DP WORLD

TRADE IN TRANSITION

REGIONAL REPORT: MIDDLE EAST AND AFRICA

WRITTEN BY The Economist INTELLIGENCE UNIT

About this research

Trade in Transition is a global research programme led by The Economist Intelligence Unit, sponsored by DP World, which presents private-sector sentiment on international trade. In this year's report, we specifically explore the impact of covid-19 on companies' trade operations and the resulting shift in approach to international trade by private-sector firms.

The research is based on two global surveys of senior executives involved in their firm's day-to-day international trade decisions and transactions. The first survey of 3,000 respondents was conducted between January and March 2020 and the second survey of 800 respondents was conducted between October and November 2020. Both surveys captured perspectives of executives across six regions (North America, South America, Europe, Middle East, Africa and Asia Pacific). The survey findings were supplemented with in-depth interviews with trade experts and senior executives across regions and sectors.

This report focuses on the key findings from the Middle East and Africa, exploring key differences between the two sub-regions.

We would like to thank the following experts for their time and insight:

George Omuga, general manager, Ngorongo Tea Factory

Navalayo Osembo-Ombati, CEO, Enda Sportswear

Sulaiman Pallak, global purchasing and supply chain, General Motors

Ashish Thakkar, CEO, Mara Phones

We would like to acknowledge the research contribution of Ofeoritse Kpere-Daibo.
This report was edited by Melanie Noronha.

Executive summary

The economic shocks induced by the coronavirus pandemic had a profound impact on trade-dependent countries in the Middle East and in Africa. Demand for key exports such as oil and other commodities slumped while supply chains for imports, including essential items such as food and medical supplies, were severely disrupted. However, as with companies we surveyed globally, those in the Middle East and in Africa remain undeterred in their intent to source from and sell to international markets, despite their recent challenging experience.

Businesses in both regions are responding by reconfiguring their supply chains, but companies in each market present vastly different responses on the time and investment allocated to this effort. In this paper, we explore the differences in their responses and the factors that will determine companies' approaches to future trade transactions.

KEY FINDINGS

- **The regional collapse in international trade since the start of the pandemic was primarily a result of a *demand shock* in the Middle East and a *logistics shock* in Africa.** Forty-eight percent of respondents in the Middle East stated that a demand shock—defined as the difficulty in selling products to customers in international markets resulting from restrictions imposed due to the covid-19 pandemic—had the greatest negative impact on their international sales. In Africa, 48% cited a logistics shock, defined as the difficulty in arranging for transport or logistics services.
- **Companies in the Middle East are more inclined to reconfigure their supply chains and are expecting to do so faster than companies in other regions.** The Middle East had the highest share of respondents (96%) whose companies were in the process of reconfiguring their supply chains in October-November 2020, higher than the share in Africa (84%) and the global average (83%). On average, they expect to reconfigure supply chains within 7.4 months, compared with the global and Africa averages of 8.5 and 8.6 months, respectively.
- **Uncertainty around pandemic-related lockdowns is of far greater concern among executives in Africa than in the Middle East.** Only 13% of respondents in the Middle East cited this as a barrier to supply chain reconfiguration compared with 38% in Africa. This may be one reason why companies in Africa may be taking longer to reconfigure their supply chains and are investing less than companies in the Middle East. African companies are reallocating only 24% of their H1 2020 revenues for supply chain reconfiguration, compared with 30% in the Middle East.
- **Businesses in both the Middle East as well as Africa are creating agile supply chains to respond to market changes.** An integral component of creating agile systems is the adoption of advanced technologies such as the Internet of Things (IoT), cloud computing and big data analytics to access real-time information. These efforts were underway much before the start of the pandemic, but were accelerated during the pandemic. Digital transformation will remain a priority for companies even after the pandemic: "Enhancing responsiveness to changes through real-time/ predictive data analytics" is among the top two factors that will determine companies' approach to future trade transactions up to 2025.

