

# LIBERALISING TRADE IN SOUTHERN AFRICA

Implementation  
challenges for the 2008  
SADC FTA and beyond



Proceedings of the Fifth  
Southern African Forum on  
Trade (SAFT) held in  
Pretoria, South Africa,  
on 6–7 August 2008

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DECEMBER 2008

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# Acronyms and abbreviations

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ACP	African, Caribbean and Pacific group of countries
AGOA	African Growth and Opportunity Act
AITIC	Agency for International Trade Information and Cooperation
APRM	African Peer Review Mechanism
ASYCUDA	Automated System for Customs Data
AU	African Union

BBR	Beitbridge Bulawayo Railway
BLNS	Botswana, Lesotho, Namibia and Swaziland
BNS	Botswana, Namibia and Swaziland

CARIFORUM	Caribbean Forum on ACP states
CCFB	Beira Railways Company
CDN	Corredor de Desenvolvimento do Norte
CEAR	Central East African Railways
CEMAC	Communaute Economique et Monetaire de l'Afrique Centrale
CET	common external tariff
COMESA	Common Market for Eastern and Southern Africa
CPA	Cotonou Partnership Agreement
CREC	China Railway Engineering Corp
CTH	change in tariff heading
CTSH	change in tariff sub-heading
CU	customs union
CUTS	Consumer Unity and Trust Society

DAC	Development Assistance Committee
DCD	Development Co-operation Directorate
DDA	Doha Development Agenda
DFIs	direct foreign investments
DfID	Department for International Development
DFQF	duty- and quota-free
DNA	Development Network Africa
DRC	Democratic Republic of Congo

EAC	East African Community
EBA	Everything But Arms
ECOWAS	Economic Community of West African States
EPA	Economic Partnership Agreement



ESA	Eastern and Southern Africa
EU	European Union
FDI	foreign direct investment
FES	Friedrich Ebert Stiftung
FOCAC	Forum on China–Africa Co-operation
FTA	free trade area
FTZ	free trade zone
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GIS	Geographic Information Systems
GSP	Generalised System of Preferences
GVM	gross vehicle mass
HS	Harmonised System
IEPAs	Interim Economic Partnership Agreements
IF	Integrated Framework
IFIs	International Financial Institutions
ILEAP	International Lawyers and Economists Against Poverty
IT	Information Technology
JITAP	Joint Integrated Technical Assistance Programme
LDC	least developed country
MDGs	Millennium Development Goals
MERCOSUR	Southern Common Market
MFN	most favoured nation
MIDP	Motor Industry Development Programme
MMTZ	Malawi, Mozambique, Tanzania and Zambia
MOU	memorandum of understanding
NEPAD	New Partnership for Africa’s Development
NTB	non-tariff barrier
ODI	Overseas Development Institute
OECD	Organisation for Economic Co-operation and Development
PPPs	public–private partnerships
PTA	preferential trade agreements
REC	Regional Economic Community

## ■ Acronyms and abbreviations

RISDP	Regional Indicative Strategic Development Programme
RoO	Rules of Origin
RSZ	Railway Systems of Zambia
RTA	Regional Trading Agreement
RTFP	Regional Trade Facilitation Programme
SACU	Southern African Customs Union
SADC	Southern African Development Community
SAIIA	South African Institute of International Affairs
SAPP	Southern African Power Pool
SEZ	Special Economic Zone
SKD	semi knock down
SP	specific processing
SPS	Sanitary and Phytosanitary Measures
SPV	Special Purpose Vehicle
SSA	Sub-Saharan Africa
TDCA	Trade, Development and Co-operation Agreement
TP	Trade Protocol
TRC	Tanzania Railways Corporation
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNECA	United Nations Commission for Africa
USAID	United States Agency for International Development
VA	value-added
WB	World Bank
WTO	World Trade Organisation

# Preface

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The Southern African Forum on Trade (SAFT) seeks to enhance dialogue on regional trade-related matters, involving government and non-governmental representatives and academics working in this field. Its aim is to evaluate the progress towards regional integration and development, and chart joint strategies for closer co-operation, deeper integration and improved prospects for growth and social welfare in the Southern African Development Community (SADC). The Forum was created jointly by the Friedrich Ebert Stiftung (FES) and the Institute for Global Dialogue (IGD), and has organised meetings and conferences as well as published documents on issues concerning regional development. In view of the diverse levels of commitment and achievements, providing region-wide forums is important for facilitating an exchange of views and allowing voices to be heard from across the SADC region.

The current year – 2008 – witnesses the establishment of the free trade area (FTA) in SADC, which will be followed by a customs union (CU) within the next two years. These first steps of the textbook linear approach to regional integration are indeed crucial for any further progress, not only in pursuing the grand vision of an economic union in southern Africa, but also for forging partnerships with the more economically advanced entities of the world economy, be it the European Union or emerging markets of Asia.

On the eve of the formal establishment of the free trade area, we felt it proper to evaluate the region's actual achievements with the intention of deriving conclusions and recommendations for the way forward. There is concern about the significant gap between rhetorical political aspirations aimed at fast tracking deeper regional integration, and the economic realities in SADC. Problems and deficits are well known, including persisting non-tariff barriers (NTBs), cumbersome and trade-restricting rules of origin, multiple memberships of regional integration arrangements, diverse external trade policies, and national interests that undermine regional trade.

Despite these difficulties, the SADC Summit of Heads of State and Government launched the SADC FTA in August 2008. In light of this event and in recognition of the various challenges facing the regional integration agenda, IGD and FES hosted SAFT V ahead of the high profile meeting and the SADC Summit, intending to present comments and recommendations at an opportune time. We are driven by the concern that, irrespective of formal progress in the stages of integration, the absence of tangible benefits will undermine the interests in, or the enthusiasm for, regional integration.

The participants made a case for a paradigm shift away from a simple trade-based and market-led perspective of regional integration, with its emphasis on the abolition of tariff

## ■ Preface

barriers. The Regional Indicative Strategic Development Plan (RISDP) should not be considered sacrosanct, but be revised, in particular the trade component that is underpinned by an unrealistic integration schedule. It became obvious that the problems besetting the FTA cannot be passed onto the envisaged CU. The regional agenda should instead address supply-side constraints and the high costs of trade and services in the region.

This volume presents the papers presented at the conference in order to make them available to a broader public. They merit wide recognition as they shed light on the deficits and lacunas not merely of the FTA, but the general approach and time frame of the integration process. We thank the authors for these contributions, which we hope will add to a profound review of the current situation and the prospects for regional integration in SADC.

Peter Oesterdiekhoff  
Friedrich-Ebert-Stiftung, Angola Office

# Communiqué

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*The Southern African Forum on Trade (SAFT) provides a platform for critical debate and reflection on trade-related matters in the Southern African Development Community (SADC), bringing together from the region academics, activists, policymakers, and senior officials working in the field. The 5th SAFT meeting was convened in Tshwane, South Africa from 6–7 August 2008. Its aim was to explore the implementation challenges for the SADC free trade area (FTA), which will be launched by the Heads of State at their August 2008 summit, as well as the broader road towards a CU in 2010. Participants and panellists from the region shared their views and perspectives on where SADC is heading, and what the future holds for the region's citizens. The following is a broad reflection of concerns and challenges raised by SAFT.*

## Implementation of the SADC Trade Protocol and FTA

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Intra-regional liberalisation in SADC has generally been cautious. Member states have delayed or back-loaded their adjustment in order to protect domestic industries and maintain revenue streams from custom duties. The role of private sector organisations in the negotiation process has also been weak. There appears to be a major disjuncture between the political rhetoric in support of deeper integration and the actual situation on the ground. Nonetheless, as the Trade Protocol (TP) does not require that all the conditions are met, the FTA will be proclaimed irrespective of readiness by some SADC member states.

## Trade facilitation in SADC

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Levels of intra-SADC trade remain low for most member states and have increased only slightly during the tariff phase-down period of the SADC TP. Moreover, most of intra-SADC trade still takes place under alternative legal arrangements (SACU, COMESA, bilateral trade agreements). The removal of internal tariff barriers under the new FTA alone is unlikely to have a major impact on intra-SADC trade. Trade liberalisation as a catalyst for increased intra-regional trade in SADC needs to be complemented by less cumbersome Rules of Origin (RoO) and enhanced trade facilitation. Exporters in the region face considerable technical constraints, and the cost of doing business is prohibitively high.<sup>1</sup> SADC member states should invest more in new (and speed up rehabilitation of existing) transport and communication infrastructure. Agreements to reduce NTBs, and streamline and harmonise policy, regulatory and rules frameworks, should be implemented without delay.

## Deepening regional integration

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Harmonised domestic policy and regulatory frameworks are prerequisites for meaningful regional liberalisation of trade in goods and services. Domestic rules of the game, governance policies and regulatory reform of the service sectors currently lag behind actual market liberalisation. Since an efficient services sector will enhance domestic and regional competitiveness, regional services markets need to be strategically and selectively opened to external trading partners.<sup>2</sup> However, liberalisation should not compromise the right to regulate in the public interest, to ensure affordable access to essential social services.

## The role of external partners in SADC

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The Interim Economic Partnership Agreements (IEPAs) with the European Union (EU) were finalised in a rush and reflect the considerable economic pressures facing commodity- and preference-dependent SADC countries. The IEPA negotiations exposed major divisions and fractures in the SADC regional integration project. SADC split into different configurations, each with its own separate liberalisation schedule. The current situation is incompatible with a SADC CU in 2010, which requires a common external tariff (CET). Even under the FTA, separate liberalisation schedules with SADC's main external trading partner could undermine SADC trade integration, as robust RoO and internal customs controls would have to be maintained.

SADC also needs to manage better its growing relations with new actors, such as China and India, to ensure genuine developmental outcomes (and not simply resource extraction).

## The SADC customs union (CU)

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The launch of the FTA is a step towards the CU. Although the Ministerial Task Team identified several options or models for establishing the SADC CU, insufficient time remains to meet the preconditions necessary for a successful launch in 2010. The region would be better served by focusing on deepening trade facilitation instead of pushing for a CU in 2010, a move that has no real intra-regional trade benefit.

Moreover, there can be no CU without agreement on a number of fundamental issues. The most critical factors are: establishing a common objective and rationale for the CU and its external tariff regime; common trade and industrial policies; a framework for customs revenue management and administration of the CU institutions; and the willingness of member states to relinquish or compromise on some aspects of national sovereignty. The issue of overlapping memberships must also be addressed, as it is technically impossible for member states to belong to more than one CU.

## The SADC Secretariat

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The SADC Secretariat needs more human, financial, and technical capacity to be able to fulfil its mandate satisfactorily. The secretariat must act as an 'engine room' to drive and support regional integration processes.

## Financing for development in SADC

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Development finance institutions, such as the African Development Bank (ADB), the Development Bank of Southern Africa (DBSA) and others, have played a constructive role in supporting deeper regional integration in SADC. This includes support for private sector development, cross-border infrastructure projects, and post-conflict reconstruction and development. The major challenge for SADC is not the absence of resources to finance development projects but rather the inadequacy of bankable and packaged projects (eg, one-stop border posts, etc). Different national regulations and procedures, as well as donor modalities, also impede cross-border projects. The case for greater regulatory harmonisation in the region is therefore compelling.

## Poverty reduction and social adjustment in SADC

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Poverty reduction should be at the heart of the regional integration imperative in SADC. Social mechanisms must underpin liberalisation, particularly to protect vulnerable groups (eg, the poor, women, youths, small traders, workers) from the more pernicious effects of opening up of trade. Regional liberalisation, whether under the SADC FTA or with external partners such as the EU, China or India, is likely to generate some socioeconomic dislocation and adjustment. While liberalisation may also create economic opportunities for some vulnerable groups, this process must be managed in a more socially-responsive manner.

## Two key challenges

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There is the need for a paradigm shift in SADC, away from a simple trade-based and market-led perspective of regional integration. The Regional Indicative Strategic Development Plan (RISDP) should be reviewed and reformed, particularly the trade component with its emphasis on unrealistic integration milestones (eg, CU in 2010). The regional agenda should be refocused to support sustainable production capacity, and address supply-side constraints and the high costs of trade and services in the region.

1. In the immediate future, SADC member states should prioritise the consolidation of the FTA, strengthen the trade facilitation agenda, liberalise stringent RoO, and improve co-operation (such as in infrastructure and regulation). Given the limited time remaining until 2010, an alternative approach to a CU could be an enhanced FTA, which is more realistic and provides more scope for trade creation than a CU.

## Endnotes

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1. World Bank data show that it takes on average 91 days to comply with all trading requirements for intra-regional SADC trade, compared with 53 to 60 days for trade between SADC and countries of the Organisation for Economic Co-operation and Development (OECD).
2. SADC is in the process of liberalising six services sectors within the region: construction, communication, transport, energy, tourism and finance.



# Implementation challenges for the SADC FTA: tariff and non-tariff barriers

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*Evangelista Mudzonga*

**T**he Southern African Development Community (SADC), a regional economic and trading bloc, seeks to achieve broad economic growth and development, and integration into the world economy, through trade liberalisation. However many challenges need to be addressed to ensure these goals are achieved.

This chapter looks at the implementation challenges for the SADC FTA. It provides an overview of the SADC TP and the progress made in implementation. The final section looks at the challenges SADC countries face in the implementation of the TP and offers some recommendations.

## SADC Framework for Integration

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SADC is a regional configuration of 15 countries: Angola, Botswana, Democratic Republic of Congo (DRC), Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. SADC's regional co-operation and integration is based on historic, economic, political, social and cultural factors.

Regional integration will bring economic growth and development, poverty alleviation, an enhanced standard and quality of life, and support for the socially disadvantaged people of southern Africa. The region will achieve its goals through implementing the SADC TP, which seeks to promote the liberalisation of intra-SADC trade in goods and services, based on fair, mutually equitable, and beneficial trade arrangements. It is complemented by protocols in other areas such as investment promotion and industrial development (Nhara 2003).

The central aim of article 2 of the TP is the establishment of a FTA. The FTA is the second stage of the region's integration agenda and will be officially launched at the SADC Summit in August 2008. In a linear integration model, a FTA is a prerequisite of a CU, although the East African Community (EAC) chose both a free trade area and a CU. The Regional Indicative Strategic Development Programme (RISDP) envisages the establishment of a CU in 2010, a common market by 2015, a monetary union by 2016 and a regional central bank with a common currency by 2018.

## *The SADC TP*

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The SADC TP was signed in 1996 and came into effect in 2000. The protocol's provisions include:

- ◆ elimination of intra-SADC trade barriers
- ◆ harmonisation of customs procedures
- ◆ trade laws and principles
- ◆ trade defence instruments
- ◆ trade related issues
- ◆ intellectual property rights
- ◆ competition policy
- ◆ dispute settlement provisions

The protocol's main objective is to phase out tariffs and NTBs over eight years. SADC plans to make 85 per cent of all intra-trade duty-free by 2008 and liberalise the remaining 15 per cent in 2012 when a full duty-free trade area will come into being.

The protocol allows for asymmetrical tariff reductions among SADC member states. Two preferential SADC offers were made: the SACU offer (South Africa and the BLNS countries - Botswana, Lesotho, Namibia and Swaziland), and the differentiated offer for the rest of SADC (excluding South Africa and the BLNS countries). The SACU offer phases out tariffs more gradually, which means that the rest of SADC member states will liberalise faster amongst themselves than with SACU. The SADC FTA requires member states to observe the RoO, which define where a product originates in the region.

## *Tariff phase-out*

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SADC member states identified four categories of trade tariffs:

*Category A: immediate liberalisation.* Tariffs on these products will be reduced to zero in the first year of implementation.

*Category B: gradual liberalisation.* Tariffs on these goods will reduce gradually to zero over the eight-year period, as these goods constitute significant sources of customs revenue.

*Category C: sensitive products.* Tariffs on these goods are to be eliminated between 2008 and 2012. Category C is limited to a maximum of 15 per cent of each member's intra-SADC merchandise trade.

*Category E: goods that can be exempted.* These goods are exempt under articles 9 and 10 of the protocol and their tariffs will not be touched or reduced to zero. Examples of goods that benefit from preferential treatment are firearms and ammunitions.

The special requirement is that most trade should be duty free and that 85 per cent of intra-SADC trade fall into categories A and B.

## Progress in implementing SADC TP

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SADC countries in general adopted a cautious approach to intra-regional trade liberalisation, wanting to continue protecting existing domestic industries and fearing losing tariff revenue. Unfortunately, the slow phase-down of tariffs gave countries the space to maintain protection, especially for goods that have the greatest potential to promote cross-border trade, such as tobacco, furniture, leather, beverages, and foodstuffs (Kalenga 2004).

SACU countries offered most sectors for immediate liberalisation, but applied longer periods to certain products from South Africa's key industrial sectors such as clothing, machinery and vehicles.

Member states back-loaded their tariff reductions by spreading the adjustment costs towards the end of the final phase. Non-SACU members who heavily back-loaded will experience a decline in tariff revenue when they eliminate tariffs on more than 50 per cent of their products in one year. The reduction in revenue is expected to be less than five per cent of total government revenue in all cases (Southern African Trade Hub 2008). However, this may be true in theory only, as when Zambia joined the Common Market for Eastern and Southern Africa (COMESA), revenue increased because of higher value-added tax revenue returns and better compliance.

A study by SADC (2007) on the implementation of the protocol found that:

- ◆ When the TP concludes in 2012, some countries will retain a wide range of permanent exclusions on imports from South Africa.
- ◆ Four member states are behind in implementing their tariff phase-down schedule and in some cases the reductions made are less than initially scheduled (Malawi, Tanzania, Zambia and Zimbabwe).
- ◆ Malawi made has not implemented any tariff reductions apart from two (one in 2001 and one in 2004).
- ◆ Mozambique and Tanzania approved their tariff phase-down programmes, but have not yet implemented them in accordance with the agreed timetable.

The study clearly showed that some member states have not implemented the tariff offers as planned. Although member states gazetted their tariff phase-down schedules, they delayed implementation due to various reasons. Apart from Mauritius and Zimbabwe, who updated a small number of products, most member states have not revised their tariff offers for sensitive products. SADC reports that currently only Malawi is behind in its tariff phase-down schedule.

The study also revealed that after some member states unilaterally reduced tariffs, several most favoured nation (MFN) rates are now lower than SADC-applied rates. Furthermore, countries belonging to other CUs have implemented tariffs on SADC imports, regardless of commitments made under the SADC TP. For example, Tanzania gave concessions to Kenya and Uganda upon joining the East African Community (EAC) and implementing the CET.

The audit carried out by Southern African Trade Hub (2008) showed that outside SACU, most of the intra-SADC trade takes place under either COMESA or bilateral agreements. The increase in trade between non-SACU members and South Africa has been very modest, except for the recent increase in apparel exports from Mauritius following the removal of the SACU tariffs.

The audit also found that SADC members were implementing all or most of the SADC trade facilitation instruments. However, important instruments, such as those governing transit trades and bond guarantees, are still at the pilot stage and have yet to be rolled out to the region. Their implementation will enable member states to maximise the benefits of establishing an FTA.

SACU has given some SADC member states preferential access for certain textile products through more liberal RoO, but other members are denied the same access (Southern African Trade Hub 2008). The MMTZ-SACU market access arrangement is an asymmetric trade agreement between Malawi, Mozambique, Tanzania and Zambia, and SACU that was approved in August 2001 and extended to December 2009. Eligible textile products from SADC least developed countries (LDCs) have more lenient access to SACU than similar products originating from non-LDCs such as Zimbabwe and Mauritius.

The table below summarises the status of tariff phase-down by member countries. According to SADC, of the 12 countries implementing the tariff phase-downs, only Malawi is behind. Angola and the DRC have asked for more time and are not yet participating.

**Table 1: Progress in implementing SADC tariff phase-down schedules**

Country	Description of progress in implementing tariff phase-down
Angola	Not yet participating
Madagascar	Acceded in 2004 required to meet the target of 85% of trade at 0% tariff by 2012
Malawi	Has only implemented two reductions, in 2001 and 2004 (implemented in 2007); high probability of not meeting the 2008 FTA deadline.
Mauritius	On course for FTA, but has introduced specific duties in place of <i>ad valorem</i> for some sensitive products (category C).
Mozambique	Gazetted whole schedule and is on course for FTA, but needs to deal with certain applied rates that are higher than originally offered (the result of unilateral MFN tariff reductions).
SACU	Implemented all 2008 commitments
Tanzania	Has complied, but introduced complications with a 2% levy on goods into Zanzibar
Zambia	Implemented reductions for 2008, on course for FTA
Zimbabwe	Implemented general offer (to South Africa) and differential offer (to all SADC countries except South Africa) in 2008. Some mistakes were made, which still need to be corrected, but on course for FTA

Source: ECA (2008), compiled from report by the Services Group and BIDPA interviews with SADC secretariat staff.

## NTBs

A trade barrier is defined as any restriction imposed on the free flow of trade (Gupta 1997) and can be both a tariff and NTB. Tariff barriers are the levy of ordinary customs duties within the binding commitments undertaken by the concerned country. NTBs can take various forms and can be broadly categorised as:

- ◆ import policy barriers
- ◆ standards, testing, labelling and certification requirements
- ◆ anti-dumping and countervailing measures
- ◆ export subsidies and domestic support
- ◆ government procurement
- ◆ services barriers
- ◆ lack of adequate protection to intellectual property rights, and
- ◆ other barriers.

Trade liberalisation by SADC has made the flow of goods between countries easier and economically more rewarding, but NTBs continue to be a concern. Hansohm et al (2006) argue that the outlook for NTBs is gloomy. They contend that during the process of trade liberalisation and tariff reform in the region, NTBs have become less identifiable, more arbitrary, qualitative and non-transparent.

NTBs include RoO, which in SADC are overly complex and contain many restrictions. They discourage intra-regional trade by undermining smooth trade facilitation and restricting firms' flexibility to source those inputs needed to be internationally competitive. Complicated and restrictive RoO increase administrative costs and make it difficult for exporters to take advantage of SADC preferences. As such, they constitute a serious obstacle to the liberalisation of intra-regional trade (Khandelwal 2004).

By early 2004, only SACU and Zimbabwe had formally gazetted the revised RoO approved in August 2002; however, most member states are implementing the rules by default (TSG 2004:7 quoted in Hansohm et al 2006).

Other NTBs that impede trade in the region include: communication problems; transport problems; lack of market information; services barriers such as financial, electricity, technical support; and standards and certification or technical restrictions. Transit costs and delays are significant, particularly for landlocked member countries. And some member states even impose stringent visa conditions on nationals from other SADC member states.

The 2007 World Bank (WB) cost of doing business indicators and the 2006 Global Competitiveness Report (DNA 2006) found trade facilitation barriers to be substantially higher in SADC than in all other regions. For example, to comply with import and export procedures takes on average 49,5 and 41 days respectively in SADC (and more than 60 days in five SADC member countries). The best performing economy is Mauritius where complying with all export and import requirements takes only 16 days (DNA 2006). Compliance takes on average 91 days for intra-SADC trade, compared to 53–60 days for trade between SADC and OECD. In addition, transportation costs in the SADC region are higher than in other regions, and compared to the world average port and air infrastructure is relatively poor in most SADC member states.

SADC member states agreed to eliminate core NTBs such as: burdensome customs procedures and documentation; import and export licensing/permits; import and export quotas; and unnecessary import bans/prohibitions. They also called for the gradual elimination of charges not defined as import or export duties, for example: restrictive single channel marketing, prohibitive transit charges, cumbersome visa requirements, and restrictive technical regulations.

SADC member states have also committed to removing technical barriers to trade and to implementing new RoO and sanitary and phyto-sanitary measures (SPS) (Hansohm et al 2006).

Member countries have begun implementing most of the SADC trade facilitation instruments. However, there is a lack of capacity and equipment to administer these agreements at many borders, and a lack of uniformity between member states in the application of customs procedures.

## Challenges in the implementation

To date the implementation of the SADC TP has not been smooth. Highlighted below are some of the challenges faced, which need to be addressed if the region really wants to reap fruits from its integration efforts.

### *Weak enforcement mechanisms*

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The enforcement mechanisms for implementing the SADC TP are weak and do not always conform or comply with decisions taken by member states. The TP mid-term review cited a number of problems encountered during implementation:

- ◆ RoO constraints, which prevent the region from fully utilising its trade potential;
- ◆ back-loaded tariff liberalisation schedules;
- ◆ delays in gazetting the annual reductions;
- ◆ discrepancies with original negotiated offers;
- ◆ suspension of tariff reductions due to economic constraints.

At SADC Secretariat and national levels, there is weak administration capacity for policy implementation and a lack of political commitment. Regional integration efforts also suffer from policy reversals in implementing harmonisation provisions, multiple and conflicting objectives of overlapping regional arrangements, and limited administrative resources (Iqbal and Khan 1997 quoted in Khandelwal 2004).

