Union, 2018).⁴ In parallel, countries are negotiating frameworks to foster regulatory cooperation in the services sector.

Trade in Services negotiations are very different - and often more difficult - than negotiations in goods trade

Nonetheless, it is worth acknowledging from the outset that *Trade in Services* negotiations are very different - and often more difficult - than negotiations in goods trade (Keller, 2019). Unlike goods, there are no tariffs on services. Liberalizing services is thus not about reducing the duty on a product. Instead, countries negotiate about a broad range of public

policy concerns governing market access and regulating service provision. Not only are services trade negotiations complex, but, if the European Union experience is anything to go by, implementation can be very challenging. Nonetheless, the overall assessment - and with the benefit of hindsight - of the European Union experience is one of large potential benefits from creating a more integrated regional market in services (Box 2).

Box 2: Lessons from the EU Experience of Establishing a Regional Services Market

The European Union (EU) was probably the first regional block to explicitly recognise the potential advantages of creating a regional services market. Free trade in services was enshrined in the founding Treaty of Rome of 1957. The Treaty reflects awareness of the wide variety in products of the service branches and stipulates two freedoms: to be able to provide services in another member state without having to set up an office or reestablishment in that country and; the right to set up a company in another member state to provide that service, under the same terms and conditions as a national from that country.⁵ But the step-change in EU policy with regards to service trade liberalisation came with the establishment of the European Single Market on 1 January 1993.

Initial assessments were quite modest in terms of their estimates of the potential gains. It was estimated that the completion of the internal market for services would lead to an increase of total intra-EU trade of 1 to 3 percent and a growth impulse of some 1 percent for GDP and 0.3 percent for total employment (Kox et al., 2004); (Copenhagen Economics, 2005). Subsequent evaluations have put the gains as being much larger. By use of a new generation gravity model, Mayer et. al (2018) find that the Single Market to have increased intra-regional services trade between EU members by 58 percent, lower than the 109 percent on average for goods, but still a large impact. The associated welfare gains from EU trade integration are estimated to reach 4.4 percent for the average European country, with smaller economies tending to gain more proportionately than larger ones.

⁴ In future phases, the intra-African liberalisation of the sectors of construction, distribution, education, energy, environmental, health and social services will be addressed.

⁵ A few exceptions were made, for diverse reasons, for medical and pharmaceutical professions, transport services, and banking and insurance services.

There is also evidence that price dispersion has decreased under the influence of increased competition: the index went down by one third between 1993 and 1996 and by one fifth between 1995 and 2000 (EC, 2001). This tendency has since been reinforced. In some countries, prices of international and national long-distance calls (markets in which competition is fiercest) have been cut by 30 percent or more. However, prices for local calls (a market still dominated by the former monopolists) have scarcely decreased at all. The decrease in prices of mobile phone services has been particularly significant in recent years.⁶ So the sector provides an example where liberalisation has actually boosted total output, improved the product range, reduced prices and supported net job creation (Molle, 2016).

One again, however, not all the studies converge. A study by [Badinger \(2007\)](#) used data on 10 EU Member States over the period 1981–1999 for each of 3 major industry groups (manufacturing, construction and services) and 18 more detailed industries to test whether the EU’s Single Market Programme reduced firms’ price–cost mark-ups, i.e. had a pro-competitive effect. While he found mark-up reductions for aggregate manufacturing and construction, mark-ups had risen in most service industries since the early 1990s. Badinger suggests that this latter finding confirms the weak state of the Single Market for services and suggests that anti-competitive defense strategies have emerged in EU service industries (Baldwin, 2015).

In-depth knowledge about the state of the regional services sector is of prime importance... The issues at stake are not straightforward, with every service sub-sector having its own particular characteristics

As AfCFTA service sector negotiations are still ongoing, in-depth knowledge about the state of the regional services sector is of prime importance. One of the main stumbling blocks to the implementation of trade services-related policies is the lack of understanding and quantification of services trade, and more generally, the role services play in regional and global value chains ([Karingi, 2019](#)). This document modestly sets forth some of the issues to be considered during the said negotiations, and points to areas of both strengths and weaknesses in the regional services market. The issues are not straightforward, with every service sub-sector having its

own particular characteristics. While we cover each of the service sub-sectors identified for priority liberalisation, the review is far from exhaustive. However, for policymakers wishing to see an overview of the issues at stake, we believe the current document should help gain a better understanding of what is at play.

2. Some Initial Theoretical and Practical Considerations

Why liberalise services at all? The theoretical arguments for the integration of service markets are on the face of it similar to the ones for goods markets (Francois and Hoekman, 2010, Molle, 2016): A higher degree of *international specialisation* raises the efficiency of resource allocation. Consumers will be offered a greater choice, and economies of scale and scope will be better exploited (for instance, in banking through spreading risks; in air transport by improving

⁶ However, Molle (2016: 100) notes that there is still quite some variation among the countries of the EU that can be explained by differences in regulation, notably on aspects that determine consumer switching cost such as number portability.

market access, and in telecommunications by reducing unit costs, etc.). Firms across the economy will benefit as a consequence of the resultant downward pressure on costs.

Although this may seem initially surprising given their relatively undeveloped services sectors, arguments for a more competitive, open, regional market in services gain particular traction in developing country settings because of the perceived 'revealed comparative advantage' that many developing countries possess in services trade.⁷ As we shall see in this report, in fact this is not necessarily the case for the whole of the African continent, but it certainly does seem to be true for Eastern Africa. All the more reason for regional governments to take a proactive stance in the negotiations of the service sector protocol of the AfCFTA.

It is easy to confuse arguments for wholesale liberalisation of services sectors with the arguments for the creation of an intra-regional market for services.

However, it is easy to confuse arguments for wholesale liberalisation of services sectors with the arguments for the creation of an intra-regional market for services. The conventional view has been in support of wholesale liberalisation, as opposed to selective liberalisation with regional partners.⁸ The AfCFTA is about the latter. It therefore will demand a *selective* opening in favour of service sectors providers based in other member states,

not a global opening up of services sub-sectors. The distinction is important but frequently ignored by trade economists.⁹ It matters because a lot of developing countries – including countries in Eastern Africa – were initially quite hostile to the services sector being included in the multilateral agenda in the 1990s and 2000s, seeing it as a way of high income countries to prise open markets in sectors where they had a strong competitive advantage, while simultaneously refusing to budge on the issue of agricultural liberalisation (Moon, 2000, Madeley, 2008). These opposed views in part explain the collapse of the Doha Round of WTO multilateral negotiations. Many of the concerns of developing countries were legitimate ones – it does of course matter who you open up to, particularly in view of the large competitive gap that exists between certain high-income countries with highly advanced and sophisticated services sectors, and poorer developing countries with lower prevailing levels of human capital and productivity.

⁷ Measured on a balance-of-payments basis, see, for instance, Sapir and Lutz (1981), Bhagwati (1987), Stern and Hoekman (1987) and Francois (1987). The *revealed comparative advantage* index is the ratio of a country's exports of specific products to its total exports relative to the world average. If the ratio is greater than one a country is said to have a revealed comparative advantage in the product.

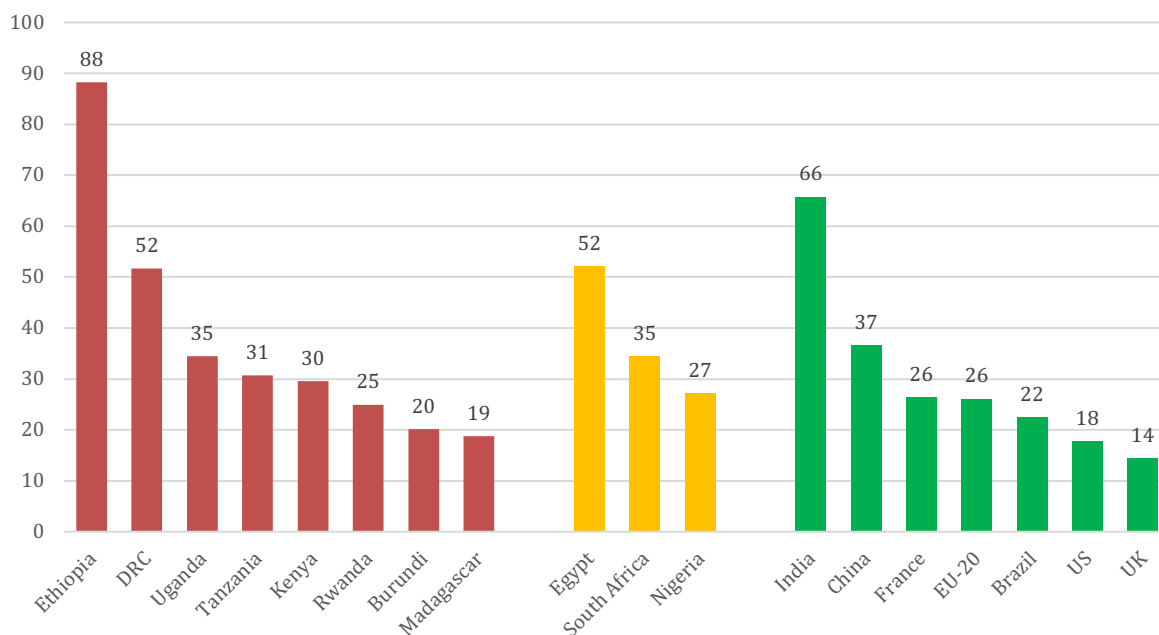
⁸ Annex A provides the results of a number of studies assessing the impact of wholesale liberalization. It is notable that often the gains are not as large as proponents of liberalization claim.

⁹ In the past there has been a blind-spot in the literature with regard to regional integration and service sector liberalisation – most of the literature has focussed on merchandise trade. For instance, in an otherwise authoritative review of empirical evidence on progress on European integration, Sapir (2011) barely mentions the evidence on services.

That said, the point of departure for economies in Eastern Africa with regards to the existing degree of service sector liberalisation is a complex one. There is quite a degree of heterogeneity in the policy stance towards the services sector across the region. We can approximately gauge this by looking at the World Bank’s Services Trade Restrictiveness Index (STRI) which, although outdated¹⁰ and with its own limitations (see [Borchert, Gootiiz and Mattoo, 2012](#)), allows a comparison of the existing degree of ‘openness’ within the service sector.

There is a marked degree of heterogeneity in the policy stance towards the services sector across the region.

Figure 1: World Bank’s Services Trade Restrictiveness Index, Selected Economies



Source: World Bank Services Restrictions database.

Note: Scores range from 0 (fully liberalized) to 100 (highest restrictions and closed for foreign investment)

¹⁰ The STRI refers to data collected between 2008-2010 for the countries in Eastern Africa. The database covers a total of 103 countries (of which 79 are non-OECD countries and 24 are OECD countries) and five sub-sectors (telecommunications, finance, transportation, retail and professional services).