Spotlight on Africa

With the African Continental Free Trade Area (AfCFTA) now in effect, the eyes of the world will be on the continent, to see if its much-touted benefits will materialise. Along with a reduction in trade barriers, a push for "Made in Africa"—as part of a strategy to improve supply chain resilience post-pandemic—may alter trade dynamics. Our survey identifies the key pain points for African businesses engaging in international trade and their priorities for the future:

- During the pandemic, 48% of respondents in Africa struggled the most from a logistics shock, defined as the difficulty in arranging transport or logistics services.
- The uncertainty around pandemic-related lockdowns has been the biggest barrier for executives in Africa as they try to adapt and respond to disruptions, and is perhaps one reason for low levels of investment in supply chain reconfiguration (only 24% of H1 2020 revenues were used for this, compared with 32% globally).
- In response to pandemic-related disruptions, African businesses are pivoting to new markets and reducing their reliance on a single source for critical raw materials, where possible. Diversifying their supplier base was among the top two factors that will determine their approach to international trade transactions up to 2025.
- To optimise trade operations during the pandemic and beyond, African companies are relying on a mix of advanced technologies: the Internet of Things (IoT) (48% of respondents), cloud computing (26%) and data analytics (20%). Enhancing their firms' responsiveness to changes through real-time/ predictive data analysis was the top factor that will determine their approach to international trade transactions up to 2025.

State of trade in the post-covid era

Global trade, which was already experiencing a slowdown in 2019, fell sharply in the second quarter of 2020 as covid-19 spread rapidly around the world. The value of global exports and imports fell by 21% year on year in Q2 2020[1] and the experience in the Middle East and in Africa was far worse. According to estimates from International Trade Centre, a multilateral agency, trade in the regions plummeted, falling by 66% year on year in Q2 2020 in the Middle East and by 55% in Africa.[2]

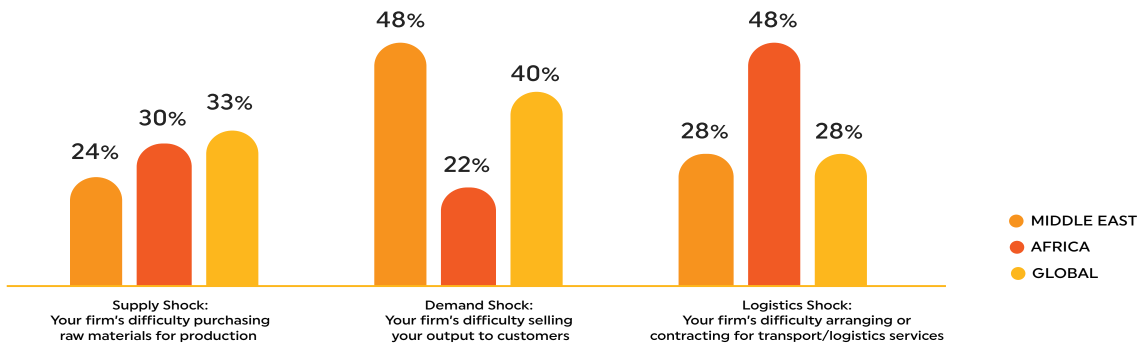
This collapse in global and regional trade was partly due to the economic shocks induced by pandemic-related restrictions on movement of people and goods. Many governments in African and Middle Eastern countries implemented strict measures by mid-March 2020 (including the UAE, Saudi Arabia, Nigeria and South Africa), shutting down international travel and closing land borders, while allowing freight to pass under tighter controls.[3,4] These national lockdowns limited companies' access to international suppliers of raw materials as well as shipping lines for transportation of finished goods to overseas markets, resulting in supply and logistics shocks. Simultaneously, business activity in key economic sectors such as retail, tourism, manufacturing, among others, ground to a halt, driving wage cuts and job losses that ultimately reduced demand from businesses and consumers.

In our global survey conducted in October-November 2020, the highest share of respondents in the Middle East (48%), indicated that a demand shock (defined as the difficulty in selling products to customers in international markets) had the greatest negative impact on their firms' international sales. This is unsurprising because the region's key exports are oil and gas products, which experienced a sharp fall in demand during the pandemic following a reduction in travel and business activity. Oil and gas comprise over 70% of total exports in Middle Eastern countries such as Saudi Arabia and Kuwait, which saw export revenues shrink significantly as a result of the oil price slump in 2020.

In Africa, the highest share of respondents (48%) indicated that a logistics shock (defined as the difficulty in arranging for transport or logistics services) had the greatest negative

FIGURE 1

Which shock had the greatest negative impact on your firm's company-wide international revenues in H1 2020?