### *Multiple memberships*

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Some SADC members belong to one or more of the regional grouping, such as COMESA, EAC, and SACU. Multiple membership fees are expensive to pay and maintain. There are also administrative costs related to the often complex RoO (Khandelwal 2004).

The conflicting goals of overlapping regional memberships are likely to undermine the TP's potential benefits. This challenge was pertinent even in the EPA negotiations that threaten the SADC trade agenda. Multiple memberships will become a problem when the regional economic communities move to a CU. SADC member states such as Madagascar, Malawi, Mauritius, Zambia and Zimbabwe, which may become COMESA CU members, must decide by December 2008 on mechanisms for relating with the rest of SADC members.

### *Loss of revenue*

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This has always been a concern, especially for those member states that depend on tariff revenues for a large portion of government revenue. The level and extent of dependency on customs revenue varies in the region. Based on 2005 data, South Africa's dependency is 2,9 per cent, compared to Angola at 5,9 per cent and Lesotho at 42,9 per cent. For most SADC members, revenue from trade taxes represents at least 10 per cent of total government revenue. Past experience suggests that African countries have very limited success in replacing lost trade taxes with revenue from other sources (Khandelwal 2004). Countries such as Malawi, Mozambique and Zambia who have back-loaded their tariff reductions are likely to experience a sudden drop in customs revenue.

## *NTBs*

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High cross-border trading costs in the form of inefficient customs procedures and other red tape, and poor transport and communication facilities, remain a challenge. African trade has been hindered by inadequate transport, information and communication infrastructures, which distort trade regimes and result in high transaction costs (Khandelwal 2004).

## *Human capacity*

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Failure to meet the set targets has been blamed on a lack of human capacity both at national and SADC levels. This is made worse by customs administrative problems due to multiple memberships.

## *Information Technology and Regional Integration*

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From 1996 to 2002 and 2007 respectively, migrating Harmonised System (HS) without amending offers contributed to the implementation challenges, as the original offer had to be matched with the new coding system

The use of various IT systems by various customs authorities remains a challenge (ECA 2008). While most COMESA member states use ASYCUDA, SADC member states not part of COMESA use various systems. Such variances are good evidence of non compliance.

## *Conclusion*

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If a linear model of regional integration is followed, an effectively implemented FTA will facilitate the implementation of the SADC CU. Member countries must be committed and understand that the FTA is a rule-based system that will be closely monitored. What is discussed at an inter-governmental level needs to be translated into practice.

Drastic action is required to eliminate NTBs, to converge external trade policies and to deal with border delays. The business community is particularly concerned about border delays, which could be improved through one-stop border posts.

The region also has to simplify customs procedures and RoO. Customs regulations and procedures need to be harmonised and institutional capacity increased, with a particular focus on human resources, and technical and management capacity.

Member states should publish applicable tariffs well in advance in order to help the business community in its planning. The region should also co-ordinate market information services to make information available region-wide.



## Implementation challenges for the SADC FTA: tariff and non-tariff barriers ■

The SADC region needs to implement a mechanism to monitor trade compliance, to ensure that member states implement agreed programmes. It should also look at developing compensatory mechanisms for countries that are likely to lose from trade liberalisation. The other option for ensuring sustained integration is to devise alternative means of raising state revenue.

Multiple trade agreements signed by some SADC countries are a challenge to SADC customs administrations. Therefore it is important to continue building capacity in trade analysis, particularly for those involved in trade, in order to ensure smooth flow of business.

# Preferential Rules of Origin in SADC: a general overview, and the state of play in recent negotiations

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*Eckart Naumann*

**P**referential RoO (RoO) set the local processing and administrative criteria for goods traded between preferential trade partners. These conditions identify what may be considered of local origin and hence qualify for preferential market access. RoO typically prescribe a minimum level of local processing required for products to be considered 'substantially transformed' under a given RoO regime.

RoO are often negotiated between vastly different trading partners, which have unique comparative advantages and invariably vested interests. Therefore, they are sometimes used to further protectionist interests. Restrictive RoO reduce competition in the domestic market, and undermine the regional and international competitiveness of producers in countries with poor availability of materials. They raise entry barriers to new investors and harm retailers and consumers, who are faced with higher prices and less variety, or even a complete unavailability of some final goods.

A case in point is the Free Trade Agreement (FTA) launched a short while ago by the Southern Africa Development Community (SADC). The negotiations for intra-regional RoO revealed that: the SADC FTA partners are highly diverse and often have 'conflicting' economic interests; the purpose of preferential RoO and its relationship with existing tariff regimes is at times misunderstood; and the complexity of the current RoO regime is contrary to the spirit of (and public commitment to) regional free trade as expressed by some of the political leaders within the region.

This chapter examines the reasons for RoO and the methodologies used to determine local content. After a discussion on the history and general basis of RoO and related provisions, the sectoral rules are explained and a brief overview given of the RoO governing specific sectors (textiles, fish, agricultural products and automotive products). The state of plan in recent intra-SADC RoO negotiation is then looked at together with the issues going forward that need to be addressed.

## Why RoO?

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RoO form a critical component of any preferential trading arrangement. Preferential RoO form part of a preferential trade arrangement between two or more countries. They can be

on a non-reciprocal (for example, the EU's Generalised System of Preferences) or reciprocal (for example, the South Africa–EU trade agreement) basis. Non-preferential RoO confer a simple economic nationality on traded goods. Their use is restricted mainly to the application of most favoured nation (MFN) tariffs, statistical record keeping, and imposition of other trade measures such as anti-dumping duties.

Preferential RoO confer an economic nationality on a good, but are also linked directly to the trade preferences agreed between countries. These may entail duty-free or duty-reduced trade for most or all product categories, as well as special quota preferences. By differentiating between goods produced in the exporting country and goods that are the output of a third country, RoO make the allocation of preferences possible. Otherwise, traders from third countries with less beneficial trade preferences could exploit the situation by simply channelling their goods through the customs territory of the preference-receiving country. Similarly, exporters within a preferential trade area could pass off goods sourced from third countries as locally-made products, to the detriment of all parties in a preferential trade area. This practice is commonly referred to as trade deflection, and has been one of the major concerns of SADC countries negotiating preferential trade rules over the past decade. In some instances shipping goods via another country to gain better market access to a third country may appear to make good business sense, but such a practice undermines the objectives of a preferential trade area.

Why would trade deflection take place in the absence of RoO? Differences in the tariff treatment of goods anywhere in the world create differentials in the tariff 'advantage' available to exporters under a given trade agreement. Loosely defined, a preference margin is the difference between the treatment of goods shipped under normal tariff relations and those shipped under a preferential trade area (this concept can also be expanded to quotas and other discriminating trade measures). Therefore, the higher the preference margin between countries for a given export destination, the greater the risk of trade deflection. Similarly, the larger the preference margin, the greater the opportunity cost of *not* complying with the RoO. As a result, producers would be more willing to change their production and sourcing parameters (even if less favourable commercially) in order to benefit from preferential market access. This obviously carries with it a fundamental economic cost.

## How can 'local origin' be determined?

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The RoO chapters of trade agreements employ various methodologies to determine local origin. The methodologies have their own inherent advantages and weaknesses, and are often vulnerable to the political economy and strategic interests of the contracting parties. Local origin is based on the 'wholly produced' requirements (EU agreements refer to 'wholly obtained'), where a product is completely produced (or made up) in the exporting country or undergoes 'substantial transformation' in line with specified criteria. These criteria can be based on a change in tariff-heading (CTH), a specific processing (SP) requirement or a minimum percentage of value-added (VA). Each methodology is discussed briefly below.

### *Change in tariff-heading (CTH)*

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The CTH test is based on the harmonised system (HS) nomenclature used widely to classify and record international trade flows, especially in the application of import tariffs. ‘Substantial transformation’ takes place when a product is classified under a different heading from its local or non-originating materials. In other words, processing that transforms materials into goods of another heading is considered sufficient to confer origin. The main drawback of this methodology is the different burdens imposed on different sectors and producers, as a CTH in one product sector will be different to the others. This methodology therefore raises concerns about equity and fairness if used in isolation of other methods, and does not consider the dynamics facing specific sectors. As the HS was not developed for applying RoO, the product classifications often bear little relation to the processing burden associated with the product. The CTH methodology also requires a ‘negative list’ of processes that are insufficient on their own to confer origin, in order to avoid superficial operations that otherwise comply (for example, fresh and dried vegetables are classified under different headings).

### *Specific processing (SP)*

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The SP (also referred to as the technical test) sets specific local processing requirements, and must therefore be negotiated on a line-by-line basis. The SP could be the most appropriate RoO methodology, as it allows origin requirements to be adapted in a way that adequately reflects the need for substantial transformation without excessively restricting trade. It also allows industry-specific dynamics to be reflected where appropriate. However, counting against these advantages are the possible protectionist sectoral influences, which can lead to RoO that suppress trade and thus protect the interests of incumbent domestic producers.

### *Value-added (VA)*

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While the VA methodology appears to be the simplest method of determining origin, its practical application raises a number of challenges. At a conceptual level, the VA basis appears desirable, as it sets thresholds for local VA. RoO regimes use this methodology either on its own, for example the United States Generalised System of Preferences (GSP) or the African Growth and Opportunity Act (AGOA), or with other methodologies, which is the case for the EU regime and optional in the Common Market for Eastern and Southern African (COMESA) and Economic Community of Western African States (ECOWAS). However, as various derivatives of this methodology exist, the denominator used to calculate a threshold determines how practical it is. A VA test can specify local content or maximum foreign content. One variant uses the final factory selling (or ‘ex-works’) price as the denominator, and determines local VA by measuring all local processing including mark-up against this denominator. Another option based on direct processing costs may be beneficial in certain instances, but has various administrative drawbacks as detailed below.

The VA calculations for proving compliance, particularly when based on direct processing costs only, involve a substantial administrative burden both for exporters and for customs authorities tasked with verifying origin. Detailed cost information and record keeping are required for proof of origin. Producers often have to divulge proprietary and sensitive company cost structures in order to prove origin. Another weakness of the methodology is its exposure to exogenous variables, such as unpredictable exchange rate fluctuations and commodity cycles. A weakening local currency raises the cost of imported materials, while commodity price changes may raise or lower the price of materials; the effects on local and imported material costs are mixed. VA may also be a disincentive to improving local operating efficiencies, as these cost savings will translate into lower (local) added value. Another important consideration is the variable impact of a local VA threshold on different sectors. Depending on the prevailing dynamics and costs structures, a specific threshold may translate into substantially different burdens on different sectors.

Therefore, no one RoO methodology can best serve the needs of all stakeholders involved or affected by the trade process. In fact, the drawbacks associated with each methodology are potentially significant to producers, traders and customs authorities alike.

## RoO in SADC

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### *General basis and recent history*

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The general structure of the current SADC RoO closely resembles the EU RoO model. Early proposals of a SADC RoO Protocol contained relatively simple rules: exporters had the choice of complying with a CTH or VA requirement for goods not wholly produced in the region. However, this protocol was never fully implemented and was replaced with new rules under the Amended TP. Underlying this shift in direction was the growing list of exceptions to the general RoO regime, where member states perceived the treatment applicable to specific sectors was not 'in their best interests.' This was a legitimate sentiment for some but for others it was driven by protectionist agendas.

The revised (current) RoO Protocol was finalised at the end of October 2004 and implemented with effect from 1 January 2005. Since 2005, the RoO of products in some sectors remain subject to review and negotiation among SADC members, as outlined in Section 3.

The *originally agreed* RoO were that:

- ◆ the goods must have undergone a CTH, meaning that the non-originating materials used can be classified under a different (HS four-digit) heading to that of the product;
- ◆ the value of non-originating materials must account for no more than 60 per cent of all materials used in the production of a product; or
- ◆ the local VA resulting from local processing must account for at least 35 per cent of the ex-works (factory) price of the product.

These rules closely resemble the RoO regime applicable in other African regional configurations, notably COMESA and ECOWAS.

The revised and current rules combine CTH, VA and SP methodologies, which are tailored to specific products.

Since their implementation, agreed changes have been made to the treatment of certain agricultural products, as well as some electrical/household appliances and automotive products. The textile and clothing section is particularly sensitive and no agreement had been reached as of the most recent technical meeting (July 2008).

### *Related provisions*

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SADC RoO permit 'cumulation' amongst SADC member states. Cumulation allows more than one country to fulfil jointly the relevant RoO provisions. In theory it alleviates the individual compliance burden and allows individual countries to use their complementary strengths to produce an internationally competitive product. Cumulation is possible because each cumulating party faces the same RoO for the export partner, which eliminates any incentive for trade deflection (which is, after all, the original purpose of RoO).

SADC cumulation is relatively flexible and goes beyond similar provisions in other agreements. For example in the EPAs, origin is conferred on the country where the last processing stage takes place (all the while dependent on the origin requirement having been fulfilled, if not individually then jointly). In some other protocols, notably the EU RoO, individual countries' processing have to go 'beyond insufficient operations' – referring to a list of processes that occurred individually or jointly would be insufficient to confer origin. Cumulation can enhance regional economic integration and trade, as it does not penalise producers who use materials sourced from within the region. In practice, however, the value of the cumulation provisions is limited, as countries at a similar level of economic development often suffer from similar shortages of materials and other supplies relating to variables such as availability, quality and price. Furthermore, high transportation costs and other cross-border issues continue to undermine regional trade in SADC, and, by extension, the ability of producers to benefit from cumulation.

The ability of producers to meet origin requirements is also affected by value tolerance rules, which specify a value threshold. The threshold can be expressed as a percentage of the factory selling price (or in some agreements production cost is a denominator), which may consist of non-originating materials irrespective of any specific requirements. In other words, if a RoO requires all fabric used in the production of a garment to be sourced from local (or regional because of cumulation) producers, then the general tolerance rule will nonetheless allow garment producers to use some non-originating fabric. In SADC, the value tolerance is set at 15 per cent. Two limitations apply: the general value tolerance may not undermine a specific tolerance of a product category (for example, the 15 per cent may not increase any specific non-originating materials threshold if a VA-based rule

applies to a certain heading,); and products of chapters 50–63 (textiles and clothing), 87 (automotive products) and 98 (other miscellaneous classifications) are excluded from these provisions.

### *SADC: sectoral rules – brief overview of textiles, fish, agricultural products, and automotive RoO*

As outlined earlier, the SADC RoO are closely modelled on the EU RoO regime and apply VA, CTH and SP methodologies as deemed appropriate. Since the initial implementation of the SADC RoO, negotiations on technical changes to the RoO have been ongoing.

The protectionist interest of member states continue to influence the SADC RoO negotiations, which raises some concerns about the commitment to increasing regional trade and economic integration. For example, a cotton-producing member state that insists on highly restrictive RoO for textiles and clothing made from cotton, and flexible rules for textile products made from other materials, clearly illustrates a conflicting national versus regional interest.

#### *Fish and processed fish products*

Fish and fish products are an economically important and sensitive sector in SADC. The RoO for preferential intra-regional trade are in two sections: the wholly produced rules, which specify conditions concerning the fishing vessel, and the list rules, which define the processing required for all fish categories listed in chapters 3 and 16. In effect the list rules complement the wholly produced rules, as the key product-specific requirement is that the fish must be wholly produced in the region to confer origin.

These regulations are slightly less onerous than those of the EU RoO. Intra-SADC RoO consider ‘the place of production of marine, river, or lake products and goods in relation to a Member State’ to be an extension of the vessel harvesting the fish products, provided the (fish) products are landed in the member state and certain vessel-related conditions are also fulfilled. For the purposes of the RoO, the vessel engaged in fishing activity is further defined as belonging to a SADC member state if:

- ◆ it sails under the flag of a member state;
- ◆ more than 75 per cent of the vessel’s officers and crew are nationals of a member state;
- ◆ nationals or an institution, agency, enterprise or corporation of the government of a (SADC) member state holds the majority control and equity of the vessel.

Unlike the EU RoO, there are no specific provisions for companies who lease or charter fishing vessels. However, EU rules required 50 per cent (intra-SADC 75 per cent) local crew until recently, when the revised Interim Economic Partnership Agreement (IEPA) removed this provision.

### *Agricultural products*

Unprocessed and processed agricultural products are subject to a wide range of RoO provisions, which are generally tailored to the specific dynamics and interests of each sector. Most unprocessed agricultural products are covered by the wholly produced requirement, with a small amount of leeway provided by the value tolerance provisions.

For chapter 9 (tea, coffee, spices), the rules allow non-originating content provided it does not exceed 40 per cent. Chapter 11 (products of the milling industry) offers no preferential RoO for wheat flour, meaning that even local milling (conversion from wheat to flour) is insufficient to confer origin. Likewise no preferential treatment is given to processed wheat-based products, which include most product categories in chapter 19 (food preparations of flour, including pasta, cereals and bread).

### *Textiles and clothing*

Textiles and clothing RoO generally require a large degree of local processing in order to qualify for preferential treatment. 'Substantial transformation' means two stages of processing: for articles of chapters 61 and 62 (clothing), which means that manufacture from yarn (converting yarn to fabric and fabric to garment) must be done locally; for textiles, this requires manufacture from unprocessed fibre for yarn and various categories of unprocessed yarn in the case of fabric. Various other value-adding activities such as printing and embroidery may also in certain instances confer origin, provided that the value of the unprinted fabric does not exceed 47,5 per cent of the product's ex-works price.

These RoO are generally considered to be relatively restrictive and not conducive to building regional supply linkages and expanding intra-regional trade in textiles and clothing. Other preferential trade regimes specify far simpler local processing requirements. Under AGOA, producers may source fabric from a third country and only the making-up of the garment must be done locally. The newly revised RoO contained in the SADC-EU IEPA also allows single transformation, after three decades of double transformation under the Cotonou and Lomé conventions. The current SADC RoO complement other protections provided to producers in the region, especially in SACU, where the CET remains relatively high at 40 per cent for clothing and 7,50-15 per cent for yarns and fabric.

The SADC RoO covering textiles and clothing also differentiate between member states' imports into SACU. Goods produced in the MMTZ are subject to simpler RoO provisions, based on annual quantitative limits. These goods are subject to a single transformation requirement, instead of the general two-stage processing requirement applicable to other member states. The MMTZ provisions were recently extended to 2009 (they had been extended in three to six month increments after expiring in mid-2006), but remain somewhat controversial. The revised terms and conditions of the MMTZ provisions (for special access to SACU) are:

- ◆ immediate and unconditional market access for Botswana, Lesotho, Namibia and Swaziland (BLNS) export products that are of interest to MMTZ, demonstrated by gazetting of revised tariff schedules upon date of implementation



- ◆ quotas to be adjusted to recent utilisation levels, and implemented accordingly as from 1 April 2007
- ◆ differentiated MMTZ quotas according to country (see schedule below)
- ◆ suspension of the MMTZ quotas on a differential basis should any MMTZ country not implement its counter-obligations as per the first point above
- ◆ quota increases to be considered annually upon request by the MMTZ.

**Table 2: Revised SACU quotas for MMTZ exports April 2007–December 2009**

HS Chapter	Unit	Malawi	Mozambique	Tanzania	Zambia
52 (cotton)	kg			1 000 000	1 000 000
55 (synthetics)	kg			500 000	
58	kg				
60	kg				
61 & 62 (garments)	pieces	6 000 000	1 000 000	500 000	500 000
63 (other made-up textile products)	Kg			500 000	

### *Automotive products*

Production of motor vehicles (and parts) is highly concentrated in SADC and takes place mainly in South Africa, where large global brands are produced. The heavy investment involved in setting up motor vehicle assembly operations, as well as first and second tier parts suppliers, means that incumbent producers in South Africa have an interest in reducing imports of non-established brands into South Africa and the region. In other words, RoO that require little local processing would pose a threat to the established operators, even though the economic dynamics in some member states could be more suitable for more superficial assembly operations than required by the current RoO. As a result of the sector's substantial value and investment concentrated South Africa, intra-SADC interests have largely reflected those of the private sector in South Africa and the country's industrial policy in this sector.

At present the RoO in this sector are tailored to the dynamics of the various products classified within chapter 87. For passenger vehicles (HS 8703), intra-SADC RoO require that: the value of non-originating materials does not exceed 55 per cent of the ex-works price of the product; the manufacture or assembly of the vehicle entails attaching the floor panels, body sides and roof panels to each other; and fitting to the floor panels of vehicle's chassis, the engine, transmission, axles, radiators, suspension components, steering mechanisms, braking or electrical equipment or instrumentation. For motor vehicle parts and accessories (HS 8708), the value of non-originating inputs must not exceed 50 per cent of the value of the final product.

In comparison, the IEPA rule for SADC exporters requires (in the case of passenger vehicles) that the value of non-originating materials used does not exceed 40 per cent (without further specific processing requirements); the rule is the same for parts and accessories. The rule for passenger vehicles is thus not directly comparable with the EU rule, which has a lower non-originating content threshold but is devoid of the specific local assembly requirements.

For parts and accessories, the intra-SADC rule is less onerous than the equivalent IEPA requirement.

## State of play in recent intra-SADC RoO negotiations

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The intra-SADC RoO process was long and arduous, as member states addressed the impact of the initial RoO Protocol, and consequently implemented a RoO regime tailor-made to individual products and sectors. The final outcome has been in force since early 2005 and closely resembles the structure of EU preferential RoO.

However, the process is ongoing and at the time of writing was still not concluded. Outstanding issues on the treatment of certain sectors and individual products within the RoO require further negotiation and revision. This overview is based on the issues outstanding as of June 2008, whereas some have subsequently been resolved. The issues outlined here illustrate the dynamics and challenges of agreeing preferential RoO among unequal trading partners, especially when negotiations are on a product level rather than a RoO generic framework, which is the case, amongst others, for ECOWAS and COMESA.

The outstanding items relate to the preferential treatment of intra-SADC traded goods, specifically certain agricultural products (from chapters 9 and 15), and industrial products (from chapters 39, 52–55, 60–63, 85 and 87).

### *Chapter 9: coffee, tea, maté and spices*

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The current rule applies to the entire chapter (with the exception of curry and mixtures of spices under heading HS 0910) and specifies that the use of non-originating materials is limited to 40 per cent of the weight of the product. For HS 0910 goods, materials must undergo a CTH and in addition all cloves used must be wholly produced in SADC.

The agreed revised chapter rule states that all chapter 9 materials must be wholly obtained (within SADC) although no consensus was reached on a revised rule for heading 0910. Various proposals for a revised tea and coffee rule are also on the table. Most member states are proposing an increased threshold (from 40 to 65 per cent) for non-originating materials used. However, there has been resistance from a small number of coffee-producing member states who prefer high local content thresholds. High local content requirements mean that coffee processors (roasters, blenders, marketers) are more dependent on local suppliers of raw materials. A reduced local content requirement (or an increased threshold for non-originating material) gives downstream processors greater flexibility to meet the demand for coffee products in terms of variety, quality and price.

*Chapter 15: animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal or vegetable waxes*

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The current rule for chapter 15 requires a CTH, although tailored rules are in place for six product headings (HS 1501, HS 1502, HS 1504, HS 1506, HS 1516 and HS 1517). These generally entail a wholly obtained component related to inputs of materials from chapters 2 (meat and meat products) and 3 (fish material).

For headings 1507 (soya bean oil) and 1512 (sunflower and cotton seed oil), which both currently fall under the general chapter rule, the general consensus is for a revised change in tariff sub-heading (CTSH) rule where the manufacturing process, from crude oil through a range of operations ('neutralisation with alkali, decolorising and deodorising') occurs in a single country. However, a minority of member states prefer that the current chapter rule (CTH) remain.

*HS 3916 to 3926: semi-manufactures and articles of plastics*

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The current requirements use elements of the CTH, WO and VA methodologies. All HS 3915 materials ('waste, parings and scrap of plastics') must be wholly produced (in other words, sourced locally). The threshold for non-originating materials of chapter 39 is currently set at 55 per cent (based on the product's ex-works price). All materials used must also undergo a CTH.

Member states would generally prefer to remove the wholly produced aspects of this rule, namely that any materials of HS 3915 be exclusively obtained from local sources. No agreement is in place on an appropriate maximum threshold for non-originating materials (from chapter 39 where applicable). A minority of member states favour a higher threshold for non-originating materials (from 55 to 60 per cent), while one member state will only agree to a higher threshold if its own proposal in an unrelated sector is accepted.

*Chapter 52: cotton, cotton yarns, fibres and fabrics*

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As already discussed briefly, two processing stages must take place within SADC before a good can qualify for preferential access. Current intra-SADC RoO differentiate between the various product categories within chapter 52, notably yarns and fabrics. For woven cotton fabrics (categorised under HS 5208–5212), the requirements are similar to those of the TDCA and Cotonou Agreement. However, the SADC–EC IEPA RoO Protocol substantially liberalises the fabric sector, as fabric may now be made from non-originating yarn.

