COOPERATION WITH AFRICA

POLICY RECOMMENDATIONS FOR THE G20

T20 Japan Task Force on Cooperation with Africa

Cooperation with Africa
Policy Recommendations for the G20

May 2019

T20 Japan Task Force on Cooperation with Africa

JICA Research Institute

10-5 Ichigaya Honmura-cho Shinjuku-ku Tokyo 162-8433, JAPAN
TEL: +81-3-3269-2357 FAX: +81-3-3269-2054

Cooperation with Africa
Policy Recommendations for the G20

Contents

Foreword iii
List of Co-Chairs iv

Fiscal and Debt Sustainability in Africa 1
Kapil Kapoor, George Kararach, Jacob Odour, Walter Odero, Edward Sennoga, Brahima Coulibaly, Ryosuke Nakata

G20 Compact with Africa 15
Rob Floyd, Kapil Kapoor, Laura Sennett

Industrial Development and ICT in Africa: Opportunities, Challenges and Way Forward 29
Gamal Ibrahim, Witness Simbanegavi, Anita Prakash, William Davis, Wilson Wasike, Ashraf Patel

Linking Smallholder Production with Value-Added Food Markets 45
Dr. Belay Begashaw, Gert-Jan Verburg, Futoshi Yamauchi, Daniele Fattibene, Fujita Yasuo

Sustainable Prevention of Food Crises in Sub-Saharan Africa 59
Ousmane Badiane, Julia Collins, Yasuo Fujita, David Laborde, Will Martin, Maximo Torero, Rob Vos, Futoshi Yamauchi

Tax Challenges of Digitalization in Africa 71
Nara Monkam, Gamal Ibrahim, William Davis, Christian von Haldenwang

Cooperation with Africa

Foreword

This publication is the outcome of collective work by the T20 "Cooperation with Africa" taskforce members who voluntarily participated in the process of producing policy briefs and recommendations for T20 Japan. I would like to express my sincere appreciation to all the taskforce members who kindly shared their precious time to produce briefs on the most relevant policy issues in African development today.

I would especially like to thank Dr. Kapil Kapoor, Director General, Southern African Regions for the African Development Bank, and the lead co-chair of this taskforce, as well as Dr. Elizabeth Sidiropoulos, Chief Executive, South African Institute of International Affairs, who chaired the Africa Standing Group (ASG) which has continuously worked on the past few T20 efforts, including T20 Japan, for African development.

We, the taskforce members, would like to thank Dr. Naoyuki Yoshino, Dean of the Asian Development Bank Institute (ADBI), and the T20 Policy Research Team led by Mr. Katsuyuki Meguro, Ms. Mari Sawada and Mr. So-heon Lee for their excellent support and coordination during the preparation of policy briefs and the logistical arrangements for the T20 summit.

In addition, we would like to appreciate the financial support provided by the German Development Institute (DIE) at the T20 summit.

Ryosuke Nakata
Chief Economist
Japan International Cooperation Agency
Lead Co-chair of Task Force on "Cooperation with Africa"

List of Co-Chairs
Cooperation with Africa

Lead Co-Chairs:

- **Kapil Kapoor,** Director General, Southern African Region, African Development Bank
- **Ryosuke Nakata,** Chief Economist, Japan International Cooperation Agency

Co-Chairs:

- **Belay Begashaw**, Director General, Sustainable Development Goals Center for Africa
- **William Davis,** Associate Economic Affairs Officer, United Nations Economic Commission for Africa
- **Rob Floyd**, Director and Senior Advisor, African Center for Economic Transformation
- **Gamal Ibrahim,** Chief, Finance and Private Sector Section, United Nations Economic Commission for Africa
- **Julia Leininger,** Head of Program Transformation of political (dis-)order, German Development Institute / Deutsches Institut für Entwicklungspolitik
- **Nara Monkam**, Director, Research, African Tax Administration Forum
- **Elizabeth Sidiropoulos**, Chief Executive South African Institute of International Affairs
- **Witness Simbanegavi,** Director of Research, African Economic Research Consortium (at the time of writing)
- **Rob Vos**, Director of Markets, Trade and Institutions Division, International Food Policy Research Institute
- **Futoshi Yamauchi**, Senior Research Fellow, International Food Policy Research Institute

Cooperation with Africa
Policy Recommendations for the G20

The international community is working together towards the achievement of the Sustainable Development Goals (SDGs) by 2030. While there is limited room for further improvement relating to these development goals in East Asia, a region that was a primary driver in the success of the MDGs, improvement in Africa is the key to the success of the current SDGs.

Africa has vast natural resources, including 60% of the world's uncultivated arable land and substantial deposits of oil and other mineral resources. Africa also has a young and fast-growing population, which could support the economic development of the region if properly employed in modern, high-productivity sectors. The G20 must deliver realistic and feasible policy messages to African and world leaders to help the continent to effectively utilize these endowments and achieve sustainable development.

This year, T20 Japan takes up the issue of "Cooperation with Africa" as one of its taskforces discussing various aspects of African development. This book is a collection of policy discussions by a volunteer group of global thinkers and development practitioners experienced in African development. This group has worked together closely for the past few months to choose the most critical issues in African development, to discuss the resulting policy challenges, and to work out policy recommendations to the G20 leaders.

The major players in African development today are not limited to OECD donors as in a few decades ago though. Many non-OECD governments are among the important contributors to African development. Also, the inflow of FDI has almost reached the level of net ODA receipts recently as a large number of private sector firms from around the world are increasing their business in Africa. And, as the African economies are becoming increasingly integrated into the world economy, many policies of the G20, which are aimed at the welfare of their domestic populations, also influence African development positively or negatively. The G20 is exactly the right forum to coordinate these economic policies, including international tax and regulatory structures, and agree on a unified framework within which the development efforts are to be harmonized.

Each policy brief discusses the challenges and opportunities as well as the policy recommendations for each policy issues. The main messages across individual policy issues can be summarized as:

- Reach agreement on a unified approach towards macroeconomic stability in Africa through attaining fiscal and debt sustainability and strengthening domestic resource mobilization;
- Mobilize and involve all development actors and tools including digital technology towards employment led growth, resilient food systems and the sustainable development of African economies;
- Enhance coordination between the G20 and Africa to achieve coherent policies toward regional and international economic integration, including the removal of G20 and individual member policies that impede development in Africa. At least, a "do no harm" approach should be guaranteed.

For the international community to work with African countries in achieving sustainable growth, policymakers need to generate a set of achievable policy packages. We hope that these recommendations by the T20 team based upon the academic and practical studies may help policy formulation on African development by the global leaders.

Ryosuke Nakata
Chief Economist
Japan International Cooperation Agency
Lead Co-chair of Task Force on "Cooperation with Africa"

Annex

Key Recommendations, Specific Actions, and Policy Briefs[1] (Task Force 5: Cooperation with Africa)

Summary of Challenge/Goal
Although a number of African economies made strong progress in economic and social development as well as poverty reduction during the 2000's, they still face various development challenges. Poverty and hunger are still widespread, with over 65 million people facing crisis-level food insecurity. Debt burdens are on the rise again, requiring policy coordination beyond the traditional development partners. Certain international trade and other policies and practices also impede African development. G20 and African countries should coordinate their development efforts and economic policies to seize new opportunities for the advancement of African economies and the achievement of the SDGs.
Key Recommendation 1: Reach agreement on a unified approach towards macroeconomic stability in Africa through attaining fiscal and debt sustainability and strengthening domestic resource mobilization.
Specific Actions
• Step up the debate among G20 on debt data reporting standards for low-income countries, especially Africa—covering contingent and parastatals' liabilities too—and assist and encourage African countries to collect and publish debt data in real time. • Put in place an orderly debt resolution mechanism given the more diffuse creditor base and other new features of African debt. • Assist in developing systems and processes that will ensure that borrowed funds, especially non-concessional, are used productively to enhance the repayment capacity; and assist in designing standard terms in negotiations over innovative sources of funding that limit the need for foreign currency borrowing and reliance on the volatile funding sources by African countries. In this context, ensure that Multilateral Development Banks are adequately capitalized. • Ensure that taxation of the digitalized economy works for Africa, especially regarding the profit allocation rules for multi-national enterprises, and enhance technical and financial support for the use of advanced technologies for improving customs and tax administrations such as the automatic electronic exchange of invoices and the digitalization of customs administration.

[1] This is an input from the Cooperation with Africa taskforce to the T20 communique. Communique was compiled from this input.

Referenced Policy Briefs
• Kapil Kapoor, George Kararach, Jacob Odour, Walter Odero, Edward Sennoga, Brahima Coulibaly, Ryosuke Nakata. "Fiscal and Debt Sustainability in Africa" • Nara Monkam, Gamal Ibrahim, William Davis, Christian von Haldenwang. "Tax Challenges of Digitalization in Africa" • Gamal Ibrahim, Witness Simbanegavi, Anita Prakash, William Davis, Willson Wasike, Ashraf Patel. "Industrial Development and ICT in Africa: Opportunities, Challenges and Way Forward"
Key Recommendation 2: Mobilize and involve all development actors and tools including digital technology towards employment led growth, resilient food systems and the sustainable development of African economies.
Specific Actions
• Enhance the alignment of various actors involved in African development, such as Compact with Africa country teams, local businesses and G20 business sectors, to foster non-resource based economic development led by the private sector. • Consolidate and enhance development support programs, including G20 support for the financing of region-wide investments in infrastructure and irrigation schemes for the development of climate-resilient agrifood systems, agricultural productivity growth and massive employment creation, under a common framework such as the Comprehensive Africa Agriculture Development program (CAADP), and enhance the coordination of individual development programs. • Promote financial inclusion as a prerequisite to business development through soft loans, credit ratings and other financial instruments. • Establish a framework for utilizing digital technology to achieve sustainable development, including an information system for food market transparency, the "fintech" development to facilitate the access to finance by local small businesses, and the revenue administration to eliminate tax leakages.
Referenced Policy Briefs
• Rob Floyd, Kapil Kapoor, Laura Sennett. "G20 Compact with Africa" • Gamal Ibrahim, Witness Simbanegavi, Anita Prakash, William Davis, Willson Wasike, Ashraf Patel. "Industrial Development and ICT in Africa: Opportunities, Challenges and Way Forward" • Belay Begashaw, Gary-Jan Verburg, Futoshi Yamauchi, Daniele Fattibene, Yasuo Fujita. "Linking Smallholder Production with Value-Added Food Markets" • Ousmane Badiane, Julia Collins, Yasuo Fujita, David Laborde, Will Martin, Maximo Torero, Rob Vos, Futoshi Yamauchi. "Sustainable Prevention of Food Crisis in Sub-Saharan Africa"

Key Recommendation 3: Enhance coordination between the G20 and Africa to achieve coherent policies toward regional and international economic integration, including the removal of G20 and individual member policies that impede development in Africa. At least, a "do no harm" approach should be guaranteed.
Specific Actions
• Realign G20 countries' agriculture trade practices, especially subsidies and non-tariff barriers that are inconsistent with WTO regulations to provide opportunities for African producers to participate in global value chains. • Step up efforts to combat illicit capital outflows, including helping track and repatriate illicit funds back to African countries. • Develop regional regulatory institutions that ensure the safety and quality of African products (especially food products) while not placing a prohibitive burden on African small and medium enterprises and smallholder farmers in complying with regulations. • Support a global and inclusive discussion of a new approach to taxation of the digitalized economy that considers Africa's perspectives and priorities, alongside those of other developing countries, and avoid penalizing African countries that fail to implement international tax standards that they do not have the capacity to implement.
Referenced Policy Briefs
• Gamal Ibrahim, Witness Simbanegavi, Anita Prakash, William Davis, Willson Wasike, Ashraf Patel. "Industrial Development and ICT in Africa: Opportunities, Challenges and Way Forward" • Belay Begashaw, Gary-Jan Verburg, Futoshi Yamauchi, Daniele Fattibene, Yasuo Fujita. "Linking Smallholder Production with Value-Added Food Markets" • Ousmane Badiane, Julia Collins, Yasuo Fujita, David Laborde, Will Martin, Maximo Torero, Rob Vos, Futoshi Yamauchi. "Sustainable Prevention of Food Crisis in Sub-Saharan Africa"Monkam, Ibrahim, Davis, von Haldenwang. "Tax Challenges of Digitalization in Africa" • Nara Monkam, Gamal Ibrahim, William Davis, Christian von Haldenwang. "Tax Challenges of Digitalization in Africa"

COOPERATION WITH AFRICA

Fiscal and Debt Sustainability in Africa

Kapil Kapoor (African Development Bank)
George Kararach (African Development Bank)
Jacob Odour (African Development Bank)
Walter Odero (African Development Bank)
Edward Sennoga (African Development Bank)
Brahima Coulibaly (Brookings Institution)
Ryosuke Nakata (Japan International Cooperation Agency) [1]

March 29, 2019

[1] In addition, valuable inputs were provided by Annalisa Prizzon (Overseas Development Institute); and Witness Simbanegavi and Njuguna Ndungu (African Economic Research Consortium).

Abstract

Fiscal sustainability concerns in Africa have increased recently following heightened fiscal vulnerabilities attributed to external factors including falling commodity prices that weakened fiscal revenues and growth, particularly for commodity-exporting African countries. To entrench fiscal sustainability, countries need to strengthen domestic resource mobilization and improve public investment management. Consequently, measures to increase tax revenue collections, savings mobilization and efficiency of public spending are critical. The G20 should support debt reporting, data harmonisation, tax compliance, combating illicit financial flows and developing effective debt resolution frameworks.

Challenge[2]

Implementing the sustainable development strategies requires scaling up financial resources. Sub-Saharan African countries (SSA) have low domestic saving rates and continue to face severe infrastructure backlogs. Concerted efforts to close the infrastructure gap, however, have contributed to the accumulating public debt. While fiscal policy may drive a country's development, it can also lead to unsustainable debt if not well managed.

Declines in official development assistance and weaknesses in domestic revenue mobilization have necessitated increased use of debt, fueling concerns about a new debt crisis for SSA (see **Table 1**).

---

[2] The more detailed analysis of the challenge facing the African countries is available at: https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/WPS_No_227_Public_Debt_Sustainability_in_Africa_Building_Resilience_and_Challenges_Ahead_H.pdf.

The number of African countries at high risk or in debt distress has more than doubled from the 8 in 2013 to 18 in 2018. Close to 40% of SSA countries are at risk of retreating into a major debt crisis (World Bank, 2018).

