UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
UNCTAD

ECONOMIC DEVELOPMENT IN AFRICA

REPORT 2020

Tackling illicit financial flows for sustainable development in Africa

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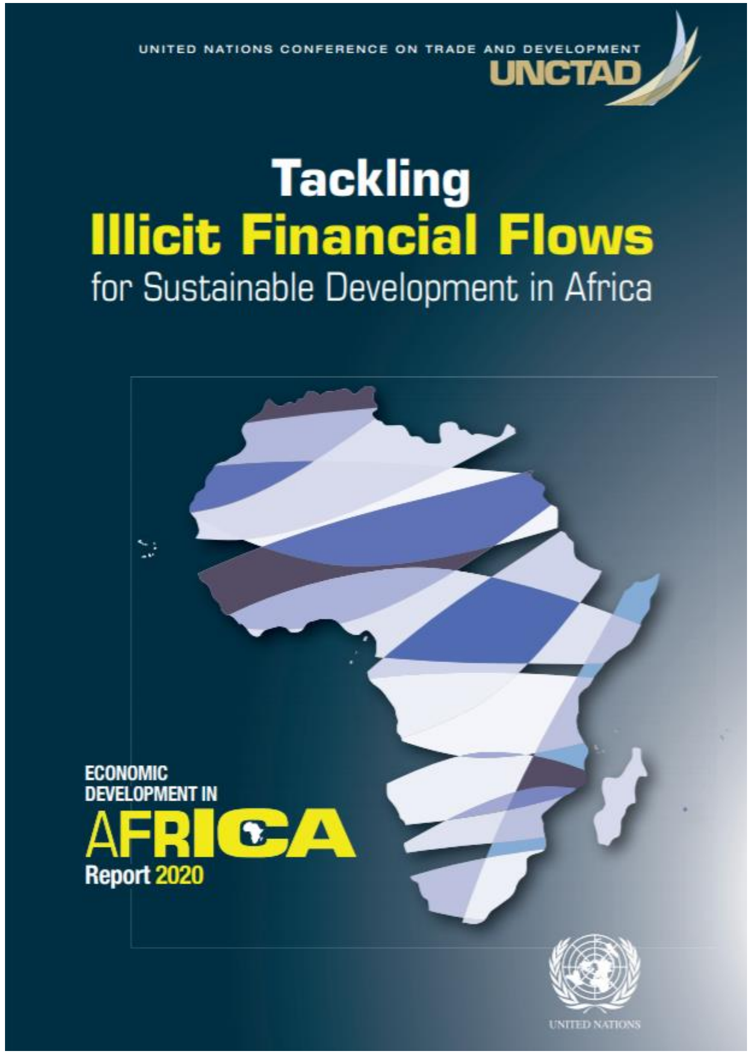

CONCEPTUAL FRAMEWORK

- **Illicit financial flows (IFFs)** and international tax evasion are a shared problem and require a multinational effort to combat them.

- IFFs present a major financial challenge to Africa's development and capital accumulation. Critically, they undermine African countries' potential to achieve the Sustainable Development Goals (SDGs) and Agenda 2063.

CONCEPTUAL FRAMEWORK

- IFFs matter for multiple dimensions of the 2030 Sustainable Development Agenda: for prosperity, for social development, for peace and security, and for the planet
- New analytical contributions across these multiple dimensions through mixed methods: economic tools, legal, political economy and international relations perspectives. With a gender lens on development outcomes and on institutional catalysts of IFFs.
- Balanced approach, inclusive of private sector perspectives.

KEY RESEARCH QUESTIONS

- What is the magnitude of specific components of IFFs in Africa?
- What are the mechanisms and regulatory loopholes behind IFFs?
- What are the root causes of IFF risks and who are the key actors?
- What is the relationship between IFFs and the economic, social and environmental dimensions of sustainable development in Africa?
- To what extent could curbing IFFs help in achieving SDGs in Africa?
- What should be done at the national, multilateral and continental levels and via the AfCFTA to curb IFFs and increase financing for development in Africa?