The majority of member states agree to this rule that includes a proposed increase (from 47,5 to 50 per cent) in the threshold of non-originating fabric where exporters chose to fulfil the alternative RoO requirement. This relates to the option that non-originating fabric may be used provided at least printing and two value-adding activities take place locally.

A minority of member states prefer a CTH requirement for cotton fabrics, which would allow producers to use yarn from any source in the manufacture of SADC-originating fabric (a single transformation process).

### *Chapter 53: other textiles of vegetable materials*

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The current RoO require a two-stage transformation requirement. The general consensus is to maintain the two-step transformation but to raise the non-originating fabric thresholds (where applicable) from 47,5 to 50 per cent. Despite this general consensus, various member states favour a CTH requirement for headings 5309–5311 (woven fabrics of other vegetable textile fibres), which, if agreed to, would allow producers to source yarn instead of the current requirement for inter alia natural fibres to be further processed into yarn and fabric.

### *Chapter 54: man-made filaments*

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The existing RoO are the same as those spelt out under chapters 52 and 53 above. The current rules still require two-stage processing with a slight amendment to the threshold of non-originating materials. Again, the outstanding issues concern the treatment of fabrics, in this case woven fabrics of man-made filament yarn (HS 5407–5408). While the majority of countries prefer that the rules remain essentially unchanged, the same countries that favour a CTH requirement for the previous chapter would also like one for this chapter. This would in effect mean single stage transformation, since yarns and fabrics are classified under different headings.

### *Chapter 55: man-made staple fibres*

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Similarly for chapter 55, the unresolved issues concern headings 5512–5516 (woven fabrics of man-made staple fibres). Again, the proposed amendments are the same as for fabric in other chapters, with a small number of countries favouring a CTH instead.

### *Chapter 60: knitted or crocheted fabrics*

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Chapter 60 currently requires manufacture from either natural fibres, man made staple fibres (not carded or combed or otherwise processed for spinning), chemical materials, or textile pulp. This entails two local transformation stages: converting the fibre to yarn, and then yarn to cloth. It matches the RoO contained in the TDCA, and previously under the Cotonou Partnership Agreement (CPA). There is no consensus on revising the rules in this sector.

Member states continue to have significantly divergent positions on which rules should replace the current requirements. Those member states with significant garment production

but little upstream processing favour a simple CTH conversion applicable to the entire chapter, which would mean yarn could be sourced from anywhere, and made up (knitted or crocheted) locally into fabric. This is in effect the rule that has been agreed in the SADC-EC IEPA RoO. Two member states favour a CTH for the whole chapter, but with product-specific exclusions where cotton-based inputs are used. The objective of maintaining a double stage requirement is to protect domestic cotton growers and highlights the continued protectionist sentiment within the region.

### *Chapter 61: clothing, knitted or crocheted*

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Revising the current double transformation requirement remains the most controversial for chapters 61 and 62. The two-stage transformation requirement ('manufacture from yarn') requires that the making up of the garment and the manufacture of the fabric be undertaken locally or within the region. It supposedly creates a downstream market for SADC textile producers. However, in the absence of an internationally competitive and diverse regional textile sector, it restricts clothing manufacturers to limited sources of supply.

There is some agreement among member states that the rule for chapter 61 should change to a CTH processing requirement, which would allow clothing manufacturers to source fabric from anywhere in the world (textiles are classified in chapters 50-60). The wording of this rule may still be changed (for example manufacture from fabric) in order to avoid a narrow definition of CTH where goods from a clothing chapter could be imported and transformed only slightly in order to qualify for re-classification under a different heading (of the same chapter).

At this stage, two SACU member states are in favour of a double stage requirement ('manufacture from yarn'). South Africa, as the only country in SADC with substantial clothing and textile production facilities, is predictably split on this issue: the clothing sector favours a single transformation CTH rule, while the textile sector is strongly in favour of the current two-stage requirement.

One other SADC country, a producer of cotton, favours a highly differentiated rule with CTH as a basic requirement for the chapter. In addition, essentially all cotton-based garments (25 proposed tariff lines at the HS6 level), would require two-stage processing (manufacture from yarn or local production of fabric). Further negotiations are needed to resolve the opposing positions, especially in view of the relationship between the current RoO regime and import tariffs in this sector. High duties (as is the case in some member states, for example SACU) and liberal RoO appear somewhat incompatible.

### *Chapter 62: clothing, not knitted or crocheted*

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The current rule requires 'manufacture from yarn' (a double transformation, as in chapter 61) or 'manufacture from unembroidered fabric provided the value of (non-originating)

unembroidered fabric used does not exceed 40 per cent of the ex-works price of the product'. No consensus has been reached among the member states.

The proposals on the table range from continuing with the status quo (two-stage transformation 'manufacture from yarn') to switching to CTH for the whole chapter (which would translate into single transformation). Some countries propose double transformation with selective CTH rules applied to certain headings. One member state proposes CTH except for 25 cotton-based sub-headings (for example for HS 6203.42: 'trousers made of cotton'), similar to what is proposed for chapter 61. Another favours CTH for a time-limited period for chapters 61–63, to allow for recapitalisation of the industry, followed by a switch back to double transformation! This last proposal seems completely incompatible with business realities and the dynamics in this sector, and would certainly not encourage business investors to set up or extend their operations in the long term.

### *Chapter 63: other made-up textile articles*

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Chapter 63 covers a wide range of textile products, including blankets, curtains, sacks and bags, textile camping goods and worn clothing, which poses some challenges for RoO. Any chapter rule will necessarily impose substantially different obligations on producers of the various product sub-sectors.

There is general agreement on revised rules for this chapter, with the requirements loosely translating into a double stage transformation rule. However, some countries have submitted proposals based on the CTH rule. One non-SACU member state proposes CTH except for eight tariff lines made up of cotton inputs, which would be 'double stage ... manufacture from yarn'. This proposal is somewhat unclear as most of the tariff lines listed, for example 6301.30 (blankets made of cotton), 6302.21 (bed linen of cotton) and 6302.51 (table linen of cotton), are items for which 'manufacture from yarn' is in effect single stage transformation, not double transformation. Perhaps what was meant was transformation from 'unbleached single yarn', and any anomalies within this proposal are likely to be ironed out during the ongoing reform process.

### *Chapter 85: electrical equipment and parts*

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The current requirements are based mainly on the VA methodology, with specific thresholds on the value of non-originating materials. The current baseline rule ('ex-chapter 85') allows non-originating materials of up to 60 per cent of the ex-works price of the product. For the other tariff lines, the maximum non-originating content thresholds range from 45 to 65 per cent of ex-works. However, special rules apply to HS 8528 (electronic receivers/circuit boards) and HS 8544 (insulated wire and cable), where the former must be made up of knocked-down components and include the mounting of components on unpopulated circuit boards, while the latter has a supplementary rule (to the VA requirement) that all copper used must be wholly produced. This avoids 'substantial transformation', and hence

preferential treatment, of imported wire using subsequent coating/insulation to confer origin.

While there is general consensus on the chapter rule, RoO for individual tariff lines remain unresolved and subject to further negotiation. One proposal being considered is to lower the non-originating content threshold from 65 to 60 per cent for HS 8504 (electrical transformers) and HS 8536 (electrical switching apparatus), while another looks at increasing the non-originating materials threshold from 60 to 65 per cent for HS 8544 (insulated wire). Another issue concerns the use of metallic conductors within HS 8544: the current requirement is that no more than 60 per cent non-originating content may be used, and yet metallic conductors of the same heading are allowed. One proposal seeks to exclude the value of non-originating metallic conductors (such as cables and wires) from counting towards the non-originating materials threshold.

### *Chapter 87: motor vehicles and parts*

The automotive sector, like the textiles and clothing sector, is considered particularly sensitive. While clothing production (textiles less so) is widely dispersed in SADC, the automotive sector is predominantly located in South Africa. Some countries, such as Botswana (part of SACU), have attracted investment in assembly operations, where semi knock down (SKD) kits are assembled locally, to supply the domestic and regional (especially South African) market. As a result of the substantial value and concentration of investment within this sector in South Africa, the intra-SADC RoO reflect the South African private sector's interests and more generally the country's industrial policy in this sector. South Africa's Motor Industry Development Programme (MIDP), which rewards exporters, has resulted in much of the foreign direct investment (FDI) and production in South Africa, as well the large export programme. A replacement World Trade Organisation (WTO) compatible scheme was recently agreed to.

Current intra-SADC RoO are tailored to different products within chapter 87. For passenger vehicles (HS 8703): the value of non-originating materials must not exceed 55 per cent of the ex-works price of the product; the manufacture or assembly of the vehicle must entail attaching the floor panels, body sides and roof panels to each other; and the engine, transmission, axles, radiators, suspension components, steering mechanisms, braking or electrical equipment or instrumentation must be fitted to the floor panels or chassis frame of the vehicle.

The reforms proposed are limited and essentially seek to extend the general chapter rule (manufacture where the value of non-originating materials does not exceed 60 per cent ex-works) to all products from HS 8701.20 to HS 8706, supported by a proposed new 'note' under the Introductory Notes of this Protocol. This 'note' essentially reflects the specific requirements that are still under the product headings HS 8701.20 to HS 8706. One proposal seeks to increase the maximum threshold for non-originating content from 60 to 65 per cent for the products above.

## Conclusion

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RoO are often blamed for the low volumes of intra-regional trade within the SADC area, and for making the region less attractive to new investment. Increasingly traders and investors are viewing the SADC market as a whole, rather than confining themselves to a particular national market. Therefore, the specifics of intra-regional RoO are closely linked to trade developments and regional economic integration.

SADC RoO are closely modelled on the EU RoO regime. The RoO are tailored (or product- and sector-specific) rather than 'global,' as is the case in other regimes on the African continent and elsewhere. SADC initially pursued a global approach but changed to a tailored one because of the large number of exceptions proposed by member states. It is important to remember that the available RoO methodologies each have substantial weaknesses, and that a global approach would impose completely different 'local transformation' burdens to different sectors. A particularly important sensitive sector may require some form of protection, which is one 'advantage' of the tailored approach. This advantage is also sometimes seen as one of the main weaknesses of product-specific RoO, as it invariably allows forms of protectionism to find their way into the agreed RoO, which clearly go beyond what might be necessary to confer local origin through substantial (local) transformation.

The SADC RoO are broadly acceptable as they do not hinder trade, and require a reasonable level of local processing. However, there are numerous exceptions, notably the requirements applicable to the textile and clothing sectors, automotives and some agricultural products (for example processed wheat-based products). These rules are restrictive, go beyond what may reasonably be considered sufficient to confer origin, and undermine regional trade and opportunities for new investment in the region. Some of the stipulated requirements may be based on valid reasons even though they appear to run counter to the objective of regional trade and economic integration. For example, would liberalising the clothing rules (double transformation) bring greater economic benefits to the region than the current restrictive approach, especially if a key incentive for using locally produced fabrics (for further processing into qualifying garments) were thus be destroyed? Would a relaxation of the motor vehicle RoO be advantageous to the region as a whole if it substantially undermines the massive investments that have taken place in the South African automotive sector? Would a RoO that allows the milling industry to use non-originating wheat be advantageous to the region as a whole (especially when regional demand is said to exceed regional supply)? The answers to these and other questions are not altogether certain and their implications are at best difficult to quantify.

A key challenge to resolving the outstanding RoO issues, and evolving and overhauling the SADC RoO regime in the future, is defining clear regional trade and economic integration policy objectives. If greater regional trade is an objective in itself without a development dimension, then RoO should confer origin based on the lowest possible local transformation requirement. Low local processing thresholds may encourage greater trade but may also carry a high opportunity cost by undermining incumbent producers who are pitted against competing products that may have enjoyed protective markets elsewhere. For example,



allowing a single transformation rule for clothing would expose local textile producers to competition from foreign fabric producers that may have been operating in a highly protected and possibly government-subsidised production environment. Issues such as these highlight some of the challenges faced by policy makers in dealing with RoO issues, especially within a sector as sensitive as the textile and clothing one. In this instance, global value chains and industry dynamics dictate that producers will not be internationally competitive if their sourcing decisions are undermined by complex and restrictive RoO, particularly in the absence of competitive local fabric suppliers.

Similar sensitivities exist in the automotive sector. The current rules are heavily influenced by the situation in South Africa, the region's only major producers of motor vehicles. Already heavily supported by the MIDP, which gives exporters generous duty rebates, the SADC RoO have further entrenched the country's dominant position within this sector. A complex local manufacturing infrastructure is required to comply with the present RoO regulations. Simplifying the RoO would reduce the local processing burden and may even attract foreign investors. What is needed is to analyse carefully the opportunity cost of current production and the incentives provided to the sector against the benefits that might flow from a more liberal regime.

The SADC RoO compatibility with other preferential trade regimes must also be part of any future discussions. Again, the textile and clothing sector may serve as a useful example. Under preferential trade regimes such as AGOA and more recently the RoO of the IEPAs, clothing producers are able to align their sourcing strategies to the demands of international clients. However, the SADC RoO restricts these producers to local suppliers, which complicates production decisions and weakens their ability to be internationally competitive. While understandable, the absence of a WTO binding standard on preferential RoO does not help and continues to undermine any reasonable hope for consistency between different RoO regimes. This is further complicated by the complex relationship between the external tariff regimes that prevails in the region. Flexible RoO that permit minimal processing would clearly undermine high tariffs in a particular sector. Therefore, a revision of the protection given to key sectors will assist policy makers in dealing with revising the applicable RoO. These interrelated tasks are complex and should be guided by regional trade and industrial policy prerogatives, which still appear to be largely absent in SADC.

# Regional infrastructural and trade facilitation challenges in Eastern and Southern Africa: Aid for Trade solutions (North–South Corridor)

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*Mark Pearson*

Infrastructure development initiatives can help Africa reduce trade costs between countries in the region and with the rest of the world. Trade-related infrastructure is financed by development banks, other international financing organisations, donors, and governments themselves. The types of financing include grant funds, national budget allocations (both from recurrent and capital budgets) and concessionary financing. Instruments used include public–private partnerships (PPPs) (when the return on investment is sufficient to make the investment attractive to the private sector and the investment can be ‘ring-fenced’), sector budget support, general budget support, grant financing and concessionary loans through a project and tied aid.

The chapter opens with an overview of the importance of upgrading trade-related infrastructure and the role that Aid for Trade can play. It examines at a regional level, the north–south corridor as a pilot infrastructure project and the trade facilitation measures in place. The final section looks at the regional infrastructure and trade facilitation challenges in eastern and southern Africa and the issues that need to be addressed.

## Upgrading Trade Infrastructure

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Improving the trade infrastructure in sub-Saharan Africa (SSA), with the ultimate aim of reducing the costs of cross-border trade in Africa, ties in with the growing interest in Aid for Trade. The World Trade Organisation (WTO) Aid for Trade task force concluded, in mid-2006, that additional, predictable, sustainable and effective financing is fundamental for fulfilling the Aid for Trade mandate agreed at the WTO ministerial meeting held in Hong Kong in December 2005. Aid for Trade is guided by the Paris declaration on aid effectiveness and is defined in broad terms. The WTO task force recommended that all projects and programmes be considered as Aid for Trade if they are identified as trade-related development priorities in the recipient country’s national development strategies. It distinguished five different categories of Aid for Trade. The first two, trade policy regulation and trade development, were already covered under programmes such as the Integrated Framework (IF) for least developed countries (LDCs) and the Joint Integrated Technical Assistance Programme (JITAP). The other three identified were: building productive capacity, trade-related infrastructure, and trade-related adjustment.

The expanding global economy has resulted in increased economic growth for many countries. However, compared to other developing country regions, SSA has not taken significant advantage of either the increased economic growth or the renewed interest in trade-related infrastructure. A common finding of many comparative studies of growth and development experiences, is that the trade in goods as a percentage of GDP (sum of merchandise exports and imports divided by GDP) is relatively high in Asian countries compared to SSA countries (Asian Development Bank 2006).

In general, Asian countries have large domestic markets, which allow infant industries to attain significant economies of scale before venturing into export markets. Most SSA countries, on the other hand, have relatively small populations with low purchasing power, which means infant industries cannot grow big enough to benefit from economies of scale before starting to export. In these circumstances a sensible industrial strategy would be to view the regional market as a domestic market; only once an industry has grown to a reasonable size in the region, would it consider competing internationally.

There are four Regional Trading Arrangements (RTAs) in the eastern and southern African region<sup>1</sup>: the Common Market for Eastern and Southern Africa (COMESA), the East African Community (EAC), the Southern Africa Development Community (SADC) and the Southern African CU (SACU – a sub-set of SADC). However, with the possible exception of SACU in some transactions, none of them represent a true single market for any of their industries. Although EAC has declared itself a CU and COMESA plans to launch its CU in December 2008, the manner in which these RTAs are administered means that regional industries will have to wait some time for a single customs territory where goods and labour move freely. A similar liberalised environment for regional trade in services is even more of a challenge.

A trade and a non-trade response is needed if smaller and LDCs in SSA are to reach the economic growth levels necessary to lift their populations out of poverty. The trade response is being negotiated at multilateral level in the WTO; at regional level under the Regional Economic Communities (RECs); and at bilateral level between countries, such as the African-Caribbean-Pacific countries (ACP) and EU discussions on Economic Partnership Agreements (EPA). The role of Aid for Trade is to enable developing countries to benefit from the liberal global trading environment – the expected outcome of the Doha Development Agenda.<sup>2</sup> All countries should gain in the long run from a liberalised trading system. However, in the short run, there will be winners and losers. Aid for Trade has the potential to obtain buy-in from short-term losers.

What still seems to be missing from the trade-related infrastructure debate is the holistic implementation of projects and programmes. Stakeholders (exporters and importers) who benefit, pass on savings to producers and consumers alike, and so that the region becomes more competitive. Unless trading costs are reduced, the region's producers and potential producers will not be globally competitive; the region will be unable to attract sufficient investment to increase production, and will not reach the economic growth levels needed for sustainable poverty reduction.

Currently trade-related infrastructure upgrades are done in a piecemeal fashion. A section of road or rail (or a bridge) is upgraded without taking into account the rest of the network, the rules and regulations governing the sector, or the impact an improvement in the road network will have on the railway network (and vice versa). Periodic and routine maintenance may ease one bottleneck only to create another, equally serious, bottleneck. The result is no reduction in transport time (or costs) from exporter to port or from port to the importer's factory gate.

## COMESA-EAC-SADC Task Force

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COMESA, SADC and EAC have long recognised the importance of improved trade facilitation in deepening regional integration, reducing cross-border transaction costs, and so improving economic livelihoods. As such, the RECs have supported a number of trade facilitation instruments and regional infrastructural development programmes.

Some countries belong to two of the three regional organisations (COMESA, EAC and SADC) but no country belongs to all three. Previously dual membership was not an issue because the functions and services of the RECs did not overlap. However, in recent years, this has changed. All three organisations now plan to become CUs, ostensibly with the objective of creating the African Union (AU). Their secretariats cannot streamline policy, as they are member driven and tasked with implementing the instructions of member states, as defined in the various protocols and the REC treaties. All they can do is work together to prevent members implementing contradictory programmes.

In 2001, during the COMESA policy organs meeting in Egypt, COMESA and SADC met at heads-of-state level to establish a COMESA-SADC task force that would work towards harmonising COMESA and SADC programmes. Until 2006, this task force met on average twice a year to exchange information. It concentrated on avoiding overlap in future projects and programmes rather than taking action to harmonise existing, on-going programmes. In March 2006, the secretariats of COMESA, EAC and SADC met in Kigali, Rwanda, and agreed to expand the task force to include the EAC. With a secretariat provided by the UK-DfID-financed Regional Trade Facilitation Programme (RTFP), the enlarged task force's mandate is to develop an implementation mechanism for harmonising trade arrangements between the three regional organisations. As of August 2008, the COMESA-EAC-SADC task force has met six times and the two sub-committees (infrastructure and trade and customs) have held additional meetings. Issues addressed include trade facilitation, trade policy and infrastructure issues.

One decision taken by the COMESA-EAC-SADC task force was to pilot a multimodal upgrade of a transit/transport route in the region. The pilot selected was the north-south corridor, which is the busiest corridor, in terms of freight volumes and values, in eastern and southern Africa. It runs from the Copperbelt of northern Zambia and southern DR Congo, to Dar-es-Salaam port in Tanzania on Africa's east coast, and ports in South Africa, predominately being a mechanism that mainstreams trade into economic policy at a regional level; Durban.

The north–south corridor pilot programme contains both hardware and software components and addresses various issues that include:

- ◆ Exploring how to reduce transport and transit costs in the region, especially those related to land-locked LDCs;
- ◆ Providing a focus for COMESA, EAC and SADC co-operation, as a vehicle through which the RECs can develop and implement common trade facilitation measures and trade-related infrastructure;
- ◆ Creating a point through which existing initiatives are co-ordinated and required actions take place with appropriate sequencing;
- ◆ Providing a vehicle for a regional Aid for Trade implementation strategy;
- ◆ Providing a mechanism for improved donor co-ordination, in line with the Paris declaration on aid effectiveness.

### Status of the transport and transit infrastructure network on the north–south corridor

Producers, exporters and importers in eastern and southern Africa face enormous challenges when moving goods within, out of and into the region. In theory, the region has a physically well-developed and flexible road, rail and port network, providing landlocked countries with several alternative and competing transport routes that serve both regional and international trade.

Traffic on the north–south corridor is characterised by the export of mining and agricultural products and the import of manufactured goods. The often severe imbalance of freight flows on this regional road route results in empty (or long waits for) return hauls, and affects transport efficiency, costs and tariffs. An empty return haul by road effectively doubles the transport cost. This imbalance is seasonal and varies from month to month: one month the problem will be to get a return load from south to north; the next month it is the other way around. Balanced freight flows are less critical for rail, because of the inflexibility of the system and the time (and cost) taken to reposition wagons and break up unit trains. Rather than waiting for a return load, it is often more efficient and achieves optimum equipment utilisation if wagons are returned as quickly as possible to pick up the next load.

The regional road transport sector is highly competitive. A deregulated private road transport system competes openly with rail services. Freight volumes have shifted from rail to road, resulting in lower transport costs. The shift in traffic is also partly due to the relatively high rail tariffs and unreliable service, which are attributed to poor management, inadequate use of assets and poor costing practices. The permissible gross vehicle mass (GVM), which at 56 tonnes is one of the highest in the world (only Australia has a higher allowable GVM), has also increased the competitiveness of road over rail. However, the high GVM also significantly raises road maintenance costs, which are not fully covered by road user charges and toll fees. A degree of cross-subsidisation of road freight comes from passenger vehicles and directly from government.

The road network is generally in good condition, although sections of the road urgently need rehabilitation and upgrading. If there is a blockage at one of the heavily used sections (such as the Kafue crossing in Zambia), the whole network closes. Recently, increased mining activities have resulted in much heavier use of the road network, with certain sections of the road operating above their design capacities.

The railway networks that run along the north–south corridor are characterised by long distances, comparatively low volumes and relatively high railway tariffs. Delays, unreliability and increased transport costs are the result of inflexible network schedules, poor intermodality, low rolling stock availability (compared to other regions of the world), disjointed railway operations, and poor tracks.

The north–south railways are all built to the ‘Cape gauge’ of 1,067 mm (3’6”) between the rails<sup>3</sup>, which means full railway interconnectivity is possible along the north–south corridor. Axle loads are generally 15–18 tonnes in the region, and up to 26 tonnes in South Africa. For rail to be more competitive than road, axle weights should not be less than 20 tonnes, thereby allowing a railway wagon to carry almost twice as much as a large combination road rig. Braking systems are gradually being upgraded to air, which will allow trains to be longer than 40 wagons.

Almost all the regional railway systems, including those in Zimbabwe (BBR), Zambia (RSZ), Malawi (CEAR), central Mozambique (CCFB), northern Mozambique (CDN) and Tanzania (TRC), have been privatised through concession agreements, which focus on improving management of the railways rather than infrastructure. They have been criticised for replacing an inefficient public sector monopoly with an inefficient private sector monopoly.

The north–south corridor includes a number of natural harbours with good access from the sea. Key operational aspects of regional ports are road and rail access, and the efficiency of the terminal handling equipment. However, the most important feature is the depth of the port and quays. Most regional ports do not have sufficient depth to handle the larger vessels (Capesize and Panamax) that transport the increasing volumes of international trade. Many ports, especially on the north–south corridor, suffer from congestion, which results in higher shipping costs because of additional storage and transport charges (as trucks wait to off-load or load), higher fees paid by ships in harbour and other costs associated with late delivery.

## Regional trade facilitation measures

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Trade facilitation is recognised as an effective way to reduce the cost of doing business and lower international trade transaction costs. Trade facilitation is part of the WTO’s Doha Development Agenda (DDA), but negotiations are limited to articles V (freedom of transit), VIII (fees and formalities connected with importation and exportation) and X (publication and administration of trade regulations) of the General Agreement on Tariffs and Trade (GATT) 1947. Although it is important to address these issues in the framework of the DDA

negotiations, for trade facilitation instruments to help reduce trans-border costs, they have to be a lot more encompassing than those being negotiated at the multilateral level.

