SACU Tariff Policies:
Where Should They Go From Here?

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Background

- National Treasury contracted “International Panel” to advise on growth strategy
- Two trade reports
  - Trade Policy Matters
  - SACU Trade Policy
- In this presentation I will present the trade policy proposals.

Outline of paper

- (A) Characterize and consider rationales for current SACU tariff structure
- (B) Evaluate Alternatives for a Tariff policy rule.
- (C) Present options for regional trade arrangements.

A. Three conclusions on SACU Tariff Structure and Rationale

Conclusion 1: Complex with high nominal and effective protection on certain sectors and a continued bias against exports

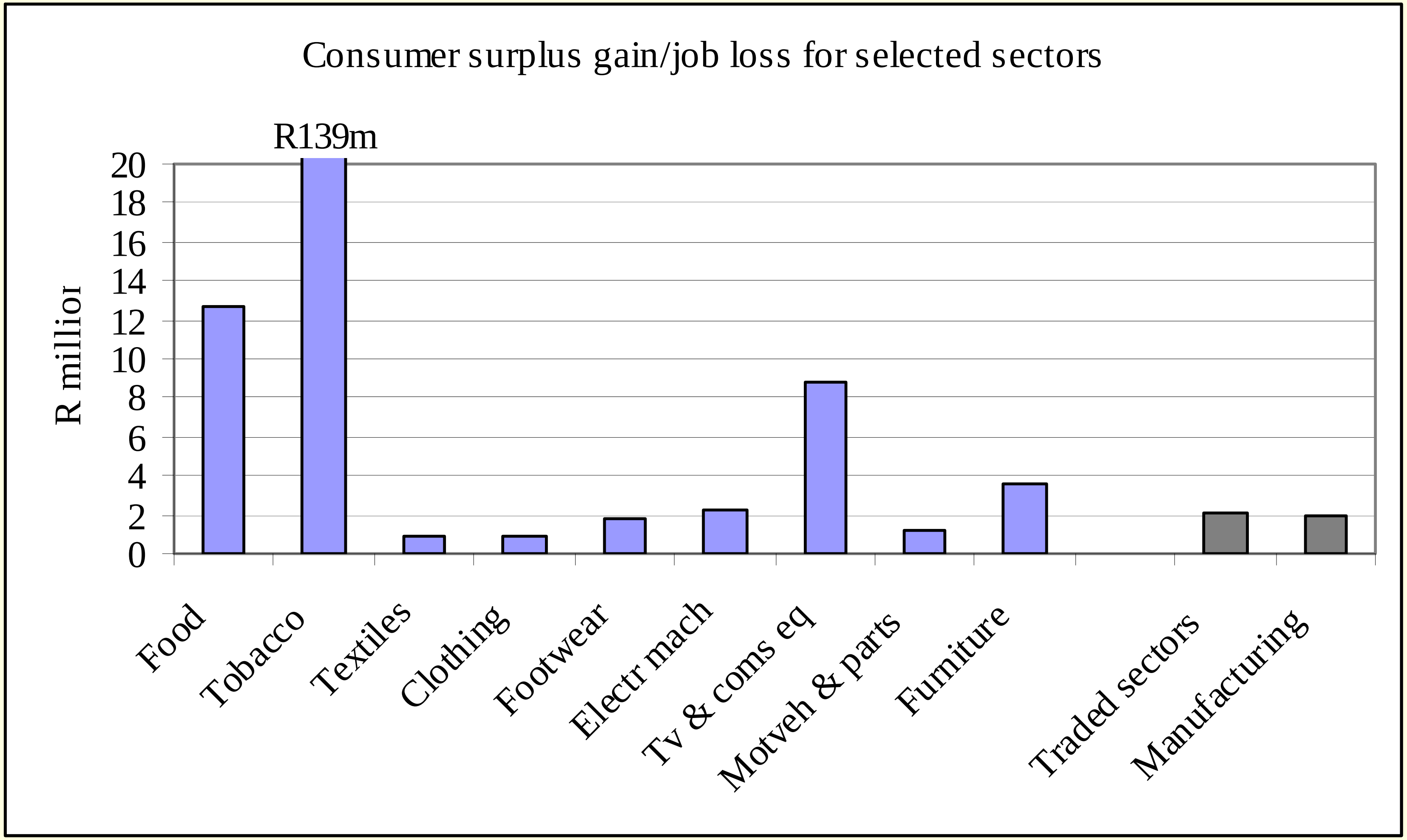
- Over 100 tariff bands vs. 6 proposed in 1994
- Effective protection exceeds 40 percent on final manufactured goods
- Anti-Export bias: Domestic production between 20 – 40 percent more profitable than export production
- Relatively complex compared to other middle-income countries

