



Brief 48: Trade policies and local pharmaceutical production in east and Southern Africa

December 2022

Manufacturing is affected by a number of policies and measures. Most countries in east and southern Africa (ESA) have policies affecting manufacturing and trade in Essential Health products (EHPs). Such policies include tariffs, non-tariff barriers (prohibitions, import and export licences, regulatory measures etc), trade facilitation measures, trade in services (transport, logistics, insurance), and intellectual property rights. This brief summarises trade policy measures implemented by ESA countries that may affect manufacture of medicines, vaccines, therapeutics, diagnostics and other health technologies/ equipment, such as personal protective equipment (PPE) and ventilation equipment. It draws on findings of research on local production of essential health products in ESA. The brief recommends options ESA countries can consider on trade policy measures that support local pharmaceutical production.

Introduction

One of the key structural deficits of African economies is their lack of diversification. The United Nations Conference on Trade and Development (UNCTAD) noted this to contribute to the slow pace of industrialisation in Africa. Production and the composition of exports on the continent reflect the fact that countries still specialize in a few primary commodities, while their imports largely consist of manufactured products. This limits the potential for growth from intraregional trade (UNCTAD 2012). Developing the manufacturing sector is thus key.

Despite having industrialisation policies at country and at regional levels, the continent is less industrialised today than four decades ago, and after adoption of liberalisation under the structural adjustment programmes spearheaded by the IMF and the World Bank. The contribution of the manufacturing sector to the continent's gross domestic product (GDP) declined from 12% in 1980, to 11% in 2013, and has remained stagnant in recent years (UNECA 2020). As a cornerstone for industrialisation, a vibrant manufacturing sector boosts productivity across the various sectors of the economy due to its forward and backward linkages.

The COVID-19 pandemic spurred ESA governments to innovate and reinvigorate their pharmaceutical industries to increase local production of health products such as PPEs, sanitiser, oxygen and medicines needed to respond to the pandemic. The pandemic came at a time when technology and innovation were being embraced by young Africans (UNECA, 2020). The inauguration of the African Continental Free Trade Area (AfCFTA) in May 2019 also provided a potential boost for local production and intra-African trade.

Trade policies and local production

SEATINI research has established that local production of EHPs, including medicines and vaccines, depends on trade policies (Machemedze et al., 2022), including:

- Exemptions on import duties for raw materials for pharmaceutical and R&D;
- Harmonisation of trade and industrial policies targeted at pharmaceutical manufacturers;
- Policy coordination on industrial and pharmaceutical parks and special economic zones;
- Ratification and implementation of key trade agreements like the AfCFTA to facilitate intra-regional and continental pharmaceutical distribution.

Policies related to tariffs, prohibitions, and import and export licenses have indirect impact, as do trade facilitation measures; and policies of trade in services including for transport, logistics, and insurance. Regulatory frameworks and intellectual property rights impact on innovation and access to health technologies, as does the facilitation of technology partnerships and transfer of technology and knowledge (World Bank and WTO 2022). For countries seeking to boost local production in a relatively complex sector like that of pharmaceutical and vaccine production, an enabling environment and productive infrastructure is key. This is discussed below for selected ESA countries.

Zimbabwe's manufacturing is relatively diversified, with a range of products including pharmaceuticals. In recent decades the manufacturing sector has, however, faced foreign currency shortages and industries have not been able to access credit lines from multilateral financial institutions. This has led to the sector's decline as a share of GDP. *Table 1* summarises the key challenges affecting the sector noted by the Confederation of Zimbabwe Industries, chief among which are "foreign currency shortages causing liquidity constraints; obsolete machinery; the high cost of imported raw materials; and electricity shortages.

Table 1: Business environment affecting manufacturing companies, 2018

Measure	Very negative	Negative	No effect	Positive	Very positive
Forex access	81	14	3	0	3
Exchange rate	65	22	8	3	3
Cash shortages	61	31	5	0	3
2% tax on electronic transactions	59	27	10	2	3
Policy instability	54	35	7	4	0
Corruption	52	31	13	3	2
Access to financing	43	28	18	6	6
Ageing equipment	36	42	19	1	2
Competition from imports	35	31	27	3	4
Interest rates	32	43	21	3	2
Power cuts	26	29	31	10	2
Electricity charges	21	31	37	8	3
Environmental requirements	19	23	47	9	3
Conformity assessment	13	28	50	4	6
Domestic demand	12	20	15	39	14
Minimum wage/labour regulations	12	29	46	7	6
Import restrictions	9	4	34	27	27