The region faces the challenge of ensuring that COMESA, EAC and SADC trade facilitation programmes do not duplicate or contradict each other. Otherwise, the cost of doing business in the region may increase rather than decrease and thus make the private sector even less competitive than it is at the moment.

The following trade facilitation instruments are in place (although not always functioning as effectively as they should) or are being developed:

### *One-stop border posts*

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A one-stop border post is a border post where border officers from adjacent countries jointly conduct cross-border and security clearance procedures. It is seen as a practical way to reduce duplication of controls and involves setting up a border post for two countries at a single physical location. A one-stop border post reduces costs for the countries concerned, and for traders, freight forwarders and transporters. It simplifies the communication of trade documentation, reduces opportunities for fraudulent exchange of invoices, decreases clearance time by unifying border control processes within a single sequence, and results in significant savings.

Establishing a one-stop border post requires strong political support, a legal agreement covering the location of staff and facilities, and the realignment and streamlining of procedures. The benefits are maximised when this approach is coupled with a single-window environment that allows traders to lodge all import and export documents with a single agency. The parties need to ensure that:

- ◆ Legislation is in place to permit extra-territorial exercise of powers by officials from both countries and the declaration of common areas of control.
- ◆ The roles, powers and responsibilities of border control officials are harmonised.
- ◆ A comprehensive manual of operational principles and standard operating procedures for the operation and management of the joint border post is drawn up. This manual should form part of the bilateral (or regional) agreement and become law in each national jurisdiction.
- ◆ Customs procedures, standards, documentation and border controls are harmonised in both countries.
- ◆ A mechanism is put in place for continuous updating of procedures.
- ◆ The infrastructure at the joint border post is adequate to meet the needs of the users.

On the north-south corridor, the first one-stop border post at Chirundu (between Zambia and Zimbabwe) is expected to be operational before the end of 2008. Other border posts

may then be transformed into one-stop border posts, as this mechanism makes entry and exit formalities more streamlined and efficient and so reduces costs.

### *Simplifying harmonisation of customs procedures and legislation*

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Countries need to be part of the GATT valuation system and use the same harmonised system of customs classification. Harmonising customs procedures and legislation will speed up the processing of documentation. Other issues include: simplifying temporary admission, re-exportation and transit procedures; harmonising exemption and other duty relief measures; dispensing with all pre-shipment inspections; and adopting regional antidumping and countervailing duty regulations.

### *Single administrative document for customs*

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COMESA, SADC and EAC all agree that a common customs-clearing document, or a single administrative document, is needed for the region, but it is not yet finalised or in use.

### *Harmonisation of IT and electronic customs management systems*

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Countries do not share customs information for legal and technological reasons. Even when two countries use the same system, such as ASYCUDA, the same data is often entered twice: once upon departure from the first customs territory, and once upon entry into the second customs territory. Furthermore, because the border posts are rarely networked, the same information may be entered twice into the customs management system: upon entry and upon exit from a customs territory.

It would save time if data could be entered once (preferably before the goods arrive at the border post so that they are pre-cleared), then shared electronically between national border posts, and made available to customs officials of the territory the goods are entering.

The border clearance process would also be faster if other services (such as immigration, health, and security) at border posts were computerised.

### *Harmonised axle loading*

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Regional freight traffic is almost exclusively carried in large double-trailer, seven-axle combination rigs, with a maximum GVM of 56 tonnes. To preserve the road infrastructure and ensure reasonable usable life times, countries in the region have generally agreed to the following axle load limits for freight vehicles:



◆ single steering axle (two tyres)	8 tonnes
◆ single axle (dual tyres)	10 tonnes
◆ tandem axle (four tyres)	16 tonnes
◆ tandem axle (dual tyres)	18 tonnes
◆ triple axle (six tyres)	24 tonnes
◆ triple axle (12 tyres)	24 tonnes
◆ combination rig (gross vehicle mass)	56 tonnes

However, as not all countries apply these axle load limits, the load weight on a freight vehicle is limited to the lowest axle load limit along the entire route.

### *Maximum vehicle dimensions*

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Countries within the RECs have agreed on maximum vehicle dimensions (height, width and length). Unfortunately, like many trade facilitation instruments in the region, despite member states agreeing to these dimensions at a regional level, few countries have passed national legislation to enforce this instrument, and even fewer countries have actually implemented it.

Some countries have valid reasons for not applying the vehicle dimensions regulations. For example, in mountainous countries where vehicles have to negotiate sharp bends and steep gradients, a 22-metre long vehicle is impracticable. In such a case, it would be better either to re-negotiate the maximum vehicle dimensions to suit all, or to have two sets of dimensions in the regional legislation.

### *Harmonised road transit charges*

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In practice road charges vary by country. The RECs have introduced a system of harmonised road transit charges, whereby most countries apply a road transit charge of US\$10 per 100km. However, there are notable exceptions. For example, Botswana, Namibia and Mozambique all have higher charges, whereas South Africa's system is based on toll roads.

### *Carrier's license*

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RECs have introduced a regional carrier's license that allows commercial goods vehicles to operate under one license, which is valid for the entire region. The region's transport fleet is used more efficiently and the cost of trade reduces, as vehicles can pick up back-loads in other countries. However, evidence suggests that the regional carrier's license is not operational or usable in all of the countries that have signed this agreement.

### *Regional third-party vehicle insurance*

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The COMESA yellow card is a vehicle insurance scheme covering third-party liability and medical expenses. A yellow card issued in one COMESA country is valid in all other countries participating in the scheme. Not having to take out insurance each time a border is crossed saves time and money. Along the north–south corridor, South Africa and Botswana include a third-party vehicle insurance levy in the price of their fuel.

### *Regional customs bond guarantee schemes*

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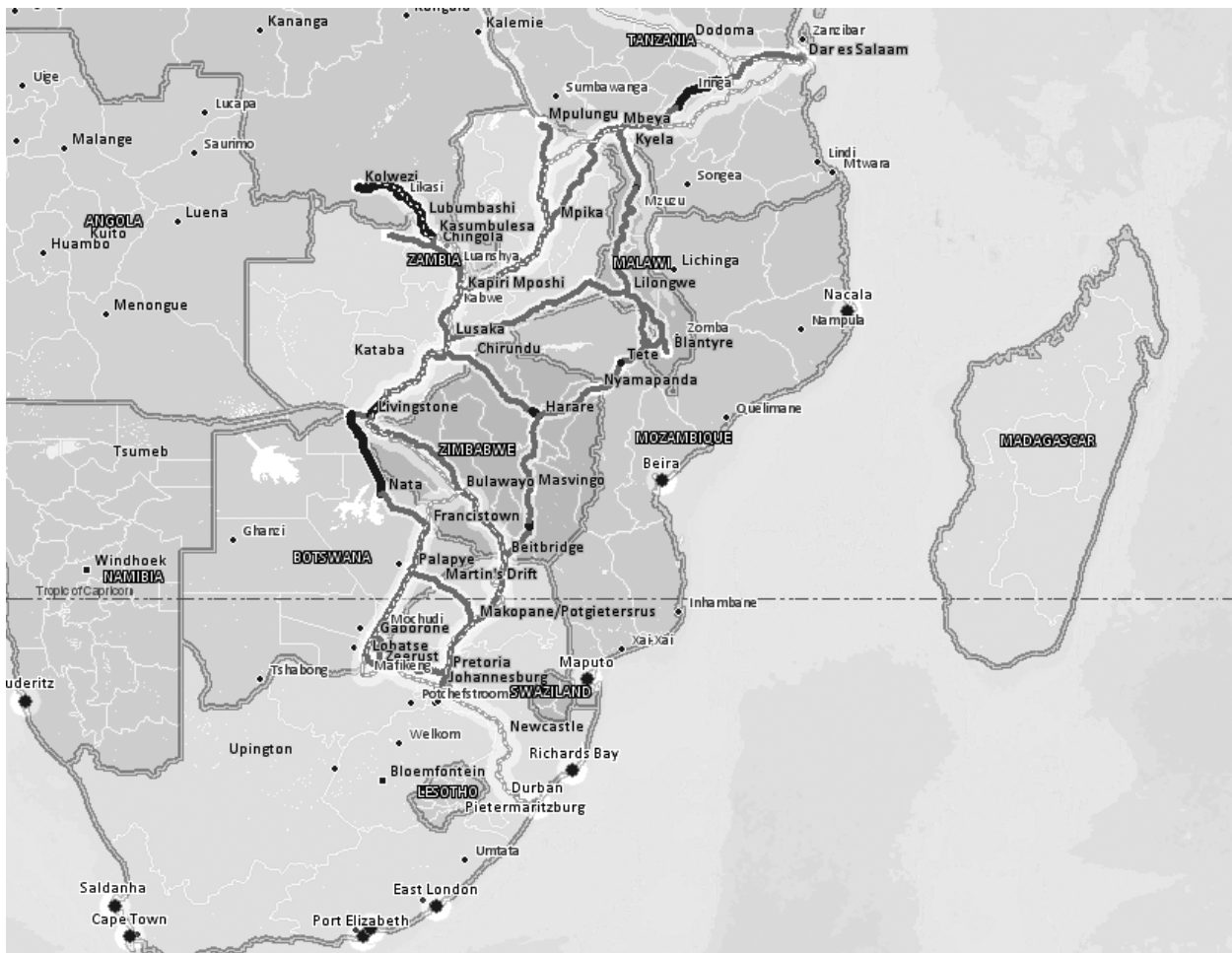
A regional customs bond guarantee scheme would eliminate the administrative and financial costs associated with the current practice of granting national customs bond guarantees for transit traffic. At present transporters transiting a country need to take out a customs bond that is at least equal to the duty payable on their cargo. Once they prove that the cargo has actually left that customs territory, the bond is released. Not only does it cost money to issue a bond, but also the process of releasing bonds takes time and ties up large amounts of money. As a result, the cost of transport is higher than if a regional system was in place.

SADC, COMESA and the private sector are working on the development of a regional customs bond. Slight and fundamental differences exist between the two systems under development (and being piloted). The challenge is to convince smaller transporters and freight forwarders in the smaller countries that a regional bond system will be beneficial to them. The two systems also need to be harmonised to create a single regional bond system. The benefits of a regional system will be greatly reduced if one country along a transport route operates a different bond guarantee system from that of its neighbours.

Safety and environmental regulation (including oil spillage, disposal of dredged material, handling of dangerous cargoes and dealing with distressed vehicles) of the regional transport sector is generally well defined and covered by international conventions and national legislation and procedures.

Ideally, in a truly competitive and harmonised environment, the regional transport sector would be self regulating (or require a minimum amount of economic regulation). To a certain extent, this is the case for regional road transport where there is open competition from a multitude of regional operators. However a degree of protection still exists in the application of cabotage rules (the transport of goods within or into a domestic market by foreign registered operators) and the restrictions on third-country operators (the transport of goods along routes which do not pass through the country of registration). The continued application of these rules requires performance monitoring and regulation. The COMESA, SADC and EAC policy documents (protocols and treaties) include as objectives the removal of all these constraints or barriers. However, before removing all barriers, the regulations and policies need to be harmonised. The existence of different import regulations, duties, fuel prices, operating conditions and so on can create competitive advantages.

**Figure 1: Road layout of the north–south corridor**



## The north–south corridor pilot Aid for Trade programme

The north–south corridor pilot project is an attempt by the COMESA-EAC-SADC task force to manage holistically, under one umbrella, all on-going initiatives along this corridor, including transport infrastructure improvements and trade facilitation measures. To reduce the time (and therefore the costs) of importing or exporting goods by surface transport requires making improvements sequentially, taking into account shortcomings and building upon progress in other areas. For example, it is no good establishing a one-stop border post along a route where the physical infrastructure (of the road or rail) has deteriorated to such an extent that the speed of traffic is reduced significantly, and the wear and tear on the vehicle transporting the goods is increased. The poor state of the physical infrastructure will negate any time and cost savings of the one-stop border post.

Unless the costs of cross-border trade are reduced, little productive investment will take place in the southern Africa region and economic growth will not be high enough to ensure sustainable and meaningful poverty reduction.

Another factor is the effect of the increased cost of commodities, especially metals and minerals, on the north–south transport and transit corridor. The transport infrastructure is already under pressure from higher traffic volumes in relation to its design capacities, and from delays at strategic points such as border posts. In addition, mining activities are rapidly increasing, especially in DR Congo and Zambia, where formerly interesting deposits of minerals have become economically interesting deposits. If the volumes of imports and exports using the north–south corridor continue to grow at the current rate, the infrastructure on the corridor will collapse unless remedial actions are taken.

Significant amounts of aid are flowing into the region and, now debt relief initiatives are in operation, there is a positive net transfer of assets. However, aid alone will never be enough to meet the development costs of an African country or a region. Developing infrastructure to meet economic needs requires significant levels of investment from the private sector and private sector financing institutions. However, the private sector will not invest at the necessary level unless investments in Africa are secure and produce an attractive rate of return.

Therefore, some of the challenges are to:

- ◆ Create an efficient transport and transit network that reduces the cost of trade within the region and with the rest of the world.
- ◆ Develop infrastructure to a level where investments in improvements and upgrades will result in economies of scale and produce positive returns.
- ◆ Build confidence in the security of investments and demonstrate that there can be, and are, opportunities for infrastructure investment in Africa.
- ◆ Allow private sector investors to channel funds into ‘ring-fenced’ investments that will ensure a positive return on investment. This could be through the creation of a Special Purpose Vehicle (SPV) or a series of connected SPVs.
- ◆ Use donor funds and concessionary loans to underwrite and leverage private sector investments.
- ◆ Develop a mechanism that allows governments and public sector entities to invest in equity and provide loans to infrastructure investments. Governments can then use the returns from these equity investments and loans to invest in other infrastructure projects.

The north–south corridor pilot programme has been operational for about 12 months. During this initial period, the focus has been on collecting data and developing a Geographic Information Systems (GIS) map<sup>4</sup> to store and display information about the north–south corridor and to serve as a scenario-planning tool. Work has concentrated on designing methodologies to identify and package programmes and how then to take them to market.

The next phase consists of a ‘pledging conference’ in March 2009 and the following planned activities:

**Table 1: Future activities**

Activity	Description
Finish GIS map and database	Much data is already on the GIS map and database but additional data, particularly on mining activities, is required to supplement the road, rail port and border post data.
Calculations of demand	Current and future demand – 5, 10 and 20 years – for transport services on the north-south corridor, based primarily on existing demand and expected outputs from the mines plus a variable for agricultural and other non-agricultural production.
Traffic simulations	Volumes of outputs and inputs along different routes and using different modes of transport. The types of models to be used will be decided on but 'switches' will determine when goods move from one mode to another or from one route to another. These simulations will provide the basis for suggested improvements or upgrades in existing road and rail infrastructures.
Packaging of interventions	The projects and programmes will be packaged either as one activity or as a sequence of activities. Recommendations will be made about when the packages should be implemented in order to realise the envisaged cost saving, or to avoid losing the initial investment (if the infrastructure collapses due to usage over and above design limits).
Improving trade facilitation measures	Improve coverage and co-ordination of existing trade facilitation instruments and, if necessary, develop new trade facilitation instruments that will reduce cross-border transaction costs.
Rate of return calculations	Once the projects have been designed and packaged, costs will be calculated with approximate return on investment rates.
Financing mechanisms	Various financing mechanisms are being designed and tested.
Road-shows to potential donors, IFIs, DFIs, and investors	After identifying the infrastructure projects, calculating costs and rates of returns and outlining a funding mechanism (meaning that packages will be either totally grant funded and/or concessionary loan-financed, or PPPs or fully private sector financed), the packages will need to be 'sold'. This will involve a team obtaining buy-in from the investor organisations and agencies.
Pledging session	The purpose of the road-shows is to sell packages of interventions to various donors and IFI/DFIs. The visited agencies and organisations will be provided with information early so that they have adequate time to consider how much and in what way they will commit funds to the north-south corridor. The pledging session, planned for March 2009, will be the occasion for all the donors, IFIs, DFIs and private sector participants to commit publicly to this Aid for Trade initiative.

## Conclusion

To address the time and cost of transporting goods to and from markets in eastern and southern Africa, the following issues must be dealt with in a coherent, holistic and sequential manner:

- ◆ Reduce border delays through the introduction of one-stop border posts, improved harmonisation of documentation, and enhanced efficiencies.
- ◆ Increase the implementation, at a regional level, of the trade facilitation measures already agreed by national governments and agencies.
- ◆ Create, where possible, more efficient regional railway operations through improved implementation of concession agreements, liberalisation of the railway operating system and infrastructure investment.
- ◆ Make ports more efficient through increased investments in infrastructure and equipment and in operating procedures.
- ◆ Enhance the efficiencies of modal interchanges, thereby reducing the delays and costs of transferring goods from one mode of transport to another.

Even if the above issues are addressed, the problem of how to finance these improvements remains. A number of infrastructure funds, established specifically for use in Africa, are not being fully utilised. These infrastructure funds are geared mainly to financing project preparation phases of commercial infrastructure projects or PPPs.

Analysis of the north-south corridor showed that some infrastructure and trade facilitation projects and programmes are vital to the corridor. If the infrastructure is not upgraded or developed, or trade facilitation measures not implemented, then the transport or transit route will remain inefficient. However, their return on investment does not make them attractive for either a PPP or a private sector investor. A funding mechanism needs to be developed, which can be used to finance these types of infrastructure. Then, if and when the return on investment is sufficiently attractive, they can be taken to a PPP or to the private sector.

For example, developing a bridge as a PPP may be possible, but the investment needed to upgrade and maintain the road leading to and from the bridge may not produce a high enough return on investment for the private sector. Therefore, unless the road is upgraded, the bridge will not have much traffic and so, in turn, will not attract private sector investment. However, if the bridge is upgraded as a PPP (using, for example, a special purpose financing vehicle) and the road is upgraded using public sector and grant funds, and concessional loans, the approach roads to the bridge could be upgraded and maintained to a high standard. The resulting higher volumes of traffic could mean that the approach roads could in the future also be converted into a PPP.

An unresolved issue is how to deal with trade-related infrastructure at a regional level. For many countries, and especially land-locked countries in sub-Saharan countries, the solution to reducing the cost of cross-border trade, and becoming more competitive, lies outside their jurisdiction and control. For example, to get goods to market, a land-locked country needs to rely on the roads, railways and port systems of neighbouring countries. All clients have to bear the costs of poor management, or inferior infrastructure, of these transport and transit systems. This translates into higher prices, lower profits, lower re-investment levels, lower economic growth and slower attainment of the Millennium Development Goals (MDGs) of the exporting country. The country approach to the problem taken by donors and aid agencies precludes a holistic solution. If, for example, the road to a port is improved but the port facilities (which may be in a different country) are not, then the port will not be able to deal with the increased volumes of cargo. Subsequently, the time and cost saved by improving the road will be lost as the costs are simply transferred down the distribution network to the port. The same can be said of improvements in the regulatory environment without accompanying improvements in infrastructure. For example, if a border post is converted to a one-stop border post, bringing time and cost savings to clients, but the road to and from the border is in poor condition, transit costs will remain high.

The one challenge is to identify the regulatory and infrastructural bottlenecks along a transport and transit route, and then to design a multimodal and sequenced series of interventions. The other challenge is to find a financing mechanism for the infrastructure projects

and programmes that are necessary: for reducing transit and transport costs; attaining high enough levels of economic growth for poverty reduction; and achieving the MDGs.

## Endnotes

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1. There are other important regional organisations in the eastern and southern African region, including the Indian Ocean Commission and the Intergovernmental Authority on Development, but these are not RTAs. The activities of these organisations are mainly concentrated on functional rather than economic co-operation.
2. Although the WTO ministerial meeting in July 2008 in Geneva was disappointing in that it did not conclude on modalities or even on a way forward for the DDA negotiations, the negotiations themselves are still expected to continue. The basic premise that the driving force for continued expansion of the global economy is trade remains valid and for trade to expand there is a need to reduce tariffs, and to put in place a level playing field in terms of rules, subsidies and national treatment.
3. The exception to this is the TRC system in northern Tanzania and the Kenyan-Ugandan systems which have a 1,000 mm gauge.
4. The GIS map and database can be accessed via the RTFP website at [www.rtfp.org](http://www.rtfp.org).

# Deeper regional integration: trade in services in SADC

*Nkululeko Khumalo*

Under the Southern African Development Community (SADC) Treaty, members commit to conclude co-operation protocols and memoranda of understanding in various areas. The protocols detail the implementation of certain agreed strategies for regional integration. They define the areas, objectives, broad strategies and timeframes of sectoral co-operation and integration, and often specify the steps required to implement such strategies. During the past decade, more than two-thirds of all SADC protocols have come into being and most of the regional integration policy's provisions are being implemented, at least partially.<sup>1</sup>

The timeframes for economic integration contained in the Regional Indicative Strategic Development Programme (RISDP)<sup>2</sup> anticipate the creation of a FTA by 2008, a CU by 2010, a common market by 2015, and a monetary union by 2016.<sup>3</sup>

SADC's regional integration agenda covers more than just trade but the TP (signed in August 1996) seems to be currently driving the integration process. The TP came into force on 25 January 2000, when it was ratified by eleven of the thirteen members. Its objectives are: to liberalise further intra-regional trade in goods and services; to ensure efficient production; to contribute towards improving the climate for domestic, cross-border and foreign investment; and to enhance economic development, diversification and industrialisation of the region.<sup>4</sup> In practical terms, its aim is zero tariffs for 85 per cent of all intra-SADC trade by 2008 and liberalisation of the remaining 15 per cent by 2012.<sup>5</sup>

By liberalising their service sectors, SADC countries will deepen their economic integration and co-ordinate their positions vis-à-vis third parties, thereby improving participation and influence at the multilateral level.

This chapter explores the initiatives undertaken by SADC countries to deepen regional integration through liberalising and co-operating their trade in services. After providing an overview of the services sector and its importance, the services trade liberalisation in accordance with the General Agreement on Trade in Services (GATS) is unpacked. The measures taken by SADC countries that had to liberalise trade in services in the region are explored. The final section looks at the challenges SADC countries face in their bid to promote deeper regional integration through liberalising trade in services and provides some policy recommendations.



## Growing importance of trade in services

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International trade in services has rapidly expanded and is expected to exceed merchandise trade by 2050. It currently comprises more than 20 per cent of world trade, accounts for an estimated two-thirds of the world's economic activity, and represents a significant share of global employment. The services sector's contribution to world gross domestic product (GDP) is now well above 60 per cent, and services represent more than half of annual global FDI flows.

Promoting trade in services offers developing countries in general, and southern African countries in particular, an opportunity to diversify trade, create jobs and boost overall economic development. During the past decade, the SADC region has roughly doubled global exports and imports of services. According to WTO statistics<sup>6</sup>, SADC<sup>7</sup> exports of commercial services rose from US\$8,5 billion in 1996 to US\$16,9 billion in 2005; while imports rose from US\$4,8 billion to US\$9,5 billion.

Needless to say, the service sector is very important for developing economies and contributes hugely to the overall GDP of most SADC countries. As table 1 below shows, in 2005 services contributed more than 60 per cent of the GDP for South Africa, Namibia and Mauritius and at least 45 per cent of the GDP for six other countries.

Core infrastructure services (or producer services) such as transport, finance, energy, and telecommunications, are essential inputs of various economic activities. These services can either facilitate or hinder trade and production of goods or services, depending on how efficiently they are made available to users and therefore either facilitate or hinder trade and production in other economic sectors – both goods and services – depending on the efficiency with which they are made available to users. While significant differences exist from country to country, in most SADC countries core infrastructure services are still inadequately and inefficiently supplied, which adversely affect trade and production competitiveness. As table 1 shows, apart from Botswana, Mauritius and South Africa, SADC countries have a low rate of fixed and mobile telephone subscribers.

**Table 1: Services-related economic indicators for SADC countries (2005)**

	Fixed line and mobile phone subscribers (per 100 people)	Internet users (per 100 people)	Services (% of GDP)
Angola	11	1	20
Botswana	52	3	45
Congo, DR	5	0	28
Lesotho	15	3	41
Madagascar	3	1	56
Malawi	4	0	47
Mauritius	82	24	66
Mozambique	8	1	48
Namibia	31	4	60
South Africa	83	11	67
Swaziland	21	4	43
Tanzania	9	1	37
Zambia	9	3	47
Zimbabwe	8	8	57

Source: WB, World Development Indicators

Services trade liberalisation measures aim to foster greater trade and competition and enhance welfare and efficiency gains by removing and/or relaxing domestic and foreign regulatory controls or barriers to entry for foreign services suppliers. In SADC, the liberalisation process is meant to help secure access (availability and affordability) for the regional citizens to quality but low-cost services, and also to make the region competitive in world trade. This is critical as Africa's low share of global trade is attributed more to lack of capacity to produce adequate quantities of quality goods and services to meet both the needs of domestic operators and export markets than to demand side constraints.