On average, debt levels are significantly lower than that triggered the HIPC and MDR initiatives. However, there is a substantial variation across countries. Country-specific policy responses are required to balance the growing demand for development financing and debt sustainability. In this regard, detailed breakdown of external debt by creditors will be critical for implementing the Argentina Communique.[3]

The composition of external public debt in SSA has changed drastically over the past decade. The share of multilateral and concessional debt in external debt decreased steadily while the share of non-Paris club sovereign creditors doubled from 15% in 2007 to 30% in 2016, with the share of Paris club creditors decreasing from 25% to 7% (Mustapha and Prizzon, 2018; World Bank, 2018). The share of market-based debt (incl. domestic debt) also has grown significantly.[4]

Increased reliance on non-traditional creditors and commercial financing has increased the cost of debt. Debt servicing costs averaged 11 percent of government revenues in 2016, up from just 4 percent in 2013 (IMF, 2018). Interest payments have rapidly risen as a share of government revenues just like the costs for public debt relative to private debt contracted over the same period (**Figure 3**). In addition, some SSA countries with large bond financing now face large bullet payments, most of which will be maturing in the next few years and

[3] Defined by sustainable financing practices for both borrowers and creditors. See Berensmann (2018) for some of these ideas.

[4] Eurobonds issues by SSA governments stood at about USD200 million in 2006 but rose to about USD 6.3 billion in 2015 (Hogan Lovells, 2017 database), a more than thirtyfold increase in just a decade. Eurobond issues by SSA have proved quite popular with investors, with many such issuances being oversubscribed (e.g., Senegal).

presenting a potential refinancing risk (World Bank (2018).

External debt and investment show a positive correlation, suggesting the increasing use of debt for growth-enhancing purpose (**Figure 4**). The quality and efficiency of public investments, however, are crucial for ensuring growth and fiscal sustainability. SSA countries compare unfavourably in terms of public investment efficiency relative to other regions, with an efficiency gap of up to 54% (see Barhoumi et al., 2018).

Despite aid and Foreign Direct Investment, Africa is a net creditor to the rest of the world of valuable development finance once Illicit Financial Flows (IFFs)[5] are taken into account. Between 1980 and 2009, illicit transfers increased within a range of US $1.22 to $1.35 trillion, amounting to 6% of Africa's GDP.[6] IFFs end up weakening financial systems and reducing legitimacy of the state in the eyes of their citizens.[7]

Proposal

Policies for fiscal sustainability: what African countries and G20 should do.

- Strengthening **public investment management** through key

[5] Defined as "money that is illegally earned, transferred, or utilized, whereby somewhere at its origin, movement, or use, the money broke laws and hence it is considered illicit" Global Financial Integrity

[6] African Development Bank and Global Financial Integrity (2013):"Africa's Illicit Financial Flows: What do They Tell us?"

[7] The relevance of countering IFFs has been recognized by the international community: with a global commitment through the Sustainable Development Goals and the Addis Ababa Action Agenda, have committed to "redouble efforts to substantially reduce IFFs by 2030."

measures; namely fact based project selection using standardized technical and financial feasibility diagnostics; streamlining delivery of infrastructure by improving the rigor of project designs, contractor selection and management; and more effective use of existing infrastructure, via effective project monitoring, adequate maintenance, and cost-reflective infrastructure tariffs. Others include strengthening multiyear budgeting and infrastructure governance and technical capabilities. Diagnostics, such as public investment management assessments and public expenditure reviews should be undertaken periodically to inform requisite remedial reform measures. G20 countries can support African countries through building and strengthening technical capacity for project appraisals, as well as strengthening public sector capacity to oversee or implement large-scale infrastructure projects.

- Increasing **domestic revenue mobilization**, by shifting from commodity taxation towards more neutral, broad-based value-added or sales taxes and personal income tax. Simplifying the registration process for businesses, leveraging new technologies to modernize the tax collection system, deepening regional integration and tax coordination, are necessary elements of a broad-based strategy to broaden the tax base. G20 countries can support African countries to strengthen capacity for tax revenue mobilisation; e.g., design of new tax codes, digitisation of tax systems, including capacity to levy taxes on e-commerce and related transactions.

- **Increasing domestic savings** by improving monetary frameworks, supporting the development of long-term savings instruments, aligning exchange rates on their long-term sustainable level, and reducing monetary financing to tame inflation.

- **Developing and implementing fiscal rules** to reduce fiscal discretion and allow for more effective fiscal policy. Fiscal rules, if well designed and implemented, can help reduce the pro-cyclicality of government spending, encouraging savings accumulation during hay days.

Policy measures for debt sustainability

Recommendations to the G20 on fiscal and debt sustainability

- Accelerate the projects on ***debt data reporting and standardization***. Support countries to establish publicly available debt registers; set up Debt Management offices, or strengthen capacity where the offices already exist; and ensure linkages between the debt management functions and other public finance management functions. Support development of medium term public investment programs that are linked to the raising of public debt.

- Put in place a ***framework for an orderly debt resolution mechanism*** in the context of more diffuse creditor base and other new features of the debt.

- Support efforts by African countries to ***enforce compliance with taxation*** in face of domestic revenues lost to profits shifting, and support DRM capacity development more broadly. This would require technical assistance in formulating revenue mobilization policies, attendant legislation and regulations. It would also require support with procurement of software for revenue recording and collection.

- Step up efforts to ***combat illicit capital outflows from Africa***, including helping track and repatriating illicit funds back to African countries. Support should be provided to assessing key risks relating to money laundering and illicit financial flows, and defining mitigation measures; building human and institutional capacity to uphold relevant laws, investigate suspicious activity and recover stolen assets; and providing the infrastructure necessary to track and report cash movements across borders.

- Ensuring ***that multilateral development institutions are adequately capitalized*** and can use their own resources - and the leverage their credibility affords - to offer countries alternative meaningful solutions to expensive or risky foreign-currency borrowing in international capital markets. Given their development mandate, political neutrality and strong technical expertise and due diligence capacity, multilateral financing is more likely to yield development benefits and have a catalytic role.

- ***Support countries to improve long-term debt management capacity, governance, and transparency including: Reviewing debt sustainability assessment methodologies*** to capture new realities, notably security-related expenditures and the quality of public investment, and take into account unique features of African economies, institutions and operations of various markets, including the financial and labour markets.

- ***Develop innovative tools to finance development.*** Support the development of African domestic capital markets, potentially through the introduction of African-wide safe assets, with senior tranches potentially guaranteed by the MDBs and marketed to international investors as a mezzanine, investment-grade exposure to frontier market debt.

- **Designing standard terms and assisting African countries in negotiations over innovative sources of funding** that limit the need for foreign currency borrowing and exploit mutually advantageous exchanges with traditional or new bilateral lenders. Attention should be paid to **crowding-in private capital through risk mitigation instruments** to unlock resources that can substitute debt. Multilateral lenders can provide benchmarks and guidelines, as well as low-risk financing tranches for long-term projects.

What African countries should do to improve debt sustainability.

Emphasis should be placed on more effective and efficient use of debt, including through institutional and governance reforms to strengthen debt management and data transparency. The specific measures include:

- **Reduce reliance on risky and volatile debt sources.** Developing innovative and alternative mechanisms of development financing such as Public Private Partnerships, securitization of infrastructure assets, privatization as recently demonstrated by Ethiopia. In addition, creation of an asset class for public projects, using the leverage afforded by safe capital from multilateral institutions is equally important. However, it is important to adequately quantify and mitigate the underlying fiscal risks from PPPs and government guarantees.

- **Increasing the maturity of external debt** when possible at reasonable costs, possibly making use of guarantees provided by multilateral institutions to tap liquidity at the long-end of the yield curve (20 to 30 year's bonds), on the model of Kenya's recent issue of a 30-year bond in February 2018.

- Using **more flexible, counter-cyclical and state-contingent debt instruments** to relieve the debt burden during recessions, through commodity hedging or GDP-indexed instruments.

Key implementation challenges should be mitigated, notably the high liquidity and novelty premium charged at first issuance and the increased risk of moral hazard, especially when the borrower assumes excessive risks in the knowledge that relief will be provided. Fiscal rules may also be considered in the management of windfalls.

- Developing **domestic safe assets** through enhanced credibility and independence of monetary and debt management authorities, with the support of the MDBs' debt management initiatives and technical assistance.

- **Greater transparency** in debt management, including commitment by governments to release in real-time all data on old and new debt from all sources. This will require efforts to standardize data gathering practices, develop data collection systems, address data gaps, notably in the accounting of SOE-related liabilities and contingent liabilities arising from sovereign guarantees to individual projects, and consolidate government accounts, across regional levels, agencies, ministries and institutions.

References

- Barhoumi, K., Ha Vu, Shirin Nikaein Towfighian, and Rodolfo Maino. (2018). "Public Investment Efficiency in Sub-Saharan African Countries: What Lies Ahead?" IMF African Department Series No. 18/09, International Monetary Fund, Washington DC.

- Berensmann. K. (2018). "The global debt governance system for developing countries: deficiencies and reform proposals", in

Third World Thematic: TWQ Journal.

- Coulibaly, Brahima, Dhruv Gandhi, Lemma Senbet. (2019). "Is sub-Saharan Africa facing another systemic sovereign debt crisis?" Policy Brief. Africa Growth Initiative, The Brookings Institution.

- Kararach, G., Kedir, A., Ajambo, E. and Souminen, H. (2017). "Fiscal Policy, Long-Term Growth and Structural Transformation in Africa", in Lopes, Carlos, Hamdok, Abdalla, Elhiraika, Adam (Eds.), Macroeconomic Policy Framework for Africa's Structural Transformation, Palgrave Macmillan.

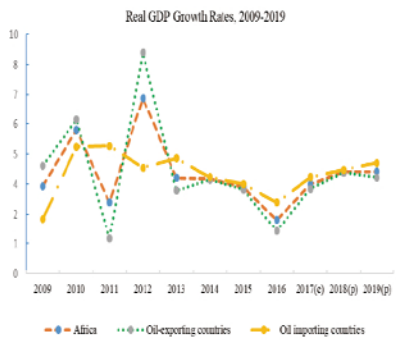
- Mustapha, S., and A. Prizzon. (2018). "Africa's Rising debt: How to Avoid a New Crisis." ODI Briefing Papers.

- World Bank Group. 2018. Africa's Pulse, volume 18. Washington, DC: World Bank.

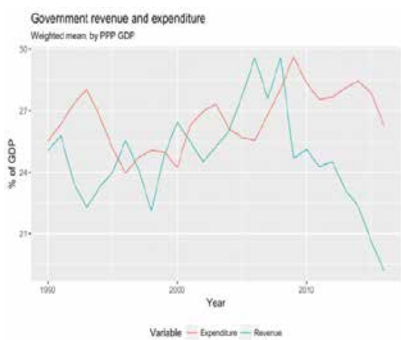
Appendix

Figure 1: Primary balance deterioration occurred mostly through deteriorating revenues

(a) Real GDP Growth

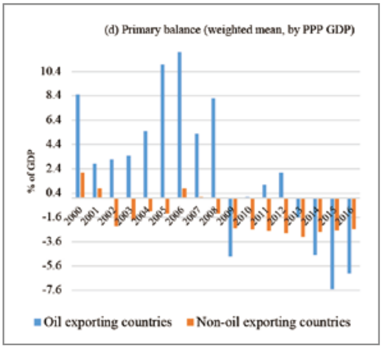


(c) Government revenue and expenditure



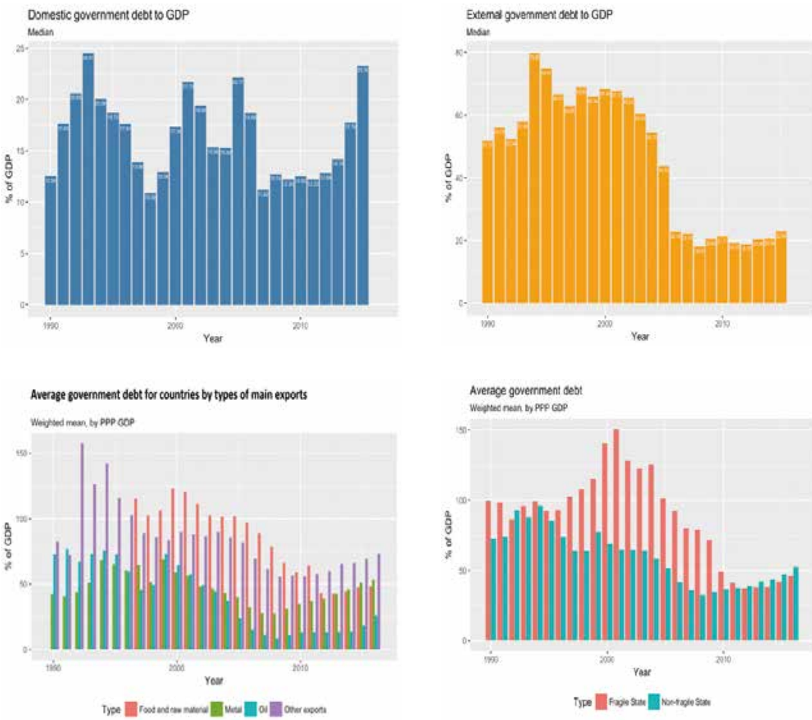
(b) Commodity prices variability over time

(d) Primary fiscal balance



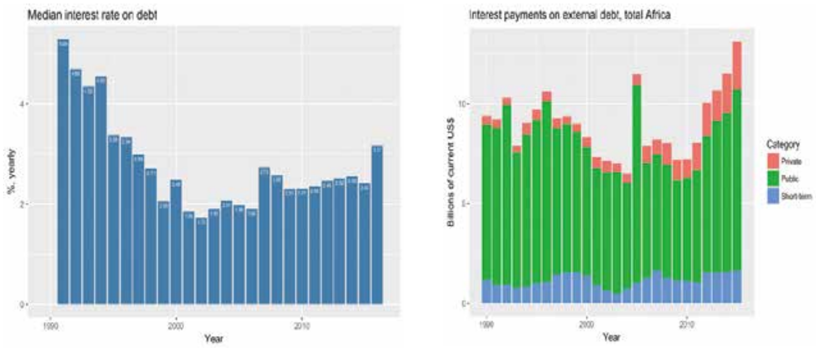
Source: AfDB Statistics Department

Figure 2: Public debt accumulation in Africa



Source: AfDB Statistics Department

Figure 3: Interest rates on Africa's debt



Source: AfDB research department

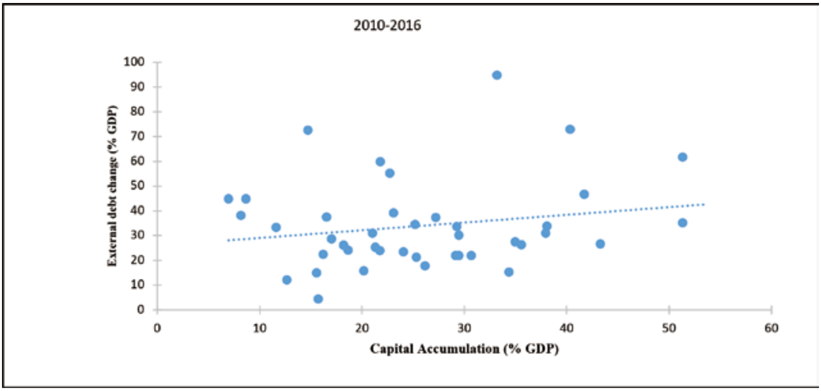
Table 1: Risk of debt distress in selected low-income African countries as from 2017