On the one hand, several economies in the region approach the continental negotiations in services having already achieved a fairly high level of liberalisation in their services sectors (Madagascar, Burundi and Rwanda) – indeed, higher than the average for the European Union. There then exists a group of East African countries where the level of restrictions is still not that high by international standards (Kenya, Tanzania and Uganda). Surprisingly, these countries are still evaluated as ‘less restrictive’ than South Africa, the continent’s largest producer of services. And finally, DRC and Ethiopia are deemed to be among the most restrictive – indeed, the latter country is evaluated as having the most restrictive of all 103 countries evaluated in the STRI.

Part of the difference in policy stance towards regulation in the service sector is explainable by the prevalence of State-Owned Enterprises, which often play a crucial role in providing services such as energy, communication, transport services etc

Part of the difference in policy stance towards regulation in the service sector is explainable by the prevalence of State-Owned Enterprises, which often play a crucial role in providing services such as energy, communication, transport services etc. This means that member states frequently have a vested interest in making sure that national interests are defended in such negotiations, with some countries traditionally having a larger degree of direct public ownership than others (e.g. Eritrea, Ethiopia Tanzania vis-à-vis Kenya, Uganda, Rwanda). The stereotypical portrayal of SOEs

being ‘inefficient’ and ‘uncompetitive’ is not always borne out by the stylised facts, either. ¹¹Ethiopian Airlines is a case in point – a company reporting a \$260 million in profit for the 2019-2020 year on the back of \$2.1 billion in revenues, making the company the second most profitable state-owned corporation in Ethiopia ([Shalton, 2020](#)) ([Box 3](#)).

Box 3: Example of a State-owned Service Provider – Ethiopian Airlines

Ethiopian Airlines is the largest carrier in Africa and its growth in recent years – including a four-fold increase in passenger traffic between 2010 and 2018 (up to 12 million in 2018) – is in marked contrast with the decline of (and allegations of corruption in) South African Airways (SAA) and in Nigeria Air. All manner of capabilities have been developed along the way, from the maintenance and technical facility to the Aviation Academy serving Ethiopian, African, and Middle Eastern airline companies, to the freight terminal and integrated airline catering facilities. While several other state-owned Ethiopian enterprises have floundered, there has been consistent support for Ethiopian Airlines as a ‘national champion’. This has allowed the airline’s management to weather periods of instability and resist intermittent interference from the government of the day. Localization ‘has been enforced by restrictive regulations governing foreign investment. These stipulate that only the Ethiopian government can provide air transport services on aircrafts with a capacity of more than 50 passengers, while only Ethiopian citizens can provide such services on aircrafts with lower capacity’.

Source: Cramer et. al (2020).

¹¹ Evaluations by organisations like the IMF (2020) have been mixed on the performance of SOEs in the sub-region, with relatively favourable evaluations of Ugandan SOEs, but being more critical of the performance of Kenyan SOEs, for instance.

Given this point of departure, what should East African countries aspire to in the negotiations? Essentially, in the context of formerly relatively closed economies¹², it frequently boils down to a question of balancing what is perceived as economically desirable with what may be politically feasible. In the case of countries which already have relatively open services sectors, the issues at stake are different. It is also the case that some aspects of services trade liberalisation are inherently controversial (see, inter alia, (Dunkley, 2016). There are certainly many examples across the world of bad practice and a failure to deliver the anticipated gains in many cases of service sector liberalisation.¹³ So the case for greater liberalisation needs to be looked at carefully, on a sector-by-sector basis, rather than a blanket endorsement of the policy of ‘maximum liberalisation’.

In this report we will take a middle ground and argue that for Eastern Africa the gains from a greater degree of selective regional integration, under the aegis of the AfCFTA, are likely to be large. But they will also be heavily contingent upon the regulatory capacity of the state – without that, the touted benefits may well fail to materialise.

In some service sectors technological developments have completely changed the balance between regulation and competition

Traditionally the markets for services are not integrated but segmented. Most service markets, whether in Africa or globally, are heavily regulated for a purpose, be it for consumer protection purposes, to enforce safety standards (e.g. medical services or air transport) or when it is difficult or costly for consumers to obtain the information necessary to

discriminate between different service providers (e.g. banking or insurance) (Francois and Hoekman, 2010; Molle, 2016). Legitimate arguments in favour of tighter regulation are often intimately tied to the existence of natural monopolies or oligopolies, particularly for “infrastructure services” that require specialized distribution networks: roads and railways, airports, or cables and satellites for telecommunications.

Yet these arguments can often be overplayed or are intentionally disingenuous to justify the status quo. As Molle (2016:89) notes, even if consumer protection is the official reason for this protectionist regulation, in practice the real reason is often that domestic firms want to be sheltered from international competition. Many obstacles overtly aim at protecting national companies. There are several reasons to do so:

Legitimate arguments in favour of regulation can often be overplayed or are intentionally disingenuous to justify the status quo

- **Strategic importance:** (e.g. maritime transport);
- **Control of macro-economic policy** (e.g. through the banking system);

¹² In the Horn of Africa, the relatively closed economies have been a legacy of the Marxist-inspired governments of the 1980s and 1990s in Eritrea, Ethiopia and Somalia (Clapham, 2017). In the case of Tanzania, socialist governments also adopted a hostile attitude towards foreign investment and an open economy, preferring an explicit policy of “Kujitegemea” (self-reliance). Of all the East African states, historically Kenya has been the only country which embraced a more liberal stance on economic affairs, but even here, the dichotomy is a little strained, as Kenyan in fact has quite a large number of state-owned enterprises.

¹³ The privatization of utility services like water and telecoms have often been especially controversial. For a critique, see Madeley (2008).

- **Enhancing national prestige** (e.g. civil aviation);
- **Control of key technologies** (e.g. telecommunication);
- **Safeguarding cultural values** (e.g. movies, television).

Member states in Eastern Africa understandably have strategic interests in some sectors which they wish to defend. For instance, both Ethiopia and Rwanda keep a relatively tight control over their national airlines and would be loath to sell a controlling stake in these businesses.¹⁴ In other sectors, however, the trade-off between limiting competition, state control and a more open market is more questionable. In the Democratic Republic of Congo, for instance, although now improving, customers of telecommunications have been poorly served by limited competition.

Moreover, in some service sectors, technological developments have completely changed the balance between regulation and competition. Networks for cable television can be used for telecommunication services, for instance, while satellites have permitted the very rapid spread in the use of mobile phones. When financing from state resources is difficult, the use of electronic tolling for certain roadways is now feasible. Our notions of competition have correspondingly changed. In view of these new circumstances, in some sectors the definition of a 'natural monopoly' is crumbling and maintaining traditional regulatory control may no longer be tenable.¹⁵

Nonetheless, in East Africa a number of member states still strongly adhere to the need for tight regulation of key services sectors. Until very recently for instance, the Ethiopian telecommunications sector was completely closed off to foreign competition, on the grounds not only of the strategic nature of the sector, but also because it was considered as the 'cash cow' for the government to be able to fund its ambitious programme for establishing 23 Industrial Parks ([Odyek, 2017](#)). For policymakers, the trade-off to make in such cases is between the revenue generated for the State from tight regulatory control or retaining government ownership on the one hand and providing citizens with higher quality and/or lower priced services on the other.¹⁶

¹⁴ The Ethiopian government had intended to include the partial sale of Ethiopian Airlines as part of a larger set of economic reforms that will see the country's telecoms, logistics and other critical sectors privatized. But the government recently announced the decision to suspend the planned privatization due to the fact that the airline is doing well and "appears robust...Maintaining the current capacity of Ethiopian Airlines is more beneficial to the economy," ([Kiruga, 2020](#)).

¹⁵ A good example is the European Telecommunications Sector, which only a few decades ago was regarded as a clear case of a natural monopoly with more than one supplier implying duplication of costly network infrastructure and hence a welfare loss for society. In most EU countries public telephone operators were state-owned organisations which tended to cross-subsidise different services at the demand of government and privilege domestic equipment manufacturers (Molle, 2016:99).

¹⁶ Abitew (2020) claims that once debt servicing is taken into account, it is untrue that the Ethio telecom sector provides positive annual revenue, arguing that earnings should be set against servicing of the \$3.1 billion strategic credit loan from the Export-Import (EXIM) Bank of China and China Development Bank to upgrade the company's operations.

None of the positive benefits from a greater degree of opening up are automatic and are dependent on the capacity of the State to provide the necessary regulatory control of the new private sector actors.

Moreover, none of the positive benefits from a greater degree of opening up are of course automatic and are dependent on the capacity of the state to provide the necessary regulatory control of the new private sector actors. In essence, there is no point in converting a public monopoly into a private one and expecting any improvement in the services provided. Public ownership is not automatically analogous with a lack of competition, just as private ownership does not necessarily lead to greater competition or an improvement in service provision.¹⁷ For

example, in the banking sector, as we shall see, the sharp rise of the presence of foreign banks in a number of countries in East Africa has not notably led to an improvement in sectoral efficiency, as measured by a sharp reduction of operational costs or a reduction in the high margins between borrowing and lending rates (Griffiths-Jones and Gottschalk, 2016). Thus the issue is clearly far more complex than simply advocating for ever higher degrees of liberalisation. Such is the conundrum that confronts policymakers in these areas.

3. How Important is Services Trade in Eastern Africa?

Partly because of their intangible nature, the empirical importance of services trade is actually a surprisingly complex question. Globally, just prior to the Covid-19 crisis, trade in services was estimated by UNCTAD (2019) to have reached an historic high of 6.0 trillion in 2019. This was

In developing economies, services' exports grew at an average of 7.6 per cent annually between 2005 and 2018

despite the generally anaemic performance of trade in goods since the global financial crisis of 2008-9. In developing economies, services' exports grew at an average of 7.6 per cent annually between 2005 and 2018, increasing services' direct contribution to total exports from 14 to 17 per cent. In Eastern Africa, the contribution of service exports to GDP is generally on the rise, with several

countries registering more than a three-fold increase since 2005 (Table 1) For a group of countries in the region (e.g. Comoros, Djibouti, Ethiopia, Rwanda Uganda and Seychelles), service exports are now the single largest source of foreign exchange.