A. Three conclusions on SACU Tariff Structure and Rationale

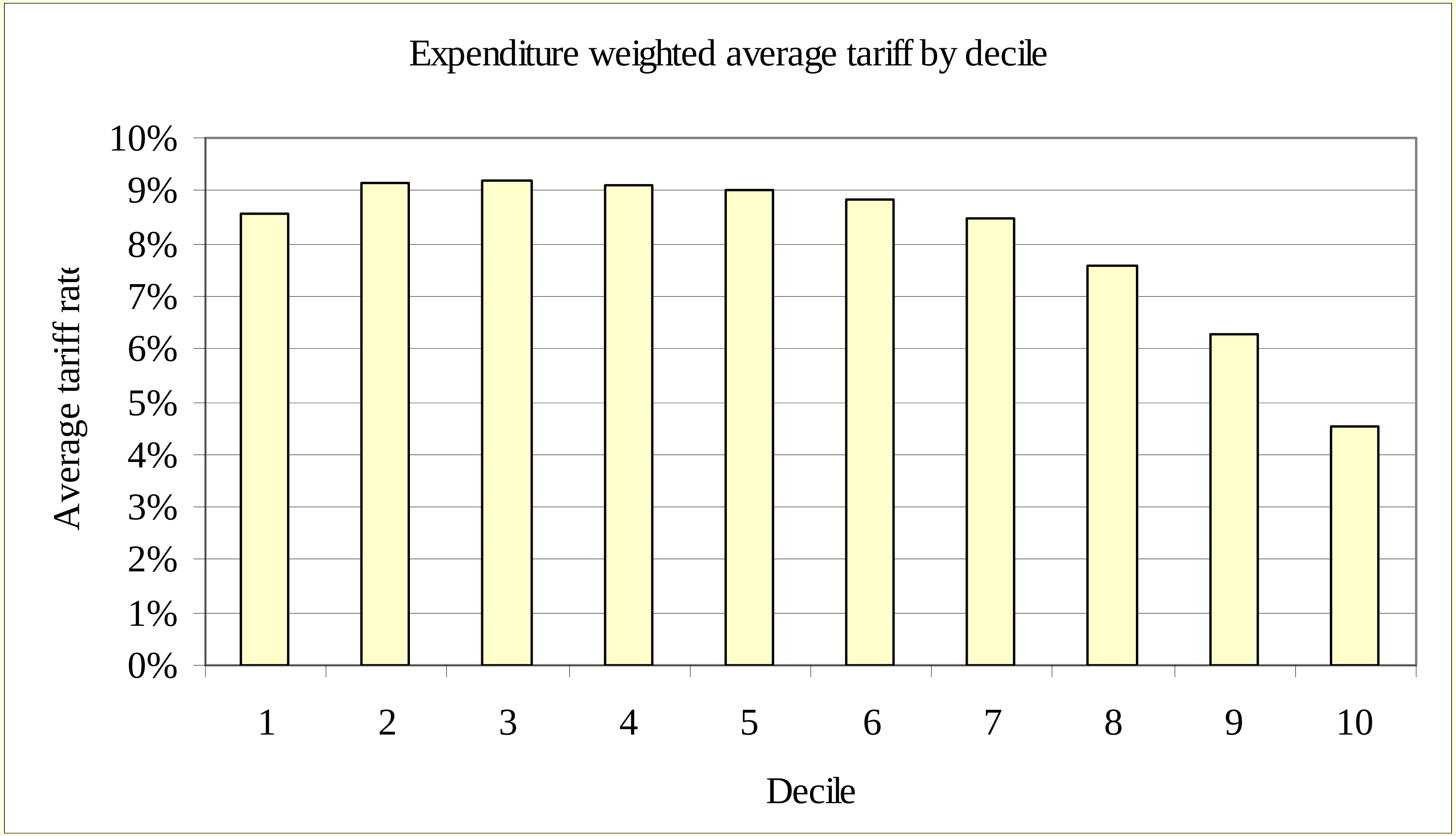
Conclusion 2: Inefficient and costly to consumers in preserving employment

- Jobs protected in clothing, textiles, footwear and motor vehicles
- But jobs lost in primary sectors and services

Leading to High Consumer Cost per Existing Job and per Job Lost



Costs Fall Disproportionately on the Poor Relative to their Income



A. Three conclusions on SACU Tariff Structure and Rationale

Conclusion 3: Protection cannot be justified on infant-industry grounds

- We consider measures of productive potential developed by Hausmann and Klinger (strategic value, density) and PRODY

- Nominal and effective protection are relatively high in sectors with low PRODY, strategic value (to a lesser extent) and density.
  - *This means that the sectors that are being given protection are not those which are likely to enhance competitive capabilities in the future.*

- But on the positive side, tariff protection does not impede export growth of sectors with high PRODY and density values.