Low risk	Moderate risk	High risk	In distress
Rwanda (Jul. 2017) Senegal (Jan.2018) Tanzania (Jan. 2018) Uganda (Jan. 2017) Comoros (Jan. 2019)	Kenya (Nov. 2018) Benin (Jan. 2019) Burkina Faso (Dec. 2018) Congo, DR (Oct. 2018) Congo, Rep (Sept. 2018) Côte d'Ivoire (Dec. 2018) Guinea (Aug. 2018) Guinea-Bissau (Dec. 2017) Lesotho (Dec. 2018) Liberia (Dec. 2018) Madagascar (Jan. 2019) Malawi (Jan. 2019) Mali (July. 2017) Niger (Feb. 2017) Nigeria (Dec. 2018) Sierra Leone (Jun. 2017) Togo (Dec. 2017)	Burundi (Dec. 2018) Cameroon (Jul. 2017) Cabo Verde (Nov. 2017) Central African Rep. (Dec. 2017) Djibouti (Apr. 2017) Ethiopia (Jan. 2019) Gambia (Jul. 2017) Mauritania (Dec. 2017)	Chad (Aug. 2017) Mozambique (Mar. 2018) South Sudan (Mar. 2017) Sudan (Dec. 2017) Zimbabwe (Jul.2017) Eritrea (Jan. 2019) Gambia (Jan. 2019) São Tomé and Príncipe (Dec. 2018) Zambia (Oct. 2017) Somalia (Dec. 2017)

Note: The assessment of debt risk is based on average CPIA scores over the recent years and two types of debt burden indicators namely, the size of debt and the debt servicing. Under each broad indicator a pair of sub-indicators is used – the share of exports and the share of Gross National Income (GNI). A set of complementary indicators is appended to each broad indicator to support the analysis (see IMF DSA analysis). A country is classified as at (a) ***Low risk****, when all the debt burden indicators are well below the thresholds; (b)* ***Moderate risk****, when debt burden indicators are below the thresholds in the baseline scenario, but stress tests indicate that thresholds may be breached if there are external shocks or abrupt changes in macroeconomic policies; (c)* ***High risk****, when the baseline scenario and stress tests indicate a protracted breach of debt or debt-service thresholds, but the country does not currently face any repayment difficulties.*

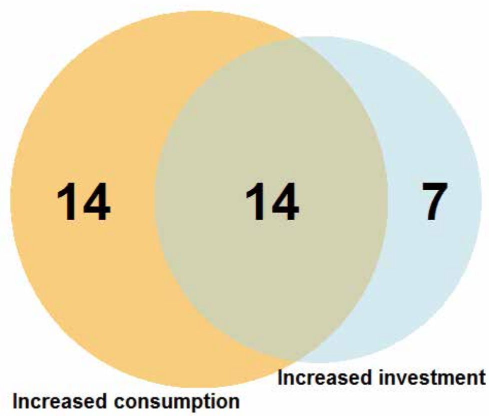
Source: Compiled by AfDB Staff from IMF Article IV, and AfDB Statistics Department

Figure 4: Debt is associated with increased public investments in Africa



Source: AfDB Research Department R^2=0.03

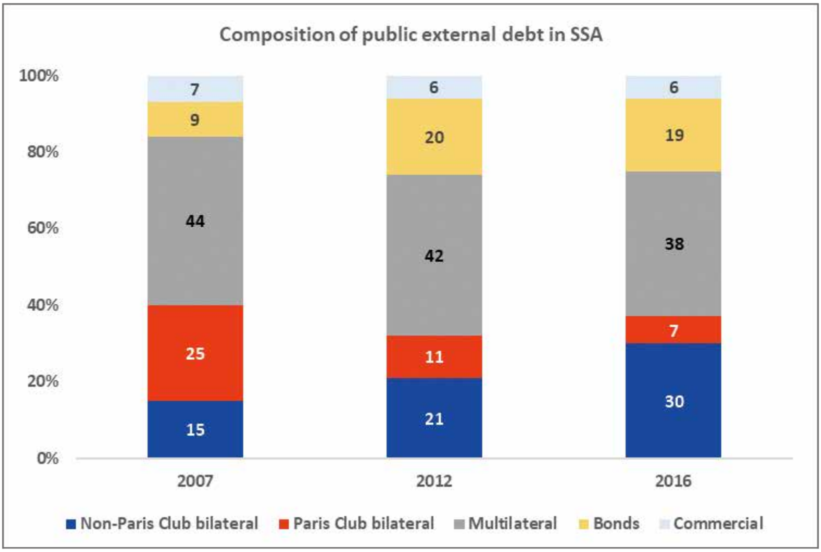
Figure 5: Number of countries with increases in government consumption, public investment, or both between 2013 and 2016



Source: Coulibaly, Gandhi, and Senbet (2019).

Sample excludes São Tomé and Príncipe, South Sudan, and Gambia due to data availability

Figure 6: Composition of public external debt



Source: AfDB Statistics Department

COOPERATION WITH AFRICA

G20 Compact with Africa

Rob Floyd (African Center for Economic Transformation)
Kapil Kapoor (African Development Bank Group)
Laura Sennett (African Development Bank Group)

March 29, 2019

Abstract

The G20 Compact with Africa (CWA), under the G20 Finance Track, promotes sustainable development in reform-minded African countries by improving the framework conditions for mobilizing private sector investments. The initiative identifies commitments in the macroeconomic, business and financing frameworks that form country-led investment compacts. The CWA is governed through the G20 Africa Advisory Group (AAG), co-chaired by Germany and South Africa. The African Development Bank Group, the International Monetary Fund, and the World Bank Group coordinate the initiative. While the CWA has been successful to date, it could benefit from further coordination of stakeholders as recommended in this brief.

Challenge

In April 2018 the AAG assessed progress in identifying policy and support actions under business, macro-economic, and financing[1] There were 101 commitments identified in the nine countries that were participants in the initiative at that time. Twenty three percent of commitments were reported as wholly achieved; and 74 percent of commitments were reported as on track.

In October 2018 the AAG assessed private sector activity in Compact countries.[2] The monitoring report signaled that sound policies to improve investment conditions are paying off and investment interest in Compact countries is growing. Total FDI inflows to CWA countries

---

[1] G20 African Advisory Group (2018), "G20 Compact with Africa – Compact Monitoring Report."

[2] G20 African Advisory Group (2018), "Trends in FDI and Cross-Border Investments in Compact with Africa Countries."

amounted to $20 billion in 2017. The total annual volume of inbound FDI to all CWA countries increased by 36 percent over the past five years, from $14.9 billion in 2013 to $20.2 billion in 2017.

While the CWA has been successful to date, the monitoring reports, peer reviews and policy notes have indicated areas for further strengthening, which are briefly summarized in this report. With the implementation of these recommendations, and with the continuing support from the G20 and international organizations, the CWA initiative promises to be an important initiative to mobilize private sector investment in the continent.

Context and Purpose of the G20 Compact with Africa

The G20 Compact with Africa (CWA) Initiative[3], under the G20 Finance Track, provides a framework for boosting private investment and increasing the provision of infrastructure in Africa. The initiative aims to help African countries achieve sustained and inclusive economic growth by mobilizing governments and their international partners to implement concrete measures to create a better environment for private investment.

Participation in the CWA sends a strong signal to private investors about the country's interest in attracting investment and their commitment to implementing key reforms. G20 and other partner countries and international organizations (IOs) coordinate more closely, step up technical assistance, and provide support for early stage project preparation. They take multilateral action to strengthen cooperation on tax avoidance, harmonize risk-mitigation instruments and make them more accessible and user-friendly to private investors,

[3] G20 Compact with Africa, https://www.compactwithafrica.org/content/compactwithafrica/home.html.

and review regulation for institutional investors. G20 members and other partner countries encourage their domestic investors to respond to the investment opportunities in participating African countries.

Areas of Focus

The CWA initiative covers the Macroeconomic, Business, and Financing Frameworks. The Macroeconomic Framework identifies considerations for maintaining macroeconomic stability, while providing for adequate investment in non-commercial infrastructure. These include: ensuring sustainability of public debt over time; increasing domestic revenue mobilization via an investment-friendly tax system; combining domestic tax reforms and enhanced international cooperation to contain profit-shifting and tax evasion; ensuring sound public investment management; and, improving the performance of public utilities.

The Business Framework aims to make Africa more attractive for private investors. This includes setting up reliable regulations and institutions; establishing investor protection and dispute resolution mechanisms; providing political risk insurance; improving project preparation; and standardizing contracts.

The Financing Framework aims to increase the availability of financing at reduced costs and risks. This includes supporting risk mitigation instruments to attract and sustain private investment; developing domestic debt markets and a domestic institutional investor base; and, creating instruments for institutional investors.

The initiative identifies commitments in these three areas that provide the basis for country-led investment compacts. Individual investment compacts are adapted to country-specific circumstances and priorities. The commitments include indicators and timelines and bilateral and multilateral support for their achievement.

CWA Countries and Partners

The CWA has twelve African participants: Benin, Burkina Faso, Guinea, Côte d'Ivoire, Ghana, Egypt, Ethiopia, Morocco, Rwanda, Senegal, Togo and Tunisia. All twenty G20 countries participate, as do some other countries which have, or had, observer status at the G20. The African Development Bank Group (AfDB), the International Monetary Fund (IMF), and the World Bank Group (WBG) coordinate the initiative.

The CWA is governed through the G20 Africa Advisory Group (AAG), co-chaired by Germany and South Africa. The UN Economic Commission on Africa, the African Center for Economic Transformation (ACET) and the OECD also participate in the CWA. G20 Development Finance Institutions (DFIs) are encouraged to maximize their investment impact in CWA countries through closer cooperation in project implementation to reap synergies and enhance peer-learning.

A "compact team" coordinates in-country activities, including updating policy matrices, coordination among development partners, and dialogue with respective governments. The compact teams consist of the Compact government, representatives from the three coordinating IOs and bilateral partners.

The Think 20 (T20) African Standing Committee advocates in particular for Africa, and under that umbrella has a working group on CWA.

Progress in Implementing the Compact with Africa

Overall, progress in implementing the CWA has been satisfactory, with sustained support from the international community, active engagement of African participants and increasing outreach to the investment community. The results of two progress monitoring reports by the AAG in April and October 2018 are summarized below.

Policy

In April 2018 the AAG assessed progress on commitments under the three Frameworks.[4] There were 101 commitments identified in the nine participating countries. Twenty three percent of commitments were reported as wholly achieved, and 74 percent of commitments were reported as on track. It was determined that Japan and Norway had supported the most private investments in Compact countries.

There was a focus on maintaining macroeconomic stability, with 43 percent of the reforms monitored relating to the Macroeconomic Framework, and 33 percent of these wholly achieved. Commitments under the Macroeconomic Framework clustered around three recurring themes: (i) achievement of macroeconomic stability and debt sustainability; (ii) increased domestic revenue mobilization; and, (iii) more effective public investment management.

The Business Frameworks accounted for 37 percent of the 101 commitments, with only 22 percent of these being wholly achieved during the period. Issues addressed included investor protections, strengthening of commercial courts, and standardization of contracts among the aspects addressed.

The Financing Frameworks accounted for 21 percent of the 101 commitments, with only 5 percent of these reported as wholly achieved. Only a few of the Compact countries—Côte d'Ivoire, Ghana, Morocco, and Rwanda—included commitments to develop domestic bond markets or alternative markets for small and medium enterprise

[4] G20 African Advisory Group (2018), "G20 Compact with Africa – Compact Monitoring Report."

listings.

A consistent commitment to reform can be seen in the progress Compact countries are making in closing the Distance to Frontier, a key measure of the annual Doing Business report. While these reforms are necessary, they are not in themselves sufficient to create an investor-friendly business environment. Additionally, there was significant misalignment between some of the areas being supported by AAG members and priority reforms as captured in the matrices. There is significant scope for Compact countries, together with private sector stakeholders and key development partners, to reassess where the most critical reforms are needed.

Investment

In October 2018 the AAG assessed private sector activity in Compact countries.[5] The monitoring report signaled that sound policies to improve investment conditions are paying off and investment interest in Compact countries is growing. At the same time, it underscored the long-term nature of this initiative, as it requires time to build up a track record that strengthens investor confidence. As the data covers the five-year period between 2013-2017, there are indications that the Compact countries were already implementing reforms before the start of the Compact that helped to attract investment.

CWA countries have demonstrated resilience as a destination for foreign direct investment (FDI) in the region against the backdrop of declining FDI inflows into Africa. Total FDI inflows to CWA countries amounted to $20 billion in 2017. The total annual volume of inbound FDI to all CWA countries increased by 36 percent over the past five

---

[5] G20 African Advisory Group (2018), “Trends in FDI and Cross-Border Investments in Compact with Africa Countries.”

years, from $14.9 billion in 2013 to $20.2 billion in 2017. During the same period, investment flows to CWA countries increased as a share of total inbound FDI to Africa, rising from 29 to 48 percent of total FDI to the region, representing a combined $92 billion in reported FDI for the five-year period. The capturing of a larger "market share" of inbound FDI by CWA countries may indicate stronger investor confidence in this group relative to other destinations in the region.

There were important variations at the country level, which is particularly significant in resource-rich countries. Since 2013, several CWA countries increased significantly the proportion of FDI inflows as a percentage of GDP. Egypt more than doubled from 1.45 percent in 2013 to 3.14 percent in 2017. Ethiopia increased from 2.82 to 4.45 percent, Senegal from 2.10 to 3.25 percent, and Côte d'Ivoire from 1.30 to 1.67 percent. Likewise, during 2017, Egypt ($7.4 billion), Ethiopia ($3.6 billion), Ghana ($3.3 billion) and Morocco ($2.7 billion) received 84 percent of total FDI flowing to CWA countries, a reflection of both their market size and level of trade integration.

G20 countries and the IOs have organized or supported more than 30 investment events that included CWA countries. On October 30, 2018 Chancellor Merkel hosted eleven African leaders and industry CEOs for the G20 Investment Summit - German Business and the CWA Countries. This was followed by the Africa Investment Forum (AIF), organized by the AfDB, which took place on November 7-9, 2018 in South Africa with CWA as an event partner. The AIF featured a "G20 Compact with Africa" panel with a high level policy dialogue between G20 members and other donors, updates from Compact country ministers on policy reforms, and discussion of two flagship investments in Compact countries. Encouragingly, $18.5 billion in investment interest was secured for specific projects in Compact countries.