Table 1: Services exports (current prices, USD million)

| | 2005-2009 average | 2010-2014 average | 2015 | 2016 | 2017 | 2018 |
|------------|-------------------|-------------------|-------|-------|------|------|
| Burundi | 47 | 96 | 57 | 73 | 98 | 105 |
| Comoros | 54 | 75 | 84 | - | 89 | 108 |
| D.R. Congo | 529 | 405 | 173 | 128 | 108 | 115 |
| Djibouti | 273 | 350 | 455 | 406 | 985 | 1041 |
| Ethiopia | 1,393 | 2,751 | 3,087 | 3,095 | 3608 | 4920 |

¹⁷ As example, Dunkley (2016) notes that the results of water privatisation around the world have often been so bad that services have been returned to the public sector. A key theoretical contribution on the issue was introduced by Baumol (1983), when he introduced the concept of 'contestability'. In essence, this claims that it is not so much ownership that matters, but rather the ability of the incumbent to be displaced, inducing competitive-like behaviour.

| | 2005-2009 average | 2010-2014 average | 2015 | 2016 | 2017 | 2018 |
|--------------|-------------------|-------------------|---------------|---------------|--------------|--------------|
| Kenya | 2,683 | 4,611 | 4,638 | 4,528 | 4,959 | 5538 |
| Madagascar | 920 | 1,203 | 1,073 | 1,186 | 1269 | 1311 |
| Rwanda | 272 | 517 | 818 | 835 | 998 | 917 |
| Seychelles | 428 | 648 | 847 | 894 | 998 | 1106 |
| Somalia | - | 268 | 355 | 373 | 393 | 405 |
| South Sudan | - | 36 | 97 | 178 | 194 | 148 |
| Uganda | 719 | 1,893 | 2,044 | 1,868 | 1,609 | 1991 |
| Tanzania | 1,705 | 2,746 | 3,411 | 3,593 | 3,862 | 4015 |
| <i>Total</i> | <i>9,023</i> | <i>15,600</i> | <i>17,140</i> | <i>17,156</i> | <i>19169</i> | <i>21718</i> |

Source: UNCTADStat (2020).

However, there is a general consensus among trade experts that the true value of services trade is systematically underestimated by such measures, for various reasons (Eacaith, 2008, Lanz & Maurer, 2015, UNCTAD, 2020):

The true value of services trade is systematically underestimated

- **The role of services as an input into manufacturing production** – often termed "*servicification*" of manufacturing – is substantial in both developed and developing economies. While services' *direct exports* are estimated to account for 14 per cent of total exports in developing economies, services represented a much higher share of the value-added in total exports: 32 per cent;¹⁸
- When also considering **services activities conducted *within* manufacturing firms**, a study by UNCTAD (2020) estimated that the contribution of services to overall exports was closer to two-thirds;¹⁹
- The economic importance of **services trade goes beyond the usual cross-border statistics**. The economics profession has traditionally viewed services as primarily non-tradeable. However, more recently a clear, internationally accepted definition of how services are traded has evolved (WTO, 2019). The General Agreement on Trade in Services (GATS) identifies four basic modalities of services supply:

- a. **Mode 1: Cross border trade** – services supplied from one territory to another territory (e.g., software services sent by email);

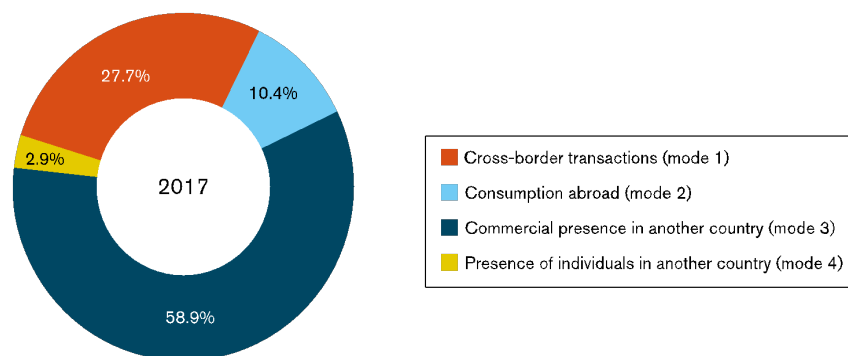
¹⁸ Estimates are for 2011.

¹⁹ If the sales of services by foreign affiliates of multinational firms are added, then the value of trade in services rises further. While we have no equivalent statistics for Eastern Africa, data in 2007 for fifteen OECD countries put the value of such sales at some \$1.5 trillion in (WTO 2009).

- b. Mode 2: **Consumption abroad** – services supplied in one territory to consumers from another territory (e.g., cross-border tourism);
- c. Mode 3: **Commercial presence** – services supplied through a business established in one territory that is operating in another territory (e.g., financial institutions with branches in other countries); and
- d. Mode 4: **Presence of natural persons** – services supplied by nationals of a territory in another territory (e.g., travelling entertainers) (WTO, 2019).

In terms of prevalence of each of these modalities of service trade delivery, we do not currently have estimates of the breakdown specifically for Eastern Africa. However, at the global level it is well established that the most frequent mode of delivery is through a commercial presence in another country (i.e. through FDI, licensing or franchising), accounting for nearly 60 percent of services trade in 2017 (WTO, 2019). By coincidence, global investment statistics show that service FDI has increased from a quarter of the global FDI stock in the 1970s to half in the 1990s and to approximately two-thirds by the 2000s (UNCTAD 2010).

Figure 2: Commercial Presence is the most important way of servicing foreign markets



Source: WTO (2019: 24)

Table 2: FDI Stocks in East African Countries, by sector and major source country

| KENYA | | |
|--------------|----------------|-----------|
| Source | 2017 (KSh m) | Share (%) |
| UK | 34,730 | 24% |
| US | 20,018 | 14% |
| Mauritius | 10,738 | 7% |
| China | 9,949 | 7% |
| France | 9,579 | 7% |
| Total | 145,144 | |

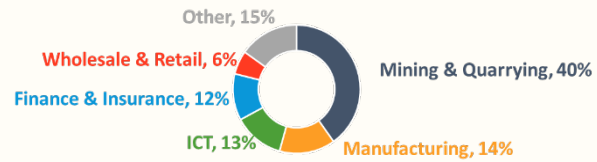
Sector Distribution

| Sector | Percentage |
|-----------------------|------------|
| Finance and Insurance | 40% |
| Manufacturing | 19% |
| Wholesale and Retail | 16% |
| Other | 13% |
| Electricity and Gas | 5% |

| TANZANIA | | |
|--------------|--------------|-----------|
| Source | 2017 (USD m) | Share (%) |
| UK | 2,727 | 20% |
| South Africa | 2,484 | 18% |

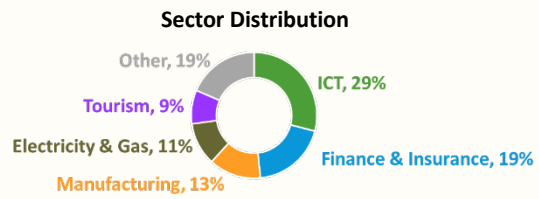
Sector Distribution

| | | |
|--------------|---------------|-----|
| Norway | 1,403 | 10% |
| Netherlands | 1,005 | 7% |
| Nigeria | 668 | 5% |
| Total | 13,500 | |



RWANDA

| Source | 2018 (USD m) | Share (%) |
|--------------|--------------|-----------|
| Mauritius | 796 | 35% |
| Kenya | 182 | 8% |
| South Africa | 179 | 8% |
| US | 108 | 5% |
| Netherlands | 105 | 5% |
| Total | 2,284 | |



Source: KNBS (2018), BOT (2018), NBR (2019)

FDI is a preferred modality for entering into the regional services market.

Detailed sectoral data for FDI is not available for all East African countries, but in a selected sample of countries, it does indeed seem clear that FDI is a preferred modality for entering into the regional services market (Table 2). For Kenya, finance and insurance alone represent 40 percent of the total FDI stock, and the total service sector share is in excess of 70 percent. For Rwanda, too, ICTs, finance and insurance, tourism and utilities represent around 70 percent of the total stock. Only in Tanzania does the share of FDI in services appear lower (at around 30 percent). To sum up, it is important that the study of the service sector in East Africa is not restricted solely to balance-of-payment trade figures, which vastly underestimate the relative importance and contribution of the sector to GDP.

4. Arguments in Favour of Creating an Intra-Regional Market in Services

Despite the historical reticence of some countries in Eastern Africa to embrace service sector liberalisation, the argument for a higher degree of liberalisation of services trade, under the aegis of the AfCFTA, may be particularly strong for Eastern Africa. While only one country in Eastern Africa has a positive merchandise trade balance, five countries currently enjoy surpluses in services. With the right policies, this report argues that trade balances in services could be even stronger for the region. Depending of course on the ultimate outcome of the negotiations, the AfCFTA certainly opens up a lot of new opportunities in trading in services. Encouraging, preliminary analysis by SRO-EA shows that, in line with previously cited studies done many decades ago for other developing countries (e.g. Sapir and Lutz, 1981; Bhagwati, 1987), Eastern Africa has a clear *Revealed Comparative Advantage (RCA)* in a range of service sub-sectors.

With the right policies, this report argues that trade balances in services could be even stronger for the region.

Table 3: Revealed Comparative Advantage in Services in Africa, 2005-2019

| | 2005-7 | 2008-10 | 2011-13 | 2014-16 | 2017-19 |
|-------------------------------------|--------|---------|---------|---------|---------|
| Africa | 0.758 | 0.730 | 0.701 | 0.817 | 0.843 |
| By Sub-Region: | | | | | |
| Northern Africa | 0.991 | 1.009 | 0.983 | 1.178 | 1.166 |
| Eastern Africa | 1.645 | 1.570 | 1.589 | 1.429 | 1.466 |
| Middle Africa | 0.169 | 0.180 | 0.180 | 0.241 | 0.227 |
| Southern Africa | 0.786 | 0.688 | 0.695 | 0.652 | 0.606 |
| Western Africa | 0.396 | 0.380 | 0.352 | 0.531 | 0.626 |
| By Country: | | | | | |
| Burundi | 1.733 | 2.204 | 2.374 | 1.501 | 1.544 |
| Comoros | 3.692 | 3.680 | 3.831 | 3.340 | 2.972 |
| Congo, Dem. Rep. of the | 0.453 | 0.405 | 0.211 | 0.083 | 0.037 |
| Djibouti | 4.004 | 3.770 | 1.769 | 1.219 | 0.978 |
| Ethiopia | 2.493 | 2.380 | 2.388 | 2.157 | 2.577 |
| Kenya | 1.914 | 1.897 | 2.207 | 1.871 | 1.970 |
| Madagascar | 1.984 | 2.204 | 2.124 | 1.531 | 1.367 |
| Rwanda | n.a. | 2.648 | 2.323 | 2.176 | 1.954 |
| Seychelles | 2.500 | 2.390 | 2.667 | 2.752 | 2.799 |
| Somalia | n.a. | n.a. | 1.364 | 1.865 | 1.928 |
| South Sudan | n.a. | n.a. | n.a. | 0.163 | 0.266 |
| Tanzania, United Republic of | 2.142 | 1.616 | 1.664 | 1.731 | 1.914 |
| Uganda | 1.535 | 1.518 | 2.092 | 1.878 | 1.635 |

Source: ECA calculations, from UNCTADStat data

Eleven of the 14 countries in the region currently have a Revealed Comparative Advantage in services... Eastern Africa is the only sub-region of Africa to possess such a strong comparative advantage in services

In aggregate, **11 of the 14 countries in the region currently have an RCA in services**. Moreover, it is noteworthy that, beside North Africa, Eastern Africa is the only sub-region of Africa to possess such a strong comparative advantage in services trade going into the AfCFTA negotiations (Table 3). Of course, the results of any exercise to calculate RCAs should not be taken too literally – it is limited to the extent that it only measures existing

areas of ‘comparative advantage’. Nevertheless, it does suggest that the region is well-placed to take advantage of the new opportunities that will arise from the implementation of the AfCFTA services protocol.