Source: EIU survey October-November 2020

[1] *Third Quarter 2020 Merchandise Trade Value.* World Trade Organization. Updated on 4 December 2020. Available online at https://www.wto.org/english/res_e/statis_e/daily_update_e/merch_value_latest.pdf

[2] https://www.trademap.org/

[3] *Nigeria imposes cargo vessel restrictions to curb coronavirus spread.* Reuters. 27 March 2020. Available online at https://www.reuters.com/article/health-coronavirus-nigeria-shipping/nigeria-imposes-cargo-vessel-restrictions-to-curb-coronavirus-spread-idUSL8N2BJ9X4?rpc=401

[4] *Coronavirus and freight forwarding in SADC.* Tralac. 9 April 2020. Available online at https://www.tralac.org/blog/article/14502-coronavirus-and-freight-forwarding-in-sadc.html

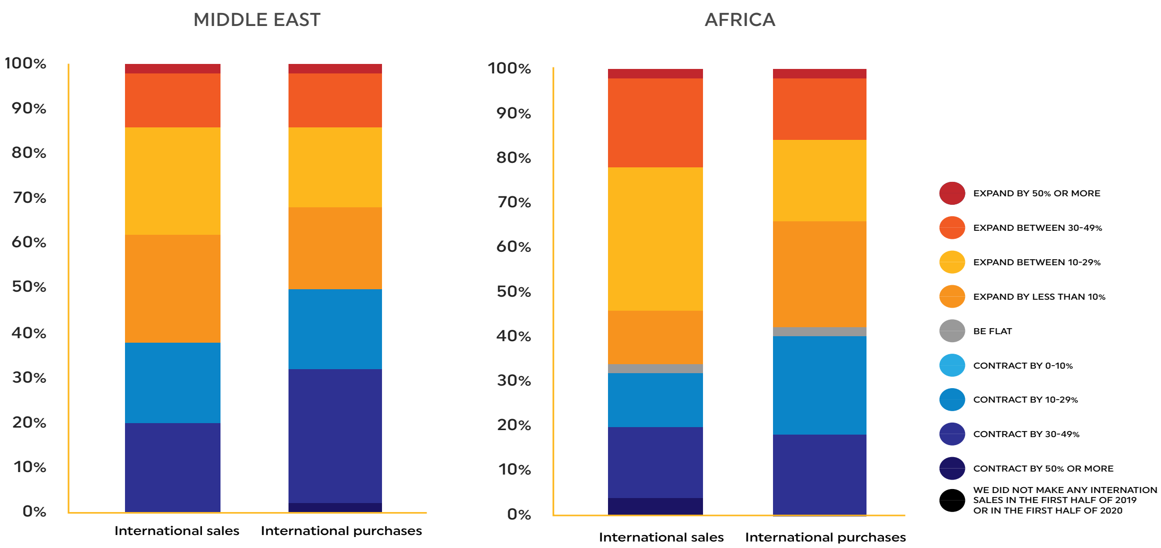
impact on international sales. Exports from the continent include a range of consumer products from food items such as tea and cocoa to clothing and footwear, staples for which there was sustained or growing demand during the pandemic. The challenge was reaching international markets. "Most of the ports in Africa were adversely affected, including the port of Mombasa, the biggest port in East Africa, disrupting the shipping of imports and exports," says George Omuga, general manager of Ngorongo Tea Factory in Kenya. Limited availability of shipping lines caused freight costs to increase sharply, he says.

As a result of these economic shocks, international sales in the first half of 2020 contracted year on year for 38% and 56% of firms surveyed in the Middle East and Africa, respectively. The share of companies that experienced a contraction was the highest in Africa, compared with 46% in South America, 39% in North America, and 37% in Europe and Asia-Pacific.

Despite the challenges, businesses in the two regions have demonstrated a degree of resilience. In the Middle East, 38% of firms surveyed expanded international sales in the same period (the same as the share that experienced a contraction) and 24% experienced no change. In Africa, nearly one-third (32%) of firms surveyed expanded international sales in the first half of 2020. For instance, South Africa saw exports of pulp (a raw material for toilet paper) and cereals increase by 163% and 113% year on year, respectively, in H1 2020.[5] The experience of Kenya-based Enda Sportswear is testament to this. Demand for sports shoes from the US and European markets soared as customers grew more concerned about staying fit during lockdown, says its CEO, Navalayo Osembo-Ombati. "We had just finished production when government [lockdown] policies were being announced and dispatched our product right away."