Additional Tools and Support

The CWA initiative has supported the development of numerous tools including the MDB Toolbox "Instruments Available to Support Private Sector Investment in Compact with Africa Countries", and the "Global Infrastructure Outlook: Infrastructure Investment Need in the Compact with Africa Countries."

The ***IFC Support for G20 Compact with Africa Initiative (ISCA)*** [6] conducts Country Private Sector diagnostics and Sector Deep Dives on Compact countries, which will create an analytical basis to identify the constraints to private sector development and attracting finance for development. It will also address the lack of a pipeline of bankable transactions, create products to address financing bottlenecks and mobilize capital, and, work to close gender and access gaps and address climate change. IFC estimates the program will cost US$41 million. The German KfW Development Bank has contributed Euro 10 million and the Norwegian Ministry of Foreign Affairs has contributed NOK 5 million.

Germany is developing "***Reform Partnerships***" to create a more favorable environment for private investments.[7] The selected countries will receive €100 million in the framework of this program. The German government also announced a €1 billion fund to tackle unemployment in Africa, to which Compact countries will be eligible.

The Government of Germany has contributed to the ***Think Africa Trust Fund*** at the WBG to support peer to peer learning, advocacy, and peer reviews for the CWA. Through the trust fund ACET, working

[6] G20 African Advisory Group (2018), "G20 Compact with Africa – Compact Monitoring Report."

[7] G20 Investment Summit: German Development Ministry expands reform partnerships. https://germanyinafrica.diplo.de/zadz-en/-/2157236

with partners such as the IMF and the OECD, has convened or supported five ***peer learning events***. The focus of the CWA peer learning for 2019 will be blended finance and public-private partnerships. At the request of the AAG, ACET also undertakes an ***independent peer review*** of the CWA semi-annually.

The WBG has also initiated a ***multi-donor trust fund to support the government of Tunisia*** in its implementation of the CWA. The fund has received contributions from Norway, the Netherlands, and Germany, totaling approximately $5m.

G20 DFIs are encouraged to increase engagement with Compact teams' work on the ground and identify priority projects in CWA countries, in line with respective comparative advantages. The AfDB is coordinating a synthesis of ***DFI action plans*** for the AAG meeting in April 2019. The IFC will coordinate a G20 toolbox covering the instruments of G20 DFIs for promoting private investment.

CWA Looking Ahead

While the CWA has been successful to date, assessments have indicated areas for further strengthening. The AAG has been active in championing quick action to address these areas.

On Macroeconomic Frameworks, Compact countries are steering an appropriate course and should remain focused on increasing domestic revenues, including pursuing reforms leading to adoption of broad-based consumption taxes, simplified tax design and improved tax administration.

On the Business Framework, countries should identify and prioritize the reforms most critical in the specific country context. Three key areas were identified:

- Promote diversification: targeting improvements in transport and energy infrastructure; simplifying regulations and administrative procedures for starting a business; increasing efficiency of the legal system; reducing regulatory uncertainty.

- Boost agricultural productivity: improving land titling; increasing access to credit for investment in new farming techniques; improving awareness in new farming techniques; improving infrastructure needed to connect farms to markets.

- Strengthen governance: working with state-owned enterprises to reduce the extent to which corruption and lack of competition continue to crowd out private investment.

Regarding Financial Frameworks, the AAG encourages development partners to commit to structured and comprehensive financial sector deepening in Compact countries. They should also commit to identify and work with institutional investors to establish a public infrastructure investment facility for Compact countries.

Proposal

T20 Policy Recommendations: Greater African Engagement

The CWA working group of the T20 Africa Standing Group makes five recommendations, based on recent assessments.

1. ***Enhance Country Teams***: Compact teams in each country should be consolidated. Closer alignment between Compact teams and other stakeholders, including existing private sector working groups, can help to foster greater engagement with the private sector. CWA countries would benefit from expanded experience

sharing Compact team experiences through case studies and peer-to-peer learning. Likewise, capturing good practice and successes and sharing these with investors will reduce risk perceptions. Compact governments should take advantage of the country teams to discuss investment needs and seek financing solutions from development partners.

2. ***Promote private sector investment***: Identify the key challenges and bottlenecks to greater private sector investment. A systematic assessment of the role of G20 international trade and investment policies for investment in CWA countries should be undertaken. G20 and bilateral partners should develop private sector involvement strategies to encourage companies in their countries to sustainably increase private investment in Compact countries. Additional monitoring of individual G20 country investments, as well as exploiting the linkages between FDI and investment promotion strategies in CWA countries, should be undertaken.

3. ***Increase Domestic Private Sector Dialogue***: CWA will benefit from greater domestic private sector dialogue in each of the Compact countries, which can provide lessons learned to scale investments. Typically foreign investors will rely on domestic partners, hence such dialogues should include SMEs and build upon recent CWA Investor Forums.

4. ***Use the AIF Project Platform***: Investment opportunities for private sector investment in Compact countries should be listed on the AIF project platform. The platform will reduce intermediation costs, improve the quality of project information and documentation, and increase active and productive engagements between project sponsors and investors.

5. ***Develop African Expertise for Infrastructure Development***: Through the CWA, G20 can support efforts to develop African

infrastructure experts. This will provide credible, pre-vetted, African technicians who can support G20 investors and infrastructure companies and ensure that any risk assessment incorporates a full appreciation of the political economy, culture, and ethnic challenges where the project is based.

References

- G20 African Advisory Group (2018), "G20 Compact with Africa – Compact Monitoring Report".
- G20 African Advisory Group (2018), "Trends in FDI and Cross-Border Investments in Compact with Africa Countries".
- G20 Investment Summit: German Development Ministry expands reform partnerships, https://germanyinafrica.diplo.de/zadz-en/-/2157236

COOPERATION WITH AFRICA

Industrial Development and ICT in Africa: Opportunities, Challenges and Way Forward

Gamal Ibrahim (United Nations Economic Commission for Africa)
Witness Simbanegavi (African Economic Research Consortium)
Anita Prakash (Economic Research Institute for ASEAN and East Asia)
William Davis (United Nations Economic Commission for Africa)
Wilson Wasike (African Economic Research Consortium)
Ashraf Patel (Institute for Global Dialogue)

March 29, 2019

Abstract

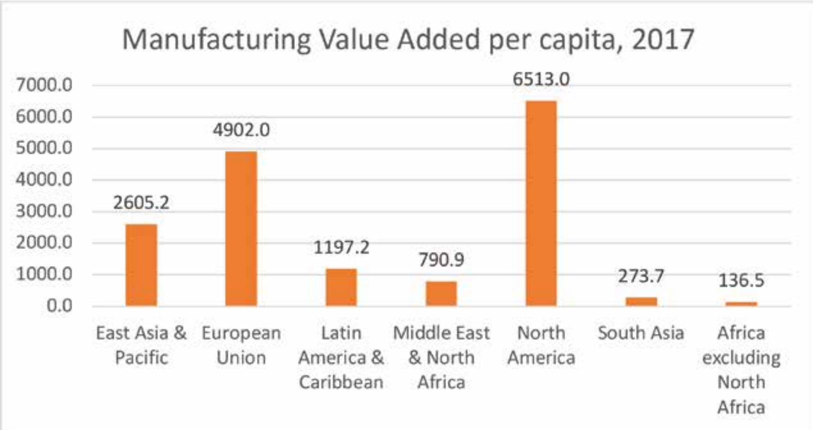
This policy brief explores how African countries can leverage digitalization and ICTs to further their goal of industrialization. With increasing digitization of global manufacturing, there is a risk that opportunities for African countries to industrialize will erode. The world economy is already undergoing a trend where historically labor-intensive production is being "reshored" to "smart" factories in developed and emerging economies. This policy brief explores strategies for enhancing African economies' manufacturing capabilities, especially in the traditional labor-intensive sectors through leveraging Information and Communication Technologies (ICTs).

Challenge

Industrialization is pivotal to Africa's long-term development and broadening and deepening the manufacturing sector will build more resilient economies. Africa is endowed with vast resources – in agriculture, mining, and maritime resources, as well as a youthful labor force, which if properly harnessed, can stimulate a resource-based industrialization strategy (ECA and African Union, 2013). Historically, industrial development has been key to sustained, inclusive and job-rich development due to the high productivity growth, labor intensity, productivity spillovers and forward and backward linkages that the industrial sector has with the rest of the economy (ECA, 2015; Signé and Johnson, 2018).

Notwithstanding these virtues of industrialization, the story of Africa is one of de-industrialization overall, with the share of manufacturing in GDP hovering around 10% for most countries while falling in some (Banga and te Velde, 2018). It appears African countries have, until now, failed to capitalize on the opportunities to industrialize, especially in light of the rising labor costs in advanced countries, and in many emerging Asian economies, in particular, China. The contrast with East Asia, which is often cited as a development model for Africa, could not be starker. Manufacturing value added in East Asia and developing Asia is much higher than in Africa (Figure 1).

Figure 1 Manufacturing Value Added in various world regions



Note: Data for Middle East & North Africa and North America are of 2016. The rest are data of 2017.

Source: World Development Indicators, World Bank, 2019

Given its labor abundance, Africa needs to diversify into the export of low value manufactures and services and integrate into global value chains.[1] This however requires enhanced productivity in the relevant sectors. The challenge for industrialization in Africa is how to leverage digitalization and information technologies to drive competitiveness of African manufacturing, and industrial development more generally.

[1] By 2034, Africa's working-age population is expected to be 1.1 billion, larger than that of either China or India (McKinsey Global Institute, 2016).

Digitalization of the economy is often viewed as being associated with the large-scale introduction of labor-saving technologies, requiring appropriate skills development for the labor-force (and general citizenry) across the region, in order to take advantage of digitalization. This, however, cannot be the focus for Africa, especially given the youth employment challenge in the region. There is need to leverage ICT technologies to support growth of productive sectors, especially those industrial sectors with high labor-intensity and strong backward and forward linkages. In addition to African manufacturers directly benefiting from the use of digital technologies, African governments can also use such technologies in public administration to enhance service delivery to (directly or indirectly) support the continent's industrialization.

Cutting-edge digital technologies such as automation are increasingly eroding the comparative advantage of low labor cost regions, including Africa. This thus requires African countries to embrace these technologies to enhance their competitiveness in producing manufactures. Indeed, erosion is already happening to some extent with the rise of 're-shoring' in advanced economies as it becomes cheaper for such economies to produce manufactures domestically with the adoption of labor-saving technologies (Banga and te Velde, 2018). For now, African countries still have the opportunity to grow their market share in the global market for manufactured goods, as automation and re-shoring have not yet affected some sub-sectors of manufacturing. That notwithstanding, there is need for African countries to adopt digitization and ICTs in manufacturing processes in order to reap the efficiency and productivity gains that come with these technologies, allowing African producers to at least keep pace with global developments, and thus maintain their competitive edge against reshoring. Indeed, ICT innovations, such as M-Pesa in Kenya, could easily be adapted to support industrialization efforts in the continent. This is important as services are increasingly becoming a key and integral component of manufacturing (Hoekman, 2018). In the longer term, the high level of concentration and barriers to entry in the global market for digital services is likely to increase the cost of these to African and other manufacturers.[2]

Opportunities

There are opportunities available to African countries to develop their industrial sectors. These include: active industrial policies on manufacturing;[3] investment in infrastructure and human capital;[4] and digitization and ICTs. While these are all essential, we focus below on "digitization and ICTs".

Digitization and ICTs

Beyond efforts to help African manufacturers to better access digital inputs, African Governments can also use digital technologies to enhance public administration's support for industrialization.

---

[2] Even though they may only remain competitive in manufacturing (and sustain a greater market share in exports of manufactured goods) for a limited time, it is still worthwhile for African countries to seize this opportunity to industrialize. This is because the positive effects of manufacturing on productivity in sectors beyond the manufacturing sector itself, as well as the positive effects on health and education of those employed in the manufacturing sector, will be felt even after manufacturing jobs have departed (Ibid; Banerjee and Duflo, 2011). Many advanced economies have de-industrialized as income levels have risen, but have not seen a reversal in their productivity or living standards that were developed during their industrial phases.

[3] Using a mix of investments, subsidies, taxes and regulations to encourage the development of priority industrial sub-sectors. Common elements for successful industrial policy are: the existence of industrial policy organizations with the authority to coordinate policy across multiple Government departments; policy that is founded on consultations with the private sector; and blending 'horizontal' policies that apply to the whole economy with sector-specific policies (ECA and African Union, 2014 and ECA, 2016).

[4] Africa's infrastructure deficit is estimated to account for 30% to 60% of productivity losses of firms and 40% to 80% of this is due to the energy sector in half the countries. Preliminary and partial AfDB estimates suggest that Africa's annual infrastructure investment needs amount to at least US$100 billion. Consequently, Africa requires investment in both soft and hard infrastructure, focusing on energy production, transport and ICTs, and skills development (see Global Competitiveness Report (2018).

Digitization can help enhance the efficiency and productivity of services associated with manufacturing, including customs administration, general logistics, etc, thereby enhancing industrial development. In particular, digitization of customs administration can help improve customs efficiency, reduce trade costs and thus promote greater intra-African trade (particularly in the context of the African Continental Free Trade Area (AfCFTA)), which, in turn, would support greater industrial development on the continent. There are a number of digital innovations in customs administration and related trade barriers that can reduce trade costs, including costs of customs clearance and trade document preparation (United Nations, 2017). One such innovation is electronic single windows, which have proven to be a cost-effective intervention to reduce trade costs in Africa (see e.g. African Alliance for Electronic Commerce, 2013).

The benefits of ICTs and e-commerce, however, do not materialize automatically or smoothly – the returns to e-commerce differ significantly across different economies and industries, depending on their ability to adapt to the digital economy. Further, the 4th industrial revolution could yield greater inequality, particularly in its potential to disrupt labor markets. As automation substitutes for labor across the entire economy, the net displacement of workers by machines might exacerbate the gap between returns to capital and returns to labor. On the other hand, it is also possible that the displacement of workers by technology will, in aggregate, result in a net increase in safe jobs. Regardless of which of the two scenarios is likely to emerge, major disruptions to labor markets in terms of the growth in wholly new occupations require new ways of organizing and coordinating work, new skills requirements in all jobs and new tools to augment workers' capabilities" (World Economic Forum, 2016) .

We cannot foresee at this point which scenario is likely to emerge, and history suggests that the outcome is likely to be some combination of the two. It is in this milieu that carefully planned industrial and HRD skills policy should be crafted and calibrated to ensure a just transition into the 4th industrial economy.