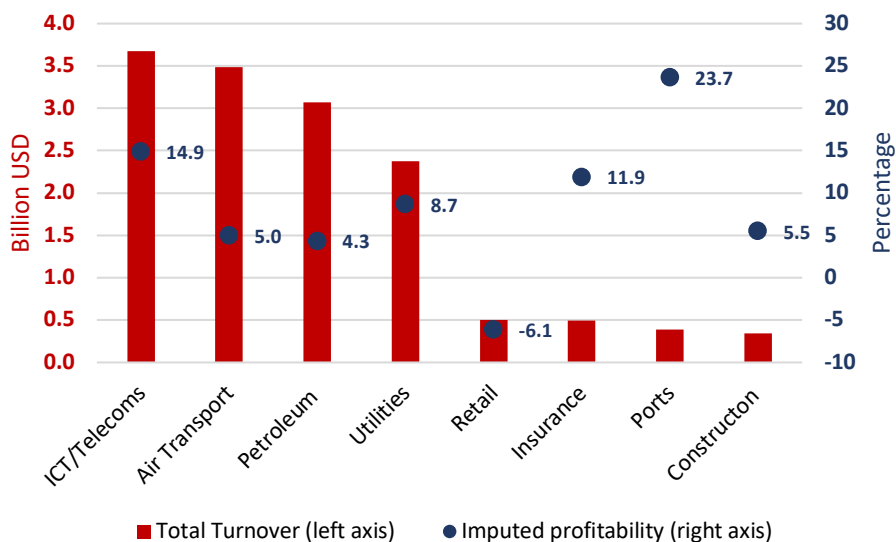
A second reason for believing that the regional economy has much to gain from the AfCFTA-related liberalisation of services is the high profitability of many service sector activities. Using the Jeune Afrique’s annual dataset of 500 Top African Firms, ECA has calculated that the level of profitability for service sector firms based in Eastern Africa is extremely high in a number of sub-sectors, such as ports, utilities, ICT/telcoms and insurance – well above the average for the African continent. Emblematic of the profitability of the service sector in the region is [Safaricom](#), which has just reported contributing *value-added* of Sh654 billion to the Kenyan economy in the year ended March 2020, equivalent to 6 percent of the country’s GDP.²⁰ The Jeune Afrique dataset does not include banking. However, figures reported by the World Bank’s Regulation and Supervision Survey (2019) reveal that, while there is quite a lot of variation around the mean among countries, the banking sector in Eastern Africa is also tremendously profitable.²¹

A second reason for believing that the regional economy has much to gain from the AfCFTA-related liberalisation of services is the high profitability of many service sector activities

²⁰ The reported contribution included value chain opportunities for other businesses, taxes and dividends to shareholders. In its annual sustainability report Safaricom claimed its operations sustained over a million direct and indirect jobs. Of those, around 19 percent are directly employed by the company, while the rest are derived from indirect activities such as suppliers and users of the company’s various products.

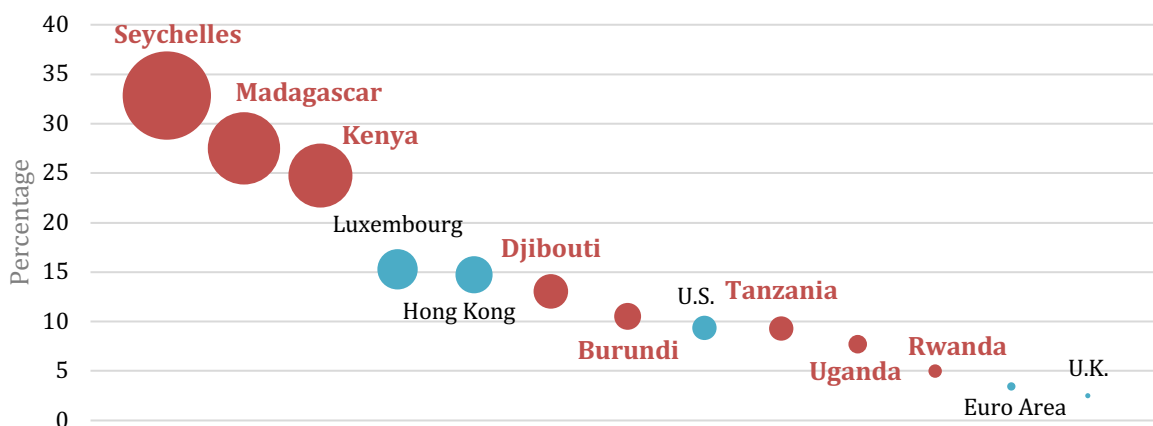
²¹ Indeed, many would argue that it is excessively profitable, and that it has not been reflected in marked improvements in customer service (see section XX). We will say more on this point in the following sections.

Figure 3: Profitability²² and Turnover of East Africa's Largest Service Sector Companies, by sector, 2017



Source: ECA calculations, from Jeune Afrique data

Figure 4: After-tax Return on Equity for the Banking System, Selected Countries, 2016



Source: World Bank's Bank Regulation and Supervision Survey (2019)

In all these cases, it would be hoped that the new opportunities created by AfCFTA implementation would be taken up by regional or continental firms. Returning to the banking sector, for instance, between 2006 and 2010 alone, the seven largest Pan African Banks (PABs) nearly doubled their number of subsidiaries, from fifty to ninety operations. Kenyan banks have been the most successful at expanding across the East African Community (EAC) since KCB started its Tanzanian operations in the late 1990s, and even more significantly, according to one analyst (Signé, 2020: 213), these Kenyan operations have often proved more efficient, with lower

²² Profitability is calculated as reported profits/turnover. For the complete dataset, see Jeune Afrique (2019).

spreads and overheads, as compared to other foreign banks that have invested in the EAC thus far.²³ There are now at least eleven Kenyan banks operating in other EAC countries, with roughly 300 bank branches Kenyan banks are also starting to move further afield. For instance, Equity Group Holdings Ltd is set to become the Democratic Republic of Congo's biggest foreign bank after completing its acquisition of BCDC – the country's second-largest lender ([Anyanzwa, 2020](#)).

A third reason in support of creating a regional services market is the apparent popularity among consumers. Eastern African consumers have benefited, for example, from the EAC's One-Area network initiative. Launched on 1st January 2015, and initially covering Rwanda, Kenya, Uganda and South Sudan, the network established uniform calling rates and elimination of roaming charges within that area.

There are proposals to take this concept further and establish a true East African single digital market. According to a study by (World Bank/SDM East Africa, 2018), the impact on gross domestic product, growth, job creation, and poverty reduction would be significant: implementing a Single Digital Market could generate up to a US\$2.6 billion boost in GDP and 4.5 million new jobs.

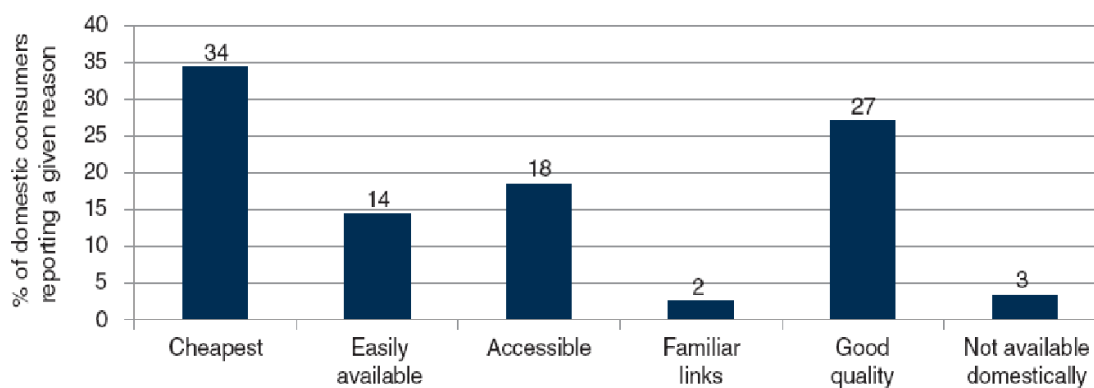
Implementing a Single Digital Market in the EAC could generate up to a US\$2.6 billion boost in GDP and 4.5 million new jobs

Moreover, the authors claim that these estimates, are conservative as they do not fully take into account the spill-over effects from a more integrated and competitive regional market, which is expected to increase innovation, technology adoption, and investment across all sectors over the medium to long term, fuelling a reinforcing cycle of productivity gains, growth, and job creation (World Bank/SDM East Africa, 2018).

Unsurprising, such initiatives are popular with the general public. The ability to purchase services across borders often allows customers to access better quality and cheaper services. Illustrative of this is a survey undertaken in the Democratic Republic of Congo by Dehil and Goswaami (2016) which showed that it was not so much that equivalent services were not available in DRC, but that consumers were generally appreciate of the more competitive pricing and better quality of the foreign services.

²³ See, for instance, [Allen et. al. \(2013\)](#), who study the operations of Equity Bank.

Figure 5: Reasons Congolese Consumers Prefer to Buy Services from Foreign Providers



Note: Interviews conducted from March to May 2015 at border posts between DRC and Rwanda and Uganda: Goma/Gisenyi, Bukavu/Cyangugu, and Mpondwe/Kasindi.

Source: Dehil & Goswami (2016)

A fourth and final argument in favour of the regional evidence from past research suggests that the success of the AfCFTA in terms of passing on welfare benefits to consumers may be heavily contingent on both the degree of competition in related service markets and the appropriate regulation being in place. The findings of a number of past studies (Raff and Schmitt, 2009; Francois and Wooton, 2010) suggest that there are risks that the gains from trade liberalisation in merchandise goods can lead to higher concentration and oligopolistic pricing in the retail or transport sectors. In other words, some services sectors could effectively hijack the gains from greater trade derived from the AfCFTA if they are also not sufficiently competitive (Francois and Hoekman, 2010: 652). Stuart (2017), for example, investigates the relationship between services trade restrictions (STR) and trade performance for a group of African countries, disaggregated by main export specialisation and finds a positive association between less restrictive services trade regulations and a better trade performance.²⁴

The success of the AfCFTA in terms of passing on welfare benefits to consumers may be heavily contingent on both the degree of competition in related service markets and the appropriate regulation being in place...