The unprecedented nature of the pandemic and government policies to mitigate its impacts called for a greater degree of responsiveness from companies engaging in international trade. From our survey results and interviews with executives, we have learned that companies in the Middle East and Africa have reconfigured their supply chains to adapt, deepening relationships with supply chain partners and accelerating the adoption of advanced technologies to optimise trade operations. From our research, it is evident that companies in the regions remain undeterred, committed to maintaining global networks for sourcing as well as sales. In the next two sections of this report, we explore how companies in the regions have responded to pandemic-related supply chain disruptions and how this has shifted their approach to trade over the next five years.

FIGURE 2
International trade performance in H1 2020 vs H1 2019



Source: EIU survey October-November 2020

[5] *ITC Trade Map.* Available at https://www.trademap.org/

The supply chain overhaul: De-risk and adapt

Since the start of the pandemic, supply chain reconfiguration has been a priority for many businesses in the Middle East and Africa as they worked to mitigate its adverse impacts. In our survey, the Middle East had the highest share of respondents (96%) whose companies were in the process of reconfiguring their supply chains in October-November 2020, higher than Africa (84%) and the global average (83%). With reconfiguration still underway for many companies, the strategies they employ in this process could potentially drive shifts in regional trade patterns.

Businesses have employed a range of strategies as they restructure their supply chains – from targeting new markets for sales to diversifying their supplier base, and from negotiating prices with suppliers to adopting advanced technologies to optimise trade operations. In this section, we take a closer look at these strategies and consider the most critical barriers faced by businesses in the regions as they reconfigure their supply chains.

SHIFTING SUPPLY CHAINS, SHIFTING TRADE PATTERNS?

As part of their supply chain reconfiguration, companies in the Middle East and Africa pivoted to new markets to offset sales lost from inaccessible markets and from the overall fall in demand for some products. The Ngorongo Tea Factory in Kenya, for instance, was unable to export existing inventory to its key markets (Egypt and the UK, among others), and so turned to the Indian market. As India went into lockdown, restrictions on movement of people disrupted operations on tea plantations during the leaf-picking season.[6] "So that gave us an advantage to meet some demand in India," says Mr Omuga, "as well as in Poland, Switzerland, Ukraine, Malaysia and Bangladesh."

However, the pursuit of alternative markets in a depressed global economy is not viable in all sectors. As Sulaiman Pallak, Dubai-based manager for global purchasing and supply chain at automotive firm General Motors, recounts: "We did explore alternative avenues and markets across Africa and across the other regions as well but, given that they are not our primary markets, we wanted to focus on regions which bring the highest returns.. Overall, the automotive industry saw a contraction because buying a vehicle is a significant purchase, so people [have decided to] put it on hold for a year or two."

The pandemic also exposed companies' overreliance on suppliers in specific countries or regions. Pre-pandemic, Ms Osembo-Ombati of Enda Sportswear in Kenya was already concerned over the firm's reliance on Asian, and especially Chinese, suppliers.

The widespread disruption to production and distribution hubs in Asia during the first half of 2020 reinforced those concerns. To address this, companies have diversified their supplier base and also sought new supply chain partners. Ashish Thakkar, founder and CEO of Mara Phones, a South African and Rwandan mobile phone manufacturer, echoed the need for diversification: "Imports of raw materials have become much less certain and costlier owing to higher transportation costs. Companies like ours have and are putting in place strategies to address the issues of unpredictability of demand and the need to control the supply chain cost, and eventually enable local producers.."

To reduce their reliance on distant markets for raw materials, African companies may shift to local production, wherever possible, which would promote trade within the region. "We are trying to service more local supply chains just because, for instance, now the supply in China has become a bit of a problem," says Ms Osembo-Ombati. Mr Thakkar adds: "African companies may consider supporting 'Made in Africa' products which have become even more relevant. There is now greater awareness and need by governments and citizens to support local manufacturing."