Source: Reproduced from Machededze et al., 2022

Fixed exchange rate policies have overvalued the local currency and encouraged informal trade in currency and industry to rely on cheaper imported raw materials. Industry has had to pay upfront for imported supplies, despite having to surrender 40% of export receipts at the prevailing foreign exchange auction rate by the Reserve Bank. A Consignment-based conformity assessment programme introduced in 2015 requires imports, including basic raw materials for the pharmaceutical industry to have a certificate of conformity before final customs clearance in the country of origin. Without this, importers face a compulsory assessment process at their expense and a 15% penalty fee, along with costs for storage, sampling, transportation and testing fees. In relation to 'ease of doing business' reforms, the indigenisation law was repealed in 2018 allowing foreign investors to select 100% foreign-owned investment partners. The Zimbabwe Investment & Development Agency Act (ZIDA) Act of 2019, established an investment promotion and facilitation body, and with other legal reforms introduced more predictable and investor friendly One Stop Investment Services. In relation to industrial development policies, before 2016, Zimbabwe restricted imports of consumer goods by raising tariffs and using discretionary import licensing to shield domestic manufacturers from foreign competition. In June 2019, the Zimbabwe National Industrial Development Policy (ZNIDP) (2019–23) steered industry towards export markets and import substitution. Anchored on innovation, investment and export-led industrialisation, it aims to increase the industrial base to 25% of GDP, with industrial parks developed by local authorities in collaboration with higher education institutions and the private sector; special economic zones hosting industrial services, and a strategy to increase local content in priority sectors from 25% to 80% by 2023 (Machededze et al., 2022).

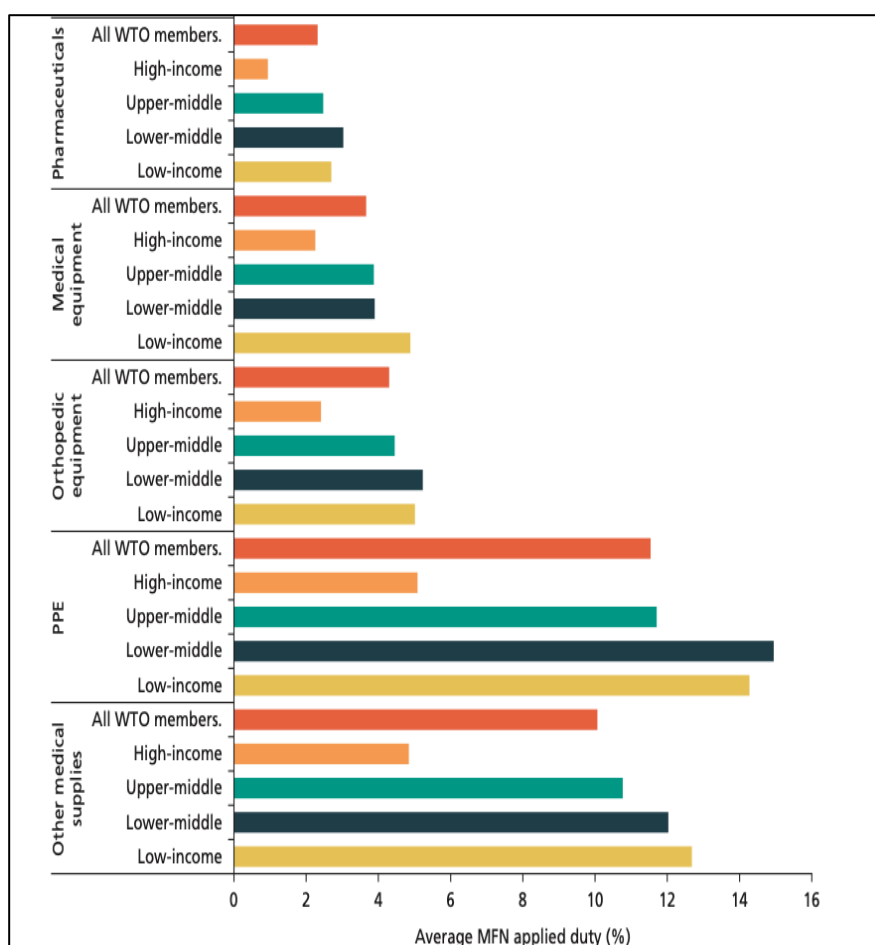
Comparing the policies in Zimbabwe with those in Kenya, South Africa and Uganda shows different features that may be more favourable to local production (Machemedze et al., 2022).

South Africa depends on multinational import of pharmaceutical products and active pharmaceutical ingredients (APIs), despite having 175 local manufacturers. Nonetheless, the country has an advantage in terms of greater levels of local production of pharmaceuticals compared to other African countries, and as the only country that meets WHO standards for manufacture of pharmaceutical products. However, its dependency on imported ingredients places its industry at risk of currency fluctuations, and its trading environment favours dominant multinationals by giving them duty free imports, giving them an advantage over smaller, newly established local producers. The government has, however, reported that it will offer support to small domestic producers.