## Services trade liberalisation in SADC

All SADC countries are members of the WTO and are involved in the current round of GATS negotiations. During the Uruguay round, these countries made services liberalisation commitments of varying breadth and depth. As table 2 below shows, the most committed countries are South Africa and Lesotho and the least committed ones are Madagascar and Mozambique.

However, the GATS commitments made by SADC countries do not reflect the actual state of liberalisation in their services sectors. In the 1990s, most SADC countries carried out significant reforms through IMF/WB programmes, especially in the financial services sector.<sup>9</sup> Most of these reforms were unilateral and were not committed at GATS. Yet there are still barriers to trade in some services sectors in SADC (Hansohm et al 2005).

At a regional level, SADC member states are currently implementing a TP, which came into force in January 2000. While the major focus of the protocol is the liberalisation of trade in goods, article 23 underlines the importance of trade in services for overall economic

development and encourages member countries to ‘adopt policies and implement measures ... with a view to liberalising their services sector’ within the region.

In pursuit of this mandate, SADC countries recently decided to develop a separate trade in services protocol. Currently at draft stage, the protocol sets out the framework for the liberalisation of trade in services between SADC members and will serve as a basis for negotiations. Starting with six key services sectors (construction, communication, transport, energy, tourism and financial), the envisaged liberalisation will eventually cover almost all sectors and modes of supply. The ultimate aim is for each member state to treat the services, and service suppliers, of other members, in the same way as its own services suppliers and services. The plan is to achieve substantial liberalisation of intra-regional trade in services by no later than 2015.

**Table 2: Existing GATS commitments of SADC countries**

Countries	1	2	3	4	5	6	7	8	9	10	11	12	Total
Angola							X		X	X			3
Botswana	X	X							X				3
Congo DR	X	X	X		X				X	X			6
Lesotho	X	X	X	X	X	X	X		X		X	X	10
Madagascar	X												1
Malawi	X		X				X	X	X				5
Mauritius		X					X		X				3
Mozambique							X						1
Namibia	X								X				2
South Africa	X	X	X	X		X	X		X		X	X	9
Swaziland	X							X	X				3
Tanzania									X				1
Zambia	X		X					X	X				4
Zimbabwe		X					X		X				3

Note on Schedules: (1) business services (2) communication services (3) construction and related engineering services (4) distributional services (5) educational services (6) environmental services (7) financial services (8) health-related and social services (9) travel-related services (10) recreational, cultural and sporting services (11) transport services (12) other services.

However, even in the absence of a formal liberalisation framework, the economic integration efforts being made by SADC could have a considerable impact on trade in services across the region. Indeed, various protocols and memoranda of understanding, containing provisions for liberalising the services sectors and harmonising regulatory regimes, have been concluded and are at various stages of implementation. These include protocols on: transport, communications and meteorology; energy; the development of tourism; education and training; and health. The recently adopted protocols on the facilitation of the movement of persons and finance and investment are yet to be ratified.

Notable achievements in sectors that are key to deeper regional integration include the following:

### *Transport services*

Co-operation has led to the construction of highways such as the trans-Kalahari and trans-Caprivi as well as development corridors such as the Maputo, Beira, Limpopo, Mtwara, Nacala and Lobito corridors, which enhance the development and trade potential of the region and have resulted in increased flow of goods and services within the region. Much still needs to be done though. SADC countries must improve transport services in all sub-sectors, and focus on increasing the efficacy of transport corridors. Private sector participation needs to be encouraged by dismantling monopolies in air travel, ports, and rail transport.

### *Energy services*

Trade in energy services (electricity) already takes place in the region through the Southern African Power Pool (SAPP), which was established in 1995 and now comprises 12 SADC countries. Its aim is to expand electricity trade and to reduce energy costs by optimising the use of available energy resources in the region and facilitating power pooling and trade. The protocol on energy commits to co-operative development of the energy sector and the creation of a climate conducive for intra-regional trade in services. Since 1995, electricity trade within the SADC region has significantly increased. Plans are also underway to increase the region's generation capacity in order to counter electricity shortages that became more acute in 2007, especially in South Africa where (among other factors) economic growth fuelled increased demand.

### *Telecommunication services*

As part of the transport, communications and meteorology protocol, progress has been made towards connectivity of the telecommunications infrastructure network and implementation of the agreed regulatory framework. SADC countries need to give more attention to this sector and, in particular, strengthen the regulatory framework following privatisation, in order to prevent large companies from abusing their monopoly positions and to ensure benefits reach the consumers.

### *Financial services*

In SADC countries, these sectors are generally open. Once ratified and implemented, the finance and investment protocol will complement the TPs. Already, banking, finance and capital markets, and investment services in SADC have unilaterally liberalised substantially through various agreements and memoranda of understanding. Further liberalisation should be used to lock in reforms but must be preceded by macroeconomic stabilisation, and accompanied by a strong regulatory regime.

### *Tourism services*

The tourism sector in the region has generally been more open than other services sectors. This is perhaps because of the wider awareness of its importance and a strong desire to attract more FDI. SADC should maximise its international competitiveness as a tourist destination by abolishing the remaining immigration and visa restrictions. The intra-SADC movement of visitors needs to be facilitated and the existing proposals for a universal visa system should be implemented soon. Easing or removing travel and visa restrictions and

harmonising immigration procedures will aid the movement of international tourists, thereby increasing the region's market share and revenue of world tourism.

Liberalisation of trade in the above services sectors must be complemented by a freer, temporary or circulatory, movement of natural persons and services providers, with an emphasis on skilled professionals. Countries need to think regionally so that professionals can move freely across the region for the benefit of all countries concerned. Efforts to confine highly skilled people are doomed to fail since many developed countries welcome them, even to stay permanently (Khumalo 2007). Member states should therefore ratify the recently signed protocol on facilitating the movement of persons, in order to increase business mobility, create greater trade opportunities, and achieve economic growth.

The education and training, and health protocols also remove obstacles to the movement of persons. In particular, article 28 of the health protocol deals with referral systems or co-operation in tertiary care services. It calls upon member states, inter alia, to build capacity in their countries and provide appropriate high quality, specialised care through the exchange and attachment of specialists, and to share information on centres of excellence in the region. The exchange and attachment of health specialists is clearly related to liberalising the movement of natural persons' service providers. At a regional level the legal framework is the protocol for the facilitation of movement of persons. The education implementation plan addresses the development of a SADC qualifications framework, which will harmonise qualifications from education systems of all member states. Such a framework will facilitate mobility of students and academic staff, especially to higher institutions of learning, and subsequently enhance labour mobility.

## Challenges and recommendations

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Some progress has been made in harmonising regulations, through: the creation of regulatory bodies in telecommunications; the creation of regional implementation bodies; services infrastructure, and strengthening the institutional framework. Actual trade liberalisation has been incidental to this process and not its goal.

A number of challenges remain. A serious concern is the slow ratification and implementation of protocols. In addition, even for those instruments ratified by the majority of member states and in force, actual implementation is very weak. The RISDP does not address this problem as it is 'indicative in nature.' Therefore a stronger implementation mechanism is required.

The current system binds only those countries that have acceded to the protocols. No mechanism ensures that members ratify and implement a minimum of agreed legal instruments. Insufficient ratification means that members who want to move forward are often held back by others. In view of the ratification difficulties, the formal services liberalisation framework should probably have been an annex of the existing TP, instead of a stand-alone protocol with its long signing and ratification process.

To counter the implementation challenges mentioned above, SADC member states should adopt a clear common agenda for the implementation of the trade in services protocol. Such an agenda should ensure that all member states automatically become part of the liberalisation process, although the speed of implementation may differ. In addition, a robust sanctions system should be in place to encourage all member states to take their obligations seriously.

Moreover, the plethora of protocols containing provisions affecting the liberalisation of trade in services makes a comprehensive understanding of the progress difficult. Overlaps from one instrument to another further complicate the situation. A consolidation process is needed to group all these provisions within a single instrument, which in this case should be the trade in services protocol. Each country's schedule of commitments would then reflect the level of liberalisation or openness of its economy accomplished under the protocols and unilateral liberalisation.

The liberalisation of services in SADC should build on existing regional instruments such as the trade capacity development mechanisms, and GATS. Furthermore, to achieve deeper regional integration, services should ideally be liberalised first within SADC and then with third parties. In this regard, the Economic Partnership Agreements (EPAs) that the European Commission (EC) is negotiating with African, Caribbean and Pacific (ACP) countries poses a significant challenge to the SADC regional agenda on services. The talks seek to replace the current non-reciprocal export preferences that ACP countries have with the EC, with reciprocal free-trade arrangements. Negotiated at regional level in terms of the Cotonou Agreement, the EPAs aim to align the parties' trade regime with WTO rules. At the end of 2007, some ACP countries initialled IEPAs to prevent trade disruptions while negotiations continue. The second stage of negotiations, which will include services, investment, competition and government procurement, is expected to result in fully-fledged EPAs.<sup>10</sup>

Only four of the 15 SADC countries will negotiate with the EC on trade in services liberalisation under the SADC banner. The other countries will negotiate under other groupings such as the east and southern Africa group. The SADC process will be severely undermined unless all the groupings offer the same or similar commitments to the EC. This is unlikely since each negotiating outcome will reflect the specific dynamics of the particular group.

To avoid being overtaken by events and becoming irrelevant, it is critical that the SADC regional agenda keeps up with the EPA negotiations. Ideally SADC should offer faster liberalisation to the EU than that offered by the regional countries, and be ahead of the GATS negotiations.

The SADC regional services liberalisation process is likely to stall because participating SADC states and the EC are focusing on the EPA and the need to meet the tight timeframes of the IEPA. More importantly, the SADC process is funded by the EC and implemented through the United Nations Conference on Trade and Development (UNCTAD). The funding cycle has come to an end and the EC has reportedly indicated that future resources will only be dedicated to the EPA. Resource constraints mean that some SADC countries are

also failing to send delegates to the SADC trade negotiations forum. It is therefore difficult to see how the regional agenda can progress and influence the EPA negotiations. What will probably happen is SADC countries will use what has been offered to the EC under the EPA as a benchmark for making commitments to one another.

## Conclusion

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It is encouraging to note that SADC member states are currently engaged in a number of developments aimed at liberalising trade in services within the region. These initiatives are clearly in line with the SADC treaty, which mandates its signatories to progressively 'eliminate obstacles to the free movement of capital and labour, goods and services and of people in the region generally among Member States' (article 5.2(d)).

Apart from critical domestic needs, pressures from the EPA negotiations with the EC means that procrastination is not an option. Timely intra-regional services liberalisation is the only way for SADC countries to co-ordinate their positions in relation to third parties and to gain clout at the multilateral level.

In order for the regional agenda to move ahead of other negotiations with external partners, SADC countries should consider using the 'negative list' approach. This is where countries are required to make across-the-board commitments in the first instance, and then qualify these with restrictions or exemptions in certain sectors (Bhatnagar & Manning 2005). It will not be of much use to follow the more flexible 'positive list' approach used in the GATS, which allows countries to pick and choose sectors in which they want to make commitments. The flexibility of this approach generally results in very slow liberalisation, as countries make commitments in already liberalised areas and in effect maintain the status quo.

From the onset, SADC countries should consider engaging in a fully-fledged liberalisation process, which covers as many sectors as possible (not just the six sectors mentioned above). The EPAs can either be a blessing (the catalyst for deeper liberalisation in the region) or a curse (a serious distraction and threat to the regional processes). In the end, much will depend on how serious the regional countries are about liberalising services in the SADC.

## Endnotes

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1. For an insightful assessment of the achievements SADC countries have made in implementing protocols and other legal instruments read a speech by South Africa's Minister of Finance, Trevor Manuel at an Integrated Committee of Ministers meeting in June 2006. See <http://www.dfa.gov.za/docs/speeches/2006/manu0622.htm>.
2. The RISDP seeks to provide strategic direction with respect to SADC programmes, projects and activities. It aligns the strategic objectives and priorities with the policies and strategies to be pursued towards achieving those goals over a period of 15 years.
3. See <http://www.sadc.int/english/documents/risdp/chapter1.php>

4. See <http://www.sadc.int/english/documents/legal/protocols/trade.php>.
5. A SADC Free Trade Area was launched on 17 August 2008.
6. See [www.wto.org](http://www.wto.org).
7. SADC comprises Angola, Botswana, DRC, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.
8. GATS article V provides for a notable exception to this principle as it allows members of a regional trade agreement to give each other preferential treatment if the agreement provides substantial sectoral coverage and eliminates all discrimination substantially.
9. Botswana is a typical example, since despite limited barriers remaining after it removed exchange controls, it still has not committed these reforms in GATS.
10. Only the CARIFORUM (Caribbean Forum of African, Caribbean and Pacific (ACP) States) countries have negotiated a comprehensive liberalisation framework. CARIFORUM member states are Antigua and Barbuda, Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Kitts and Nevis, Saint Lucia, St. Vincent and the Grenadines, Suriname and Trinidad and Tobago. Cuba became a member in October 2001. The UK and Dutch OCTs have observer status while active co-operation is pursued with the French DOMs.



# The impact of the SADC EPAs on regional integration

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*Christopher Stevens*

The Southern Africa Development Community (SADC) heads of state agreed to complete the CU by 2010. However, in December 2007 the member countries took decisions that made this impossible. The decisions were about whether or not to initial Economic Partnership Agreements (EPAs) with the EU and, if so, within which EPA framework.

The EPAs are not the only issue affecting the 2010 deadline. There are many good reasons why so few CUs survive. Constituents have to make major economic compromises without the offsetting adjustment measures that are possible within a single political unit. The problems highlighted by the EPA may simply reflect underlying differences of interest between SADC states. But, by raising the stakes, the challenge posed to the region by the EU has not helped. An essential pre-condition for reducing (or resolving) the difficulties, is to understand how the current, unsatisfactory state of affairs came about. This chapter explains how the EPA issue arose, the current state of play, and the implications for the future.

## The origin of EPAs

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The EU has had preferential trade and aid agreements with the African, Caribbean and Pacific (ACP) countries since 1975. The latest, the Cotonou Partnership Agreement of 2000, specifically provided for recasting the trade regime and implementing a successor by 2008 (although the rest of the accord remains in force until 2020). This is because of the adverse rulings against the trade provisions of Cotonou's predecessor, the Lomé Convention, during the 1990s, first in the General Agreement on Tariffs and Trade (GATT) and then in the World Trade Organisation (WTO). The issue was that the EU discriminated in favour of some developing countries (the ACP), which is not allowed under WTO rules. At the Doha ministerial summit, after two years of negotiations, WTO members granted the EU a waiver that allowed this discrimination to continue – but only to the end of 2007.

The EU's preferred option to make preferential access for ACP exports 'WTO legal' has been to recast the relationship, so it falls under the WTO provisions that allow discrimination if the countries concerned are forming a free trade agreement (FTA) or a CU. An essential feature of such recasting, and the source of much debate over EPAs, is that the ACP countries liberalise imports from the EU. Controversy also arose because the EU's negotiating mandate went further than was needed to deal with the WTO ruling. The EU sought changes to

ACP policies that included liberalising services and investment compatible with the General Agreement on Trade in Services (GATS), aspects of government procurement, and rules on competition policies. Although the Caribbean and Pacific negotiators were keen to progress in the services negotiations, no other group was happy with rapidly concluding these topics. Critics have alleged that the EU's hard-line negotiating tactics with the ACP on these so-called 'Singapore issues'<sup>1</sup> can be explained as an attempt to influence the Doha negotiations through the back door.

By early 2007, negotiations had barely begun on the details of the FTA, and insufficient time remained to complete them, as is the norm in trade negotiations (which habitually overrun precisely because the devil is in the detail). As the deadline rapidly approached, in November 2007 the EC agreed to split the negotiations into two stages. But this 'compromise' only deferred the non-goods issues until 2008. Furthermore, as the 'interim agreements' initialled before the end of 2007 had to include complete provisions on goods, they did not allow the goods offer to be agreed at a more reasonable pace.

The EPA negotiations were formally conducted between the EU and, until the last months, six separate sub-groups of the ACP: the Caribbean, West Africa, Central Africa, Eastern and Southern Africa (ESA), Southern Africa and the Pacific. The initial SADC split occurred in May/June 2004, during the run-up to the creation of EPA negotiating groups. One group of SADC countries joined the negotiations under the ESA banner with their COMESA neighbours; the other group negotiated as 'SADC-minus', which initially comprised Botswana, Lesotho, Namibia and Swaziland (BLNS) plus Angola, Mozambique and Tanzania.

Negotiators then realised (very belatedly by the EU) that, as a member of the same CU as BLNS, South Africa could not be excluded from the negotiations. No such constraint had existed back in the 1990s, when South Africa negotiated the Trade, Development and Co-operation Agreement (TDCA) with the EU. South Africa could do more or less what it wanted within the original SACU. However, the new SACU agreement, negotiated in 2004, made the organisation more like a 'normal' CU. One of the changes made was that no member could negotiate a new external trade regime without the consent of the others. This is why South Africa has been a party to the SADC-minus negotiations since 2006.

During the second half of 2007 the five countries of the East African Community (EAC) – Burundi, Kenya, Rwanda, Tanzania and Uganda – made known that they were considering negotiating as a separate region. This was only confirmed in December, when they created a seventh group (taking members from ESA and SADC-minus).

## Differing ACP interests

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Although the negotiations were with six (and then seven) 'regional' groups, there was little overlap with the pre-existing regional groups. With the exception of the CARIFORUM and EAC, all EPA regions 'lost' members that have not initialled interim EPAs. Two countries of

one region (Ghana and Côte d'Ivoire of the ECOWAS region) have even signed EPA treaties that have different details! But SADC has been the most affected pre-existing region.

### *The three categories*

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ACP countries fall into three categories, which differ in the degree to which they are vulnerable to the EU threats made to countries that did not join an EPA. On 1 January 2008, the preferential Cotonou tariff regime that covers EU imports from ACP states ceases to exist. If by this date, countries do not have an EPA-based tariff regime, their exports will be taxed on the basis of the next-most-favourable tariff regime for which they were eligible. For least developed countries (LDCs) this means the Everything But Arms (EBA) scheme under which the EU imports virtually all goods duty free (subject to transition periods for rice, sugar and bananas, the last of which will finally expire in 2009). But for non-LDCs, the next-most-favourable regime is either the standard Generalised System of Preferences (GSP) or, for products not covered by the GSP, the most favoured nation (MFN) scheme. Tariffs under these regimes can be high.

#### *Category 1: preference-dependent non-LDCs*

These are countries that stand to lose in a very tangible way if the pre-existing export regime does not continue or improve. For example, if downgraded to the GSP, Kenya would face the imposition of significant tariffs on horticulture and processed tropical fruit exports.

Exports from SACU states are highly dependent on preferential regimes. For example, if preferences had ended in 2008, Botswana's beef exports to the EU would have become commercially unviable, as EU import taxes would have been equivalent to 80 per cent of the exports' value (ODI 2007). If Swaziland had been downgraded to the standard GSP, about 87 per cent of the country's exports to the EU (by value) would have experienced an increase in tariffs.

The end of Cotonou will not result in immediate, significant increase in export barriers for countries in the other two categories. Hence they can face this prospect with equanimity, but for different reasons.

#### *Category 2: countries with a safety net*

The larger of the two groups consists primarily of LDCs. Since 2001, under the EBA initiative, the EU has extended duty- and quota-free market access to all LDCs (both ACP and non-ACP). Hence, the end of Cotonou for these countries means only different export forms to be filled in under EBA. Some may have problems because of differences in the RoO, especially losing the right to 'cumulate', or achieving the required target by combining processing done in more than one state. But, after making the administrative changeover, most would not suffer any disruption to trade.

This group comprising primarily LDCs, included an additional member: South Africa, which, under the TDCA, has preferential access to the EU market, although not to the same

degree as other ACP states. Failure to agree an EPA would neither improve the status quo ante nor lead to deterioration.

Lesotho was in a similar position, straddling categories 1 and 2. As an LDC, the country can benefit from the EBA scheme, whereas the changes to the RoO represent a significant boost to its clothing industry. Under Cotonou, and also under EBA, clothes made in Lesotho from Chinese cloth were subject to the full MFN tariff, as the EU considered them of Chinese and not Basotho origin. Under the modest changes to the EPA RoO (agreed but subject to further review) these items would be considered as Basotho and, hence, eligible for duty-free access to Europe. Therefore, if Lesotho stayed outside the EPA, the country would not lose tariff preferences, but would forgo the improved origin rules.

The SACU states were distributed between categories 1 and 2. Botswana, Namibia and Swaziland (BNS) were very firmly in category 1. Lesotho and South Africa were between categories 1 and 2: not joining an EPA would mean keeping the status quo ante broadly intact but giving up an improved regime that would, in the case of Lesotho, greatly improve access to the EU. This difference has had an impact both on the negotiations and the outcome as of January 2008.

#### *Category 3: non-sensitive exporters*

The third group did not fear the end of Cotonou because their main exports are all non-sensitive products subject to either zero or very low EU standard tariffs. The group includes oil exporters Nigeria, Gabon and Congo and the non-signatory Pacific states which export mainly fish to the EU (where the 'real' negotiations may be on Fisheries Partnership Agreements).

### *Did countries act in line with objective interests?*

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The answer to this question is broadly yes. Figure 1 plots each category to show whether or not they acted in a predictable way based on the objective situation. In other words, one expects that category 1 countries would initial the EPA to avoid their exports taking a hit, but that category 2 and 3 countries would have no such need to initial an EPA.

What we find is that most countries behaved as predicted. Almost all the vulnerable countries have initialled EPAs, whereas most (but not all) with a good alternative have not. Just over half of those with non-sensitive exports also avoided initialling the EPA. Most of the countries that have initialled and have a 'good alternative' are in the EAC, which demonstrates that they give higher priority to regional integration than to avoiding liberalisation towards the EU.

**Figure 1: EPA status by ACP category**

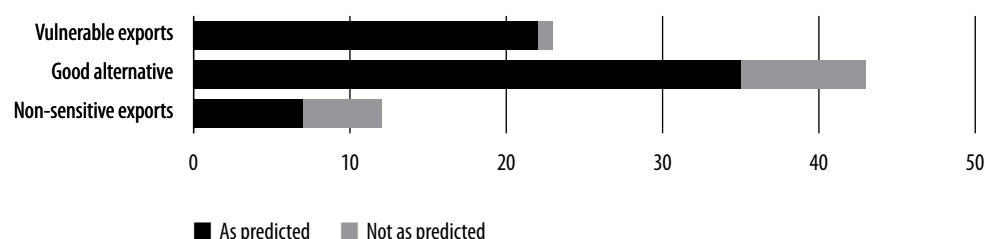


Table 1 confirms this finding. The table shows the result by country, identifying by region which countries have initialled and which are LDCs. Of the 76 states listed, only 35 have initialled.<sup>2</sup> But more non-LDCs (26 out of 37) have done so. The non-LDCs that have failed to sign (and are currently facing GSP or MFN tariffs) are the Republic of Congo, Gabon, seven of the Pacific Islands, and Nigeria (plus South Africa, which continues to export under the TDCA).

**Table 1: Overview of EPA signatory states as at 1 January 2008**

	Members	Initialling states in December 2007 <sup>a</sup>	Countries falling into EBA/Standard GSP	Proportion of signatory countries	Number of liberalisation schedules
ESA EPA	Comoros	Comoros	Djibouti	45%	5
	Djibouti	<i>Madagascar</i>	Eritrea		
	Eritrea	Mauritius	Ethiopia		
	Ethiopia	Seychelles	Malawi		
	Madagascar	Zimbabwe	Sudan		
	Malawi		Zambia		
	Mauritius				
	Seychelles				
	Sudan				
	Zambia <sup>b</sup>				
	Zimbabwe				
	EAC EPA	Burundi	<i>Burundi</i>		
Kenya		Kenya			
Rwanda		<i>Rwanda</i>			
Tanzania		<i>Tanzania</i>			
Uganda		<i>Uganda</i>			
SADC EPA	Angola	Botswana	Angola	71%	2
	Botswana	Lesotho			
	Lesotho	<i>Mozambique</i>			
	Mozambique	Namibia			
	Namibia	Swaziland			
	South Africa				
	Swaziland				
CEMAC EPA	Cameroon	Cameroon	Chad	12.5%	1
	Chad		Cent. African Rep.		