[6] *Coronavirus brews trouble for tea, disrupts supply as demand spikes.* The Chronicle Herald. 29 April 2020. Available online at https://www.thechronicleherald.ca/business/reuters/coronavirus-brews-trouble-for-tea-disrupts-supply-as-demand-spikes-443350

"African companies may consider supporting 'Made in Africa' products which have become even more relevant. There is now greater awareness and need by governments and citizens to support local manufacturing."

Ashish Thakkar, CEO, Mara Phones

Together, the shift to new markets and supply chain partners in different locations could alter the region's trade patterns, if these changes stay in place following the pandemic.

DEEPENING TIES WITH SUPPLY CHAIN PARTNERS

While diversifying the supplier base has been one strategy pursued by companies during the pandemic, others have relied on closer collaboration with existing suppliers. "The approach we took was not to switch or to change our supply partners during a challenge, but rather work with them more closely and understand requirements and engage with them," says Mr Pallak of General Motors. "Our philosophy is that we have really strong partnerships with our suppliers." General Motors assessed risks across multiple tiers of their supply chain. In doing so, it was able to identify challenges on the ground and thus better estimate demand and supply levels. General Motors was also able to negotiate prices and payment terms by committing to supply chain partners for the longer term, allowing them to reduce costs during the pandemic.

ACCELERATING TECH ADOPTION FOR TRADE OPERATIONS

To sustain operations during the pandemic, businesses around the world have accelerated their digital transformation, and supply chain digitalisation has been an integral part of this. Unsurprisingly, executives in the Middle East and Africa indicated that IoT, cloud computing and big data analytics were the top three technologies their companies relied on to optimise trade operations during the pandemic.[7] IoT and big data analytics have been critical for accurate forecasting, allowing companies to respond quickly to market changes and effectively manage risks and minimise losses. Cloud computing has been vital for remote access to company files and transactions during lockdown.

The pandemic has essentially forced companies to "think outside the box" and become more innovative in the way they engage with suppliers and distributors, in many instances using digital channels. Mr Omuga explained that Africa's leading tea auction, which usually takes place in-person in Mombasa, was forced to go online to prevent disruption of Africa's tea trade.[8]

Some of the digital transformation that helped companies during the pandemic was underway well before the start of the pandemic. In the Middle East, digital transformation in the energy sector was aimed at making energy trade more cost-effective. For example, Saudi Aramco (Saudi Arabia's national oil company) embarked on a digital transformation strategy a few years ago. Such efforts could enable the company and its global subsidiaries to identify weaknesses in the supply chain and assess evolving supply chain issues, as well as enable real-time collaboration between buyers and suppliers.

The UAE's blockchain strategy is aimed at accelerating adoption in the country's trade and logistics sector, among others. Such shifts to more digital platforms, made more urgent during the pandemic, could immensely strengthen the region's trade operations and its place as a global trade hub. But as they do so, policymakers and executives must be mindful of the growing threat of cyberattacks in a digital ecosystem and take steps to ensure data security.

BARRIERS TO SUPPLY CHAIN RECONFIGURATION

There are numerous barriers slowing down or impeding companies' efforts to restructure their supply chains, such as the uncertainty around pandemic-related lockdowns and legacy contracts with existing vendors, in addition to the time and costs associated with the process.

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[7] Middle East: IoT (46%), cloud computing (36%), big data analytics (28%); Africa: IoT (48%), cloud computing (26%), data analytics (20%).

[8] *The Mombasa Tea Auction. East African Tea Trade Association.* Accessed on 8 February 2021. Available online at https://www.eatta.com/the-mombasa-tea-auction

Globally, companies we surveyed expressed that uncertainty around pandemic-related lockdowns was the greatest barrier to reconfiguring supply chains (cited by 28% of worldwide respondents) (see Figure 3). In comparison, a significantly higher share of respondents in Africa (38%) and a significantly lower share in the Middle East (13%) cited this barrier. This could be one reason why companies in Africa are investing less and taking more time than those in the Middle East to reconfigure their supply chains.