The formation of the EAC led to a 65 percent increase in bilateral services trade among member states.

To sum up, there are thus a series of compelling reasons why East Africa is well placed to benefit from the selective liberalisation of services under the AfCFTA. The experience of the East African Community, in terms of its estimated impact on services trade (Box 4), in providing a further impetus to services trade is encouraging – using a new form of the gravity equation, we econometrically estimate that the formation of the EAC led to a 65 percent increase

²⁴ In a similar vein, Hoekman and Shepherd (2016) found that a general 10 percent improvement in service sector productivity was associated with increased merchandise exports of EAC countries by between 0.24 percent to 0.5 percent. These improvements may seem small, but in aggregate they could make a marked difference to the competitiveness of regional economies.

in bilateral services trade among member states. This is in line with estimates of the impact for the European Union (Mayer et. al. 2018) cited in Box 2.²⁵ It is also important to note that, like for goods trade, the distance variable is significant and negative, suggesting that proximity still has an important role to play in the cross-border provision of services, and that regional partners may be well placed to take advantage of the opportunities opened up by greater service sector liberalisation in Eastern Africa.

Box 4: Effect of the EAC Integration on Services Exports: A Structural Gravity Model Approach

We can gain some insights into the potential for the AfCFTA to impulse further intra-African trade by looking at the impact of the establishment of the East African Community (EAC) on services exports using bilateral trade data from 1995 to 2012. The data on services exports were obtained from the OECD-WTO Balanced Trade in Services Database (BaTIS) while the data on the other covariates were obtained from the CEPII website. Following Anderson and Yotov (2011) and Silva and Tenreyro (2006), the following structural gravity model is estimated using the Poisson pseudo-maximum likelihood estimator (PPML) that controls for heteroscedasticity and allows for bilateral zero trade values between trading partners.

$$X_{ijt} = \exp\left(\beta_1 GDP_{O_{it}} + \beta_2 GDP_{D_{ijt}} + \beta_3 \ln DIST_{ijt} + \beta_4 BRDR_{ijt} + \beta_5 LANG_{ijt} + \beta_6 CLNY_{ijt} + \beta_7 EAC_{ijt} + EX_i + M_i\right) + e_{ijt} \dots \dots (1);$$

where, X_{ijt} are services exports from East African countries to the rest of the, $GDP_{O_{it}}$ and $GDP_{D_{ijt}}$ are exporter and importer GDP, $\ln DIST_{ij}$ stands for the logarithm of bilateral distance. $BRDR_{ij}$, $LANG_{ij}$ and $CLNY_{ij}$ capture the presence of contiguous borders, common language and colonial ties, respectively. EAC_{ijt} is a dummy variable for the EAC trade agreement between African countries i and j at time t . EX_i and M_i are exporter and importer fixed effects.

Table 4 below reports the panel regression results. As a baseline estimation, Column 1 was estimated using the OLS estimator. In Column 1 the coefficients of the standard gravity variables including logarithm of exporter and importer GDP, bilateral distance, and the dummy variables for common borders, colonial ties, and a dummy variable EAC were significant with the expected signs. However, the OLS model is biased due to heteroscedasticity and endogeneity.

Column 2 and 3 presents results from the gravity model estimated using the PPML estimator. The equation in column (3) was estimated with the PPML estimator, importer, exporter fixed effects and pair fixed effects to control for endogeneity. Results in column (3) showed that the EAC had a positive significant on services exports, **the formation of the EAC led to an average increase of 65 percent in EAC services exports among member countries.**²⁶

Table 4: Estimating the Effects of the EAC regional trade agreement on service trade

| | (1) | (2) | (3) |
|------------------|---------|----------|-------------------|
| | OLS | PPML(FE) | PPML(Endogeneity) |
| Log exporter GDP | 0.529** | | |
| | (0.045) | | |

²⁵ Our results are however significantly larger than the average impacts estimated econometrically by Guillin (2013) for 65 RTAs that specifically include services in their provisions. She concludes that belonging to such an RTA increases trade between signatories by 18-32 per cent.

²⁶ The formula applied for the calculation of elasticity is $([\exp(0.5) - 1] \times 100) = 65$

| | | | |
|------------------------|----------------------|---------------------|---------------------|
| Log importer GDP | 0.571** (0.045) | | |
| Log distance | -0.709** (0.126) | -1.633** (0.284) | -0.543** (0.043) |
| Common border | 1.118** (0.257) | -0.199 (0.295) | -0.091 (0.166) |
| Common language | 0.213** (0.076) | 0.411** (0.103) | 0.712** (0.140) |
| Colony | 1.484** (0.385) | 1.345** (0.108) | 3.307** (0.185) |
| EAC | 1.205** (0.186) | 1.288** (0.305) | 0.495* (0.255) |
| Constant | -13.651** (1.289) | 16.907** (2.180) | 8.081** (0.556) |
| Number of Observations | 31730 | 32560 | 32560 |
| Pair FE | No | No | Yes |
| Exporter FE | Yes | Yes | Yes |
| Importer FE | Yes | Yes | Yes |
| R-squared | 0.789 | 0.908 | 0.934 |
| * p<0.10 | ** p<.05 | ***p<.01 | |

Source: Authors' calculations.

Notes: All estimates are obtained using exporter and importer fixed effects. The estimates of the fixed effects are omitted for brevity. Column (1) applies the OLS estimator and column (2) uses the PPML estimator but does not control for endogeneity. Column (3) uses the PPML estimator and adds pair fixed effects to control for endogeneity. The estimates of the pair fixed effects are omitted for brevity. Standard errors are clustered by country pair and are reported in parentheses. The p-values read as follows: *p < 0.10; ** p < 0.05; and ***p < 0.01.

5. Two Steps Forward, One Step Back? - Covid-19's Impact on Services Trade

Undoubtedly, the positive narrative espoused here about the role of services and services trade in regional growth and development has been dealt a blow by the Covid-19 crisis. The [WTO \(2020-April\)](#) was already predicting that services trade had been the component of world trade most negatively affected by COVID-19, principally through the imposition of transport and travel restrictions and the closure of many retail and hospitality establishments. Subsequent data confirmed this picture, with a global decline in services trade of -30 percent in the second quarter of 2020. Tourism was hit particularly hard, with international travellers' expenditure down 81 percent and transport down 31 percent. How the crisis will

Services trade had been the component of world trade most negatively affected by COVID-19

impact services trade over the long run is yet to be determined. These global impacts were of course reflected in services trade in Eastern Africa. The tourism sector has been worst affected of all sectors in East Africa. High frequency data on tourism-related sectors paint a grim picture. For a region in which many countries are heavily dependent on tourism revenues, this is clearly a significant blow.²⁷

Figure 6: Tourism Arrivals in Kenya and Seychelles (1000s), Jan 19-Aug 20



Source: KNBS (2020)

Source: XXX (2020)

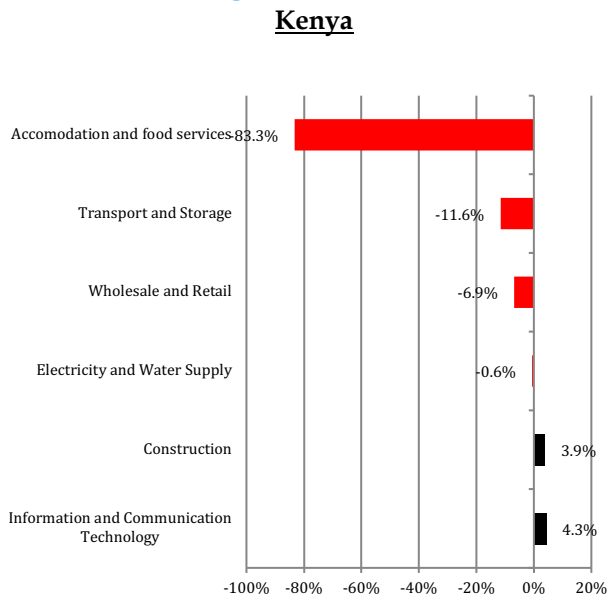
The economy-wide impacts of these declines in services trade are likely to be large. For instance, using a Computable General Equilibrium (CGE) simulation, UNCTAD predicts that Kenya will be one of the most 15 affected countries globally in the tourism sector, precipitating a loss of -5% in GDP over the course of 2020. Rwanda and Kenya – the two countries which have published detailed second quarter data – the scale of the decline in tourism-related sectors has been dramatic (Figure 7). Education, transport and retail trade have also been hit hard by the crisis.

Regional airlines have tried to mitigate the heavily negative impact on passenger travel by switching their focus to cargo. Those strategies have met with mixed success. Ethiopian Airlines reported that revenue generated from the transportation of goods had allowed the company to keep up monthly fixed payment, including servicing loans, aircraft leases, salaries and rentals, and expected its accounts to remain in the black for the fiscal year, despite the gravity of the crisis impacting on its passenger business (Gebre, 2020). Despite introducing similar measures, Kenya Airways (KQ) by contrast reported a -48 percent drop in revenue for the six-month period ending July 2020 as a result of the cessation of scheduled operations from the second quarter of 2020. Compared with the same period in 2019, losses before tax rose by 68 percent (Busiweek, 2020).

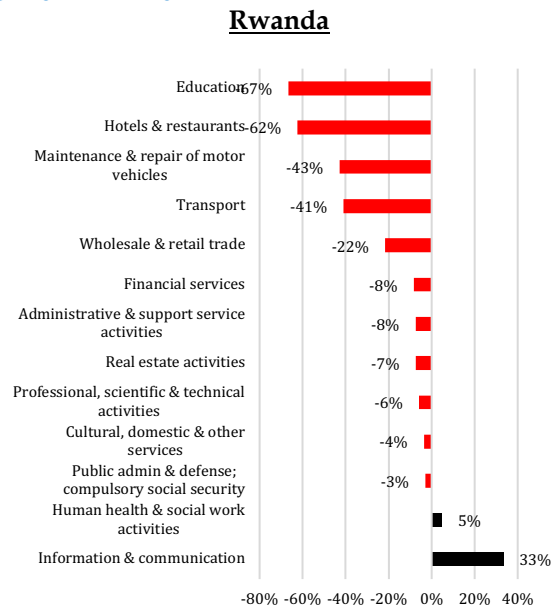
Conversely, some services are clearly benefiting from the crisis. This is particularly true of information technology services, demand for which has boomed as companies try to enable employees to work from home and people socialise remotely. For instance, the ICT sector in Rwanda expanded in the second quarter by 33%.

²⁷ Despite the fact that Tanzania did not implement national lock-down measures against Covid-19 in the same way as some other countries (e.g. Rwanda, Kenya) in the region, national data also reveals that its tourism sector revenue collapsed. This reflects the sharp decline in tourism arrivals from outside the country due to restrictions placed on travel elsewhere.