	Members	Initialling states in December 2007 <sup>a</sup>	Countries falling into EBA/Standard GSP	Proportion of signatory countries	Number of liberalisation schedules
	Cent. African Rep. Congo DR Congo Eq. Guinea Gabon S. Tomé/Príncipe		<b>Congo</b> DR Congo Eq. Guinea <b>Gabon</b> S. Tomé/Príncipe		
ECOWAS EPA	Benin Burkina Faso Cape Verde Côte d'Ivoire Gambia Ghana Guinea Guinea Bissau Liberia Mali Mauritania Niger Nigeria Senegal Sierra Leone Togo	Côte d'Ivoire Ghana	Benin Burkina Faso Cape Verde <sup>c</sup> Gambia Guinea Guinea Bissau Liberia Mali Mauritania Niger <b>Nigeria</b> Senegal Sierra Leone Togo	13%	2
PACP EPA	Cook Islands Fed. Micronesia Fiji Kiribati Marshall Islands Nauru Niue Palau Papua New Guinea Samoa Solomon Islands Tonga Tuvalu Vanuatu	Fiji Papua New Guinea	<b>Cook Islands</b> <b>Fed. Micronesia</b> Kiribati <b>Marshall Islands</b> <b>Nauru</b> <b>Niue</b> <b>Palau</b> Samoa Solomon Islands <b>Tonga</b> Tuvalu Vanuatu	14%	2
CARIFORUM	Antigua/Barbuda Bahamas Barbados Belize Dominica Dominican Rep. Grenada Guyana Haiti	Antigua/Barbuda Bahamas Barbados Belize Dominica Dominican Rep. Grenada Guyana <i>Haiti</i>	–	100%	1

Members	Initialling states in December 2007 <sup>a</sup>	Countries falling into EBA/Standard GSP	Proportion of signatory countries	Number of liberalisation schedules
Jamaica	Jamaica			
St Kitts/Nevis	St Kitts/Nevis			
St Lucia	St Lucia			
St Vincent/Grenadines	St Vincent/Grenadines			
Suriname	Suriname			
Trinidad/Tobago	Trinidad/Tobago			

Notes: a) Countries in italics are classified as LDCs. In the table compiled by the Commission (European Commission 2008), Somalia and Timor-Leste are listed as LDC non-signatories (in the ESA and PACP groupings respectively).

b) Since neither has played any part in the negotiation of EPAs, they are omitted here.

c) Cape Verde has been classified as non-LDC since January 2008 but will be able to export to the EU under the EBA initiative for a transitional period of three years.

## The EPAs and SADC

### *Group membership*

The SADC countries are split into three EPA groups (those that initiated the Interim EPA) and the group of countries outside the EPA. These are the SADC minus ESA EPA; EAC EPA; and the non-signatories. How did such an unsatisfactory situation come about? The main contributory factor is certainly pressure from the EU. But the group's splintering also reflects underlying fault lines.

#### *The implications for regionalism*

The EU claimed during the negotiations that EPAs would strengthen regionalism within the ACP. It was unclear whether the EPAs, always a sickly child, would indeed be the catalyst that forces governments to implement their numerous declarations on regionalism, or bring the whole hesitant, crab-like process to a halt.

By definition CU signatories must have a common set of tariffs on *most* imports. They can have preferential as well as MFN regimes (as the EU does) so long as the regimes are nearly identical. A CU member cannot have zero tariffs on some EU imports (by virtue of its EPA commitments), while its neighbour maintains tariffs on these goods but removes them on others (which is why the EPA position in SACU is anomalous). Members can have different implementation schedules and maintain different rates if a CU is not yet complete (which is the case for SADC and COMESA), but not once the CU is finalised.

States that belong only to a regional FTA have more latitude since they retain separate and different external tariff regimes. But, the lack of harmonised liberalisation schedules gives countries another incentive to retain rigorous border controls. For example: country A excludes flour from liberalisation and maintains a 100 per cent tariff, while its neighbour, B, removes all duties. Traders can circumvent A's restrictions by transporting EU goods across the border from B. To avoid this, either the tariff difference between A and B must be sufficiently small to make such trans-shipment commercially unviable, or rigorous border

controls must be maintained to prevent trans-shipment. The latter would undermine A's milling industry and in the process hurt intra-regional trade. Research shows that the most serious constraint to intra-regional trade is the paraphernalia associated with physical barriers at land borders, rather than differences in trade policy, although of course the latter underpins the former (Charalambides 2005; Hess 2000; Visser & Hartzenburg 2004).

There is no intrinsic reason for creating a barrier between neighbours that join or do not join an EPA. However, in practical terms, a country achieves little by staying outside an interim EPA (which applies only to goods) unless it erects a barrier against its neighbour. The principal reason to remain outside such an EPA is to avoid reciprocity. But, cross-border trade will undermine this goal if the outsider also participates in an effective FTA/CU with EPA member countries.

Incompatible trade policies, as described above, are all the more problematic for countries not liberalising any product. In effect, an absolute barrier has been erected between EPA signatory and non-signatory countries, and a potential barrier has been created between signatories of agreements that differ from those of their regional partners. These two groups include all the countries of SADC.

Tanzania's position has long illustrated the inconsistencies of African regionalism. Although a member of EAC, the country also remained a SADC member and, until the last months of the EPA process, was negotiating in an entirely different group from all of its EAC partners. Since then, Tanzania has joined the EAC EPA, and (with Kenya, Rwanda, Burundi and Uganda) accepted the associated disciplines, which suggests that a decisive shift might have been made. The commitments of these countries to reduce tariffs are all based on the EAC CET. In other words, the countries have pledged themselves to implement this tariff before the start of the first tranche of EPA tariff reductions in 2015.

Madagascar, Mauritius and Zimbabwe have signed a different text from the one negotiated in SADC-minus and have established liberalisation schedules related to the COMESA CET (even though details of exclusions vary). Like Tanzania, therefore, their liberalisation will not be organised around a common SADC list.

Mozambique is the only remaining SADC state apart from the BLNS countries to have initialled an EPA. However, its schedule is quite different from the BLNS' common schedule, which is based on, but not identical to, the TDCA.

#### *SACU's position*

At the time of writing, all SACU members except for South Africa had initialled the interim EPA, but negotiations were continuing. A possible outcome is that South Africa will also initial. Alternatively, some or all of the BLNS may decide not to confirm their membership.

An EPA with the EU that does not include all five members would appear to be legally unenforceable in SACU. What this anomaly means in practice remains to be seen (if not removed by further negotiation). The status quo is stable so long as neither the EU nor South Africa



chooses to destabilise it. The EU has granted EPA treatment to BLNS exports, although their initialled agreement appears unenforceable across SACU. So long as South Africa does not actively object, these countries could in fact apply the EPA tariff to EU-origin goods that enter SACU through their territory. For example, Botswana customs authorities could tax direct imports by air to Gaborone at the EPA rather than the TDCA tariff rate, if they are different. However, only a very small proportion of the EU-originating goods consumed in BLNS actually enter through the territories of these four countries. Most are imported in bulk into South Africa and split into smaller consignments, some of which are trans-shipped to BLNS. These imports will necessarily pay the TDCA tariff so long as South Africa remains aloof.

The situation could continue indefinitely (or at least until 2012, when the final tranche of TDCA liberalisation will make South Africa's tariff regime very similar to that in the EPA), so long as one of three things occurs. The first is neither South Africa nor the EU objects to the status quo. The second is the opposite of this *laissez faire* position: South Africa joins the EPA. The third is a midway position: South Africa remains outside the EPA but acts autonomously to remove discrepancies between the TDCA and EPA tariffs. All that is required for this midway position is for South Africa to agree in the SACU ministerial council that it will alter the tariffs on EU imports to EPA levels. Whether or not this would be in South Africa's best interests (and whether the EU would accept this 'solution') depends on what happens in practice; which tariffs go down further or faster than required under the TDCA. What is important is to realise that the midway position exists, at least on paper. South Africa does not necessarily have to commit to further negotiations on services and other non-goods issues in order to stabilise BLNS's trade relationship with the EU.

### *The obligations of the SADC EPAs*

How great are the differences in the liberalisation schedules initialled by SADC states, and how soon will they emerge? The answers will determine the size of the barriers to regional integration created by EPAs among signatories and between signatories and non-signatories. However, the answers are not straightforward, as predicting the pace and extent of implementation means making judgements about future interests and policy.

#### *Comparing the provisions of the EPAs*

Table 2 compares the position of the SADC states and other African countries that have initialled EPAs, based on three criteria. The top band shows the liberalisation period. With Tanzania being covered by EAC, SADC states fall into all three bands.

The implementation period is very short for BLNS because of the need to dovetail their commitments with those of the TDCA. Similarly, BLNS will start liberalising very soon (as will Mozambique and Mauritius) but Tanzania and the other SADC states will not do so for six or more years.

Four of the SADC states exclude less than 15 per cent of their imports from liberalisation but four exclude more than 20 per cent. However, this calculation can be distorted by the exclusion of a small number of major imports (as is the case in Botswana).

**Table 2: How SADC compares**

<b>Duration</b>	<b>15 years or fewer</b>	<b>16–20 years</b>	<b>20+ years</b>
	<b>BLNS</b> Comoros Côte d’Ivoire Ghana <b>Madagascar</b> <b>Mauritius</b> <b>Mozambique</b> Seychelles	Cameroon <b>Zimbabwe</b>	All EAC
<b>Liberalisation starts for positive-tariff goods</b>	<b>2 years or fewer</b>	<b>3–5 years</b>	<b>6+ years</b>
	<b>BLNS</b> Côte d’Ivoire Ghana <b>Mauritius</b> <b>Mozambique</b>	Cameroon	All EAC Comoros <b>Madagascar</b> Seychelles <b>Zimbabwe</b>
<b>Exclusions</b>	<b>Under 15%</b>	<b>15–20%</b>	<b>20+%</b>
	<b>Lesotho</b> <b>Mauritius</b> <b>Namibia</b> Seychelles <b>Swaziland</b>	Côte d’Ivoire Kenya Uganda Comoros <b>Madagascar</b>	<b>Botswana</b> Burundi Cameroon Ghana <b>Mozambique</b> Rwanda <b>Tanzania</b> <b>Zimbabwe</b>

*The SADC-minus details*

Figures 2 and 3 compare the extent of liberalisation and the timetable for liberalisation for SADC members minus EPA. BLNS are shown separately from Mozambique, as the four SACU states have identical commitments.

Figure 2 confirms that Mozambique is excluding a significantly higher proportion of imports from liberalisation than BLNS (although this proportion may fall, as the EU continues negotiations with Mozambique). A high proportion of BLNS’ imports are liberalised, as the CU had already committed to the liberalisation of a wide range of products through the TDCA. BLNS do not import in any great quantity products excluded from the TDCA, which accounts for their very small share of the value of trade.

**Figure 2: SADC EPA: extent of liberalisation**

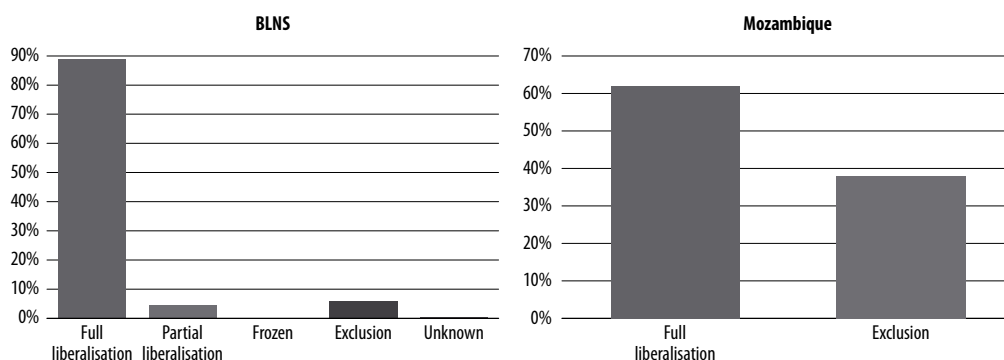


Figure 3 shows that, if the EPAs go ahead, the majority of imports will be liberalised in 2008. The proportion remaining to be liberalised (in 2018) is small in Mozambique (partly because nearly 10 per cent of imports are already duty free) and miniscule in BLNS. Tariffs will be removed from almost all products that are to be liberalised by 2012 (the TDCA implementation date).

**Figure 3: SADC EPA: timetable for liberalisation**

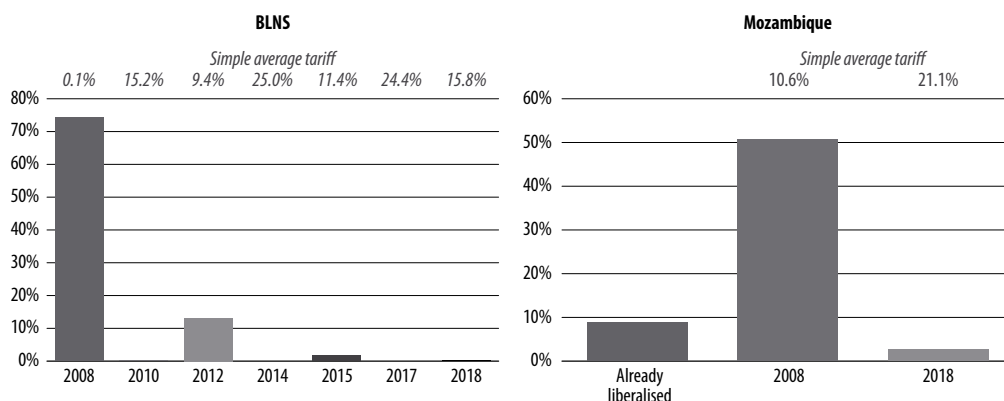
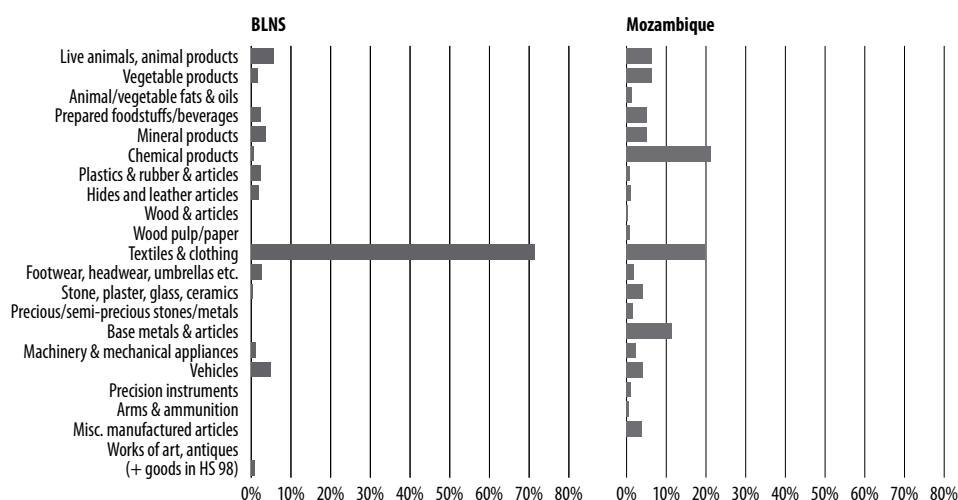


Figure 4 compares the exclusions of BLNS and Mozambique. Clothing and textiles are the largest group of items excluded by BLNS. They are also important exclusions for Mozambique, in addition to chemical and base metal products, and a range of agricultural goods. Critically, only one-fifth of BLNS and Mozambique exclusions overlap, which means that only one in five of the products excluded from liberalisation by BLNS is also excluded by Mozambique, and vice versa.

**Figure 4: SADC EPA: exclusions**



*Implementing the EPA*

The speed of liberalisation is important, as it indicates how much ‘time’ countries have ‘bought’ before they need to take difficult decisions on tariff levels. The longer the period, the more time is available to reflect and to mitigate the costs of not remaining a member. As noted above, most of the countries initialising EPAs are vulnerable to an abrupt removal of trade preferences. Some may face ‘preference erosion’, which is when the commercial value of the preference is reduced through (for example) improving access for competitors. Others may be able to diversify their exports to new markets. However, calculating whether the costs of EPA membership outweigh the benefits might not produce the same conclusion in, say, 2012 as in December 2007.

The EPA commitments made by ACP countries will only have a direct impact if implemented. Implementation tends to occur only if the associated costs are lower than those of non-implementation. This distinguishes ‘conditionality’ under an EPA from that related to ‘policy based aid lending’. The latter requires aid recipients to act quite quickly. The borrower’s stratagems are able to offset, to varying degrees, the lender’s objective bargaining strength. Repayment to the lender (in the case of the development banks and IMF) depended in part upon the country being given a ‘clean bill of health’ in order to continue receiving aid from other sources.

A similar sort of ‘balance of power’ shift also applies to EPAs. The capacity of the EU to enforce implementation is linked to:

- ◆ Its ability to obtain evidence that implementation is not happening.
- ◆ An inclination to monitor implementation sufficiently closely to notice this evidence.
- ◆ The availability of sufficiently strong sanctions to enforce change.
- ◆ A willingness to use the sanctions.

The first and third requirements involve the collection and analysis of factual evidence; the other two relate to attitudes. While the attitudinal requirements are a matter for speculation (especially given the time that elapses before 'non-implementation' occurs), doubt exists over the more factual requirements.

Establishing whether an EPA is being implemented is not as straightforward as it may sound. By the time countries start to reduce tariffs, the nomenclature used for the EPA commitments will have evolved further, and some of the codes listed in the schedules will no longer exist. It will be extremely difficult (and very time-consuming) for the EU to check whether the items liberalised in, say, 2015 are in fact the same as those agreed to in 2007.

The existence of strong sanctions is also uncertain. As a major source of aid for the ACP, the EU (and its members) will always have significant leverage over policy decisions through the threat of withholding (or amending) flows. This leverage is quite independent of the EPAs, which do not (at present) contain any financial provisions over and above what countries can receive under Cotonou and the member states' bilateral programmes. The EPA's extra leverage is currently limited to the EU renouncing its preferences for ACP exports.

Hence, EU action against an ACP not implementing the EPA trade commitments is limited to the commercial value of the preference. This will diminish over time as the EU extends more favourable tariff treatment to an increasing number of countries. The speed at which the preferences erode is not easy to predict and will certainly vary between products. But it is reasonable to suppose that the more time elapses, the greater the change in the nomenclature, and the more substantial the erosion of preferences.

The timing of SADC liberalisation commitments is therefore relevant to the credibility of implementation. Liberalisation in BLNS and Mozambique is relatively fast compared to other ACP states. By 2018, BLNS will have removed all tariffs on goods not excluded from liberalisation (or subject to partial liberalisation). And yet, most of the BLNS liberalisation simply recognises *de jure* the tariff cuts that the TDCA obliges countries to make *de facto*. In Mozambique, the process is also due to be completed by 2018, and might not have taken place without the EPA. In Madagascar, Mauritius and Zimbabwe, by contrast, any item subject to a positive CESA CET will not need to be liberalised before 2013. Hence, these initial efforts will not go beyond what is needed to comply with COMESA commitments. Items subject to positive COMESA tariffs will only be liberalised after 2013, in a process to be completed by 2022.

**Table 3: SADC exports for which EPA membership offers the greatest commercial advantage**

Country	Ex HS chapter	Product
Botswana	02	Fresh/frozen beef
	16	Preserved beef
Mauritius	03	Fresh, chilled, frozen fish
	10	Manioc/rice starch
	15	Preparations of animal or vegetable fats or oils contain milkfats
	16	Preserved fish
	17	Sugar and confectionery
	19	Cereal preparations
	20	Preserved fruit and vegetables
	21	Miscellaneous edible preparations
	22	Beverages and spirits
	23	Bran, sharps and other residues
	24	Cigarettes
	25	Salt suitable for human consumption
	64	Miscellaneous footwear
	87	Bicycles
Namibia	02	Fresh/frozen beef
	03	Fresh, chilled, frozen fish
	07	Fresh or chilled beans
	08	Fresh table grapes
	64	Slippers
Swaziland	02	Fresh/frozen beef
	03	Fresh or chilled fish
	07	Vegetables
	08	Citrus fruit
	10	Maize
	17	Sugar
	20	Preserved fruit and vegetables
Zimbabwe	03	Fresh, chilled, frozen fish
	07	Vegetables
	08	Citrus fruit, peaches, nectarines, plums
	10	Maize
	16	Preserved beef
	17	Sugar
	18	Chocolate
	19	Cereal preparations
	20	Preserved fruit and vegetables
	22	Wine and ethyl alcohol
	24	Cigarettes and tobacco
64	Women's shoes	

### *The EU's liberalisation*

What will be the future commercial value of EPA preferences by 2013? This depends on which products currently receive a favourable preference and are important SADC exports to the EU. The EU has since January accorded duty- and quota-free access to all its imports from EPA states, apart from sugar and rice. Access of these two products will be phased in over the period to 2015 and 2010 respectively.

The EU is likely to negotiate further regional trade agreements and the Doha round will eventually conclude. Therefore, it is reasonable to assume that goods currently subject to the standard GSP tariff of 10 per cent or less will retain little commercial advantage. EPA membership will continue to be commercially attractive only to those goods with an *ad valorem* tariff of over 10 per cent and/or a specific duty under the standard GSP (or the MFN if the item is not included in the GSP).

As all LDCs have access to the EBA scheme, only non-LDCs would face a potential tariff hike if they left an EPA. Table 3 lists the export groups in which each non-LDC SADC signatory currently has tariff preferences of this rate. The main product groups are beef, grapes, fish, citrus, sugar, and processed foods containing sugar or cereals.

Assessing changes to EU tariffs over the next five or more years must necessarily be speculative. Nevertheless, several SADC states could face a significant commercial shock if just some of their exports were downgraded to the standard GSP/MFN regime. Hence, it seems at first sight that, by the time the non-SACU states have to start reducing significant tariffs, the value of EPA preferences may offer the EU some leverage in the region.

## Conclusion

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The EPA status quo is clearly inconsistent with a SADC CU. The EPA may not be the only factor preventing the 2010 deadline being met, but policing the different trade regimes with Europe will also reduce the likely gains from the FTA. Will these differences persist?

In the medium term, not all exports from SADC countries will be vulnerable outside an EPA; in some cases the exports may have disappeared. The key variables for beef, for example, are the cost of meeting sanitary standards and EU liberalisation to other suppliers. The EU may cease to be a profitable market if the cost of sanitary compliance continues to rise. And if the EU offers Mercosur (Argentina, Brazil, Paraguay and Uruguay) increased tariff quotas (either in the context of a regional agreement or under Doha), which make commercial sense, these countries may take over BNS markets. It is unlikely that southern African could compete on price. The best that can be said is that the continued commercial value of EPA membership for beef in five years' time is 'uncertain.'

For sugar, the key variables (which are linked) are the future EU price and the extent to which LDC suppliers expand exports. Under duty- and quota-free access, the EU will retain safeguards on non-LDC sugar exports even after 2015. The same will apply to processed

sugar. It seems likely that Swaziland, at least, will have a continued interest in exporting to the EU, but the position of Mauritius is more uncertain.

In most other cases, though, it seems likely that EPA membership will continue to offer commercial advantages during the period when most SADC states are completing their tariff cuts. This suggests that if countries exit the EPAs, they will incur a real commercial loss.

This implies that SADC states must identify the precise differences in their schedules in order to determine the implications for further regional integration. Reducing or removing the key differences may ease the barrier to regional economic integration provoked by the EPAs. However, this task may prove difficult, as the differences presumably reflect the differences in national perceptions of trade interests. If this is the case, then the EPA may best be seen as a mirror that reflects the underlying trade and economic policy differences between members. EPAs may have crystallised these differences and made them harder to remove, but they have not created the incoherent national policies.

## Endnotes

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1. Investment, competition, transparency in government procurement, and trade facilitation have become known as the 'Singapore issues'.
2. Only 75 of the 77 countries that receive Cotonou trade preferences negotiated an EPA. Somalia and East Timor did not. In addition, South Africa (which does not receive Cotonou preferences) was a negotiating party - making 76 negotiating countries in total.



# Looking East: disaggregating the role of China and India in SADC?

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*Sanusha Naidu*

In recent years, the rapidly evolving relationship between Asia's emerging giants, China and India, and Africa has been the subject of much debate. Most commentaries have focused on macro implications and the impact of Asia's involvement on the continent's geo-political and strategic landscape. At the same time most empirical studies (especially relating to China) have focused on three core aspects: trade, investment and aid. The studies and commentaries looking at the developmental impact of China and India's relations across Africa confine themselves to analysing the bilateral impact. These assessments do not consider the regional implications, in particular the possible effect of the Chinese and Indian involvement on the continent's regional integration project, which is at the core of the AU's development programme. The critical question that needs to be examined is: can China and India advance Africa's regional integration model or will the result be a variable geometry process, which will benefit the more structurally stronger economies in regional blocs such as South Africa in SADC, Kenya in the EAC, Zambia in COMESA or Nigeria and Ghana in ECOWAS.

In examining the rise of China and India in Africa, issues that must be considered are the role played by these Asian economies in regional economic communities and the influence of regional FTAs and CUs on their actions across the continent. The focus of this chapter is not to provide answers to these and other compelling questions but rather to raise critical issues for future empirical studies into the involvement of China and India in Africa at a sub-regional level.