Companies in the Middle East expect to restructure their supply chains within 7.4 months compared with 8.6 months in Africa and 8.5 months globally. Over half of the respondents in the Middle East (54%) expect to reconfigure their supply chains within 6-12 months, compared with 33% in Africa and 39% globally. Middle Eastern companies are also reallocating roughly 30% of their H1 2020 revenues to reconfigure their supply chains (in line with the global average of 32%). However, respondents in Africa are reallocating less—on average, about 26% of their H1 2020 revenues.

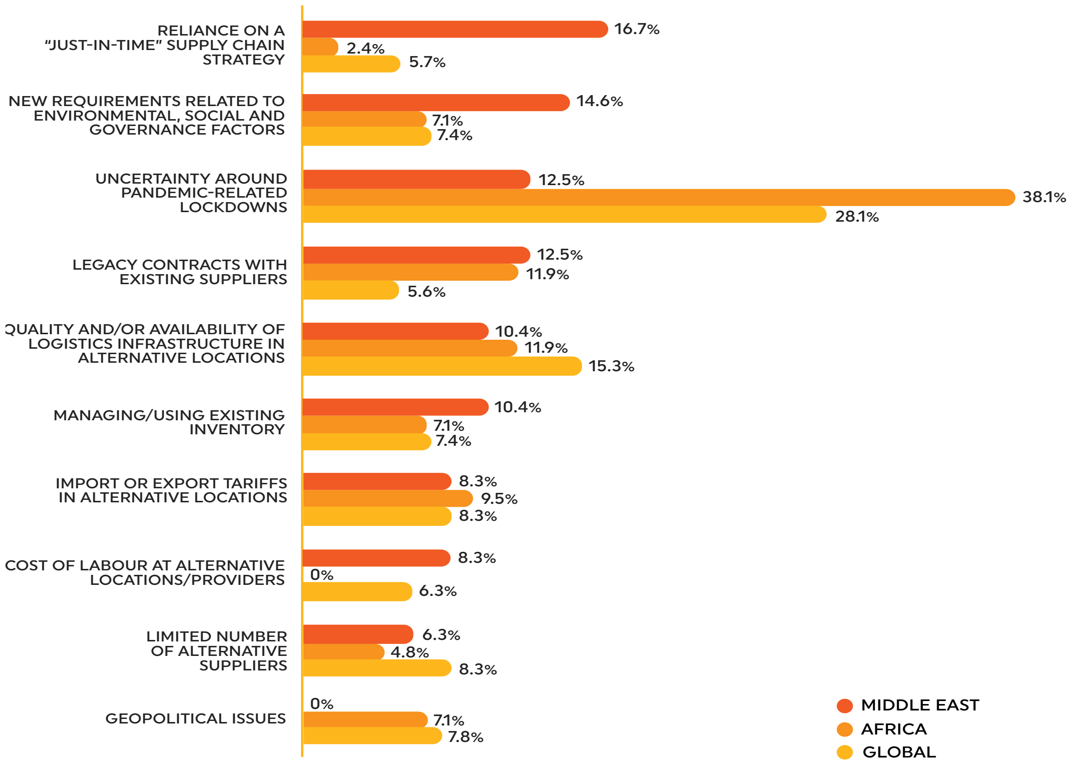
Uncertainty around lockdowns makes choosing alternative locations to source from or sell to a more challenging task. A similar link between lower-than-average revenue reallocation and uncertainty around pandemic-related lockdowns was evident among executives surveyed in Europe too.

Importantly, the pandemic is driving a shift in the very objective that typically underpins modern supply chain management. Sporadic disruptions caused by continually changing lockdown policies have required companies to move away from a "just-in-time" strategy to allow for some buffers in inventory. Reliance on a "just-in-time" supply chain strategy was cited as the top barrier to supply chain reconfiguration by respondents in the Middle East. "Here, our distribution centre is designed and configured in a way that we do not hold significant inventory," says Mr Pallak. "Where we were unable to secure capacity from shipping lines, we couldn't get [inputs] and hence could not [optimise factory] floor planning. That was a significant challenge."

In the Middle East, new supply chain requirements related to environmental, social and governance (ESG) factors were cited as the second greatest barrier to reconfiguration.

FIGURE 3

Barriers to supply chain reconfiguration in the Middle East and Africa vs globally



Source: EIU survey October-November 2020

This is unsurprising given the region lags in ESG regulation.[9] As governments, commercial partners and consumers around the world demand greater transparency on ESG within corporate supply chains, a trend which accelerated during the pandemic,[10] Middle Eastern companies must pay closer attention to ensure they meet global standards.