At the regional level and particularly in the AfCFTA context, reductions in trade costs are forecast to have substantial positive impacts on intra-African trade, and thus welfare across the continent (Mevel and Karingi, 2013; Depetris-Chauvin and others, 2016; Valensisi, Lisinge and Karingi, 2016). Given the high share of manufactures in intra-African trade, reductions in trade costs resulting from digitization should promote industrialization in Africa.[5] In addition, providing African manufacturers an opportunity to export within the African market could provide a springboard to global markets. In particular, integration into regional value chains tends to support greater integration into global value chains (and potentially capture higher value-added activities, which tend to provide better employment prospects and have greater effects on output – see ECA, 2015) than trade integration with the rest of the world. This is because international value chains are mostly regional (International Trade Centre, 2017). Further, African markets tend to be less standards-intensive than non-African export markets meaning that African manufacturers are more likely to be able to export to such markets, providing opportunities for learning and thus quality and productivity enhancements (see for instance, Bigsten and others, cited from Collier, 2007). Therefore, technology enabled intra-African trade can help raise productivity of African firms, positioning them to compete globally.

Using digitization to reduce non-tariff barriers to trade (NTBs) should boost intra-African trade in manufactures. Full implementation of the AfCFTA is itself expected to have significant positive impacts on the continent's industrialization (ECA, African Union and African

[5] In 2017, manufactured goods accounted for around 45 per cent of intra-African trade, compared to around 20 per cent of Africa's trade with the rest of the world (authors' calculations based on UNCTAD, 2019).

Development Bank, 2017). Yet currently, implementation of paperless trade measures (trade facilitation using digital technology) in Africa remains very limited (United Nations, 2017). This suggests further measures are needed in this regard. Intra-African e-commerce strategies can also help to boost intra-African trade, especially since e-commerce is relatively under-developed in Africa (see UNCTAD B2C e-commerce index 2017).

Proposal

We ask African and G20 leaders to take urgent and decisive action to harness digital technologies to support Africa's industrialization.

A. *African countries should adopt active industrial policies and urgently use a range of industrial policy tools to support African manufacturers' access to digital services to strengthen their businesses, with financial and technical support from G20 countries.*

In order for digitization and other ICTs to augment manufacturing competitiveness in Africa, African countries need to pursue a range of different active industrial policies to strengthen manufacturing sectors. Such policies include developing and building ICT backbone infrastructure, including fiber and submarine cables; developing appropriate technical skills, achieving better financing for digitalization (through attracting private investment in the sector[6] and supplementing

[6] For example, upgrading workers' skills is an important way in which this can be accomplished – see e.g. ECA (2013).

this through the use of public funds where appropriate[7]), taxes and incentives, boosting firm capabilities, the development of national innovation systems and related ICT infrastructure, and facilitating integration (both backward and forward)[8] of digital service providers into global value chains (Banga and te Velde, 2018). G20 countries can provide financial and technical support to Africa to institute these policy reforms and to implement the relevant programs.

B. *Africa and G20 countries should establish a framework for ensuring that the transformative impact of technology is directed towards the SDGs*

In the current global economy, characterized by a huge digital divide and dominance of multinational companies (MNCs) in global value chains, appropriate and strategic industrial policies by African countries are needed to reap the benefits of digital economy for structural transformation and to ensure that the transformative impact of technology is directed towards the SDGs. The framework should emphasize the impact of digitalization on industrial development that integrate a rethinking of governments on the education system, labor markets and governance dimension of the digital economy. One of the other key policy questions confronting African policy makers is the extent to which investments made in education and vocational training are preparing citizens for the digital economy, and how governments and other stakeholders can assist citizens to manage the transition. The challenge is compounded by the failure to generate

[7] In particular, Government support could usefully be provided to start-ups, which often struggle to attract finance in Africa, in both manufacturing and digital services. It could also usefully be provided to technological/innovation hubs. However, in order to maximise their contribution to economic transformation, efforts to finance start-ups should focus on those with high growth and economic transformation potential.

[8] Backward integration may help to improve competitiveness through access to efficient inputs, while forward integration may help to boost productivity as providers gain feedback from demanding customers in expert markets.

sufficient formal sector jobs for the young which is fueled by scarcity of fiscal resources, with many African countries experiencing high levels of debts, limiting their capacity to borrow. The framework should include building data and cloud computing infrastructure, enhancing digital skills as well as financial and technical co-operation, technology transfer and flexible approaches to intellectual property that balance incentives for innovation with the public interest of broader access to technology.

Also, the digitalization strategy for manufacturing sectors should address the governance challenges; these include supporting the adoption of legal frameworks in Africa providing for both ownership of data and sharing it at the regional level[9] , supporting the upgrading of regional digital infrastructure and developing anti-trust policies to address the challenges posed by large global tech firms. Finally, African countries should also regulate the cross-border supply of digital services and prioritize liberalization of intra-African trade in digital services through AfCFTA negotiations.

C. Continuous improvement of processes in manufacturing, management and supporting business practices, with financial and technical support from G20 countries.

Africa's trade and investment relationships with G20 economies can be leveraged to enhance quality of products and to raise productivity and thus global competitiveness of African manufacturers. African firms and producers can potentially benefit, in terms of productivity and managerial process improvements, from FDI spill-overs and from adopting and, where necessary, adapting managerial approaches – such as KAIZEN – that have been perfected elsewhere. The efficacy of

[9] This should allow development of customized products and services based on such data as well as the benefits of economies of scale from supplying such products/services at regional level.

these initiatives has been proven in many African economies, *especially in selected sectors such as autos, leather and textiles. In addition, IT use may also address the deficiencies in various managerial skills. Another challenge in Africa is the lack of opportunities for the disadvantaged groups* (low income families, women entrepreneurs etc.) who do not have adequate formal training. The "embedded" knowledge in technologies, such as the use of mobile payments which helps in preparing the proper bookkeeping without the formal knowledge of accounting, can be very helpful to disadvantaged groups and small and micro enterprises.

D. G20 countries should provide financial and technical support for African countries to use advanced technologies to improve their customs and tax administrations, intra-African trade by implementing paperless trade reforms and facilitating intra-African e-commerce.

Tax administrations in Africa can leverage new technologies to mobilize additional resources by allowing automatic electronic exchange of invoices used at import and export to ensure that they have not been re-invoiced (a common practice – see ECA, 2018; Hakelberg, 2018; Monkam and others, 2018). In addition, broader digitalization of tax and customs administration can allow data to be more easily analyzed by automated risk models to identify cases that carry a high risk of tax evasion or unlawful tax avoidance. This can also help countries to more easily analyze patterns in accounting and firms' transactions, helping them to identify which *legal* tax avoidance techniques are most commonly used, so that they may close the associated loopholes. African countries should try to access country-by-country MNC reports by requiring that the corporations operating in their territories file their country-by-country reports locally.

The WTO Trade Facilitation Agreement offers an opportunity for African member countries to mobilize financial and technical support for trade facilitation measures such as paperless trade reforms and the digitalization of customs administration. This is because the

Agreement provides for countries to designate trade facilitation (including digital trade facilitation) measures that they will only implement upon receipt of financial and technical support from rich (G20) countries. Yet so far, only 19 out of 47 African countries that are members have notified the measures for which they will require technical and financial support. As such, African countries may need to be more proactive in notifying such measures (WTO, 2019a and 2019b). G20 countries should also work with African countries that are not WTO members to support the implementation of similar reforms. Furthermore, G20 countries should provide financial and technical support to the remainder of the AfCFTA negotiations and ratification. However, due to concerns among some African countries around conflicts of interest for technical support provided so far to the negotiations, G20 countries may do well to provide such support through institutions that African countries know and trust, for instance, the African Development Bank, UNECA, etc.

To boost intra-African e-commerce, the following tools could be considered: e-commerce readiness assessment and strategy formulation; ICT infrastructure and services; trade logistics and trade facilitation; payment solutions; legal and regulatory frameworks; knowledge and skills development; and access to financing for digital entrepreneurs. At the same time, it is important to consider changes in tax policy to ensure that e-commerce does not undermine tax collection that is used for the domestic spending on industrial policies needed to achieve industrialization.

References

- African Alliance for Electronic Commerce. 2013. Guidelines for Single Window Implementation in Africa. Dakar: African Alliance for Electronic Commerce.

- Banga and Te Velde (2018). DIGITALISATION AND THE FUTURE OF MANUFACTURING IN AFRICA. Available from https://set.odi.org/wp-content/uploads/2018/03/SET_Digitalisation-and-future-of-African-manufacturing_Final.pdf. Accessed 14 and 15 January 2019.
- COLLIER, P. (2007). The bottom billion: why the poorest countries are failing and what can be done about it. Oxford, Oxford University Press.
- Conde, Carlos, Philipp Heinrigs and Anthony O'Sullivan. (2015). "Tapping the Potential of Global Value Chains for Africa." The African Competitiveness Report 2015. OECD. Paris.
- Depetris-Chauvin, Nicolas, M. Priscilla Ramos and Guido Porto (2016). "Trade, growth, and welfare impacts of the CFTA in Africa". Available from https://editorialexpress.com/cgibin/conference/download.cgi?db_name=CSAE2017&paper_id=749.
- ECA and African Union (2013). Making the Most of Africa's Commodities: Industrializing for Growth, Jobs and Economic Transformation Economic Report on Africa 2013. ECA: Addis Ababa.
- ECA (2013). Building trade capacities for Africa's transformation: A critical review of aid for trade. ECA: Addis Ababa.
- ECA and African Union (2014). Dynamic Industrial Policy in Africa: Innovative Institutions, Effective Processes and Flexible Mechanisms Economic Report on Africa 2014. ECA: Addis Ababa.
- ECA (2015). Economic Report on Africa 2015: Industrializing through Trade. ECA: Addis Ababa.
- ECA (2016). Transformative Industrial Policy for Africa. ECA: Addis Ababa.
- ECA (2017). EXPANDING AND STRENGTHENING local entrepreneurship for structural transformation in Africa. ECA: Addis Ababa.

- ECA (2018). Base Erosion and Profit Shifting in Africa: Reforms to facilitate improved taxation of multinational enterprises. ECA: Addis Ababa.
- ECA, African Union and African Development Bank (2017). Assessing Regional Integration in Africa VIII: BRINGING THE CONTINENTAL FREE TRADE AREA ABOUT. ECA: Addis Ababa.
- The Global Competitiveness Report 2017–2018.
- Hakelberg, Lukas (2018). Their hands untied but still imprisoned? National tax policy under the automatic exchange of information. Presentation made at the conference Paradise Lost? Inequality and Tax Justice held in Lima, 13 to 14 June 2018.
- International Trade Centre. (2017). "Promoting SME Competitiveness in Africa. International Trade Centre: Geneva.
- Mayer, J (2018) Digitalization and industrialization: friends or foes? UNCTAD Research Paper No. 25 UNCTAD/SER.RP/2018/7.
- Mckinsey Global Institute. (2016). Lions on the Move II: Realizing the Potential of Africa's Economies.
- Mevel, S. and Karingi, S. (2013). TOWARDS A CONTINENTAL FREE TRADE AREA IN AFRICA: A CGE MODELLING ASSESSMENT WITH A FOCUS ON AGRICULTURE. In Cheong, D., Jansen, M. and Peters, R (eds.). Shared Harvests: Agriculture, Trade, and Employment. International Labour Office and United Nations Conference on Trade and Development.
- Monkam, Nara, Ibrahim, Gamal, Davis, William and von Haldenwang, Christian (2018). Tax Transparency and Exchange of Information (EOI): Priorities for Africa. Available from https://t20argentina.org/wp-content/uploads/2018/07/TF5-5.2-Taxation.pdf. Accessed 15 January 2019.
- Signé, L. and Johnson C. (2018). "The Potential of Manufacturing and Industrialization in Africa." The Brookings Institution.

New York.

- United Nations (2017). Trade Facilitation and Paperless Trade Implementation Global Report 2017. Available from https://www.unescap.org/sites/default/files/Global%20Report%20Final_26%20Oct%202017.pdf. Accessed 14 January 2019.
- United Nations Conference on Trade and Development (2019). Merchandise: Intra-trade and extra-trade of country groups by product, annual. Available from http://unctadstat.unctad.org/wds/TableViewer/tableView.aspx. Accessed 15 January 2019.
- United Nations Economic Commission for Europe. Not dated. Retrieved from http://www.unece.org/fileadmin/DAM/cefact/single_window/draft_160905.pdf.
- Valensisi, G., Lisinge, R. and Karingi, S. (2016). The trade facilitation agreement and Africa's regional integration. Canadian Journal of Development Studies / Revue canadienne d'études du développement, 37:2, 239-259, DOI: 10.1080/02255189.2016.1131672
- WTO (2019a). Members and Observers. Available from https://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm. Accessed 15 January 2019.
- WTO (2019b). Notifications list. Available from https://www.tfadatabase.org/notifications/list?notificationtype=c. Accessed 15 January 2019.

COOPERATION WITH AFRICA

Linking Smallholder Production with Value-Added Food Markets

Dr. Belay Begashaw (SDG Center for Africa)
Gert-Jan Verburg (SDG Center for Africa)
Futoshi Yamauchi (International Food Policy Research Institute)
Daniele Fattibene (Istituto Affari Internazionali)
Fujita Yasuo (Japan International Cooperation Agency)

March 29, 2019

Abstract

Demographic pressures and climate change in Africa are rendering subsistence farming an unviable livelihood strategy for smallholder farmers. However, urbanization and economic growth are creating new markets for fresh and processed foods in the region. To enter this market, African smallholders need to adopt new production strategies that will increase income and make farming more appealing to the next generation. The G20 can encourage this transition by supporting the growth of a rural-based food processing sector, the reorientation of smallholder agriculture to commercialization, and the development of infrastructure to link farmers to markets.

Challenge

Agriculture is a mainstay of the African economy. Although officially, agricultural production directly accounts for about only 15 percent of GDP in the region (FAO Statistics Division, 2019), this figure understates the importance of agriculture in most countries. As shown in the figure below, countries with high GDP tend to have a lower share of agriculture in their economies. Thus, agriculture is more important in countries with higher poverty rates. Continentally, agriculture is a major source of employment for 70% of the population, and accounts for more than half of total employment (OECD/FAO, 2016). Agriculture is also an important part of regional trade, accounting for 10% of regional exports, although this share has been decreasing in recent decades (Badiane, Odjo, and Collins, 2018).