This chapter examines the role played by China and India in SADC, analyses China and India's political and economic actions in SADC and the opportunities and challenges that these pose for further regional integration in the southern African sub-continent.

SADC, like other regional economic communities, is affected by numerous structural challenges, not least the issue of overlapping membership, which complicates efforts inter alia to harmonise trade tariffs and RoO structures. Therefore, when looking at SADC's regional integration efforts, it is not enough simply to assess the relationship with traditional development partners, whether within the context of Economic Partnership Agreements (EPAs) or the AGOA. It is also critical to understand the role of southern partners such as China and India that are important features of the African landscape and have benefited from the continent's trading relations with the United States and the EU. To this end, an overview of the

factors influencing China and India's engagement in SADC will help unpack whether a 'Look East' policy is a viable alternative in the context of the current global financial uncertainty.

## Looking East

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China and India's involvement in southern Africa is rooted in a historical relationship. Both Beijing and New Delhi strongly supported the region's liberation movements and have used this historical platform to engage with the continent as part of the South-South partnership (Taylor 2007).

As on the rest of the continent, this relationship has undergone significant changes.

The first change came in response to the unilateral character of the post-cold war international system. As the United States stood as the unitary superpower, the overriding preoccupation was to promote a multilateral international order. During the 1990s, both Beijing and New Delhi advanced a multilateral order that resonated with the principles of the non-aligned movement. In China this dovetailed with the Communist Party's anti-hegemonic stance (Taylor 2007), while in India the policy of reinventing and rejuvenating the old relationship was implied in a 'confluence of interests around justice in the global order levelled at increasing the leverage and influence of their respective global positions and promoting a new international order' (Naidu 2008). These ideological undertones of China and India's foreign policy remain in place, at least on a rhetorical and superficial level.

For southern Africa, China and India represents a break from the past predictable relations with traditional western development partners. Indeed, China and India have opened up a new policy space for diplomatic manoeuvrings in Africa. For instance, as the crisis in Zimbabwe deepened, President Robert Mugabe commented: 'The sun rises in the East and sets in the West', implying that partners other than the traditional western ones may be more sympathetic and willing to respond to Africa's socio-economic plight. Although President Mugabe's 'Look East' policy may have produced few dividends, since China remains ambivalent about its relationship with Harare,<sup>1</sup> China and India have nevertheless shifted the continent and the region's geo-political dynamic. African leaders have been encouraged by the growing involvement of China (and to a lesser degree India). The playing field has been opened up and traditional development partners have to accommodate the emerging southern partners.

This shift became apparent at the recent Aid Effectiveness meeting held in Accra, Ghana in September 2008. The principles of the Paris Declaration on aid effectiveness and harmonisation reflect clearly that the experience of southern partners in international development assistance compelled traditional donors to consider initiating a trilateral co-operation with non-DAC donors.<sup>2</sup>

The second response was to the structural weaknesses of most regional economies. Following the failure of the market-liberalisation prescriptions known as the 'Washington Consensus', most southern African economies found themselves in a precarious position. Lacking sufficient market liquidity and industrial capacity to deal with fundamental issues such as dilapidated infrastructure, the countries were also facing increasing socio-economic development challenges. At the same time the structural adjustment programmes adopted underlined the inability of regional markets to compete in the global economy. In the 1990s, the global political and economic focus shifted to the Eastern European bloc. Africa and indeed the southern African region was depicted as the 'Hopeless Continent'. During this period, as South African capital crossed the Limpopo, the country became an important investor in the region and across the continent' (Daniel et al 2004). In 2001 China adopted the 'Going Out' strategy, which promoted the overseas expansion of state-owned enterprises, and enabled Chinese investment in the southern African region, especially in regional infra-structural projects.

Building on the international power shifts described above, China and India have expanded their political and economic incursion into southern Africa. In India, it was only in the 1990s that New Delhi has liberalised the economy after years of following the Soviet style economic model. Therefore, in the current overview of Chinese and Indian involvement in southern Africa, New Delhi trails Beijing to a certain extent.

## Vested interests

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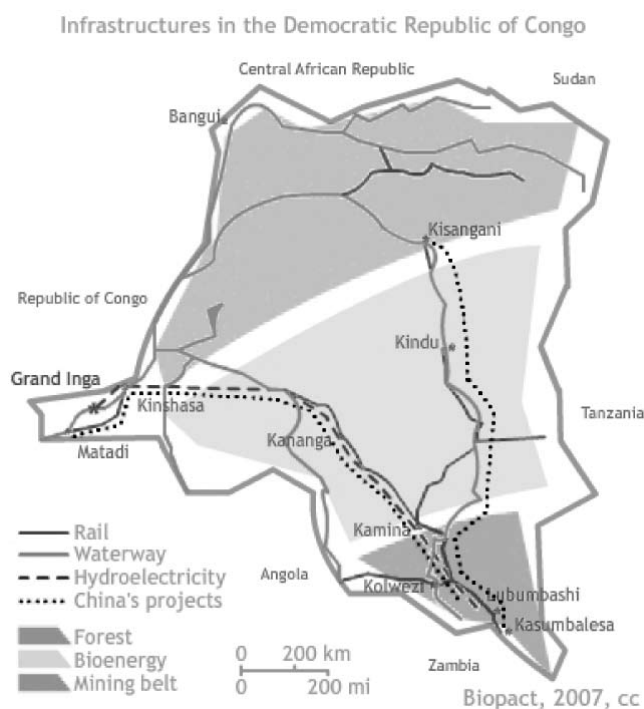
While the region seeks to attract new investors to revitalise deficient infrastructure and inject new sources of capital, China and India have their own vested interests. The region has become an attractive source of renewable and non-renewable resources for a China needing to sustain its impressive economic growth to meet domestic demand, and for an India embarking on an economic restructuring (Naidu & Davies 2006). Access to such resources has deepened Beijing and New Delhi's relations with strategic regional economies such as Angola, Zambia, Namibia, the DRC and South Africa, among others. These countries have become strategic partners and are in some respects seen as gateways into the region. This is particularly true for South Africa where both Chinese and Indian corporates have set up their headquarters in the country's financial capital, Johannesburg, to provide them with greater leverage for entering regional and continental markets.

Nevertheless, access to resources remains the main focus, as resource security, especially energy security, is vital. In 2003, China signed a US\$2 billion oil-backed loan with Angola for infrastructural development at a very low interest rate (Corkin 2008). China's infrastructural investments are welcomed in a country, which is hoping to become a regional powerhouse. A recent WB study estimated that Beijing's funding for infrastructure projects across the continent peaked in 2006 at US\$7 billion, up from just US\$1 billion in 2001/2003 and US\$1,5 billion in 2004/05, but then fell to US\$4,5 billion in 2007 (Foster et al, 2008). Most of the funding has been in the power (mainly hydropower) and transport (mainly roads)

sectors. However, China is not the only emerging economy financing infrastructure projects in Africa; others include India’s Exim Bank and Arab development funds.

In September 2007, Beijing and Kinshasa concluded a mineral-backed loan of approximately US\$8 billion in return for infrastructural development in the DRC. The deal includes a ‘US\$3 billion loan for mining development, along with loans from China’s Eximbank to the Chinese companies, China Railway Engineering Corp (CREC) and Sinohydro, to finance over US\$5 billion in infrastructure’ (Curtis 2008). According to the agreement, ‘CREC will build railway lines and roads, including a 3 200 km railway from Matadi in Bas-Congo to Sakania in Katanga and a 3 200 km road from Kisangani in Orientale province to Kasumbalesa on the border of Zambia’ (Curtis 2008). These planned projects are shown on the map below. In addition Sinohydro will construct power lines, power plants and distribution centres supplying water. Other projects in the deal include the building of over 30 hospitals, 145 health centres, four universities and more than 20 000 housing units.

**Figure 1: Map of infrastructures in the DRC<sup>3</sup>**



In return a joint venture company called Socomin (Société Congolaise Minière) has been created to mine the region’s rich iron and other commodity resources. Under the agreement, Gecamines (the DRC’s large state-owned mining company) holds 32 per cent of the shares in the joint venture company, while CREC and Sinhydro (the Chinese state-owned enterprises) hold the other 68 per cent. Socomin’s profits from the first phase will be used to pay off the US\$3 billion mining loan while 66 per cent of the profits from the second phase will go towards repaying the US\$5 billion infrastructure loan. The Chinese appear to have used the Angola model in the DRC and created a mineral mining belt across the DRC and Zambia, thereby guaranteeing access to and extraction of the resources.

The Indian government is following a similar strategy of tapping into Africa's resources by linking to the continent's development needs ie infrastructure rehabilitation. Indeed, the grave concern over China's deepening footprint in Africa has enabled India to enter African markets largely unnoticed. Like China, India's Africa strategy is based on 'quest for resources, business opportunities, diplomatic initiatives and strategic partnerships' (Pham 2007).

As a latecomer, New Delhi has had to deal with Beijing's existing leverage in the region and to play 'catch up' in securing contracts, particularly in the energy sector. One example was in 2003/2004 when India tried to acquire 50 per cent of Royal Dutch Shell's equity in one of Angola's offshore oil blocks for US\$600 million. The deal was thwarted by the Chinese offering a US\$2 billion oil-backed deal (Sethuraman 2005). But such setbacks have not deterred the Indian government.

As part of the Indian government's energy diversification programme, New Delhi has created an energy panel to look at ways of accessing and consolidating Indian oil interests in Africa, particularly as strategic suppliers (Dutta 2007). In June 2007, the Indian foreign minister, Anand Sharma, led a delegation to Angola to discuss signing accords in the areas of oil, geology and mining, agriculture, health, education and tourism. India sees great possibilities in Angola as a supplier and there is talk of New Delhi building an oil refinery. It is rumoured that the Sinopec-Sonangol initiative to build the Lobito refinery under the oil-backed deal has been delayed and that the Angolan government is looking to diversify its coterie of investors. This could be an important entry point for increased Indian investment in the Angolan market and perhaps into other regional markets.

But oil is only one aspect of the Indian interests in the region. Now that the United States administration has ratified the Nuclear Civilian deal, India is seeking to accumulate sufficient uranium resources for its nuclear energy programme. Namibia is a strategic investment destination as the country has sufficient deposits of uranium to satisfy these interests. Indian companies are prospecting in Niger and considering similar plans in Namibia. Taurian Resources is one of the Indian companies likely to be interested in these deposits. Beijing is also on the hunt for uranium resources to assist in its energy programmes.

A common feature of China and India's policy in the region is large-scale concessional finance coupled with development assistance. The resource factor has become the backbone of China and India's foreign policy in the region and the rest of the continent. However, the region also represents an attractive market.

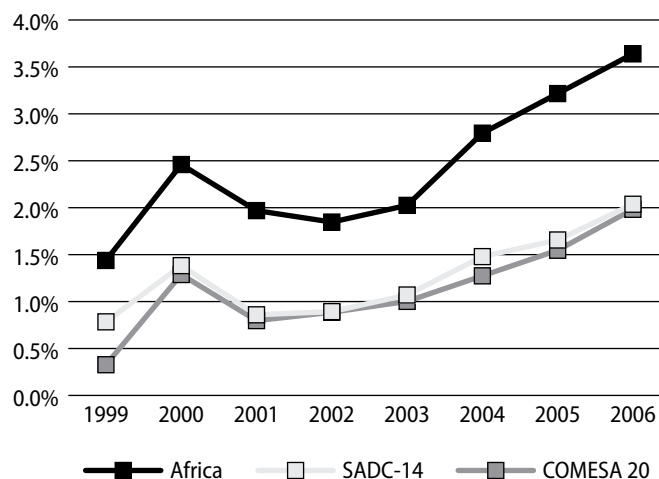
## The trade and investment factor

Even though the trade aspect of China and India's involvement in the region remains small, the trends and patterns cannot be ignored and are highlighted in the graphs below.

At one level the relationship represents a typical core-periphery arrangement: raw materials such as iron ore, oil, copper, aluminium, and other mineral resources are exported in return

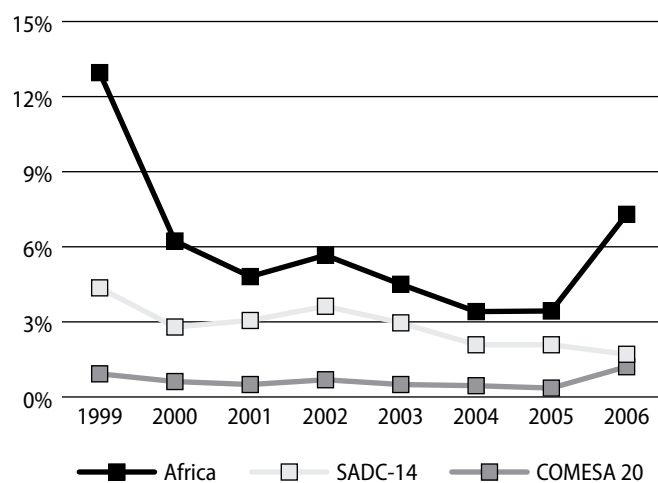
for processed and manufactured goods (mainly finished apparel, electronic goods, clothing and textiles).

**Figure 2: SADC's share of China's imports<sup>4</sup>**



On the other hand, the region has become a strategic avenue for accessing new markets. China and India have both sought to secure their interests in the Indian Ocean Rim (a distinctive area consisting of coastal states bordering the Indian Ocean), which contains the main commercial shipping lanes for both countries. China's establishment of a special economic zone on the island of Mauritius not only gives Beijing fresh impetus to access markets along the East African coast (ie in COMESA) but also acts as a transient trading hub. This hub will undoubtedly link into the metals special economic zone (SEZ) in Zambia and the possible trans-shipment SEZ in Tanzania, both of which were announced at the 2006 Forum on China–Africa Co-operation (FOCAC) Summit in Beijing (Davies 2008).

India also sees the Indian Ocean Rim as a strategic political and economic neighbourhood from which to penetrate African economies through East Africa. The region is also significant because of India's 2004 Maritime Doctrine, which allows naval and security exercises to be conducted in the region with its Indian Ocean partners. New Delhi considers this region as its backyard and is increasingly aware of China's penetration via Mauritius, as well as competing interests in the Seychelles. India closely monitors Chinese and Pakistan activities in the African–Indian Ocean Rim and concerns about Chinese expansionism have led to India deepening its defence and commercial relations with the Seychelles, Madagascar, Mauritius and Mozambique' (Vines & Oruimeka 2008).

**Figure 3: SADC's share of India's imports<sup>5</sup>**

Driven by the need to expand into new markets, both China and India have institutionalised their relations with the SADC region and Africa through the FOCAC process, conclave meetings and more recently the India–Africa Summit. The aim is to bolster trade and investment through a web of investments ranging from telecommunication and transport corridors to hydro power and regeneration projects.

Some major Chinese deals include:

- ◆ A US\$230 million ferro-chrome mine and smelter project in South Africa.
- ◆ A US\$200 million copper project in Zambia.
- ◆ Rural fixed-line telephone project by the Chinese telecommunication firm Huawei in Angola.
- ◆ The Chirundu Road Rehabilitation (WB Tender) by Chinese construction company CHICO.
- ◆ Infrastructure projects in the DRC, Angola, Mozambique and Madagascar.

India's public and private sectors have also been taking advantage of opportunities created. At the three conclave meetings held to date, Indian businesses have discussed joint ventures valued at over US\$30 billion with their African counterparts. Many of these deals are still being negotiated but Indian corporates have had the following successes:

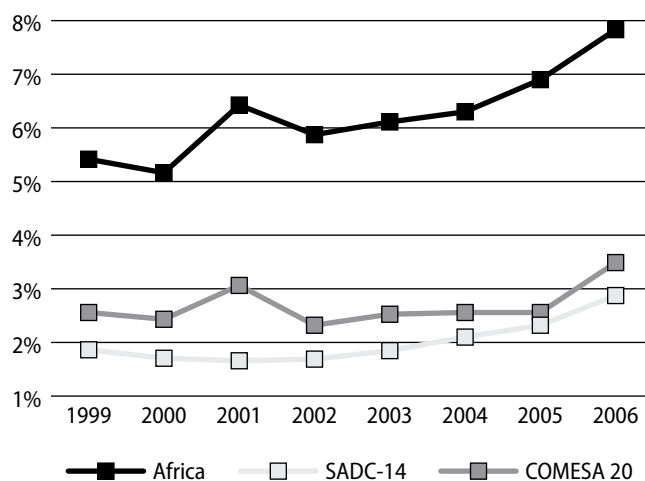
- ◆ A US\$11 million contract awarded to Kamani Engineering Corp for the construction of a transmission line between Zambia and Namibia.
- ◆ A railway rehabilitation project by Rites International in Huila Province, Angola.
- ◆ A concession to Ircon International for the rehabilitation of the 600 km Beira railway system in Mozambique.

Of all the major Indian investors, the Tata Group has the most extensive presence on the continent, operating in Ghana, Mozambique, Malawi, Namibia, South Africa, Tanzania and Uganda. The Tata Group claims to employ over 700 people in Africa and is involved

in activities that range from infrastructure development, to energy, hospitality, financial and communication services, to automotive production. The Group’s regional investments include the following:

- ◆ A US\$800 million renovation of the Taj Pamodji Hotel in Lusaka.
- ◆ A vehicle assembly plant at Ndola in Zambia.
- ◆ The construction of a 120 megawatt power plant to supply energy to Zambian mines.
- ◆ A US\$108 million high-carbon ferro-chrome plant at Richards Bay in KwaZulu Natal, South Africa.
- ◆ The provision of 250 buses to the DRC at a cost of US\$46 000 per bus.

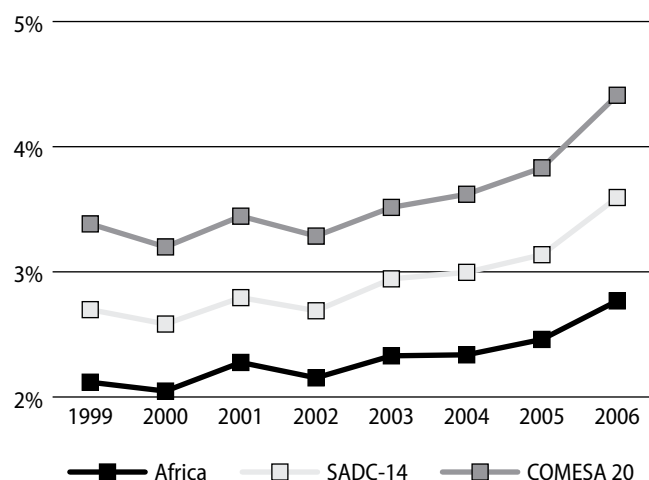
**Figure 4: SADC’s share of India’s exports trade<sup>6</sup>**



SADC’s share of export trade with China and India is slightly higher than its share of import trade because of the resource factor. However, the EU still accounts for the lion’s share of the region’s trade and China and India, even between them, represent marginal differences in their trade with the region (see figures 4 and 5).

China and India’s main trading partners are respectively Angola and South Africa. In fact, Angola has overtaken Sudan and Nigeria to become the main exporter of oil to China.



**Figure 5: SADC's export trade with China<sup>7</sup>**

Chinese and Indian companies have also used the region's preferential trade access agreements (such as AGOA) to take advantage of the trade concessions with the United States and EU markets. With the free trade zone (FTZ) already in place, it would be interesting to determine what impact this would have on China and India's regional trade relationship. And the implications for traffic structures and RoO once the FTZ extends all the way to the COMESA market. Who will benefit most from the FTZ: China and India or regional member states? The pending CU by 2010 and the possible FTA to be negotiated between the Southern African CU (SACU) and India pose yet more challenges for tariff harmonisation structures and leaky borders. In brief, will the region be able to deal with the deluge of cheaper Chinese and Indian goods that could enter regional markets through the backdoor if the tariff structures and trade regimes are not properly implemented?

## The South African factor

South Africa is perhaps the only SADC country that has made some significant inroads into the Chinese economy and, to a lesser extent, the Indian market. There are about 20 South African-based businesses with offices in China (Naidu 2008). The list is impressive (see table 1) and includes resource, mining, and financial conglomerates that are anchors of the South African economy, as well as other small companies in the agricultural or cut flowers industry. Provincial and city twinning agreements support much of the small-medium investment and have been a popular form of two-way investment for the Chinese.

Two interesting developments stand out among South Africa's investments into the Chinese market. The first is the memorandum of understanding (MOU) that Sasol has signed with two Chinese companies to develop two plants in the coal-rich western part of China. The purpose is to convert coal into liquid fuels in the Ningxia autonomous region and the Shaanxi province, using technology developed by Sasol during the apartheid years when South Africa wanted to be self sufficient in fuel. The Chinese have identified this technology as particularly useful in developing their alternate fuels project.

The second development is the US\$5.5 billion deal between Standard Bank and the Industrial and Commercial Bank of China (ICBC), which will enable Chinese companies to increase their presence in the African market. The deal establishes a US\$1 billion equity fund that will be used to invest in mining projects and other sectors. Thus the China factor provides a competitive advantage for South African corporates expanding in the region and will no doubt extend into the telecommunications industry where South African companies like MTN and Vodacom have a notable presence in terms of services.

In contrast, South African corporates are only now beginning to break into the Indian market, where that economy was only recently liberalised. Domestic laws still need to be changed to accommodate new investors in the market. The Shoprite Group’s sizeable investment in a hypermarket in Mumbai has not been profitable, yet others are queuing up to take advantage of the opportunities created by the growing middle class in India. They include MTN, SABMiller and even energy companies with useful technology for India’s nuclear civilian programme.

**Table 1: South African companies investing in China<sup>8</sup>**

Company	Sector
Naspers/MIH	Media
Metspan	Manufacturing
Freeplay	Manufacturing
Beijing Axis	Consulting/Research
Frontier Advisory	Consulting/Research
Kumba Resources	Mining/Metals
AngloGold Ashanti	Mining
Anglo American	Mining
Anglo Coal	Mining
Goldfields	Mining
Old Mutual	Financial
Standard Bank	Financial
First Rand Bank	Financial
Sasol	Energy
SABMiller	Beverages
African Explosives Limited (AEL)	Engineering
Bateman	Engineering
Landpac	Engineering
Spur	Restaurant/Hospitality

## The regional impact

So far China and India’s role in SADC has not been any different from their relations with the rest of the continent. What is interesting to note is that both countries have used a bilateral model for their relationship with regional member states. This may prove expedient for

China and India but still remains a significant issue for the SADC Secretariat that is developing a regional strategy. The immediate concern is to harness China and India's concessional finance to promote regional public good through infrastructural projects, which is critical in shaping the regional integration project. An important development was the recent ECOWAS economic forum hosted in Beijing, September 2008, where the Chinese authorities and West African states discussed regional trade and investment projects that will benefit regional development. As much as these member states used the occasion to seek greater trade and investment linkages with China, it was done under the banner of the ECOWAS community, which indicates that China is beginning to show interest in promoting regional integration strategies. At the same time the ECOWAS Secretariat was able to assemble a regional strategy around regional projects, which is something policy-makers in the SADC Secretariat could learn from.

Second, as China and India penetrate further into the southern African region, regional member states need to understand the implications for the debt issue in the region. Both China and India may have settled debt but their concessional finance model could lead to other forms of debt vulnerability. SADC member states must be prepared for the effect that the current turbulent global financial environment and pending stabilisation of the global commodity boom will have on their economy and hence their position in the global economy.

This leads to the third consideration ie the impact on local livelihoods and human security. Both China and India advocate that their involvement in Africa is aimed at securing human security and stimulating self sufficiency. But regional governments should remember that China and India are also developing countries facing similar challenges of poverty and inequality. Therefore, regional member states (and the SADC Secretariat) must be able to address their own development challenges, especially social justice issues and pro-poor policy growth initiatives.

Nevertheless, although China and India have acted at a bilateral level, their actions have stimulated regional development through:

- ◆ Providing much-needed impetus to the region's dilapidated infrastructure.
- ◆ Reducing transactional and transport costs of doing business.
- ◆ Creating and connecting markets.
- ◆ Giving access to goods.
- ◆ Making available alternate credit finance.
- ◆ Setting up joint ventures with the region's private sector (especially South African corporates).
- ◆ Underlining the region's development.
- ◆ Acting as a catalyst for industrialisation and development.
- ◆ Fueling a commodity boom.
- ◆ Advancing the regional integration agenda – financing for development.

To take the relationship to the next level will require refocusing the policy orientation, which will compel the SADC Secretariat and regional leaderships to address the following issues:

- ◆ Friction over trade, ie RoO, procurement practices.
- ◆ Friction over business model and operations.
- ◆ Friction over values and norms ie the APRM process.
- ◆ Long-term viability of state-to-state engagement.
- ◆ The replacement of the North-South axis by a South-South axis but still the East-South power reconfiguration.
- ◆ Business as usual for the region or not?