Figure 7: Service Sector GDP change (year-on-year) 2nd Qtr 2020



Source: KNBS (2020)



Source: NISR (2020)

The crisis has created what has been described as a “windfall opportunity” for ICTs

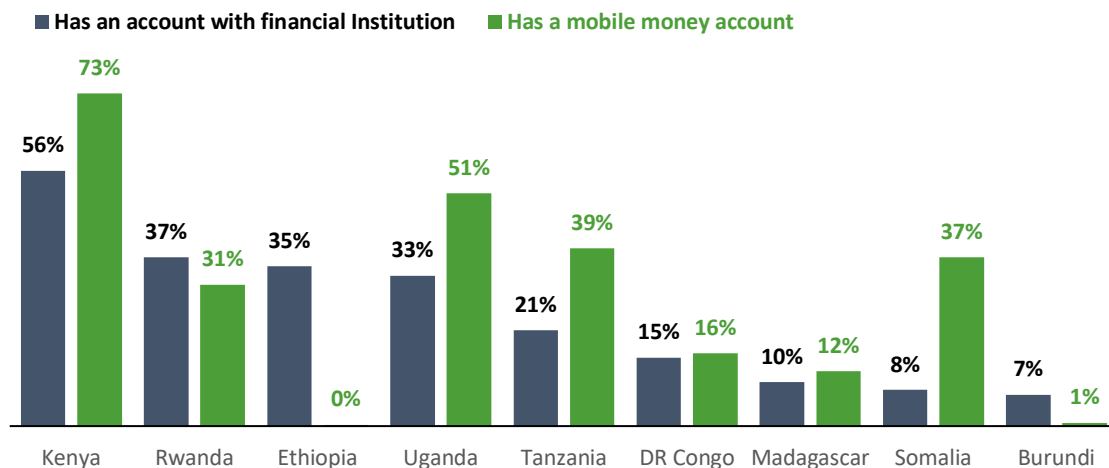
The rise in demand for digital services in Eastern Africa during the crisis merits greater attention. The crisis has created what has been described as a “windfall opportunity” for ICTs (UNCTAD, 2020c). Even prior to the crisis, digital services were making inroads into markets like financial services – traditionally the purview of the formal banking sector (Figure 8). The spread of mobile money services, an efficient and cost-effective facilitator of economic

transactions, has been particularly impressive in Eastern Africa, and has generated innovative solutions in banking, insurance, health, consumer markets, and many other vital economic sector (Signé, 2020: 76-7). There is associated evidence that this has contributed to poverty reduction in the region.²⁸

Figure 8: Financial Inclusion Rates, 2019

Percent of population 15+ years that...

²⁸ May et al.’s (2014) survey of East African households, for example, finds that access to ICTs results in a net gain of \$21 per month, and Diga (2013) argues that internet access in Tanzanian villages contributed to a reduction in poverty across seven different criteria.



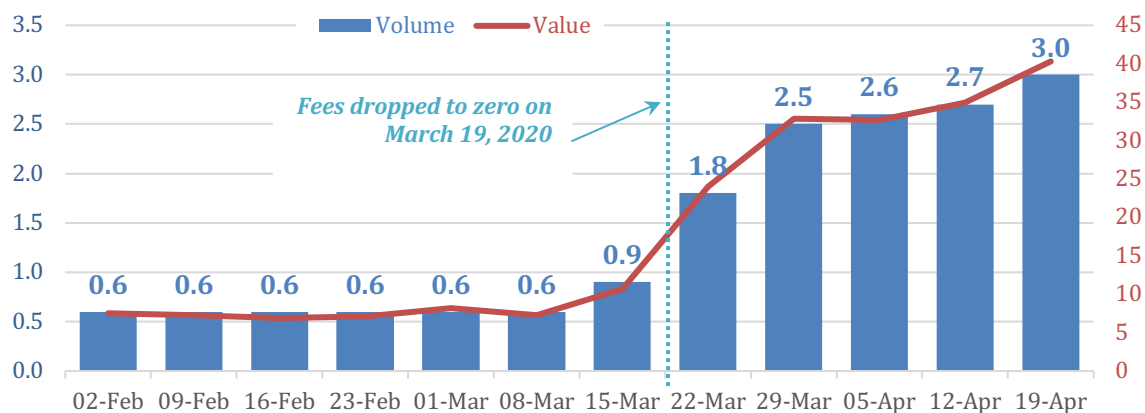
Source: DataReportal (2020)

The crisis has given a strong impetus to these pre-existing trends (World Bank, 2020). For instance, to curb the spread of COVID-19, some Eastern African governments and mobile money providers moved to promote the use of digital payments. The National Bank of Rwanda removed charges and raised the cap for mobile money payments and transfers for three months from mid-March 2020.²⁹ The immediate result was a 400% increase on the weekly number and value of person-to-person transfers (Carboni & Bester, 2020).³⁰ Other countries also recorded an increase in the value of mobile money transactions, such as Tanzania, where 1Q2020 transactions valued 19% more than 1Q2019.

The removal of charges on mobile money transactions in Rwanda during the Covid-19 crisis led to a 400% increase in the value of person-to-person transfers

Figure 9: Weekly Mobile Money Transfers Volume and Value in Rwanda, Feb-19 Apr-20

Millions of transactions (volume) and RwF billions (value)



²⁹ The impact was monitored by the telecommunications regulator, Rwanda Utilities Regulatory Authority and researchers insight2impact.

³⁰ Interestingly, there appears to be some gender impacts of the policy - the proportion of female senders increased from 31% prior to the lockdown to 36%.

During the Covid-19 crisis, the transition to remote work and home-based entertainment for many Eastern Africans was often curtailed by the very nature of their work, and more importantly, by the limited access to reliable and affordable internet connections. Internet penetration rates are relatively low in the region, and frequent internet users often depend on work-based connections for much of their internet consumption. Many of these users would have had to shift from unlimited internet access at work to mobile data plans financed from possibly strained disposable incomes. Furthermore, mobile internet speeds are relatively slow – frustrating remote work.

Nonetheless, preliminary evidence does indeed suggest that internet use rose. In Kenya, the most internet-penetrated country in Eastern Africa, data usage on the Safaricom network surged by 70% in the month after the first reported COVID-19 case (Reuters, 2020). Liquid Telecom’s fortunate timing in being the first to connect fibre internet in South Sudan in early 2020 led to a 10% month-on-month growth in internet traffic during the pandemic. In general, the demand growth in Eastern Africa has strengthened Liquid Telecom’s case for further investment in the region, and expansion of its fibre-to-the-home service (Roberts, 2020). Providers have also mentioned a shift in online buying habits – from primarily luxury items to a greater share of essentials such as food and hygiene products.³¹

The Covid-19 crisis comes at a time when, because of the ongoing AfCFTA negotiations, countries were already re-evaluating service sector strategies

To sum up, the Covid-19 crisis comes at a time when, because of the ongoing AfCFTA negotiations, countries were already re-evaluating service sector strategies. It is clear that assuming a ‘business as usual’ approach is not going to be viable. For instance, in light of the collapse of foreign and conference tourism, there is a certain need to reconsider the long-term implications of an excessive dependence on international visitors. In line with the spirit of the AfCFTA, an increased reliance on national and regional tourism may provide an

appropriate response. Similarly, it is evident that the Covid-19 crisis is going to accelerate the digital transformation of the region ([World Bank, 2020](#)). Eastern Africa was already a leader in some technologies, such as digital money (M-Pesa). But to maintain that momentum, there will need to be the necessary investments in human capital: the highly skilled and specialised nature of work in many service sectors poses challenges to generate an appropriate labour force for ‘modern’ services (such as finance, ICTs, tourism and real estate). (Berhuria and Goodfellow, 2019).

³¹ Ben Roberts (Liquid Telecom) and Kyle Spencer (Uganda Internet eXchange Point), Webinar, *Effects of COVID-19 on the African Internet*, hosted by Internet Society on September 1, 2020.

6. The AfCFTA Protocol on Services - A Step-Change in the Regional Integration Agenda

What then are the next steps for the region in terms of implementing the AfCFTA 'Protocol for Trade in Services.'? The aim of the protocol is to progressively open services trade across the African continent expanding the depth and scope of liberalization, in line with Article V of the General Agreement on Trade in Services (GATS). But in fact, beyond the controversies earlier mentioned with regard to multilateral service trade liberalisation, while GATS was created to serve as a primary platform for trade liberalization in services, since the late 1990s, more trade liberalization in services has been manifested through regional trade agreements than through the GATS (Mattoo et al, 2019).

It is worth noting that many Eastern African countries have inscribed the GATS through their membership of WTO (Burundi, DRC, Djibouti, Kenya, Madagascar, Rwanda, Seychelles, Tanzania and Uganda). However, there are significant differences in their schemes of commitments within GATS which in effect exposes each country to a different degree of multilateral openness. Furthermore, a number of countries in Eastern Africa do not endorse the GATS because of being non-members or observers of WTO (Comoros, Ethiopia, Eritrea, Somalia and South Sudan).

Since the late 1990s, more trade liberalization in services has been manifested through regional trade agreements than through the GATS

Member states of the East African Community (EAC) are probably the countries in the region that have taken service trade liberalisation furthest, though adopting a positive list approach to GATS, i.e., identifying selected service subsectors for liberalization across all supply modes in varying degrees. However, different countries in the block have committed to different number of sectors among which, Rwanda is the most liberalized, having committed to opening 101 service subsectors, primarily in the Business, ICT, and Transport spaces.

Table 5: Number of GATS Commitments, by sector, for EAC Member States

| | Burundi | Kenya | Rwanda | Tanzania | Uganda |
|-------------------------------|-----------|-----------|------------|-----------|-----------|
| Business (46) | 31 | 15 | 32 | 7 | 33 |
| Communications (24) | 6 | 17 | 21 | 17 | 21 |
| Distribution (5) | 3 | 3 | 4 | 2 | 4 |
| Education (5) | 4 | 4 | 5 | 4 | 5 |
| Finance (17) | 9 | 12 | 15 | 16 | 11 |
| Tourism and Travel (4) | 4 | 3 | 4 | 4 | 4 |
| Transport (35) | 17 | 9 | 20 | 9 | 20 |
| TOTAL (136) | 74 | 63 | 101 | 59 | 98 |

Source: WTO (2019)

Currently the deadline for submitting specific sector commitments for services is end of October 2020 to be finalized and enforced by January 2022. Some countries in Eastern Africa have already put forth their offers namely: Comoros, Democratic Republic of Congo and Madagascar. There is some discrepancy of opinion as to whether countries that are part of RECs should support

individual or common offers because beyond regional priorities, countries also have national priorities based on the competitiveness of different sectors. However, countries are not required to go deeper than the commitments made at any REC the country participates in.