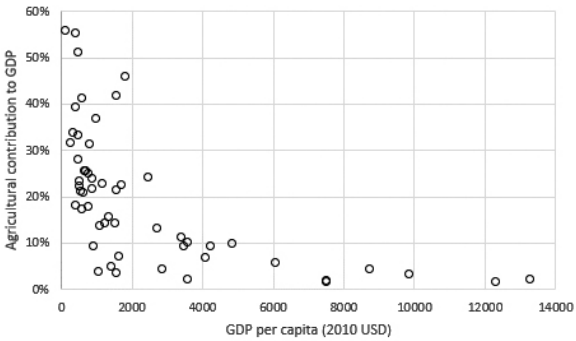


Figure 1: Agricultural GDP in African countries at different levels of income in 2016. Calculated by author using FAOSTAT data

Despite agriculture's eminence in exports, the regional trade balance of agricultural goods has been negative since 2001. Although agricultural exports have grown at annual rates of 8% in the period of 1998 - 2013, aided by high commodity prices, growth in imports has outpaced exports and increased fivefold in the same period. This is driven by several important megatrends, including high population growth, rapid urbanization, economic growth and changes in diets (Badiane, Odjo, and Collins, p. 4). In urban centers and among middle classes, food consumption has shifted away from staple crops and toward processed and fresh foods, which are increasingly sourced through markets (Tschirley, Reardon, Dolislager, and Snyder, 2015). Unlike in Asia, these megatrends have not been accompanied by substantial investments in infrastructure or the provision of credit for farm technology for domestic agricultural production, in order to fulfill domestic food demand (Reardon, 2015).

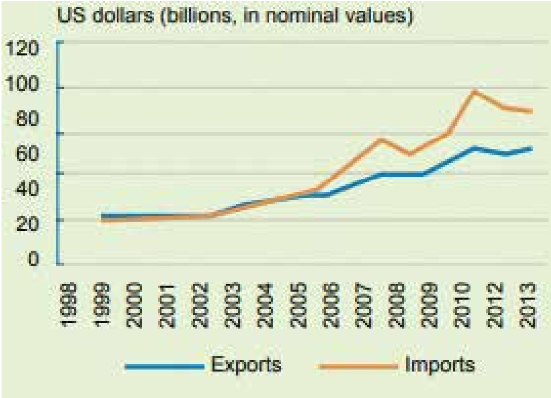


Figure 2: Total agricultural trade flows, 1998-2013 (Badiane, Odjo, and Collins, p. 5.)

On the supply side, African agriculture largely remains characterized by a subsistence-level regime with low levels of inputs, output, and investment. Mixed smallholder farming is the predominant model, constituting 80% of farms and employing 175 million people directly (Alliance for a Green Revolution in Africa, 2014). Smallholder farms are typically smaller than 2 hectares, and only sell surplus production in markets, with the majority of the produce consumed within the household. Production growth has been relatively stagnant, and has not kept pace with the growing demand for food in urban centers and by middle classes. As a result, Africa has become a net importer of food, despite having 60% of the world's unused arable land (Mulangu, 2015).

Thus, the challenge today is to link rural smallholder farmers to growing markets as a means of improving rural livelihoods and to make farming appealing to the next generation of young entrepreneurs. There is a growing gulf between domestic food production and largely-urban food demand, which is threatening to exclude vast portions of the continent's population from burgeoning economic growth, prolonging the prevalence of poverty of farming households, and contributing to the exodus of young people to growing cities in search of economic opportunities. According to the FAO, already 90% of citizens living in suburbs are food insecure and these trends are likely to continue in the next decades due to the urbanization trends in particular in small and medium-sized cities.

Proposal

Overcoming the challenges of rural poverty and vulnerability requires transforming smallholder farms from subsistence operations into profitable, commercial-oriented businesses, as well as strengthening their links to growing food markets. The change in food consumption patterns taking place in cities and among growing middle classes presents a major opportunity to add value to domestic production. Moreover, a favorable global food balance means that African farmers can orient their production to align with resource endowments and export opportunities, and are not limited to producing food solely to fulfill domestic food requirements (Alliance for a Green Revolution in Africa, 2017). The objective of agricultural policy in agrarian African countries should be to make domestic agriculture more competitive, both domestically and globally, with the rest of the world, especially in terms of quality.

Agroprocessing

The lack of a robust agroprocessing sector has been identified as an important "missing link" in connecting smallholder producers to high-value markets, both in the context of international trade as well as within country borders (Halvorson, 2017). Currently, in most African countries the food and beverage subsector accounts for 30-50% of the manufacturing industry, and is growing in response to increased domestic demand for processed and fresh foods. Despite this growth, the sector is not generating growth in employment, despite it being more labour-intensive than most other manufacturing sectors (FAO, 2017). This is owing to the fact that most food processors are small-scale, family-based enterprises that are not competitive in processed food markets, while large-scale agroprocessing enterprises are not based in rural areas, are capital-intensive and do not contribute substantially to employment. Thus, policy and interventions are needed to upgrade rural food processing enterprises so that they can be more competitive in food markets while retaining their capacity for rural employment.

In order for this sector to benefit smallholder farmers and have maximal effect on poverty alleviation, it is best for small-scale processing centers to be established close to the productive areas, providing easy access for farmers to market their production as well as being an important source of off-farm employment. Small and medium-sized enterprises (SMEs) located in rural areas have the most potential to generate employment and accrue benefits to low-income families who have limited employment opportunities. While the private sector should bear primary responsibility for the development of these enterprises, they are not likely to emerge through market forces alone. There is significant scope for intervention, by governments and other partners, to facilitate this transformation. These interventions should prioritize SMEs over large agroprocessors, since SMEs have greater potential to become an important source of off-farm employment to rural inhabitants.

The emergence and success of these enterprises is not inevitable. Many entrepreneurs in the agroprocessing industry do not have the business skills or the capital required to establish their own SMEs, and need support to become established in value-added food markets. With the expertise and experience amassed in the food processing industry of some of its members, the G20 can support the integration of the Africa's agricultural production into global and domestic agro-food value chains by actively promoting the rural-based private food processing sector. Partnerships with successful food processing companies from some G20 members can facilitate this process. Lastly, the G20 can encourage partnerships between African agroprocessors and buyers in the G20 to develop regulatory institutions that ensure the safety and quality of food without being a prohibitive barrier to entry for SMEs. Such support can allow small food processing enterprises to attain experience and establish more robust links both upstream and downstream, allowing them to eventually scale up their operations as farm productivity increases among farmers and the demand for value-added products continues to grow.

As part of the G20's commitment to developing "integrated, inclusive and equitable development" (G20, 2018) of the global food system, it should promote policies and practices that provide opportunities to smallholder farmers, rural families, women and young people in the agroprocessing industry. The G20 can support the inclusion of smallholder farmers in the following areas:

- Working within the framework of the Comprehensive Africa Agriculture Development Programme (CAADP), the G20 can collaborate with African countries to incorporate programs to improve the prospects of agroprocessing SMEs into National Agricultural Investment Plans (NAIPs), including:

    - Disseminating knowledge, promoting technology transfers, and teaching business skills that will allow rural-based food processors to upgrade processes to attain ISO-compliant phytosanitary, technical, and logistical standards, and enabling these SMEs to compete in both domestic and international value-added food markets

    - Setting up funding arrangements to allow capital-constrained rural agroprocessors to invest in processing facilities, machinery, transportation, and appropriate storage facilities

- G20 member nations must look closely at their own trade practices, especially subsidies and non-tariff barriers that are inconsistent with WTO regulations, and re-evaluate them in light of stated intentions to promote smallholder farmers' participation in global value chains. Anticompetitive practices ultimately undermine G20 members' standing in international trade negotiations. It is in the G20's interest for member nations to observe the rules that they themselves have set without input from any African nations other than South Africa.

Smallholder Productivity

Ultimately, the productivity of agriculture is the most important factor to harnessing the potential of the non-farm economy in rural areas, because one of the major constraints to the growth of the agroprocessing sector is an unreliable supply of raw materials. It is therefore necessary to support farmers in these areas directly to enable them take advantage of new market opportunities, especially to produce high-quality inputs for the agroprocessing sector. To integrate smallholder farmers into value-added food markets, numerous recent experiences from market-oriented agriculture interventions for small-scale farmers all over the region are tremendously useful. In principle, such projects aim to transform farmers' orientation from a "produce *and* then sell" strategy to "producing strategically *to* sell". In this process, farmers are expected to become entrepreneurs instead of subsisters.

To be successful actors in globalized food value chains, smallholders need to make decisions directly in response to market opportunities and uncertainties with respect to the climate. Although prices are generally set outside of smallholders' control and they are therefore price-takers with respect to both input and product markets, farmers can become more strategic actors who mitigate risks and take advantage of market opportunities that appear. Farmers with more accurate and direct information about markets are more involved in marketing, both with middlemen as well as market wholesalers, in response to market demands. The mitigation of information asymmetries improves allocative efficiency in crop production, since farmers that are better informed on price variations and movements are enabled to optimize crop choice, planting timing, and crop marketing. Extension workers are well-positioned to support decisions made by farmers (e.g., crop choice) and improve productivity, rather than forcing farmers to plant crops recommended by the government. Extension workers can also facilitate the dissemination or real-time market information that can help farmers make informed production decisions. Alongside skill trainings, the provision of a package of market information relevant to farmers' production is a critical role in the smallholder transformation that extension agents could fulfill.

Examples abound of smallholder market interventions led by state and non-state actors among smallholder farmers in Africa. One example is the Smallholder Horticulture Empowerment and Promotion (SHEP) project, which has been supported by the Japan International Cooperation Agency (JICA). The SHEP model explicitly links farmers and markets to mitigate imperfect information on market prices, chronically faced by farmers. In this program, smallholder farmers are trained to think strategically and to take actions to increase their income from their horticultural produce, and farmers are intrinsically incentivized to decide on best responses to more complete market information. Like this program, the G-20 can play a key role through concerted efforts in supporting smallholders in the continent to access accurate market information and improve their ability to manage and decide on farming practices.

In summary, the G20 can support African smallholder producers by:

- Supporting business development programs like SHEP, in the continent's horticulture, cereal crop, and livestock sectors.

- Cooperating with African countries to extend the Agricultural Market Information System (AMIS), and engaging in capacity building, with an emphasis on supporting food market transparency and the dissemination of market information, especially to farmers at the very end of GVCs.

- Promoting better climate change adaptive management, including indexed rainfall insurance schemes, water harvesting, drought-resistant crop varieties.

Infrastructure

In addition to the development of agroprocesssing and smallholder farming, investments must continue to be made in strategic infrastructure to connect farming regions to markets. The improvement of roads is necessary to reduce the burden of transport costs within the value chain. Market infrastructure has been significantly improved with the integration of ICTs to facilitate the negotiation of prices between producers and dealers, and such practices should be promoted further. In addition, agroprocessors need stable power supplies in order to run milling machines and other equipment, thus the continued extension of power networks and the upgrading of power supply is imperative.

Since the cost of establishing infrastructure for food processing is prohibitive in some instances, especially in low-income settings, one strategy that has been developed to reduce the user costs of infrastructure is the development of agroprocessing industrial parks. This strategy is currently in development in Ethiopia, and is being scaled up to service 17 regions throughout the country. By developing agro-industrial clusters, enterprises can share the costs of electricity, transportation, water and sewage, workforce training, cold storage, communications and logistics, and other elements. In Ethiopia, these clusters are also served by Rural Transformation Centers, which source agricultural raw materials from farmers as inputs to the agroprocessing sector in the catchment areas of the agro-industrial parks[1]. These industrial parks are typically designed to produce at scale, thus making their value-added products more competitive and able to compete in world markets.

To develop market infrastructure in Africa, the G20 can:

- Promote last-mile electrification, telecommunications, and roadway projects as part of CAADP initiatives and other areas of collaboration between the G20 and African countries

- Consider the prospects of agroprocessing industrial parks clusters to reduce costs of storage, sanitation, logistics, and other elements, and integrating them into agricultural development strategies where prospects are favourable.

Conclusion

None of the policies described beforehand will be sufficient to integrate smallholder farmers to burgeoning food markets in isolation. Simply increasing productivity and developing agroprocessing domestically does not guarantee that it will benefit smallholder farmers. In order for this proposed agricultural transformation to be inclusive and conducive to growth, all of the aforementioned policy measures must to be implemented concurrently, which the G20 can support in varying capacities. A coordinated strategy is necessary to address all the issues simultaneously. Strategies in the manufacturing sector need to align

[1] https://isid.unido.org/files/Ethiopia/Integrated-Agro-Industrial-Parks-in-Ethiopia-booklet.pdf

with strategies in agriculture, and appropriate infrastructure needs to be established to link these sectors. If executed appropriately, this strategy could provide an effective means of reducing rural poverty, and promoting economic growth.

References

- Alliance for a Green Revolution in Africa (2014), Africa Agriculture Status Report 2014 (Nairobi, Kenya: Alliance for a Green Revolution in Africa, September 2014) <https://reliefweb.int/sites/reliefweb.int/files/resources/agra-africa-agriculture-status-report-2014.pdf> [accessed 17 January 2019].
- Alliance for a Green Revolution in Africa (2017), Africa Agriculture Status Report 2017 (Nairobi, Kenya, 2017), p. 8 <https://agra.org/aasr2017/> [accessed 15 January 2019].
- Badiane, O., Odjo, S., and Collins, J. (2018), Africa Agriculture Trade Monitor 2018 (Washington, DC: International Food Policy Research Institute, 2018) <https://doi.org/10.2499/9780896293496>.
- FAO (2017), Leveraging Food Systems for Inclusive Rural Transformation, ed. by FAO, The State of Food and Agriculture, 2017 (Rome: Food and Agriculture Organization of the United Nations, 2017).
- FAO Statistics Division (2019), 'FAOSTAT', FAOSTAT, 2019 <http://www.fao.org/faostat/en/#home> [accessed 15 January 2019].
- G20 (2018), 'G20 Agriculture Ministers Declaration 2018' <http://www.g20.utoronto.ca/2018/2018-07-28-agriculture.html> [accessed 11 February 2019].
- Mulangu, F. (2015), 'Agroprocessing in Africa: The Low-Hanging Fruits', Africa Up Close, 2015 <https://africaupclose.wilsoncenter.org/agroprocessing-in-africa-the-low-hanging-

fruits/> [accessed 17 January 2019].

