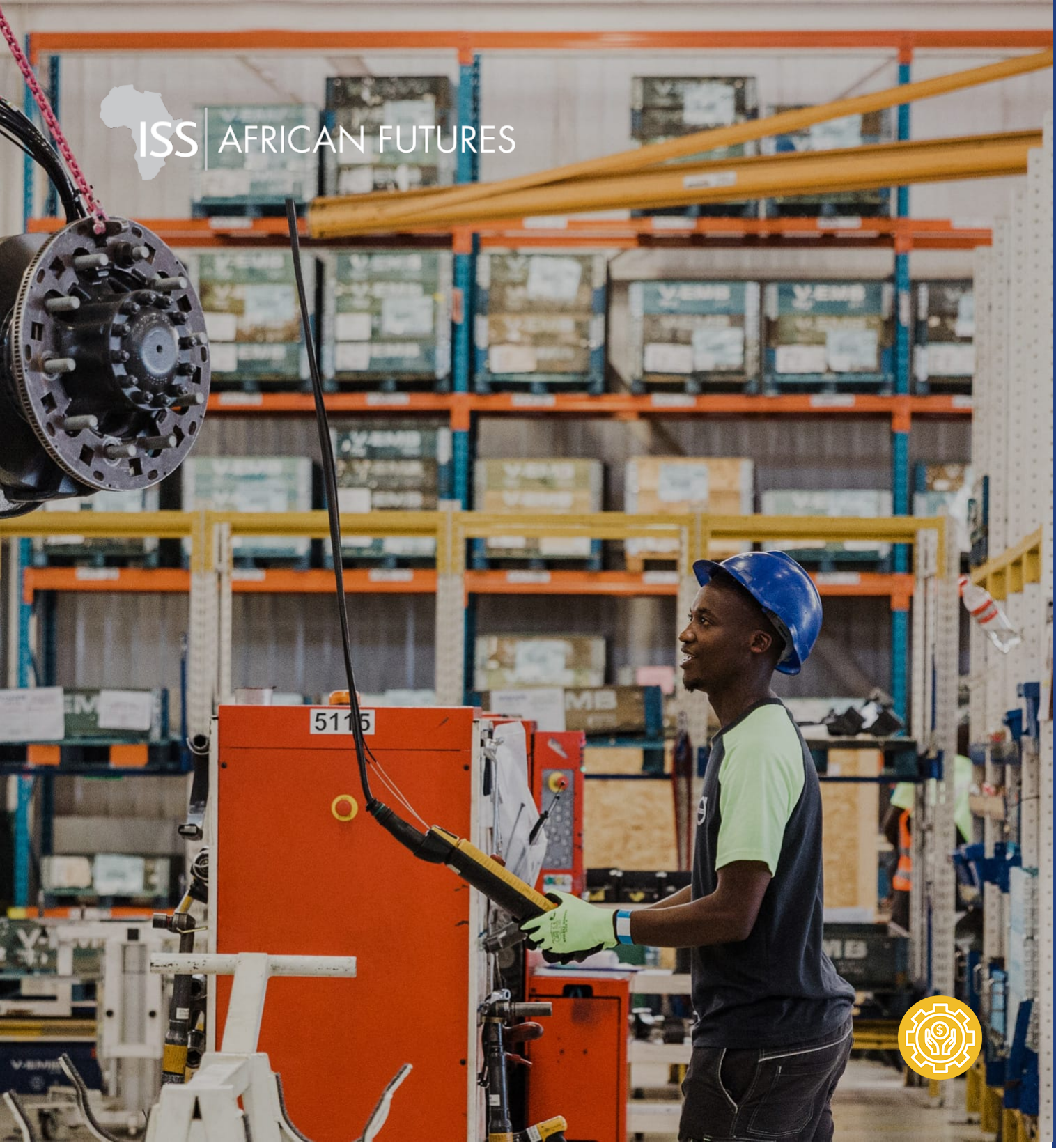

Manufacturing

What could the future hold for industrialisation in Africa?

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What could the future hold for industrialisation in Africa?

There are many things that raise hope in Africa's industrialisation:

- A recent analysis shows that FDI flows to Africa are diversifying into manufacturing and other non-mining sectors.[1]
- Also, the decline in manufacturing's share of Africa's GDP seems to have bottomed out in some African countries.
- According to the 2019 *Africa's Development Dynamics Report* [2] by the African Union and the OECD, Africa's domestic demand, anchored on a young and growing population, is now shifting towards more processed goods and is growing 1.5 times faster than the global average. The publication also shows that demand for many other products such as motor vehicles, manufactures of metals and industrial machinery is also expanding faster than the global average.
- The continent's auto industry, valued at US$30.44 billion in 2021, is expected to grow to US$42.06 billion by 2027—a nearly 40% increase in value. Across the continent, there is an average annual demand for 2.4 million motor cars and 300 000 commercial vehicles.[3] This rising domestic demand—due to the continent-wide increase in disposable income, strong growth of the middle class and rapid urbanisation—is currently being met primarily by imported used vehicles. However, domestic production has also been growing by an average of 7% annually over the past few years. Today, Morocco and South Africa are leading the way as major players in the automotive sector, making up 80% of African exports, with Algeria also experiencing rapid growth.[4]
- Africa is endowed with essential raw materials for electric vehicles and new technologies required to reach the net-zero carbon emissions. There is also a huge market for motorcycles in Africa—especially in West, East and North Africa—as well as electric two-wheelers.
- Pharmaceuticals also offer a great opportunity for Africa to enhance manufacturing given the high product complexity, which can lead to greater opportunities for high local value-added production. The pharmaceutical industry is projected to grow at about 5% annually between 2022 and 2027 in Africa.[5] Within pharmaceuticals, packaged medicines make up the largest import shares for Africa (65% of the US$17 billion pharmaceutical imports[6]) and present a big opportunity, given their high percentage of imports and the sourcing and manufacturing stages that constitute the value chain.
- China and other countries in East Asia are restructuring their economies to meet growing domestic demand, which will create space for Africa to compete with countries such as Bangladesh as the low-end manufacturing market of choice for future relocation.[7]

However, the biggest opportunity to grow domestic manufacturing is with intra-Africa trade. Manufactured products dominate intra-Africa trade, and evidence suggests that there is considerable room to grow intra-Africa manufactured exports through trade liberalisation. For instance, the German auto giant Volkswagen, already a key player on the continent, has recognised the potential of the African Continental Free Trade Area (AfCFTA) to catalyse local production of automotives and meet local demand.[8]

Close to 60% of African imports are manufactured goods, while exports are dominated by energy commodities such as oil, coal and gas. Many of the imported goods can be manufactured locally and can boost the value of regional trade. There is great potential to increase intra-Africa trade in a host of foodstuffs, beverages and cigarettes, rubber and plastics, electronics, motor cars, non-metallic mineral products and pharmaceuticals.[9] Processed and semi-processed goods constitute 61% of intra-Africa trade, and intra-Africa exports are more diversified and technologically advanced than those to other regions. [10] The full implementation of the AfCFTA will help to overcome the challenge of narrow domestic

markets and create a positive cycle of increased regional manufacturing. Small and isolated markets made it impossible for African countries to compete with Asian manufacturers.[11] The continental market will help sustain greater economies of scale.

Replacing imported manufactured goods with locally produced goods will not be easy and will start with low-value goods. This is because global value chains have higher efficiencies and reduced prices, making it difficult for new entrants to compete. Still, it remains a crucial step in transforming African economies, and the evolution of global value chains could harbour opportunities for Africa.[12]

The entry point for manufacturing traditionally involved labour-intensive segments of regional manufacturing value chains, meaning that labour costs need to be competitive. Given that Africa suffers from various disadvantages, such as poor physical infrastructure,[13] a high disease burden, poor rule of law, low regulatory and policy quality, and a lack of policy certainty, the general view is that African labour costs need to be cheap enough to compensate for these deficits.[14] However, a 2017 study on Africa's manufacturing labour costs[15] concluded that poor African countries have higher labour costs than their average income levels would suggest. The study compared 12 African countries to 17 non-African countries. Only Ethiopia compared favourably. In all other African countries reviewed, labour costs were higher than those of their non-African peers. In this regard, South Africa stands out as a middle-income country with particularly high labour costs and a very capital-intensive industrial sector—partly explaining its extraordinarily large burden of unemployment and high levels of inequality. Manufacturing labour costs in low- and low-middle-income countries such as Kenya, Tanzania and Senegal—three relatively stable coastal countries with strong business sectors—are higher than in Bangladesh, a country with a comparable World Economic Forum competitiveness rating and income levels.

However, with the advent of the Fourth Industrial Revolution, the importance of labour costs in the location of industry is declining. In addition, current trends point to manufacturing preferentially being located closer to end markets.

For these reasons, industrialisation in Africa remains possible, although its nature will differ from that in other regions. Newman and colleagues describe three considerations:[16]

First, economic changes are taking place in Asia that create a window of opportunity for late industrializers elsewhere to gain a toehold in global markets. Second, the nature of manufactured exports themselves is changing. A growing share of global trade in the industry is made up of stages of vertical value chains – or tasks – rather than finished products. Trade in tasks offers late industrializers an opportunity to enter global markets in areas suited to their factor costs and endowments of skills and capabilities. Third, trade in services and agro-industry is growing faster. These 'industries without smokestacks' broaden the range of products in which Africa can compete, and a number of them are intensive in locations specific factors abundant in Africa.

Endnotes

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