In the past, African trade negotiations have often been hindered by various conflicting objectives of overlapping regional trade agreements (Khandelwal, 2004). In Eastern Africa, there are a series of overlaps: four countries (Burundi, Kenya, Rwanda and Uganda) between EAC and COMESA; one country (Tanzania) between EAC and SADC; and one country (Seychelles) between COMESA and SADC. As stated in its agreement, the AfCFTA intends to resolve the challenges of overlapping memberships and expedite the regional and continental integration processes; although practical details of how this will be fulfilled have not been negotiated yet. Therefore, negotiations must be free from fractures in order to avoid the destabilization that can occur when multiple trade regimes are at a crossroads. Bearing this in mind, the secretariats of all eight RECs in Africa have been included in the AfCFTA task force in order to streamline the continental commitments nested within the regional commitments.

The AfCFTA's scope is not limited to free trade in goods and services, but also covers free movement of professionals and investment which has close significance to Mode 3 (commercial presence) and Mode 4 (movement of natural persons) of trade in services.

It is also important to remember that the AfCFTA's scope is not limited to free trade in goods and services, but also covers free movement of professionals and investment which has close significance to Mode 3 (commercial presence) and Mode 4 (movement of natural persons) of trade in services. Therefore, among the various aspects of negotiations Mutual Recognition Agreements (MRAs) deserve especial attention. MRAs allow one country's suppliers to provide services in any other country in the regional block without needing authorization from host countries. Developing strong MRAs is imperative for culminating AfCFTA into a common market through

enabling the flow of professional services and investment across the continent. Looking back, members of the East African Community (EAC) were the earliest in the region to negotiate MRAs, starting with accounting services in 2011. By way of example, Table 6 below shows the discrepancies in regulations that existed for professional accounting services in the EAC countries in 2010.

Subsequently, the concept of MRAs spilled over to SADC and COMESA since all EAC countries overlap with either one of these blocs (World Bank, 2016). Currently, the latter two RECs also include MRAs in their system. Moreover, EAC has signed additional MRAs (architectural services in 2011, engineering services in 2012; and veterinary services in 2016) and have ongoing negotiations for legal and health services. Another Eastern African country, Seychelles is negotiating MRAs for accounting services, together with a few other COMESA member states (Malawi, Mauritius, Zambia and Mozambique) under the auspices of Accelerated Programme on Economic Integration (APEI). In SADC, veterinary service regulators are conducting consultations to develop MRAs.

Table 6: Restrictions on Professional Accounting Services within the EAC, 2010

| Country | Restrictions |
|----------------|---|
| Burundi | Limits on ownership by foreign nationals and non-locally licensed professionals; one-third must be locally licensed nationals or residents. |

| Country | Restrictions |
|----------|---|
| Kenya | Establishing a branch is not allowed. Ownership by non-locally licensed professionals is not permitted. |
| Rwanda | Branches not allowed. |
| Tanzania | Ownership by foreign nationals is limited to 50 percent. Ownership by non-locally licensed professionals is not permitted. There are differences in licensing criteria for foreign and domestic applicants. |
| Uganda | A branch is not allowed. There is no limit on ownership by foreign nationals, but, in practice, if all partners are foreign, at least one should be resident in Uganda. |

Source: World Bank Services Trade Restriction Database cited in World Bank (2016)

However, the coexistence of separate MRAs from multiple RECs that are participated by Eastern African countries may lead to entanglement in the harmonization processes. Hence it is a prerequisite for the AfCFTA task force to come to the same page as the RECs regarding MRAs at the inception of the negotiations. One of the major hurdles of negotiating MRAs in Africa is the overlapping membership between RECs (World Bank, 2016). It complicates negotiations of MRAs because the overlapping RECs have stark differences in regulatory framework, leading to difficulties in reaching a common ground.³²

Additionally, the EAC has launched a regional qualification framework (RQF) in 2015 with the name of EAC Common Area for Higher Education. The SADC also has an RQF which is currently being partially implemented through the exercises of quality assurance assessments; development of guidelines for recognition of prior learning; articulation and credit accumulation and transfers; and review of national qualification framework to ensure conformity (Sawere, 2019). COMESA, by contrast, has still not advanced in the RQF sphere.

On this front, the overarching goal is to establish the African Continental Qualifications Framework (ACQF) which emerged from the *Revised Convention on the Recognition of Studies, Certificates, Diplomas, Degrees and Other Academic Qualifications in Higher Education in African States 2014*. The aim of this is to support an objective of AU Agenda 2063 which is about facilitating harmonization efforts and ensuring mobility of skills and transparency of qualifications (African Union, 2019).

³² Setting up MRAs demand substantial resources at the outset; being living documents they require periodic revision and are thus expensive to maintain especially for developing countries (ADB, 2017). ADB (2017) discusses three approaches for negotiation of MRA's in the context of ASEAN which may also be useful for AfCFTA negotiation of MRAs.

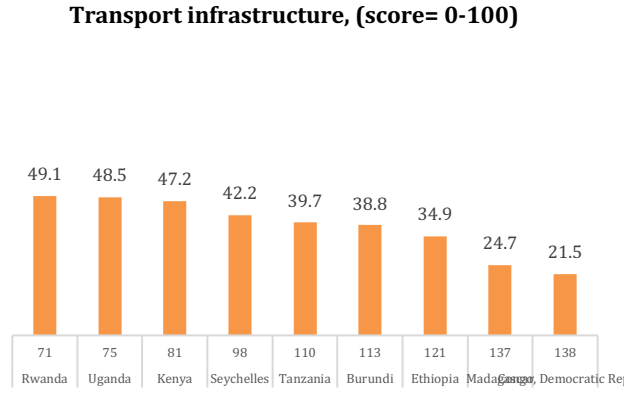
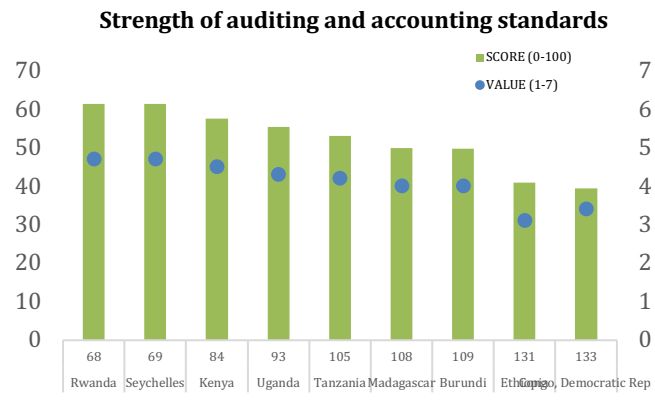
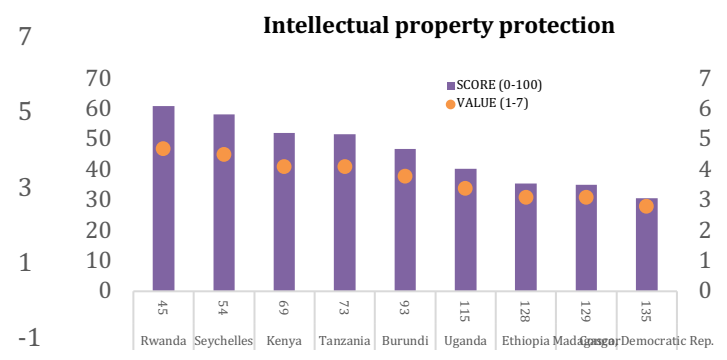
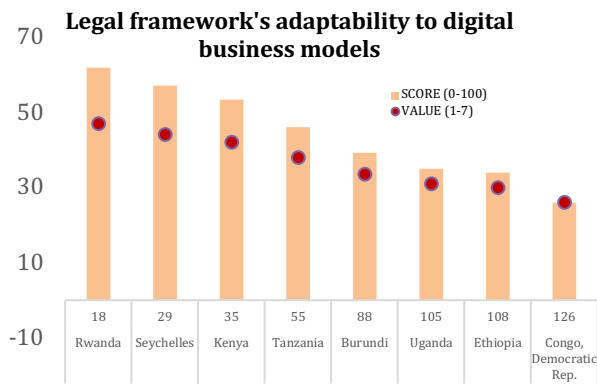
Because of their inherent nature, services require sector-based regulatory frameworks. For the negotiation of new regulatory frameworks for continental integration, the existence of EAC, COMESA and SADC is an advantage because their current regulatory frameworks can be used as a basis for further strengthening, harmonization and expansion to Eastern Africa and beyond to the rest of the continent. This can be termed as a 'low hanging fruit approach' whereby instead of starting from scratch, the RECs build on their current institutions (Hartzenberg, 2020). For example, in case of dispute settlement, the East African Community Court of Justice (EACJ) is a supranational court that operates by taking referrals from its constituent national courts and makes rulings for issues that fall under EAC jurisdiction (Oneyema, 2020). Going forward, the present structure of the EACJ could be expanded in scope to facilitate the negotiations of dispute settlement regulation for AfCFTA.

Current regulatory frameworks can be used as a basis for further strengthening, harmonization and expansion to Eastern Africa and beyond to the rest of the continent. This can be termed as a 'low hanging fruit approach' whereby instead of starting from scratch, the RECs build on their current institutions

Another important aspect for negotiation of regional integration in services is *competition law* which predominantly affects mode 3 of services trade. For this aspect also the region has previous experience to draw from. Nineteen years ago, while liberalizing their air transport sector, EAC-COMESA-SADC realized the need for harmonized competition law. Multiple joint stake-holders meetings ensued, reviewing the competition regulations and finally in September 2002 the Ministers for Transport at a meeting in Pretoria adopted common regulation for competition of air transport services in EAC-COMESA-SADC. This shows that the region already has some grounding on unification of competition regulation to enhance productivity, competitiveness and consumer protection in the service sector.

Finally, *intellectual property rights* are yet to be separately acknowledged for services in any of the current regional blocks. Hence it is important that the AfCFTA prioritizes this as a separate topic. In line with the *low hanging fruit* approach, they may also draw from the already established intellectual property frameworks (Hartzenberg, 2020). Since the negotiations regarding MRAs, dispute settlement, competition laws etc. for AfCFTA are yet to evolve to a mature stage, the definitive direction of the negotiations is yet to be seen. Rankings for the World Economic Forum (2020) in the different dimensions of these services suggest some countries are better placed than others. Rwanda, for instance, peaks in score for all four different categories presented in [Figure 10](#). Seychelles ranks second highest for all except transport infrastructure (fourth rank), thus also suggesting it is relatively well-prepared. By contrast, the Democratic Republic of Congo consistently occupies the lowest rank, reflecting the need for significant support in some of these areas.