- OECD/FAO (2016), OECD-FAO Agricultural Outlook 2016-2025 (Paris: OECD Publishing, 4 July 2016), p. 136 (p. 65) <http://dx.doi.org/10.1787/agr_outlook-2016-en> [accessed 15 January 2019].
- Halvorson, K. (2017), 'Food Processing as the Missing Link in Africa's Value Chains', Business Fights Poverty, 2017 <https://businessfightspoverty.org/articles/food-processing-as-the-missing-link-in-africas-value-chains/> [accessed 24 January 2019].
- Reardon, T. (2015), 'The Hidden Middle: The Quiet Revolution in the Midstream of Agrifood Value Chains in Developing Countries', Oxford Review of Economic Policy, 31.1 (2015), 45–63 (p. 50) <https://doi.org/10.1093/oxrep/grv011>.
- Tschirley, D., Reardon, T., Dolislager, M., and Snyder, J. (2015), 'The Rise of a Middle Class in East and Southern Africa: Implications for Food System Transformation', Journal of International Development, 27.5 (2015), 628–46 (p. 644) <https://doi.org/10.1002/jid.3107>.

COOPERATION WITH AFRICA

Sustainable Prevention of Food Crises in Sub-Saharan Africa

Ousmane Badiane (International Food Policy Research Institute)
Julia Collins (International Food Policy Research Institute)
Yasuo Fujita (Japan International Cooperation Agency)
David Laborde (International Food Policy Research Institute)
Will Martin (International Food Policy Research Institute)
Maximo Torero (Food and Agriculture Organization)
Rob Vos (International Food Policy Research Institute)
Futoshi Yamauchi (International Food Policy Research Institute)

March 29, 2019

Abstract

Food crises and distress migration will continue to plague the African continent in the decades ahead unless massive investments are made to make the region's agriculture and food systems more resilient. The G20 should support and invigorate region-wide efforts to: (a) massively expand irrigation systems for smallholder farms to boost agricultural productivity and enhance resilience against the impacts of climate change, (b) achieve a "big push" in infrastructure, technology and finance to develop robust agri-food systems, and (c) enact concerted reforms of agricultural price and trade policies to strengthen trade integration, diversify domestic food supplies, and enhance country-level capacity to adjust to food shortages.

Challenge

Although the incidence of extreme poverty in Sub-Saharan Africa has fallen from 54% in 1990 to 41% in 2013, the absolute number of poor people has increased from 278 million to 413 million due to high population growth. At going trends, over 80 percent of the world's poor will be living in Africa by 2050 (Thurlow, et al., 2019). Africa also lags behind other regions in non-income dimensions of welfare. After having declined in recent decades, food insecurity has increased again in recent years with the prevalence of undernourishment increasing from 20.7% to 23.2% between 2014 and 2017 and the number of hungry people in the region rising to 256 million (FAO, et al., 2018). Much of the recent rise is on account of impacts of climate change and bursts of conflict causing protracted food crises in several parts of the continent. While the prevalence of stunted children has declined, the absolute number of affected children has increased. Stunting reduces productivity of the future labor force and income per capita. The adverse impact of stunting on per capita incomes in Africa is estimated to be around 9% (Galasso and Wagstaff, 2017).

Any poverty reduction and food and nutrition strategy in Sub-Saharan Africa needs a strong focus on agriculture. Agriculture productivity growth is crucial for poverty reduction in Africa. Nearly 60 percent of the labor force overall and 78 percent of the working poor rely on agriculture for their livelihoods. There is thus enormous potential for accelerating poverty reduction if agricultural productivity is boosted. In recent years, much of agricultural growth in Africa has been due to land expansion, rather than productivity growth. African countries typically grossly underfund high-return investments, especially in research and development, as well as in mechanization, irrigation, other basic infrastructure and extension services. Only 5% of the region's agricultural land is irrigated. Access to finance for these high-return investments also poses a challenge. Fragmented markets prevent producers from benefitting from intra-country and regional trade and significant changes in policies to promote regional trade, not only by reducing tariff barriers but also by focusing on non-tariff barriers, are essential. While African countries have increased rice imports from Asia at relatively low cost in recent years, prices are expected to rise because of increases in the cost of rice production in Asia (Otsuka et al., 2016). Finally, climate change threatens agriculture and increases food insecurity. Rapidly degrading soil and water points to a challenging production future, especially in a context of climate change. All these factors conspire against food security and income opportunities for Africa's poor, but in addition they can fuel feelings of dispossession and, hence, conflict and forced migration.

The fact that growing demand for food exceeds supply capacity offers major opportunities for Africa's poor and its farm population to break away from poverty and recurrent food crises. Policies need to be targeted to address vulnerability and enhance resilience of rural livelihoods, while substantially reducing the levels of stunting and malnutrition of the region.

Proposal

In 2018, G20 Agricultural Ministers reconfirmed their commitment to end hunger and all forms of malnutrition, emphasizing that the development of sustainable food systems will also contribute to tackling other challenges like the forced displacement of people. They also recognized that: “A sustainable, integrated and inclusive future for food systems requires our concerted efforts and can only be achieved on the basis of collaboration among governments, international organizations, farmers’ community, civil society, the various stakeholders in the food supply chain and the educational and research communities.”[1]

Such a concerted approach will be essential to fight hunger and sustainably prevent the recurrence of food crises in Sub-Saharan Africa. This Brief proposes that the G20 can promote agriculture and food security and nutrition by stepping up internationally concerted efforts in three priority areas of actions:

- Stepping up investments in irrigation
- Improving incentives and infrastructure for agro-food businesses
- Realigning agricultural trade and incentives policies

Targeted interventions to extend the productive season in chronically vulnerable regions, especially in arid areas of Africa

With between 200 and 600 mm of rainfall concentrated in a few weeks

[1] Declaration of G20 Agricultural Ministers, July 27-28, Buenos Aires (available at: http://www.g20.utoronto.ca/2018/2018-07-28-agriculture.html).

per year in Africa's (semi-)arid zones, massive investments in sustainable small-scale irrigation coupled with value chain development interventions will be required to improve yields and extend the productive season, while creating opportunities for crop and income diversification and providing year-round productive employment for smallholder communities. More diversified production patterns would also make it possible to grow more nutritious fruits and vegetables for income and better diets. The G-20 could promote an initiative to make more investment finance available for these purposes, e.g. through the multilateral development banks.

Dependence on rainfed agriculture limits the period during which African farmers can be productive, presenting a severe constraint to increasing productivity enough to reduce poverty. Semi-arid regions, such as the Sahel, not only experience low annual rainfall, but rain tends to concentrate in short periods of the year. This allows, at best, for a very short productive season. It does not allow farm households to support a year-round living. More broadly, drought forms a key risk factor for food crises. Interventions to increase yields during the limited growing season are not enough.[2]

Studies by the World Bank (You, 2008) and by IFPRI (Xie, et al., 2014) highlight the enormous potential to increase irrigation in Sub-Saharan Africa and that much of this potential is in the form of much more economical small-scale schemes, rather than large dam-based schemes. Even small schemes based on groundwater are likely to require development of policies for water allocation to avoid costly and conflictive races to the bottom.

---

[2] For example, the most productive farmers growing groundnuts, a major export crop, in Senegal's groundnut basin show yields of around 1 ton per hectare. With prices around US$0.40 per kg and average holdings of one hectare, even tripling yields would increase farm incomes only to $1,200 per year—not enough to lift a family of five from poverty.

Expanding irrigation would extend the growing season in some of the poorest and most vulnerable regions in Africa and greatly raise farms' productive potential. The ability to work more than three months of the year will increase labor productivity with the potential of considerably reducing poverty rates. The stable availability of irrigation water will permit farmers to integrate arboriculture and livestock for year-round income and to diversify into higher-value and more nutritious crops such as fruits and vegetables, resulting in greater resilience and better household nutrition. However, the effects of extended growing seasons reach beyond the farm and help accelerate transformation of the rural economy. The availability of surplus production will enable more rapid growth in the agro-processing sector, and increased incomes for farm households will spur demand for a wider range of products and services, stimulating the rural economy and creating opportunities for off-farm activities.

Although expanding irrigation has costs, the scale of the benefits is much larger. An IFPRI study finds that small-scale irrigation technologies—motor pumps, treadle pumps, communal river diversions, and small reservoirs—are highly cost-effective in semi-arid zones and have large potential for expansion (Xie, et al., 2014). The potential for expanding irrigated areas ranges from 1 to 3 million hectares for the Sahel region and from 20 to 30 million hectares for Sub-Saharan Africa as a whole. Depending on the technology, irrigation expansion would benefit between 113 million and 369 million rural people and produce net revenues of between US$14 billion and US$22 billion per year in Sub-Saharan Africa, just for the Sahel region, between 7 million and 30 million rural people would benefit from a potential total net additional farm revenue of between US$0.3 billion and US$1.2 billion per year.

The G-20 could play a leading role in encouraging and supporting an initiative that would massively scale up irrigation to expand the productive season and – as spelled out below – facilitate at the same time increases in complementary investments in extension services, improved farm management practices, and value chain development.

In this regard, the G20 and the African Union, with the support of multilateral financial institutions, could set up a partnership for technical and financial cooperation to facilitate sufficient investment finance is made available to support the irrigation and complementary investment plan, as well as to coordinate of the further actions and call for policy coherence, as proposed in the remainder of this Brief. Accordingly, the Comprehensive Africa Agriculture Development Programme (CAADP) national investment plans would be strengthened and scaled up. The joint financing facility could further leverage other sources of long-term agricultural investment finance and multi-year allocations of international development assistance.

Investment finance and technical support to facilitate enterprise growth, efficiency gains and food quality improvements in the growing food processing and distribution sector

To reap the benefits of agricultural productivity growth from irrigation investments, complementary investment is needed. Sub-Saharan Africa so far has not taken advantage of green revolution technologies, in part because of lack of investments in irrigation and extension systems.[3] First, therefore, it will require improved farm management practices for successful and sustainable intensification, through investments in the capacity of extension systems to promote improved cultivation practices, high-yielding modern varieties and chemical fertilizers. Second, access to credits for smallholder farmers need to be enhanced to facilitate investments in irrigation systems and farm equipment.

[3] See e.g. Otsuka (2019) for the case of rice production in Africa

Third, supply chain development will be needed for farmers to bring increased production to market. This will require investments to improve market infrastructure and other interventions to better connect smallholders to other value chain actors, for instance, through support to develop and strengthen producer organizations and incentives to (private sector) investments in temperature-controlled storage and transportation and food processing capacity.

Extending the production season and enabling surplus production will fuel the emerging transformation in Africa's food systems, with a growing number of small firms producing processed versions of local staples. This growth is in response to rapidly increasing demand for processed, perishable, and higher-value foods resulting from income growth and urbanization. Research predicts continuing strong growth in overall food demand, particularly for high-value foods. For example, in Eastern and Southern Africa, the share of processed foods in all purchased food is projected to increase from an already-high 70 percent to 79 percent between 2010 and 2040 (Tschirley, et al., 2015). Although some processed food products are imported, traditional staples are also increasingly being consumed in more convenient processed forms, produced by small domestic firms. However, the thousands of one- to five-person domestic firms behind this transformation tend to have low productivity, and face barriers to growth including high costs, limited skills and human resources, low access to land, energy and finance, and lack of reliable access to quality raw materials (Hollinger and Staatz. 2015). As a result of these barriers, small firms are operating at a fraction of their potential. In addition, concerns about food safety and quality are dampening demand for local processed food products (Hollinger and Staatz, 2015). Poor connectivity resulting from inadequacies in transport and communications infrastructure as well as insufficient cold- and dry-chain development are hampering agricultural productivity growth to translate into higher farm incomes and are sources of high rates of food losses (Delgado, et al., 2018).

The G-20 can play a key role in addressing these food security related challenges by fostering international collaboration and strengthening the financial sector policy framework to increase access to finance. Specifically, it could promote concerted efforts to mobilize resources to: (a) significantly expand investment in transportation, market access and distribution networks including cold-chain and dry-chain development to reduce high transactions costs, as well as food losses at various stages of the food value chains; (b) improve integration of local and regional market networks and lower barriers to finance and facilitate access to technology for innovation to allow the nascent local agribusiness sector to continue to expand and secure a larger share of the growing urban food demand, and, in this sense, the G-20 could support the rapid development of the FINTECH agenda in the region by fostering international collaboration and strengthening national financial sector policy frameworks; and (c) facilitate opportunities for skills training (technical, entrepreneurial), especially for youth, to help accelerate innovation and upgrading of food value chains and promote job creation for Africa's rapidly growing young population, so as to structurally improve rural livelihoods and reduce distress migration.

Realigning agricultural incentive and trade policies

Institutional trade barriers constitute substantial constraints for many food producers, as well as exporters and importers. These barriers to trade flows are harmful to food security in Africa and impede the development of competitive agricultural value chains and agribusinesses.

Many countries in Africa continue to implicitly "tax" agriculture by setting prices substantially below world prices. While this is politically attractive in holding down food prices in urban areas, it frequently reduces the incomes of poor farmers who rely on net sales of food to meet their income needs for school fees and other purchases. Many countries in Africa focus strongly on ensuring that demand for food staples is met solely from domestic supplies or from trade managed by government entities. This policy emphasis on food self-sufficiency can become a source of domestic price instability, for instance, when a drought reduces food supply which then cannot be offset through an increase in imports. A recent study of Zambia's maize policy showed that a precautionary export ban introduced in response to expected reductions in domestic supply caused by the El Niño phenomenon in 2016 in effect increased food insecurity as the trade restriction caused a loss of real income of net sellers of maize, mostly poor farmers (Al Mamun, et al., 2018). Other studies have equally shown that the poor integration of regional markets is leaving Africa's populations more vulnerable to climate shocks as the capacity to adjust through trade to short-term food shortages is limited and domestic food supplies are concentrated in few key staples (Gouel and Laborde, 2018).

Reforms of domestic policies by limiting such restrictions on food trade would help to reduce Africa's vulnerability to output shocks from its largely rain-fed agriculture. To be effective such reforms should be internationally and regionally coordinated. The G20 could support this. The proposed Continental Free Trade Area in Africa could further help countries diversify food supplies, not only by requiring a degree of opening of their markets, but by raising confidence that other countries would make food supplies available when needed.

Improvements in transport infrastructure are also potentially a very important way to increase diversification of food supplies. This challenge may seem impossible to achieve in a reasonable time frame. However, recent World Bank research (Kunaka and Carruthers, 2014) suggests that opening up key transport corridors—many of which are currently being developed—would bring most of the potential gains from a more comprehensive network and would, of course, be particularly beneficial for landlocked countries. Even given these corridors, however, much more development of secondary rural roads will be needed to ensure that the most vulnerable households gain the enormous benefits associated with access to the transport network.

