SACU Workshop 8-9 November 2018

On 8-9 November 2018 **tralac** brought together participants from the public and private sectors in South Africa, Botswana, Lesotho, Namibia and eSwatini to discuss the future of the Southern African Customs Union ('SACU').

Trudi Hartzenberg, tralac Executive Director opened the workshop by posing the titular question: Is SACU now at a tipping point? It is no secret that SACU has been facing challenges for some time. The 2002 Agreement which entered into force in 2004, is not and is most unlikely to be fully implemented. The membership is divided on this score, with some holding steadfastly that it should be implemented. Setting SACU in a broader African context, it is noteworthy that almost approximately half of total intra-African trade takes place within SACU. Africa has embarked on an ambitious integration initiative, to establish a continental free trade area. There is a rush to ratify and a diplomatic impetus for African Continental Free Trade Area (AfCFTA) to enter into force, despite the fact that negotiations are not complete.

The World Trade Organisation (WTO) is facing a complex set of challenges. It is increasingly clear that the trade rules of the WTO are not appropriate to deal with China's model of state capitalism. The US and the EU have very different views and expectations of the WTO – the US supports a transactional system, to support and enforce the agreements of the WTO, while the EU supports a broader remit for the dispute settlement system to contribute to rule-making.

Brexit news is uncertain. Since all SACU member states are parties to the Southern African Development Community (SADC) Economic Partnership Agreement (EPA), it is important to monitor this process. The future UK – EU relationship could have important implications not only for the future relationship with the UK, but also with the EU - on matters such as tariff rate quota's for South Africa, and practical trade facilitation matters such as border management, standards and rules of origin. What we can learn from Brexit, is how difficult it is to undo a deep integration arrangement. The United States' trade policy is volatile. The Africa Growth and Opportunity Act (AGOA) ends in 2025; currently it appears that the US prefers free trade agreements with key African partners. SACU was created as a customs union with a very specific purpose; to facilitate the management of Great Britain's trade and fiscal affairs in southern Africa. Although the legal arrangement (SACU Agreement) covers trade in goods, SACU is more than that. SACU is also an excise union, and four of the five members also belong to the Common Monetary Area (CMA). The commercial reality is that SACU is the most integrated economic space in terms of subregions on the continent. So, when we consider the future of SACU, we must consider more than just what we see in the legal instruments.

Facilitated by Trudi Hartzenberg, Gerhard Erasmus and Anton Faul, over the course of the 1.5-day workshop, participants debated and discussed the issues in an open and frank manner.

Lack of implementation of the SACU Agreement

Participants focused, in particular, on SACU developments since the entry into force, in July 2004, of the 2002 SACU Agreement. Participants noted that the history of SACU is one of non-implementation and question what the potential for moving forwards is, and in which direction.

Points of reference for the discussion included the evolution of the SACU Work Programme. This programme started as a comprehensive 11-point plan, adopted in July 2010, was then consolidated into the 7-point agreed in April 2013, which covered the following issues:

i. Regional Industrialisation
ii. Establishment of institutions
iii. Initiatives to promote intra-SACU trade & trade facilitation
iv. Unified engagement in trade negotiations with third parties
v. Sharing of SACU Revenue, and financing options for cross-border projects
vi. Trade in Services, and
vii. Strengthening the capacity in the Secretariat.

At the June 2017 Summit, the programme was pared down to three priority areas:

i. Development of an appropriate architecture for tariff setting
ii. Public policy interventions for industrial development and regional value chains
iii. Sharing of SACU revenue and financing options for cross border projects

While there are areas of agreement among the member states across these three work areas there are also fundamental differences in views about the way forward for SACU. Progress is being made on the industrial development priority, under which members have agreed to use the SADC Industrialisation Strategy as a basis and to identify 2-3 cross-border projects for immediate implementation and financing.

The revenue sharing arrangement is often described as the 'glue' that holds together the customs union. The dependence of the smaller member states on revenue from the SACU pool is well-documented. Exacerbating this, is that midst the current economic challenges, which include low growth rates and structural unemployment, fiscal challenges feature very prominently. Discussions about future options for revenue sharing have to reckon with a shrinking pool as tariff revenues decline.

SACU: The 21st century reality

Participants agreed that the SACU reality is one of deep market integration. SACU accounts for more than 50% of intra-Africa trade; South Africa, as the SACU economic powerhouse, is the anchor for this trade nexus. Notably, Botswana and Namibia rank amongst South Africa's top global trading partners, making SACU important not only for South Africa's African trade footprint, but also for its global trade strategy.

Although the SACU Agreement does not cover trade in services, cross-border trade in services linkages are well established. These linkages are consolidated through mode 3 (establishment of commercial presence) in key sectors such as financial services, logistics, wholesale and retail distribution services, communication and professional services, predominantly from South Africa to the BLNE.

The CMA means that the South African Rand is legal tender in all but Botswana, and that South Africa's monetary policy is effectively implemented by Lesotho, Namibia and eSwatini. Payment facilitation across the CMA region, using the Rand, is a big advantage; and exchange rate risk among these members is eliminated. But the volatility of the Rand in recent years, has brought its own set of challenges for the smaller economies.

The import tariff remains an important trade, industrial and fiscal policy instrument in SACU. As a customs union, the member states have given up trade policy space, and articulate a common trade in goods policy which centres on the common external tariff (CET) and the management of the import tariff in its various manifestations. For South Africa, a strategic tariff policy is a central feature of its current trade policy and it states clearly that the tariff is a favoured instrument of industrial policy. This means also that the country is a prolific user of anti-dumping duties, and more recently of safeguards to address unfair trade practices and to stem surges in imports that harm domestic industry. Impacting directly on the domestic price of imported goods, it can change relative prices in favour of domestically produced goods to shift demand away from imports. South Africa is unlikely to agree to joint decision making (in a consensus decision making model) on the import tariff. For the other member states, the tariff is an important determinant of the revenue that they will receive from the pool. But they too, would like to use a particular manifestation of the import tariff – rebates – to promote their industrial development.