A common barrier to supply chain reconfiguration for respondents in the Middle East and Africa was legacy contracts with existing suppliers, which was cited among the top barriers in both regions.

The lack of financing at affordable rates, a perennial challenge for businesses in the Middle East and Africa, was another impediment to quickly adapting supply chains during the pandemic. "We had to spend a lot of money because it was not in our budget and had to apply for asset financing from our local banks," says Mr Omuga. "[The cost of financing is] usually expensive in Africa, the interest rate is very high."

To close the funding gap, business owners are turning to international investors, notably from Asia. Ms Osembo-Ombati noted that she is eyeing funding from an Indian investor, and added that Asian investors see the long-term potential of investing in African entrepreneurs.

The barriers discussed above slow down decision-making or serve as impediments to the rapid transformation of supply chain networks. Even in the face of unprecedented lockdowns, these barriers make supply chains stickier than one might expect, and may only lead to a gradual shift in regional and global trade patterns. The impact on trade flows will be determined by the supply chain reconfiguration strategies that are retained post pandemic; we explore these strategies in the final section of this report.

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[9] *ESG and Sustainable Finance in the Middle East: Roundtable Discussion.* GFC Media Group. 5 November 2019. Available online at https://gfcmediagroup.com/content-images/bondsloans/pdfs/ESG-Roundtable-report-2019.pdf

[10] *Why ESG investing is on the rise in 2020. RBC Wealth Management*. Accessed on 8 February 2021. Available online at https://www.rbcwealthmanagement.com/gg/en/research-insights/why-esg-investing-is-on-the-rise-in-2020/detail/

Rules of engagement for a 'new normal'

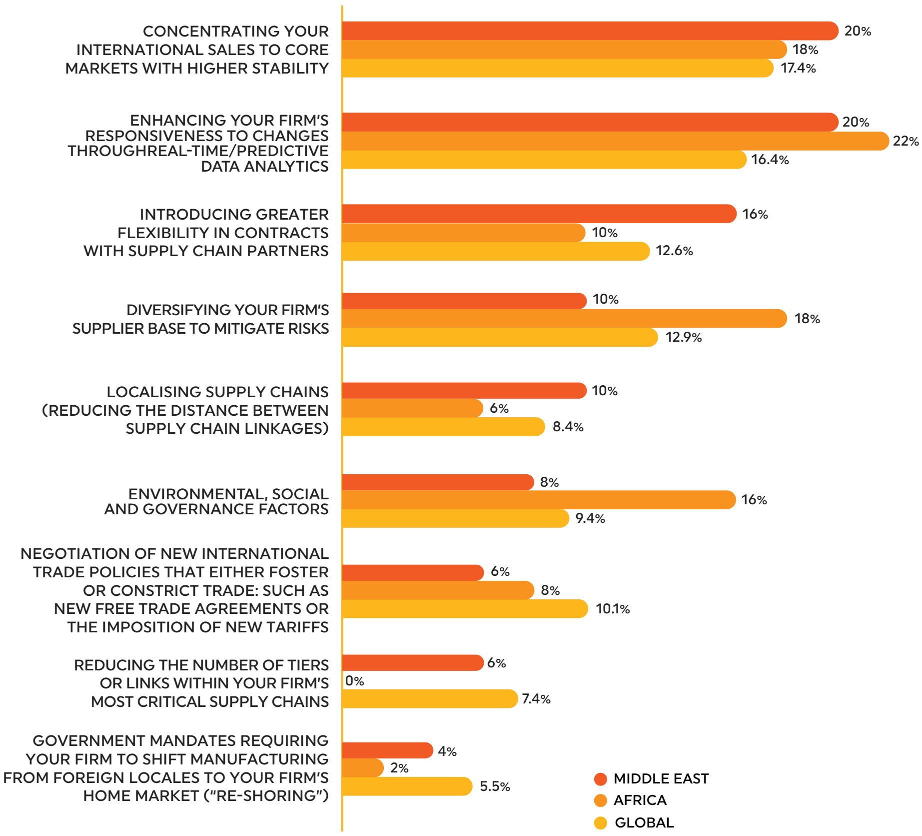
Despite the challenges endured during the pandemic, businesses worldwide are hopeful of a return to pre-covid levels of trade and expect to continue to engage in global supply chain networks. Respondents in the Middle East and Africa are the most optimistic about global trade recovery. Fifty percent of respondents in the Middle East and 38% in Africa believe it will take less than a year for global trade to recover to pre-pandemic levels, compared with 23% of respondents in Europe, 27% in Asia-Pacific and 28% in North America.