References

- Al Mamun, A., A. Chapoto, B. Chisanga, S. D'Alessandro, J. Koo, W. Martin, and P. Samboko. 2018. Assessment of the Impacts of El Niño and Grain Trade Policy Responses in East and Southern Africa to the 2015–16 Event. Washington D.C.: IFPRI and World Bank.
- Delgado, L., M. Schuster, and M. Torero. 2018. The reality of food losses: A new measurement methodology. IFPRI Discussion Paper No 1686. Washington D.C.: International Food Policy Research Institute.
- FAO, IFAD, UNICEF, WFP and WHO. 2018. The State of Food Security and Nutrition in the World 2018. Rome: FAO.
- Galasso, E., and A. Wagstaff, with S. Naudeau and M. Shekar. 2017. "The Economic Costs of Stunting and How to Reduce Them." World Bank Policy Research Note, PRN/17/05.
- Gouel, C. and D. Laborde. 2018. The Crucial Role of International Trade in Adaptation to Climate Change, Washington D.C.: IFPRI (mimeo).
- G20, 2018, Declaration of G20 Agricultural Ministers, Buenos Aires
- Hollinger, F., and J. Staatz. 2015. Agricultural Growth in West Africa: Market and Policy Drivers. Rome: FAO, African Development Bank, ECOWAS.
- Kunaka, C., and R. Carruthers, 2014, Trade and Transport Corridor Management Toolkit, World Bank.
- Otsuka, K. 2019. Evidence-based Strategy for a Rice Green Revolution in Sub-Saharan Africa, Policy Note, JICA Research

Institute.

- Otsuka, K., Y. Liu, and F. Yamauchi. 2016. Growing advantage of large farms in Asia and its implication for global food security. Global Food Security 11: 5-10.
- Thurlow, J., P. Dorosh and B. Davis. 2019. “Demographic Change, Agriculture and Rural Poverty”. In: Clayton Campanhola and Shivaji Pandey (eds.). Sustainable Food and Agriculture: An Integrated Approach. London: Elsevier/ Academic Press, pp. 31-54.
- Tschirley, D., T. Reardon, M. Dolislager, and J. Snyder. 2015. “The Rise of a Middle Class in East and Southern Africa: Implications for Food System Transformation.” Journal of International Development (27)5: 628–646.
- Xie, H., L. You, B. Wielgosz, and C. Ringler. 2014. “Estimating the Potential for Expanding Smallholder Irrigation in Sub-Saharan Africa.” Agricultural Water Management 131: 183–193.
- You, L., 2008, Africa Infrastructure Country Diagnostic: Irrigation Investment Needs in Sub-Saharan Africa, Background Paper 9, World Bank

COOPERATION WITH AFRICA

Tax Challenges of Digitalization in Africa

Nara Monkam (African Tax Administration Forum, ATAF)
Gamal Ibrahim (United Nations Economic Commission for Africa, UNECA)
William Davis (United Nations Economic Commission for Africa, UNECA)
Christian von Haldenwang (German Development Institute, DIE)

March 29, 2019

Abstract

The G20/OECD project on tackling base erosion and profit shifting provided broad recommendations but did not address in detail the tax challenges of the digitalized economy, deciding to return to the issue at a later date (Action 11) (OECD, 2017). Discussions are currently ongoing as to what form international co-operation on the tax challenges of the digitalized economy should take. However, currently, Africa faces challenges in effectively participating in international discussions in this area. As such, this policy brief discusses the role of African countries and the G20 in ensuring that international approaches to taxing the digitalized economy are undertaken in consultation with Africa and reflect Africa's interests. In addressing the tax challenges of digitalization in Africa two important principles of international tax cooperation emphasized by the Addis Ababa Action Agenda (AAAA, arts. 28, 29) must be respected: to be universal by fully taking "into account the different needs and capacities of all countries" and be inclusive (UN FfD, 2015).

Challenge

In the context of the G20/OECD BEPS project, the Inclusive Framework for BEPS Implementation (IF) was created with the objectives to level the playing field for all committed (interested) and relevant jurisdictions and ensure that they are involved on an equal footing in the setting of the future standards relating to BEPS issues, the implementation and monitoring of the BEPS outcomes, including tailoring implementation solutions for BEPS outcomes that are appropriate for all capacity levels. Currently, as of February 2019, 128 jurisdictions (including 22 African countries) have joined the IF (OECD, 2019).

There are a few African representatives in OECD Working Parties on international tax matters, who may not represent the full diversity of African countries and views. Moreover, even for those African countries that can participate, the participation at the OECD's Committee on Fiscal Affairs (CFA) and working parties has challenges and will continue to challenge African countries' resources and capacities to the limit. The current level of participation is not sustainable over the longer term. In addition, the fact that African countries that are members of the IF need to implement the BEPS Minimum Standards (which is a challenge for many of them) is a further obstacle to their participation, as observed in international tax discussions (Salm and Ibrahim, 2018). This is especially the case since the peer review process that is part of IF membership contains a large number of technical elements, which will put further capacity constraints on African tax administrations. Meeting the minimum standards will also require changes to domestic legislation and to tax treaties. Considerable advocacy work will be needed to obtain political support for these changes.

The above is compounded by the fact that G20 members have taken or are threatening to take punitive measures against African countries that fail to implement international tax standards such as the BEPS Minimum Standards and standards of the Global Forum (OECD, 2018). This could amount to penalizing countries for processes that are meant to be voluntary in the quest for tax transparency. Aside from the direct negative effects of such punitive measures, they would also undercut African countries' ability to influence global discussions on tax issues, as the threat of sanctions may force them to implement standards in which they have no say.

In addition, as African economies become more digitalized, countries are increasingly concerned about the ensuing tax challenges. Digitalization enables multinational enterprises (MNEs) to carry out business in African countries with no or very limited physical presence in those countries. This impedes the establishment of taxing rights over the profits made by an MNE from the business activities it carried out in a specific African country; thus, rendering the *nexus rule* inefficient in protecting Africa' s tax bases.[1] It is important here to note that these business models go beyond social media platforms, search engines and online market places. In fact, digitalization affects the economy, especially the value chains of a wide range of businesses.

These new business models stemming from the digitalization of the economy raise questions as to whether fundamental changes are needed to the two key underlying principles of the international tax rules: the *nexus rules* mentioned above and the *profit allocation rules.*[2] In particular, digitalization raises the question of how taxing rights on income generated from cross border transactions should be allocated between jurisdictions. The allocation of taxing rights between residence and source jurisdictions has been an issue of considerable concern for African countries for many years. African countries are generally source countries and tax on a source basis.[3] African countries often report that they consider the current nexus and profits allocation rules are weighted too heavily in favor of the residence jurisdiction to the detriment of the source (African) jurisdiction.

Such business models with these associated challenges are becoming more and more prevalent in Africa and this is largely explained, among others, by the following factors:

- The continent is a huge consumer of e-commerce and global

---

[1] The nexus rule allocates taxing rights to a country where a non-resident enterprise creates sufficient physical presence.

[2] The profit allocation rule determines how the MNE's global profits are allocated between jurisdictions, primarily using transfer pricing rules.

[3] Source taxation means that the income is taxed in the country in which it arises no matter where the recipient is tax resident.

telephony.

- There is a substantial development in ICT infrastructure and increase in internet penetration in Africa. According to the ITU statistical dataset (2017), internet penetration reached 21.8% by end of 2017 from just 6.7% in 2010 mainly due to rapidly increasingly mobile penetration. According to the ITU 2018 global and regional ICT estimates, of all regions, Africa experienced the strongest growth in the number of people using the internet, with the percentage increasing from 2.1% in 2005 to 24.4% in 2018 (ITU, 2018).

Youthful demographic profile also leads to the growing use of the internet, social media platforms, cloud computing and other technological advances.

Proposal

We ask G20 and African leaders to take urgent and decisive action to ensure that taxation of the digitalized economy works for Africa, through actions at the national, sub-regional, pan-African and global levels.

A. G20 countries should support a global and inclusive discussion of a new approach to taxation of the digitalized economy that considers Africa's perspectives and priorities, alongside those of other developing countries

1. Though African countries can participate in discussions on tax issues as part of the IF, there are significant challenges for

African countries to implement the requirements of the IF membership as noted earlier in the present policy brief. Therefore, G20 countries need to change their approach to who can participate in global tax discussions and on what terms to fully include African countries. This should mean either supporting a greater role for the United Nations in global tax discussions or relaxing the requirements for IF membership so that it is easier for African countries to be members and fully participate.

2. In addition, the following guiding principles reflecting the concerns of African countries must underpin any amendments to the international tax rules currently being debated:

- The current nexus and profit allocation rules are not ensuring appropriate taxing rights for source countries, particularly African countries. They are inappropriately skewed in favor of residence jurisdictions. This is encouraging illicit financial flows (IFFs) out of Africa through artificial profit shifting to low tax jurisdictions and the loss of taxes African countries need for development.

- The current profit allocation rules do not properly reflect the value created for the MNE by the brand perception in the minds of the customers in the market jurisdiction. In addition, other unique and valuable contributions to the profits of the MNE are not reflected in the profits allocated to the market jurisdiction, resulting often in a significant under-allocation of profits for tax purposes to the market jurisdiction.

- The drive for more effective administration would require, on the one hand, the significant reduction of the complexity of the current nexus and profit allocation rules which hinder their effective implementation by tax administrations and impairs tax certainty for African governments and businesses. On the other hand, it would need to consider simpler collection mechanisms including the use of withholding taxes which ATAF members report is a very effective taxation mechanism in Africa.

- Further work should be undertaken to address artificial profit shifting. That work should focus primarily on addressing base eroding payments that reduce the taxing rights of the source country. Such rules again need to be simpler to ensure effective implementation is possible by all tax administrations.

B. G20 countries should seek not to penalize African countries for failing to implement international tax standards that they do not have the capacity to implement

African countries should not be punished for failing to implement tax standards that the continent mostly does not have the capacity to implement and had no say in developing (except for South Africa). In particular, the G20's intention to take defensive measures against jurisdictions failing to implement tax transparency measures should exempt African countries. Instead of penalizing African countries, the G20, as outlined in proposal A above, should focus on supporting them to implement such standards and give all African countries an opportunity to debate international approaches to tax policy on an equal footing, without the strings that are currently attached to membership of the Inclusive Framework.

C. African leaders should support the development of a common African position on the tax challenges of digitalization

Africa is in a unique position to seize the opportunities presented by the tax challenges of digitalization to take a proactive role in the international tax cooperation where it would contribute to steering the direction of the global standard agenda rather than providing inputs in a pre-determined agenda; thereby seizing the opportunity for more inclusiveness in international tax governance.

To that end, a multipronged strategy can be explored.

1. Extensive regional consultations in Africa would have to take place, where digitalization, its extent, challenges (including tax) and impacts are discussed in relation to countries' specificities and level of economic development and where solutions are designed and publicized that are suitable to the African context.

2. The outcomes of these regional consultations could then be debated at the level of the Network of Tax Organizations (NTO)[4] where the various proposed solutions can be unpacked and refined. In this instance, the NTO would represent a key link between national interests and international considerations. This can be done in parallel with bringing together technical committees, task forces and working groups at ATAF, NTO, UN Committee of Experts on International Cooperation in Tax Matters, and OECD levels to shape together the global standards agenda.

[4] The Network of Tax Organizations (NTO) came into effect at the CIAT General Assembly, 15-17 May 2018, in Ottawa, Canada, with the signing of a Memorandum of Understanding (MoU) by the eight tax organizations Secretariats for enhanced cooperation and coordination: 1) the African Tax Administration Forum (ATAF), 2) the Association of Tax Authorities of Islamic Countries (ATAIC), 3) the Commonwealth Association of Tax Administrators (CATA), 4) the Inter-American Centre of Tax Administrations (CIAT), 5) the Caribbean Organization of Tax Administrators (COTA), 6) the Centre for Exchange and Studies of Tax Administration Leaders (CREDAF), 7) the Intra-European Organization of Tax Administrations (IOTA) and 8) the West African Tax Administration Forum (WATAF).

3. Taking this work forward will require strong political support in Africa and for countries to work in a collaborative manner, sharing experiences, challenges and best practice. Such political support should be garnered at the level of the African Union through the *establishment of a political institution or platform where tax policy and tax administration issues will be discussed, standards set, and recommendations made at the highest level for implementation by governments*. Other African bodies such as the Regional Economic Communities, the United Nations Economic Commission for Africa (UNECA), the African Development Bank and regional tax organizations, such as ATAF and CREDAF, could contribute to this process by coordinating a common African position.

4. African countries should adopt measures as a priority to address the avoidance of permanent establishment by cross-border e-commerce companies, by adopting the ATAF's African Model Double Taxation Agreement (DTA).[5] It is a combination of the most appropriate provisions from both the UN and OECD Models with some variations which are not in either of these Models. The provisions included are all those which are more in favour of developing countries.

References

• Blimpo, M. P., Minges, M., Kouamé, W. A., Azomahou, T. T., Lartey, E. K., Meniago, C., . . . Zeufack, A. G. (2017). Leapfrogging:

[5] The ATAF Model DTA is the ATAF model agreement for the elimination of double taxation with respect to taxes on income and the prevention of tax avoidance and evasion.

the key to Africa's development - From constraints to investment opportunities. World Bank Group and China Development Bank. Retrieved from http://documents.worldbank.org/curated/en/121581505973379739/Leapfrogging-the-key-to-Africas-development-from-constraints-to-investment-opportunities
- Diop, M. (2017, October 11). Africa can enjoy leapfrog development. Retrieved from http://www.worldbank.org/en/news/opinion/2017/10/11/africa-can-enjoy-leapfrog-development
- G20 Argentina. (2018). G20 Leaders' declaration, Building consensus for fair and sustainable development.
- ITU. (2017). ICT Facts and Figures 2017. Retrieved from International Telecommunications Union: https://www.itu.int/en/ITU-D/Statistics/Documents/facts/ICTFactsFigures2017.pdf
- ITU. (2018, December 7). ITU releases 2018 global and regional ICT estimates. Retrieved from International Telecomunications Union (ITU): https://www.itu.int/en/mediacentre/Pages/2018-PR40.aspx
- OECD. (2017). Background Brief, Inclusive Framework on BEPS. OECD. Retrieved from http://www.oecd.org/ctp/beps/background-brief-inclusive-framework-on-beps.pdf
- OECD. (2018). OECD Secretary-General Tax Report to G20 Finance Ministers and Central Bank Governors. Buenos Aires, Argentina. Retrieved from http://www.oecd.org/g20/oecd-secretary-general-tax-report-g20-finance-ministers-july-2018.pdf
- OECD. (2019, February). Members of the Inclusive Framework on BEPS. Retrieved from Inclusive Framework on BEPS - Composition: https://www.oecd.org/ctp/beps/inclusive-framework-on-beps-composition.pdf
- UN Financing for Development (FfD). (2015). Addis Ababa Action Agenda of the Third International Conference on Financing for Development (Addis Ababa Action Agenda). (pp. 13-14). United Nations Department of Economic and Social Affairs, Financing for Development Office. Retrieved from http://www.un.org/esa/ffd/wp-content/uploads/2015/08/AAAA_Outcome.pdf