DATA SOURCES

- **UNCTAD's calculations**; based on UN Comtrade data for 8 commodity groups 2000-2018
- Capital flight estimates from PERI (Ndikumana & Boyce).

- **Tax revenue data** from the ICTD & UNU-WIDER government revenue database.
- Revenue losses due to tax avoidance from Political Economy Research Institute database.
- Returned stolen assets from WB & UNODC Stolen Assets Recovery (StAR) Initiative .

- **Health and Education expenditure** from WB World Development Indicators.
- **Natural disaster** events and costs from Centre for Research on the Epidemiology of Disasters (CRED).
- Annual climate change-related finance needs by 2030 from Shimizu & Rocamora (2016).
- **Resource contracts database** from Resourcecontracts.org and reports of OECD Consultations on Pillar One on Natural Resources Dialogue.

MOTIVATION

- Achieving the 2030 Agenda for Sustainable Development will require an unprecedented mobilization of resources worldwide as the global financing gap currently stands at of $2.4 trillion.
- To deliver on the SDGs, African governments need to raise additional $200 billion annually.
- Africa has an annual infrastructure deficit of $93 billion.
- Africa's fiscal vulnerability has been further increased by COVID-19 for which Africa needs to raise between $110- US$ 154 billion to recover from its social economic impacts.

MOTIVATION CONT'D

- However, domestic resource mobilization is undermined by capital flight which costs Africa about $88.6 billion annually more than its respective annual ODA inflows ($48 billion) and FDI inflows ($54 billion).
- IFFs add fuel to inequality and conflict.
- Accordingly, the report
  - Aims at equipping African governments with the knowledge for identifying and understanding the risks associated with IFFs.
  - Provides solutions for curbing IFFs in Africa.

WHAT ARE IFFS

- Movement of money and assets across borders that are illegal in source, transfer or use.
- They are broadly categorized into four groups:
  - Tax and commercial practices: biggest channel in Africa accounting for 65% of IFFs
  - Illegal markets
  - Theft-type and terrorism financing
  - Corruption

KEY FINDINGS

- **IFFs are a major drain on capital in Africa:**
  - Trade misinvoicing cost Africa $30-52 billion annually
  - Africa losses about $148 billion to corruption annually
  - About 10% of Africa's corporate tax was lost to tax avoidance in 2015
  - 2.5% of total tax revenue was lost to tax havens in 2014
- **The risk of trade misinvoicing is greater for high-value low weight commodities and is not necessarily specific to countries.**

KEY FINDINGS

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- **IFFs undermine Africa's potential to achieve the SDGs**

  - **Low labour productivity and growth**
  – IFFs undercut labour productivity: countries with high IFFs have only 1/3 of the agricultural productivity levels of countries with low IFFs
  - **Low investment levels**
  – Countries with high IFFs spend 25% less on health and 58% less on education than countries with low IFFs
  - **low institutional capacity and poor financial sector regulation**
  – Only 45 out of 53 African countries provide trade data to UN Comtrade in a continuous manner.
  – About half of the countries in Sub-Sahara Africa still do not have any form of domestic transfer pricing rules.

KEY FINDINGS

- **IFFs Undermine domestic resource mobilization**
  - Curbing an annual capital flight of $88.6 billion from Africa could bridge about half of its annual SDG financing gap of US$200 billion
- **Corruption enables IFFs**
  - Corruption compromises the international financial system for money laundering purposes and weakens domestic institutions
- **AfCFTA provides a potential framework for cooperation and institutional capacity to combat IFFs**
  - Although we did not delve into this issue in the EDAR 2020, our recent work shows that the AfCFTA opens a new era of trade governance in Africa.