Figure 10: Preparedness for the AfCFTA Service Sector Liberalisation - Selected Indicators



Source: WEF (2020)

7. Conclusions and Policy Highlights

This document has highlighted the potential of the AfCFTA in terms of spurring the development of the services sector in Eastern Africa. We have argued that the sub-region starts from a position of relative strength because of a strong performance in certain service sub-sectors. Beyond the spur to greater intra-regional FDI in services, this report has highlighted the potential of greater service sector trade under the AfCFTA. In stark contrast with its merchandise trade performance, a number of regional economies already enjoy positive trade balances in services. And that service sector trade is highly dynamic: our own econometric estimates show that the formation of EAC membership on intra-regional trade in services will be 65% over a short time frame, hinting at the enormous possibilities that are to arise from greater continental integration under the AfCFTA.

This relatively strong performance in services may initially seem surprising given the low prevailing rates of productivity (as reflected in per capita incomes) and average low levels of educational attainment (as expressed in indicators such as average number of years of schooling). Yet it reflects a number of characteristics of the sub-region, including the possession of some high-performing centres of higher education³³ and a well-qualified returnee diaspora. It also, arguably, reflects the innate innovative capacity of the region to search for new solutions in response to constraints on the ground. Thus, for example, Eastern Africa has taken a lead in mobile banking simply because of the manifest deficiencies of the traditional banking system. Necessity is very much the mother of invention.

Despite these relative strengths, by global standards the service sector in Eastern Africa is still relatively undeveloped and in need of injections of more capital, technology transfer and managerial expertise. In this report, we argue strongly that deficiencies can at least in part be addressed by attracting more intra-African investment. There have been a number of studies that show that South-South or intra-African investment may have greater spillover effects and create more employment (Amighini and Sanfilippo, 2014; Gold et. al., 2017). Through acquisition of complementary assets, greater scale and brand value, it may also spur greater competitiveness (Kruger and Strauss (2015).

Despite relative strengths, by global standards the service sector in Eastern Africa is still relatively undeveloped and in need of injections of more capital, technology transfer and managerial expertise

One leading example of pan-East African FDI is the banking sector. When Barclays withdrew its holding from Africa in 2016, banks successfully filled the void (Signe, 2020). Nigerian EcoBank and Kenyan Equity Bank are now major regional players and have helped improve access to finance. In the telecom sector, South African firm MTN has become a successful regional investor, being the first major telecoms investor in Rwanda, and now in collaboration with Chinese firm ZTE, in early 2020 MTN Uganda announced the launching of the first 5G SA network in East Africa ([ZTE, 2020](#)). In tourism and

³³ In their econometric analysis of the determinants of intra-African investment, UNECA (2020) actually finds that the prevalence of secondary school education as negatively related to the level of intra-African investment flows. This is a plausible outcome if investment is more sensitive to higher levels of skill attainment (e.g. tertiary).

hospitality, Serena Hotels, originating in East Africa, has made its mark in many countries across the continent. These examples illustrate the potential benefits greater pan-African investment could confer on the region.

Nonetheless, this report has also highlighted the extent to which the effectiveness of more open service sector policies is contingent on the right national regulatory frameworks being in place. Without the right regulatory environment, the opening up of the service sector to greater intra-African investment is unlikely to yield the desired results. In this sense, there will also be a continued role of state-owned enterprises (SOEs) in the provision of some services. While SOEs are commonly perceived as inefficient, SOEs continue to play an enduring role in the global economy and can be catalysts for public sector value creation if operated effectively (PwC, 2015). One example is Ethiopian Airlines, which in 2019 ranked as the top airline in Africa – and is likely to be the only airline which posts a profit in 2020, despite the disruption caused by the Covid-19 crisis.³⁴ It thus finally boils down to appropriate regulatory measures needed to ensure competitiveness (or ‘contestability’) in the provision of services, regardless of ownership.

More will need to be done in the educational sphere too - the highly skilled and specialized nature of much work in the service sectors poses challenges in creating the requisite forms and quality of labour. This will require a greater investment in both TVET and in tertiary education

Given this context, it is quite clear that in the sphere of services AfCFTA negotiations on services are going to be complicated. Currently, substantial heterogeneity exists among policy stances for the services sectors, reflecting different levels of public ownership, regulatory regimes and market development. A greater degree of common understanding and harmonization will be required if progress is to be made rapidly in creating a regional services market. As countries submit their offers for AfCFTA services sectoral commitments, there is thus a need to ensure that the partner states of Regional Economic Communities are on the same page - by using existing regulatory systems and

frameworks within RECs as a basis, a low-hanging fruit approach will accelerate implementation and may also help streamline any existing loopholes present within regional blocs (Hatzenberg, 2020). For instance, complementary to greater FDI in services is the free movement of professionals across the continent, and this will be contingent on reaching *Mutual Recognition Agreements*. More will need to be done in the educational sphere too - the highly skilled and specialized nature of much work in the service sectors poses challenges in creating the requisite forms and quality of labour.³⁵ This will require a greater investment in both TVET and in tertiary education (Berhuria and Goodfellow, 2018).

³⁴ <https://www.worldairlineawards.com/best-airlines-2019-by-region/>

³⁵ Incentives set by external interests are partly to blame for this. In 1986, the World Bank argued that the social returns for higher education were lower compared to those of pre-primary education, an argument which laid the foundation for ‘university bashing’ from other donors and NGOs in Africa (Mkandawire 2011, p. 17).

Finally, as the date of the coming into force of the AfCFTA approaches rapidly, a new issue to take into account is the Covid-19 pandemic. Covid-19 has negatively impacted the services sector in the Eastern African region, as reflected in the slump in service sector GDP in the second quarter of 2020. The future direction is yet to be seen as the pandemic unfolds, but its impact on services trade is likely to be profound. If social distancing persists, because of the necessity of physical proximity between consumers and suppliers it will be particularly disadvantageous for services transacted via- Mode 2, 3 and 4 (Shingal, 2020). Investments which seemed at one point lucrative (e.g. in tourism sectors targeting international visitors) may no longer be viable. Going into the negotiations, member states should pay heed to this and alter their existing strategies accordingly.

The long-term impact of the Covid-19 pandemic on services trade has been profound. Going into the negotiations, Member States should reflect on how this changes their existing strategies for service sector development.

Covid-19 has negatively impacted the services sector in the Eastern African region as reflected in the slump in figures in the second quarter of 2020. The future direction is yet to be seen as the pandemic unfolds further, but its long-term impact on services trade is likely to be profound. Going into the negotiations, Member States should reflect on how this changes their existing strategies for service sector development.

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Annex A

| PAPER | DESIGN | RESULTS |
|---|---|---|
| Chadha, R., Brown, D. K., Deardorff, A. V. and Stern, R. M. (2000), "Computational analysis of the impact on India of the Uruguay Round and the forthcoming WTO trade negotiations", Working Paper no 459, Research Seminar in International Economics, Michigan: University of Michigan. | <ul style="list-style-type: none"> • Computable general equilibrium model • GTAP version 4 dataset (1995-2005) • 15 developing countries and 5 developed countries | A 33% reduction in tariff equivalent of services barriers results in welfare gain of 2% for developed countries and 2.5% of developing countries. |
| Brown, D. K., Deardorff, A. V. and Stern, R. M. (2002) "Computational Analysis of Multilateral Trade Liberalization in the Uruguay Round and Doha Development Round," Working Papers 489, Research Seminar in International Economics, University of Michigan. | <ul style="list-style-type: none"> • The Michigan Model- a computable general equilibrium model designed to assess the potential economic effects of trade liberalization • The GTAP-4 database (1995-2005) • 20 countries or regions (plus rest-of world) and 18 production sectors | A 33% reduction in ad valorem equivalent of services barriers results in a welfare gain of 413.7 billion USD. |
| Francois, J. et al., 2003, Trade Liberalization and Developing Countries under the Doha Round , Tinbergen Institute Discussion Paper TI 2003-060/2, Erasmus University, Rotterdam, August (papers.tinbergen.nl/03060.pdf). | <ul style="list-style-type: none"> • Computable general equilibrium model • GTAP version 5.2 dataset (benchmarked to 1997) • Social accounting data aggregated to 17 sectors and 16 regions | In case of full services trade liberalization, total effect on national income (assuming increasing returns to scale) for: <ul style="list-style-type: none"> • the World is 53,053 millions USD (or 53 billion USD) • Sub-Saharan Africa is 394 millions USD |
| Konan, D. E. and Maskus, K. E. (2006), "Quantifying the impact of services liberalization in a developing country", <i>Journal of Development Economics</i> 81(1):142-162. | <ul style="list-style-type: none"> • Computable general equilibrium model of a small open economy (benchmarked to 1995) • Tunisian Economy disaggregated to 15 sectors | For Tunisia, percentage gain in macroeconomic variables because of full liberalization of mode 1 and mode 3 of services: <ul style="list-style-type: none"> • Welfare, household income (5.30%) • Consumer price index (- 8.04%) • Real returns to labor (4.23%) • Real returns to capital (8.23%) • Labor turnover (3.73%) • Capital turnover (5.35%) |

| PAPER | DESIGN | RESULTS |
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| <p>Mattoo A., Rathindran, R. and Subramanian, A. (2006). 'Measuring Services Trade Liberalization and its Impact on Economic Growth: an Illustration.' Journal of Economic Integration, 21, pp. 64-98.</p> | <ul style="list-style-type: none"> • Cross-country regression analysis • Sample of 60 countries • Time period: 1990-1999 | <ul style="list-style-type: none"> • With a global sample, countries with complete Liberalization of the financial and telecom sector grew 1.5 percent faster over the 90s • With a sample of only developing countries, countries with complete liberalization of the financial and telecom sector grew 2.8 percent faster over the 90s |
| <p>Balistreri, E.J. and D.G. Tarr (2011). Services Liberalization in Preferential Trade Arrangements: The Case of Kenya. World Bank Policy and Research Working Paper No. 5552.</p> | <ul style="list-style-type: none"> • Comparative static general equilibrium model • Models a 55 sector small open economy for Kenya • Data from social accounting matrix for Kenya (2003) | <p>For welfare gains in Kenya (provided no initial rent is captured):</p> <ul style="list-style-type: none"> • Liberalization with respect to African partners will lead to a welfare gain on 0.02 percent of consumption • Liberalization with respect to EU will lead to a welfare gain of 0.06 percent of consumption <p>Liberalization with respect to all foreign partners will lead to a welfare gain of 0.16 percent of consumption</p> |
| <p>Jouini, N., Rebei N, 2014, The welfare implications of services liberation in developing country. Journal of Development Economics, 106 (): 1-14</p> | <ul style="list-style-type: none"> • Economy of Tunisia modeled using two-sector small open economy dynamic and stochastic general equilibrium (DSGE) model • Uses data from 2000Q1 till 2010Q4 | <p>The percentage gain from eliminating services trade barriers in Tunisia on the following are:</p> <ul style="list-style-type: none"> • welfare (2.92%) • production (2.25%) • services production (1.12%) • goods production (3.04%) • export of services (7.22%) • exports of goods (3.63%) • investment (3.71%) • service real price (-0.66%). |