The import tariff features in many important SACU debates and is therefore responsible for tension among the member states. For these reasons, the establishment of the SACU Tariff Board remains a contentious issue. South Africa's International Trade Administration Commission (ITAC) serves, in terms of a mandate accorded by the SACU Council of Ministers, as SACU's Tariff Board. The mandate is wide in scope, without detail and clarity on the procedures for involvement of the BLNE in decision making on tariff matters. It is notable that ITAC is a South African institution and functions in terms of the mandate provided in South Africa's International Trade Administration Act (ITAA) to serve South Africa's trade and industrial policy objectives. No other SACU member state has a functioning trade body yet. Botswana and Namibia have developed laws for international trade administration, but don't have functioning institutions; eSwatini and Lesotho have neither.

SACU is a member driven structure with consensus decision making. South African will not be willing to accept a consensus decision making model on the import tariff. This is not unexpected, given South Africa's dominant share of regional industry. The state of South Africa's industrial sector, with challenges of deindustrialisation and significant competitiveness hurdles, raises the stakes for South Africa. At the same time, the smaller countries want policy instruments to develop their very limited industrial sectors. Non-sugar producing countries have for example been mobilising very strongly for a sugar rebate, to support downstream industries such as beverages. Prospects for success look very slim.

SACU's trade agreements

Participants were updated on progress, and shared views on SACU's existing agreements and those under negotiation.

SADC-EU EPA (Economic Partnership Agreement) is the only functional EPA with Africa. It is essentially a SACU (and Mozambique) FTA with the EU. It entered into force in October 2016. It is making Brexit easier to handle for SADC.

SACU-EFTA (European Free Trade Area) Agreement

This is currently under review. EFTA is proposing new issues particularly binding commitments around trade and sustainable development and trade facilitation. We are part of these agreements where these are governed, but EFTA seeking enforcement under trade agreement. The SACU agreement does not explicitly give jurisdiction over sustainable development issues and we will increasingly face this kind of problem because SACU is an incomplete arrangement in relation to the needs of a 21st century trade agreement.

SACU-India

There are "ongoing" PTA negotiations, and a new scoping round (after a 10-year hiatus) is scheduled soon.

Southern African Development Community (SADC)

SADC is much more than just a trade agreement. There is a long list of formal legal instruments but that alone is not evidence of well-functioning deep integration. On trade in services, negotiations are ongoing. Namibia only joined negotiations recently.

Dispute settlement remains an issue, as does overlapping membership and Zimbabwe's request for special dispensation.

Tripartite Free Trade Area (TFTA) & African Continental Free Trade Area (AfCFTA)

TFTA was an ambitious integration initiative by the 26-member states of SADC, EAC and COMESA. A key objective was to solve the problem of overlapping membership. This ambition was diverted by senior officials once the negotiations began, and now only those member states (or customs unions, such as SACU) that are not party to the same FTA are to negotiate bilateral tariff concessions. Active negotiations are between SACU & EAC-minus Tanzania, SACU-Egypt and Egypt-Tanzania. Among the outstanding negotiations for SACU are: Eritrea, Somalia, Tunisia, South Sudan, and Djibouti.

TFTA also has work programmes on industrial development, infrastructure and trade facilitation – however not much progress has been made.

South Africa has ratified the agreement, as have Egypt and Uganda. It is not clear when agreement will enter into force and it has been overshadowed by the African continental free trade area (AfCFTA).

The aim is to liberalise 90% and the objectives are very ambitious. However, there are limitations. One must look at the fine print - RECs continue to exist and existing RECs will not see further liberalisation and retain ROOs. Similar modalities in AfCFTA means same challenges we see in SADC will also hamper intra-African trade

The AfCFTA is closely linked to the AU's Boosting Intra Africa Trade (BIAT), but it is important that the AfCFTA is not viewed as a vehicle for creating a continent-wide import substitution arrangement, but as a platform for enhancing competitiveness to support trade with all trade partners. But the opportunity windows are starting to close. 11-member states have now ratified (mid-November) and 22 are needed for entry into force – the aim is to reach this by end January. It may well be that this threshold is reached by end January, but that tariff concessions and specific sector commitments will not have been negotiated. At this stage, we have not agreed on negotiation modalities for tariff concessions and services sector commitments. And for RoO, while much progress has been made, the tough negotiations (related to sensitive products) still have to take place. The bottom line is that a free trade area requires, at minimum, preferential tariffs and rules of origin.

It is a great pity we haven't been able to come up with innovative approaches and modalities, in services - we have not paid attention to sector development strategies, enhancing competitiveness of the sector.

Nigeria has not yet signed the agreement and is engaged domestic consultation processes. There is no indication yet as to when Nigeria can be expected to sign and ratify.

Phase II will cover cooperation on investment, competition and intellectual property. The negotiations on sector commitments in services may well be pushed down the line and will run alongside phase II negotiations. This may well have advantages in terms of the potential for cross-referencing to ensure internal consistency and coherence, given the close connections for example between sector regulation and competition policy.

Where to now?

An extraordinary Summit was scheduled for 30 November – but this will no longer take place. It seems to be the case that SA is reviewing the arrangement, while the remaining economies continue to advocate for full implementation of the 2002 agreement. It is unclear whether consensus can be reached, but participation from the private sector and domestic policy processes can be improved.