There are already signs of a recovery in manufacturing output and trade volumes as different countries reopen. Africa's exports have been supported by good harvests and rising prices of several commodities, including copper, gold and iron ore.[11,12] Although respondents expect trade activity to return to normal, the factors that determine how companies will conduct their international trade transactions may be evolving.

Companies in the Middle East expect to concentrate international sales in core markets with higher stability. Additionally, for respondents in both the Middle East and Africa, enhancing their firms' responsiveness to changes through real-time/ predictive data analytics was among the top three factors shaping their medium-term international trade transactions. This represents a focus on digital transformation that was underway before the

FIGURE 4

Factors determining how companies in the Middle East and Africa will conduct international trade transactions up to 2025



Source: EIU survey October-November 2020

[11] *2020 may turn out to be a 'brilliant' year for SA agriculture - thanks to good rain and bumper crops.* Business Insider South Africa. 30 August 2020. Available online at https://www.businessinsider.co.za/bumper-crops-in-the-agricultural-sector-2020-8

[12] https://www.ft.com/content/27086ad8-bc84-4e2e-9195-91880fa6916f

pandemic, but, as discussed in the previous section, has become even more urgent in the post-pandemic era, to drive agility.

For respondents in Africa, diversifying their supplier base was among the top two factors expected to determine international trade transactions up to 2025. "The pandemic made us realise that reliance on one market is extremely difficult," says Ms Osembo-Ombati of Enda Sportwear. "I think a lot of businesses now are thinking we never want to be in that situation again, where if the market has collapsed, then you don't have any product."

African companies may find opportunities for supplier diversification within the region, since the AfCFTA came into effect on January 1st 2021. However, these opportunities may materialise only in the medium term due to implementation delays and disputes among AfCFTA partners. "This trade agreement is still non-functional because some countries still believe that they have to protect their own, promoting their own products and discouraging imports from other countries," says Mr Omuga.

In the short to medium term, companies in Africa and the Middle East are likely to retain close links with suppliers and clients in key Asian, European and American markets. China remains African countries' major trade partner – its trade with African countries was up 2.2% year on year in 2019, amounting to US$208 billion[13], and it remains a major consumer of the Middle East's energy supplies.

It is noteworthy that in both the Middle East and Africa, strategies mandated by some governments for reshoring and reducing the number of tiers within supply chains were the least important factors shaping future international trade transactions (see Figure 4). "I think this protectionist idea that [some] countries are promoting is not sustainable when the world is already a global village," says Mr Omuga of Ngorongo Tea Factory. "Every country is interdependent. So [although protectionist policies are being implemented], I believe post-covid, those systems will not work. The WTO should ensure that these new protectionist tariffs and non-tariff barriers that some countries have introduced are adequately addressed and removed."

In our first survey conducted between January and March 2020, the trade war between the US and China was the top reason for pessimism about global trade among Middle East and Africa respondents.

To stay ahead, Middle Eastern and African companies will continue investing in digital solutions and work towards a more efficient, diversified and secure supply chain environment. Building buffers in their supply chain, deepening relations with existing suppliers and collaborating more closely with domestic suppliers may be important elements of companies' strategy. "We do still leverage our complex global supply," says Mr Pallak. "Rather than changing the model, [we want to] make it more efficient, make it more robust, make it more resilient'."

"I think this protectionist idea that [some] countries are promoting is not sustainable when the world is already a global village."

George Omuga, general manager, Ngorongo Tea Factory

[13] *EIU to confirm: China's trade with Africa grows 2.2 per cent in 2019 to US$208 billion.* SCMP. 18 January 2020. Available online at https://www.scmp.com/news/china/diplomacy/article/3046621/chinas-trade-africa-grows-22-cent-2019-us208-billion