The regional dilemma of how to respond to the involvement of China and India raises the following questions:

Can a regional consensus be developed? Especially

- ◆ around the NEPAD programme.
- ◆ What are the environmental security and climatic conditions?
- ◆ What is the impact of geo-politics? Ie, where does the region fit in?
- ◆ How will regional leaders leverage their relations with China and India? Will it increase their bargaining power in the global system? (eg the Doha Development Talks).
- ◆ Who benefits? Regional elites or citizens?
- ◆ What will be the role of continental institutions such as the AU and NEPAD in developing a cohesive relationship?
- ◆ Is this a repeat performance of the commodity boom of the 1970s? And, is the region prepared?
- ◆ Who are the real winners? The bigger states or the smaller states?
- ◆ What are the implications of overlapping regional membership?

## Conclusion

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The SADC region is a diffuse community. While it is easy to become involved in differences of opinion about the role of traditional development partners compared to that of China and India, what really matters is whether SADC is benefiting to the maximum from its external relationships. As the global financial system reaches uncertain crossroads, it is important that member states (like other regional communities) examine the effect on regional economies and integration strategies.

The current financial meltdown will probably see a maturing of China's relationship with Africa and, indeed, the southern African region. Beijing's multi-billion dollar packages of the past may not be as generous in the future. In the same way, for India the priority will remain addressing growing social tensions in the domestic economy. Therefore, while China and

India may be seen as alternate development partners, the SADC community must ensure that relationship is based on a set of policies that benefit the SADC people.

## Endnotes

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1. It is rumoured that President Mugabe was asked by the Chinese leadership not to attend the 2008 Beijing Olympics and therefore had to make a detour to Singapore a day before the opening ceremony of the Games.
2. See the final Accra Agenda for Action (<http://www.accrahl.net/WBSITE/EXTERNAL/ACCRAEXT/0,,menuPK:64861886~pagePK:4705384~piPK:4705403~theSitePK:4700791,00.html>).
3. Source: Biopact 2007: <http://biopact.com/2007/09/china-opening-up-congo-for-minerals.html>.
4. Source: World Trade Atlas available on Trade Law Centre for Southern Africa (Tralac) website [www.tralac.org](http://www.tralac.org).
5. Source: World Trade Atlas available on Trade Law Centre for Southern Africa (Tralac) website [www.tralac.org](http://www.tralac.org).
6. Source: World Trade Atlas available on Trade Law Centre for Southern Africa (Tralac) website [www.tralac.org](http://www.tralac.org).
7. Source: World Trade Atlas available on Trade Law Centre for Southern Africa (Tralac) website [www.tralac.org](http://www.tralac.org).
8. Source: Naidu (2008).

# SADC and the challenge of CU status in 2010

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*Paul Kalenga*

The Regional Indicative Strategic Development Plan (RISDP)<sup>1</sup> of the Southern African Development Community (SADC) envisages the establishment of a SADC CU by 2010. This follows the launch on 17 August 2008 of the SADC FTA, which is being implemented by 12 of the 14 SADC member states.<sup>2</sup> An essential feature of a CU, generally referred to as a CET, is that all members should levy identical tariffs on their imports from the rest of the world. The understanding is that SADC countries do not necessarily need to adopt a CET for every tariff line by 2010. A transitional implementation period can be developed to allow for a negotiated convergence of their levels of external protection.

Members will first need to agree on the common rationale or parameters for the setting of the tariff. Achieving this objective remains a formidable challenge for a variety of reasons. Moving from a FTA to a CU requires compromising domestic policy, as countries give up control of an important industrial policy instrument – the tariff. Trade policy will no longer be a matter of national sovereignty but the outcome of regional compromise. In the context of economic asymmetry, divergent national trade policies and conflicting rationale for tariff determination, reaching such a policy compromise is likely to pose many political, economic and institutional challenges. This paper explores such challenges.

## CUs and SADC

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Given the multiplicity of challenges involved, negotiating a SADC CU arrangement is likely to be a complex and lengthy process. In the short to medium term, a realistic approach towards deeper regional integration is probably to implement effectively the SADC FTA (including reducing existing NTBs to trade in goods and services) while working on converging external trade policies. Such an approach may facilitate the move towards a future SADC CU in the long run.

A significant number of SADC countries already belong to CUs – the Southern African CU (SACU) and the East African Community (EAC) and a potential COMESA CU, which is currently being negotiated by most SADC members and expected to be launched in December 2008. In this context the principle of variable geometry, whereby those that are ready can move faster in appropriate CUs, may be a preferable integration strategy to the ‘one-size fits all’ approach.

It is also important to consider that the value added by such a SADC CU is likely to be determined by its ultimate objective or motivating factor. Is it an inward-looking strategy to extend and protect the SADC regional market from external competition, thereby causing trade diversion? Or is it a strategy to integrate the SADC economies into the global market through greater trade openness? Currently, there are no clear answers to these questions.

## Overview of the SADC economies

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The RISDP, a 15-year plan being implemented in five-year phases, remains SADC's vehicle for regional economic integration and has set the following milestones: FTA by 2008; CU by 2010; common market by 2015; monetary union by 2016; economic union by 2018. Clearly, a political desire exists to achieve these objectives of deeper regional integration. However, such ambitions should be seen in the context of the challenges posed by existing economic realities to the regional integration process.

### *Economic asymmetry*

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Much has been written about the economic asymmetries among SADC countries. A mere look at comparative economic indicators suggests that the process of regional economic integration will be fraught with complex challenges that cannot be addressed overnight.

According to the UN per capita income classification, SADC consists of eight low-income countries; three lower middle-income countries; and three upper-middle income economies. South Africa is considered to be the most developed in terms of overall economic size, as measured by gross domestic product (GDP). The country contributes close to 70 per cent of the region's total income (compared to only one per cent for Malawi and Lesotho), but has the largest poor population in the region. Some of the pressing problems facing South Africa are the high level of inequality and unemployment. As the most developed economy, South Africa's economic policy for addressing such challenges is likely to have implications on regional economic integration.

Wide differences in economic size, economic growth rates and development exist among SADC countries. Available data suggests that most SADC economies in the region have grown relatively slowly over the past decade. The lack of convergence in economic growth rates poses significant challenges to the process of regional economic integration as envisaged in the RISDP. With the exception of SACU economies, which showed strong GDP per capita convergence between 1980 and 2005, there has been continued dispersion of GDP per capita between the SADC and SACU economies throughout the period (DNA 2007).

Trade and industry indicators also tell a challenging story. The industrial structure of SADC economies is highly diverse. The majority of countries are heavily dependent on the production of a few agricultural or mineral products, which are exported to industrial countries. Manufacturing's contribution to value added in traded goods is not significant in SADC

countries, except for some countries such as South Africa and Mauritius. With such diverging manufacturing structures, the setting of the CET on intermediate and final products constitutes a challenge.

The policies and approaches that exist for developing the manufacturing sector are varied. For example, the manufacturing sector occupies a significant position in the development strategies of the government of South Africa<sup>3</sup>, and the tariff still remains an important industrial policy instrument in SACU. On the contrary, successive governments in Mauritius have prioritised the growth of a highly skilled services industry as the next stage in the country's development. The country's trade policy focuses on improving trade competitiveness by overhauling the incentive framework, reducing distortions and biases and turning Mauritius into a duty-free island. The tariff liberalisation programme aims to achieve a low and uniform level of protection for the manufacturing sector in Mauritius.<sup>4</sup>

### *Intra-regional trade flows*

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Generally a CU is expected to enhance trade among its members. A rule of thumb is that trade enhancement is more likely if there is a higher percentage of trade with potential partners. This suggests that the larger the share of intra-regional trade in total trade for SADC countries before the CU, the more likely trade creation will dominate trade diversion. Tables 1 and 2 provide insight into intra-SADC trade flows. The value of intra-SADC trade as a share of total imports grew from 1,6 per cent in 1980 to 10,6 per cent in 2003. Similarly, intra-SADC exports as a share of total exports grew from 0,9 per cent to 10,6 per cent over the same period. However, these figures mostly reflect SADC countries' imports from South Africa rather than their exports to SACU.

Although recent data is not available, the front-loaded SACU tariff offer made in accordance with the SADC TP led to a reduction in SACU tariff barriers against SADC economies. This has contributed to a relative rise in SACU (mainly South Africa) imports from SADC. In particular, there has been an increase into South Africa of apparel and clothing items imports from SADC (mainly from Mauritius, Malawi and Zimbabwe). Despite some positive trends, intra-SADC trade flows are still low. This low level of trade appears to suggest that a SADC CU is likely to be of marginal value to intra-SADC trade expansion.



**Table 1: Percentage share of SADC trade in SADC country imports<sup>5</sup>**

Country	1980	1985	1990	1995	1999	2003
Angola	0,0	0,6	0,8	7,1	10,0	–
DRC	0,4	1,6	1,1	18,1	31,5	–
Malawi	36,7	53,0	24,8	49,2	64,4	57,5
Mauritius	14,5	4,2	9,9	11,3	11,2	13,2
Mozambique	3,7	5,0	7,6	55,5	58,6	39,5
SACU	0,1	1,8	1,8	2,1	1,9	2,7
Tanzania	0,7	0,7	1,3	13,9	13,3	15,0
Zambia	1,2	10,9	7,9	49,1	65,5	65,0
Zimbabwe	8,3	31,7	33,1	51,2	51,2	56,1
Intra-SADC share	1,6	4,7	5,1	9,9	10,2	10,6

**Table 2: Contribution of each country to intra-SADC exports<sup>6</sup>**

Country	1980	1985	1990	1995	1999	2003
Angola	0,2	0,0	0,0	0,0	0,9	–
DRC	0,4	0,1	0,1	2,7	0,1	–
Malawi	11,1	6,1	0,5	1,9	2,3	1,8
Mauritius	2,2	0,1	1,4	0,6	0,6	0,7
Mozambique	1,8	0,1	0,1	1,4	0,0	4,7
South Africa	64,2	50,5	56,0	76,5	77,8	71,4
Tanzania	9,6	0,1	0,2	0,3	1,3	1,4
Zambia	4,4	4,1	1,0	1,3	2,0	7,0
Zimbabwe	6,0	38,9	40,7	15,4	14,9	13,0

## Rationale for a SADC CU

A recent study<sup>7</sup> on the appropriate model for a SADC CU concluded that enhancing intra-regional trade alone is a weak basis for forming the CU. The fact that most countries are already partners in the SADC and COMESA FTAs and nearly all intra-COMESA and intra-SADC trade is currently duty-free further supports this argument. Moreover, COMESA, SADC and the East African Community (EAC) have announced their intention to form a wider FTA. Thus, the rationale for establishing a SADC CU has to be sought elsewhere.

A possible motivation for forming a CU is the dynamic effects of greater openness and harmonising SADC countries' external trade policies and tariffs. As this really means that a potential CU will need to 'lock in' the current lowest and simplified tariff regime of SADC countries, most SADC countries would have to make substantial competitiveness and revenue adjustments. The critical policy challenges confronting this strategy are outlined in the following section.

## Policy challenges towards formation of a SADC CU

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For a group of countries with such diverse economic structures and levels of development to move from a FTA to a CU means many challenges, some of which are highlighted below.

### *Establishing a CET*

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In forming a CU, the critical policy challenge facing SADC countries relates to the negotiation and establishment of the CET. This process will require the convergence of 11 individual tariff policies into one uniform Most Favoured Nation (MFN) tariff regime. The SADC countries' preferential trade agreements (PTAs) with third parties make matters worse. For example, in the case of the Economic Partnership Agreements (EPAs) with the EU, the tariff structures vary considerably from country to country. The process of negotiating a SADC CET is likely to be further complicated by the pattern of emerging extra-regional preferential trade agreements such as South Africa EU-TDCA, SACU FTAs with EFTA, Mercusor and possibly China and India.

Table 3 below shows that there are vast differences in the MFN tariff structures, levels and complexity of SADC countries.

Moving or converging to a CET will require SADC economies to make considerable adjustments to their tariff policies and structures. This is likely to put pressure on negotiations aimed at a mutually acceptable CET, especially for those countries with higher applied MFN tariff rates or facing significant tariff escalation. The rationale for tariff policy is not the same for all SADC members: some use tariffs as an industrial policy instrument to protect their sensitive industrial sectors; a few use lower tariffs as a vehicle for their integration into the global economy; and the majority use tariff as a revenue-generating instrument.

A close examination of the SADC tariff regimes reveals substantial differences. On the surface the level of protection appears similar across countries ranging from an average of 3,5 to about 14 per cent. Simple average tariffs for Mauritius (3,1 per cent), Angola (7,1 per cent), and SACU (8,2 per cent) are substantially lower than the rest. The distribution of tariff rates also varies considerably, with Madagascar ranging from zero to 20 per cent and others ranging from zero to more than 500 per cent. Current trade-weighted average tariff rates range from three to 21 per cent. The number of tariff bands is between four and 100, with Zambia, Malawi and DRC having the lowest and SACU the highest number of tariff bands. The number of tariff peaks and the number of duty-free MFN rates also vary considerably. For example, over 80 per cent of tariff lines in Mauritius are duty free.

**Table 3: SADC MFN tariff structure<sup>8</sup>**

Country	Number of tariff bands	Tariffs bound %	Maximum duty bound	Duty-free bound rates %	Duty-free MFN applied rates %	Maximum duty applied	Simple ave. MFN applied %
Angola	7	100,0	80	0,0	0,0	30	7,2
Botswana	100	96,6	597	14,8	56,9	504	8,0
DRC	5	100,0	82	0,0	0,0	30	12,0
Lesotho	100	100,0	200	0,0	56,9	96	7,9
Madagascar	4	29,7	30	0,0	1,8	20	13,3
Malawi	7	31,2	125	0,0	8,7	> 1 000	13,5
Mauritius	21	17,8	122	3,2	83,3	219	3,5
Mozambique	5	13,6	100	0,0	2,2	25	12,1
Namibia	100	96,6	597	14,9	56,9	343	8,0
South Africa	100	96,6	597	14,9	56,9	> 1 000	8,0
Swaziland	100	96,6	597	14,9	56,9	504	8,0
Tanzania	11	13,4	120	0,0	36,4	100	12,7
Zambia	4	16,7	125	0,0	18,7	25	13,9
Zimbabwe	17	21,0	150	1,7	–	–	–

There are also countries that have a significant number of 'bound' tariffs – duty rates that are committed in the WTO and are difficult to raise. The levels and coverage of these bound tariffs would to some extent determine the maximum levels at which CET tariff can be set. Products bound at zero, for example, could not be increased without the agreement of other WTO members. The difference in the coverage and levels of bound rates also reflects the flexibility enjoyed by member states through special and differential treatment. However, in a CU such flexibility may be eroded by the need to adopt a uniform CET across member states. For example, in the case of SACU, uniform tariffs are applied by all members despite the stark difference in the levels of development – ranging from Lesotho (a least developed country [LDC]) to South Africa (the largest economy in the group with a diverse manufacturing base).

The summary above highlights the wide differences among SADC members in their objectives and rationale that underpins the respective tariff schedules. Therefore, the main challenge for SADC members is to reach a common agreement on the principles that would inform a CET, taking into account individual country economic situations and their obligations and commitments to WTO schedules and extra-regional agreements. For example, if Mauritius becomes part of the SADC CU, many countries will have to adjust their tariff structures substantially downward, especially the LDCs, and those developing countries that have bound their tariffs at significantly higher levels in the WTO.

### *Dealing with the revenue challenge*

Customs revenue is another critical policy challenge facing the formation of the SADC CU. For a large number of countries, customs revenue constitutes a significant part of government revenue. However, as table 4 below illustrates, the level and extent of dependency on

customs revenue in SADC varies. In general, most SADC countries rely on customs duties as a significant source of government revenue, which poses a challenge to the design, determination and setting of a SADC CET. For example, in the tariff analysis above, Mauritius stands out as the country with the lowest MFN tariff averaging 3,5 per cent. If this tariff is used as the basis for establishing the CET, a number of countries are likely to experience drastic downward revenue adjustments.

**Table 4: Taxes on trade as a percentage of total revenue (2003)<sup>9</sup>**

Country	%
Angola	5,9
Botswana	6,8
DRC	41,0
Lesotho	42,9
Madagascar	49,0
Malawi	11,0
Mauritius	21,8
Mozambique	15,1
Namibia	29,6
South Africa	2,9
Swaziland	37,6
Tanzania	37,6
Zambia	28,5
Zimbabwe	6,8

Note: Figure for Botswana represents receipts from SACU as percentage of GDP in 2004.

Countries that depend significantly on customs revenue dependence have simplified tariff structures. Common among LDCs, the tariff regimes are designed to generate revenue by applying a moderate, simple and, where possible, uniform tariff structure. Such tariff schedules minimise transaction and administrative costs and discourage any incentives to undervalue imports. The rationale for tariff setting in most of these countries is largely revenue generation. This is in sharp contrast to a country such as South Africa and its SACU partners, where the tariff structure is designed to serve industrial policy objectives. Nevertheless, the smaller SACU members still rely significantly on trade taxes. The formidable challenge facing the negotiation and subsequent establishment of a SADC CET will be balancing the diverse and conflicting revenue and industrial policy interests of the SADC states.

In addition to the revenue challenges, the question of how to collect and distribute customs revenue will affect the design of the CET. Given the number of landlocked countries, the option of individual countries collecting revenue for themselves at the first point of entry appears to be not feasible. Lessons from the SACU revenue-sharing formula can be useful in this respect, although the SACU regime has had its own challenges and the current revenue-sharing formula is probably going to be reviewed. Designing an acceptable SADC revenue-sharing formula will be yet another formidable challenge because of existing income disparities and differences in economic development. The SADC Treaty of 1990

provides for the establishment of the SADC Development Fund, which has not yet materialised. However, such a fund could be a possible way of dealing with revenue distribution challenges of a SADC CU.

### *The challenge of overlapping membership*

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A challenge to the formation of the SADC CU is the overlapping memberships of SADC member states in the three main regional integration schemes (COMESA, SADC, EAC). It would be impossible to belong to two CUs with different CETs, not to mention the related complexities of designing and administering different CETs. For example, if Tanzania were to belong to the EAC and SADC CUs, it would be impossible to implement two different tariff schedules. It would be equally difficult if Swaziland were to belong to a SADC, SACU and COMESA CU. These practical issues must be addressed before a SADC CU can be created.

### *Enlarging existing CUs or FTAs*

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A possible alternative to a SADC CU by 2010 is to recognise the existing CUs (SACU and EAC) and the potential COMESA CU and to encourage SADC members to join them. This option is not necessarily exempt from the challenges elaborated in the preceding section.

One option is for SACU, the oldest CU in the world, to drive deeper integration by opening up to new entrants (for example Mozambique and Angola). However, SACU is well-known for its complex CET.<sup>10</sup> The DNA (2007) study, which evaluated options for a SADC CU, argued that setting the CET at a level and complexity comparable to the current SACU regime would produce the smallest gains for the region, substantial trade diversion; significant revenue losses for most members; and few offsetting gains for consumers and users of imported goods. These arguments are supported by a number of studies on SACU tariff policy. Edwards and Lawrence (2008) argue that a major reform of SACU tariffs is required and would make sense especially for the BLNS countries, which would gain access to cheaper inputs and final products.

SACU's revenue-sharing formula is another obstacle to using SACU as a platform for an enlarged CU. Around 15 per cent of the revenue pool is reserved as a 'development component' to be used to address differences in per capita income. The SACU revenue-sharing formula has a very strong redistributive impact, as it reallocates revenues from the one large member (ie South Africa) to smaller and relatively poorer ones (the BLNS). The distribution of tariff revenues is based on members' shares of intra-SACU trade, which contradicts a key feature of a single customs territory by requiring members to monitor and keep records of intra-SACU trade.<sup>11</sup>

**Table 5: Receipts from SACU revenue pool, 2006<sup>12</sup>**

	Excise	Development	Customs	Total	Total % of GDP	Total % government revenue	Total per capita
	R million						
Botswana	586	483	4 565	5 634	9,0	20,1	3 692
Lesotho	85	560	2 191	2 836	28,2	53,0	1 398
Namibia	357	523	4 584	5 463	12,2	41,0	2 695
Swaziland	152	534	3 023	3 708	24,1	56,9	4 256
South Africa	13 512	493	3 620	17 625	1,0	3,9	666

Extending the SACU approach to collecting and distributing customs revenue to new entrants is likely to pose problems. The SACU revenue-sharing formula remains controversial and is unlikely to be sustainable in an enlarged CU.

EAC began to implement its CU in January 2005 by gradually reducing internal tariffs, which will be completed in 2010. Unlike SACU, the EAC and COMESA have a similar concept of the tariff. EAC has adopted a CET with a three-band structure: zero per cent for raw materials and plant and machinery; 10 per cent for intermediate goods and 25 per cent for finished goods. COMESA is scheduled to launch a CU in December 2008. Initial work on the CET commenced in 1997. Analysis of the proposed CET structure has been conducted into the revenue implications, regional competitiveness as well as the effect on WTO provisions. The analysis has taken over ten years but by mid-2008 an agreement was reached on the CET for around 6 000 tariff lines. Certain sensitive tariff lines are not included as national specificities mean they require considerably greater attention.

Information about how COMESA will deal with revenue collection and distribution is not readily available. However, COMESA has been developing budgetary assistance measures to minimise revenue gaps arising from CET implementation. The setting up of a COMESA Fund to this effect has been approved.

Apart from Angola and Mozambique, all SADC countries are associated with existing or potential CUs outside the SADC configuration. An alternative option to the formation of a SADC CU is to explore ways of consolidating these processes on the basis of variable geometry. Nevertheless, the ability to arrive at common perspectives on the tariff and collection/distribution of customs revenues remains critical in this process.

Otherwise, SADC countries can simply focus on consolidating the FTA while retaining their national trade policy space. The FTA process is further given impetus by the COMESA-EAC-SADC tripartite Summit of Heads of State and Government that took place in Kampala, Uganda, and endorsed politically the establishment of a pan-regional FTA. The priority areas for this prospective FTA include, amongst others, harmonising inter-REC tariff regimes, RoO and related trade facilitation issues.

## Conclusions

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The SADC regional integration agenda envisages moving from a FTA to a CU. The rationale or motivation for forming a single customs territory in SADC is not yet clear. It is this rationale that will influence the design of such an arrangement, in particular the setting of a CET.

An assessment of the various tariff structures has shown that wide differences exist among SADC members. This vast difference can be seen in the levels and complexity of individual countries' MFN and preferential tariff structures, which need to be converged into a single, uniform MFN tariff regime. In addition, SADC countries perceive the tariff's role differently, as an instrument either of trade and industrial policy or for generating revenue. To achieve the SADC CU would require: the convergence of SADC countries' different tariff structures; a common agreement on the objective of tariff policy; and setting the tariff levels.

For a large number of SADC countries, customs revenue constitutes a significant part of government revenue, which creates challenges for designing the CET regime and establishing procedures for collecting and distributing customs revenue. There are likely to be countries which will face significant revenue adjustment challenges.

Deepening regional integration does not necessarily mean following a CU model of integration. Indeed, this approach is particularly challenging in view of the countries' underlying divergences relating to economic conditions, interests and policies. Alternative options exist such as adopting a variable geometry approach whereby countries that are ready can join the existing CUs; or concentrating on effective implementation of the SADC FTA, which includes reducing and eventually eliminating barriers to trade in goods and services. The FTA approach can also be extended to include strategies aimed at greater convergence of SADC countries' external trade policies and tariff structures and improved international competitiveness. Achieving these goals will take time unless members are prepared to make drastic adjustments, which seems very unlikely for most SADC countries.

Finally, to be desirable and necessary, a CU must promote sustainable economic growth and development. Therefore, it must be designed to raise and enhance SADC countries' integration with each other and with the global economy. This will require a simpler, lower and more uniform tariff structure, which takes into account revenue and domestic competitiveness challenges. From this perspective, integration behind a CET is likely to be a complicated, lengthy and challenging exercise. It is necessary that a broader stakeholder consultation is encouraged in moving towards a SADC CU by 2010 or beyond.

## Endnotes

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1. The RISDP was adopted by the SADC Heads of States and Government in August 2003.
2. Angola and the DRC are not yet implementing the SADC FTA Protocol.
3. The Economist (2007), South Africa Country Profile.
4. Source: Calculations by Development Network Africa (DNA) based on SADC trade database.
5. Source: Calculations by Development Network Africa (DNA) based on SADC trade database.
6. Source: World Tariff Profiles, 2006.
7. Source: World Bank, 2005.
8. WTO Trade Policy Review, 2003.
9. For further discussion see Flatters and Stern (2006).
10. Source: Flatters and Stern (2006).



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- Note: these references were removed from the list. The exception was the one from Eva's paper, which I removed from the text as reference was invalid.



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