POLICY RECOMMENDATIONS

Specific to relevant stakeholders and is centered around 4 pillars of development

- **African governments**
  - **Economic:**
    - Intensify the fight against corruption and money laundering (recovery of stolen assets)
    - Improve regional cooperation on tax reform and strengthen engagement in international taxation reform
    - Build the capacity of personnel at ports, customs & tax authorities
  - **Social**
    - Protect civil society, whistle-blowers and investigative journalists

POLICY RECOMMENDATIONS

- **African governments**
  - **Institutions:**
    - Strengthen domestic regulatory frameworks
    - Rekindle trust in multilateralism to fight IFFs
    - Invest in data infrastructure and transparency
  - **Environment**
    - Engage MNEs on taxation and sustainable development
    - Invest in research on IFFs and climate change

POLICY RECOMMENDATIONS

- **International community**
  - **Economic**
    - Engage MNEs on "responsible tax" and the sustainable development agenda
  - **Institutions**
    - Rekindle trust in multilateralism through tangible actions in the fight against IFFs
- **Government revenue authorities, policy makers and researchers**
  - **Economic**
    - Treat wide and persistent trade gaps for a commodity group as a "red flag" for further investigation

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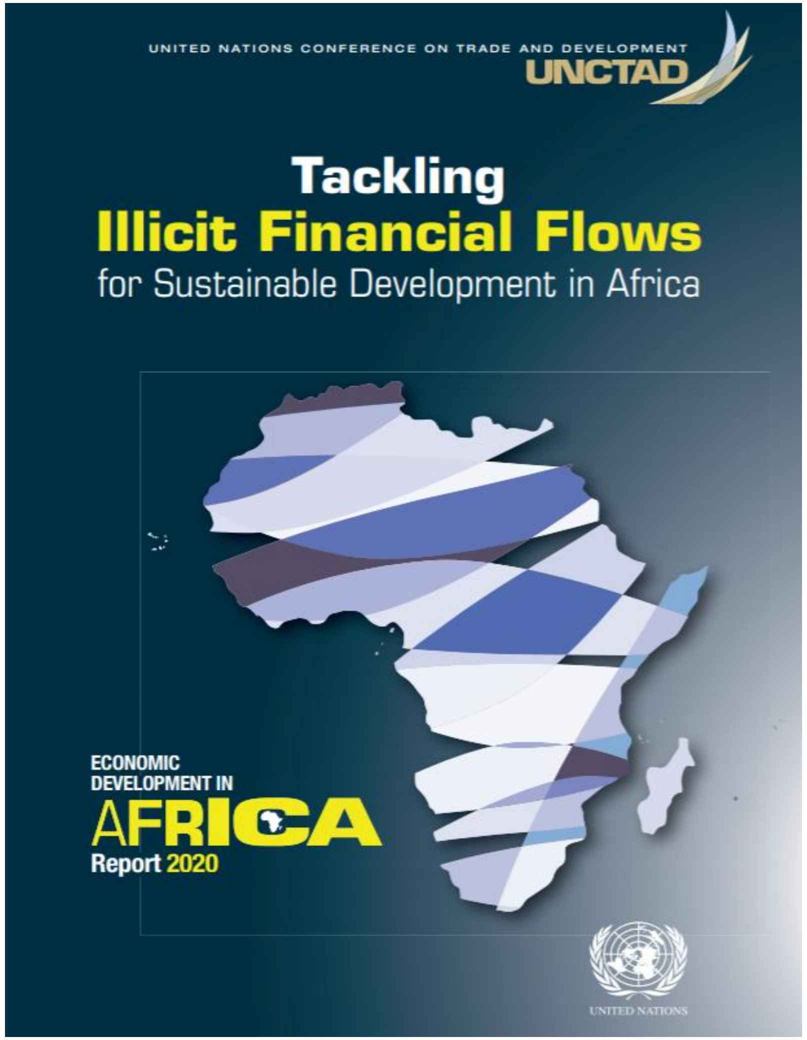

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