Since 2013, the WTO reports improvements in the business environment in East African Community countries, noting progress in reforms in Rwanda, Kenya and Uganda and their rising ranking globally in their ease of doing business. Rwanda is, for example, ranked the second easiest country to do business in in Africa, following Mauritius. Kenya has various duty rebate and suspension schemes available at east African regional level. It offers fiscal incentives in the form of tax holidays, reduced tax rates and allows for deduction of investments in taxable profits. These incentives are available under the Export Processing Zones regime and the Special Economic Zone regime, while sector-specific incentives are available for the manufacturing sector.

Raw materials and the pharmaceutical industry

Figure 1: Tariffs for Medical Products



The pharmaceutical industry in most ESA countries depends on imported APIs. Tariffs have, however, strangled imports of raw materials in many low income ESA countries (See Figure 1 for low income countries).

Figure 1 illustrates the impact of tariffs across various EHPs. In some countries, tariffs may help boost revenues and support domestic industry. Elsewhere, low tariffs may benefit consumers by reducing the prices of goods. Low to zero tariffs, particularly on raw materials, may stimulate domestic industry to import APIs for local production of EHPs.

Source: World Bank and WTO, 2022

In South Africa, all imported pharmaceutical products are tariff-free, so raw materials for the pharmaceutical sector pay no duty. However, tariffs range between 10% and 30% for pharmaceutical products, with 15% on medicines, the country's biggest import.

In Uganda, raw materials for the sector, including APIs, are mainly imported from India, China and European countries. The process to import APIs may take over six months, while the prices of raw materials fluctuate. Most packaging materials are available on the local market, except for glass bottles and aluminium. However, some manufacturers prefer to import packaging materials for pharmaceuticals as the locally available materials may not be of the desired quality. Related to this, keeping production lines running calls for very high raw material inventories to be kept, depleting working capital. At regional level, the East African Community (EAC) began implementing a common external tariff in 2005, with 0% for raw materials and capital goods, 10% for intermediate goods and 25% for final/consumer goods.

Kenya, South Africa, Uganda and Zimbabwe have low tariffs on raw materials, facilitating local production. However, the challenge lies in the need for foreign currency to purchase these raw materials, with exchange rate movements affecting costs. This may set up a disincentive to produce locally, if finished products are cheaper to import.

Recommendations on trade measures

In the short to medium term a range of trade measures maybe recommended, all of which call for policy coordination between the different sectors and actors involved.

Production of APIs is central to local production of EHPs. ESA countries should engage with multinationals holding patents and licenses to build and shape relationships, partnerships and secure APIs in a way that enables local production to be profitable.

ESA countries should support their local pharmaceutical sectors through measures such as restricting imports of medicines that can be or are locally produced, such as by raising import taxes on such imported pharmaceutical products;

ESA countries can strengthen measures to exempt duty and VAT on imported pharmaceutical raw and packaging materials to stimulate local production, and provide public sector incentives to companies that use local resources for local medicines production.

Further resources

1. Machededze R, Wade H, Were N, Kiiza A (2022 in press) Local production of essential health products in east and southern Africa, EQUINET Discussion paper 128, SEATINI, EQUINET, Harare
2. UNCTAD (2021) 'Improving access to medical products through trade: what can regional trade agreements do in times of crisis?' UNCTAD. available at: https://unctad.org/system/files/official-document/ditctncd2020d4_en.pdf
3. United Nations Economic And Social Council (UNECA) (2020) 'Recent Economic and Social Conditions in Southern Africa for 2020, and Prospects For 2021'. UNECA, Geneva. Available at: <https://www.uneca.org/sites/default/files/SROs/Southern-Africa/27icsoe/economic-and-social-conditions-in-southern-africa-2020.pdf>
4. World Bank, World Trade Organization (WTO) (2022) 'Healthy Trade: Deepening Trade Cooperation to Improve Global Health Security'. Washington, D.C.: World Bank. doi:10.1596/978-1-4648-1885-1. License: Creative Commons Attribution CC BY 3.0 IGO
5. WTO (2019) 'Trade Policy Review (East African Community): Report by the Secretariat', WT/TPR/S/384, WTO Geneva. Available at: https://www.wto.org/english/tratop_e/tpr_e/s384_e.pdf
6. WTO (2020) 'Trade Policy Review (Zimbabwe)', WT/TPR/S/398 WTO, Geneva. Available at: https://www.wto.org/english/tratop_e/tpr_e/s398_e.pdf