B. An Alternative Structure:

Aim: A tariff structure that

1. Preserves key labor-intensive activities.
2. Stimulates non-commodity export orientation
3. Facilitates regional integration.
4. Enhances the value of industrial policy.
5. Assists consumption of the poor.

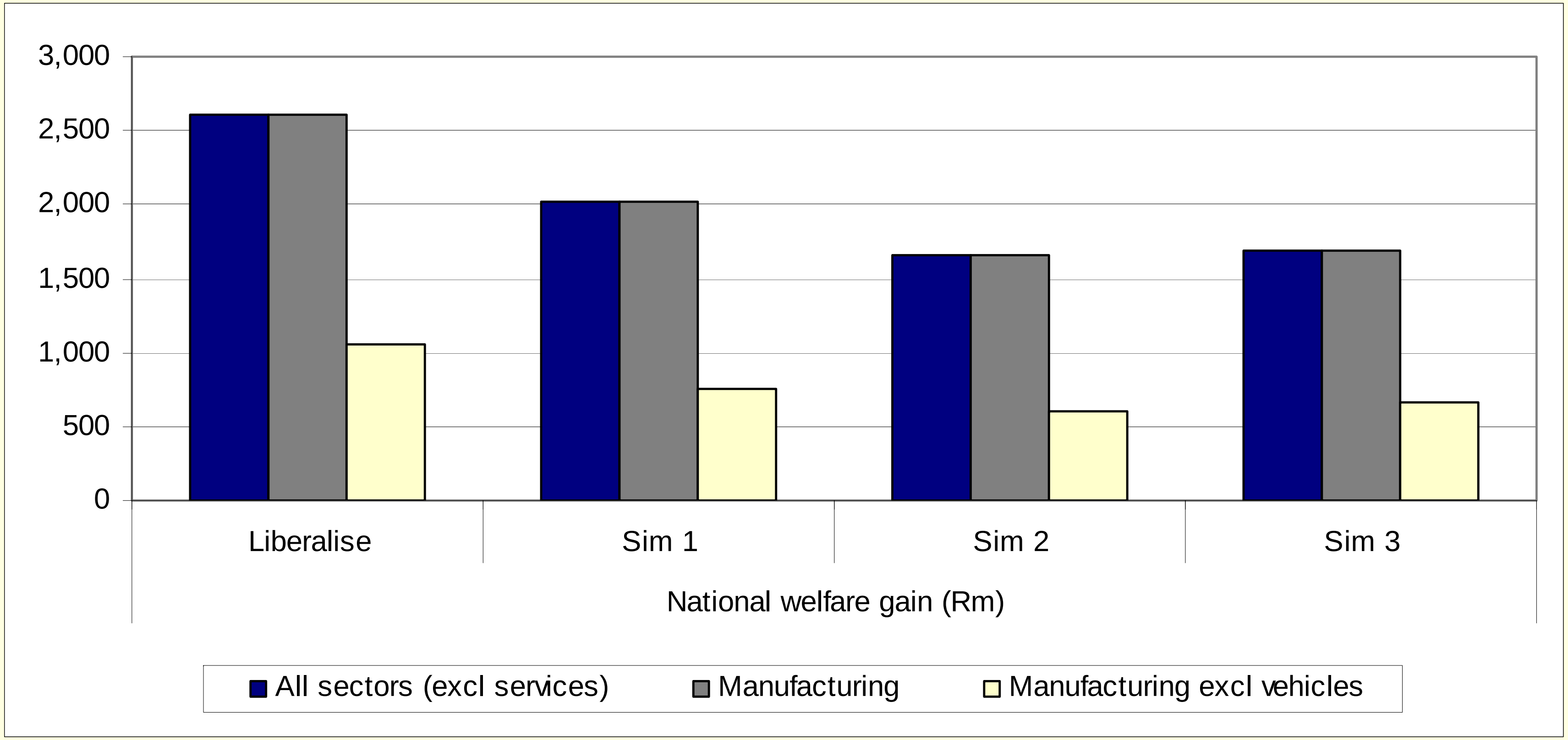
The Key Ideas

- Concentrating on reducing input tariffs can both promote exports by reducing export taxes and will increase effective protection on remaining sectors.
- Indeed, by reducing input tariffs, there may be scope to provide benefits to final consumers by reducing some tariffs without reducing protection for some producers.
- Further, simplification reduces the burden of administering rebates, provides a transparent signal for resource allocation and is less open to corruption and industry lobbying

Simulation Scenarios

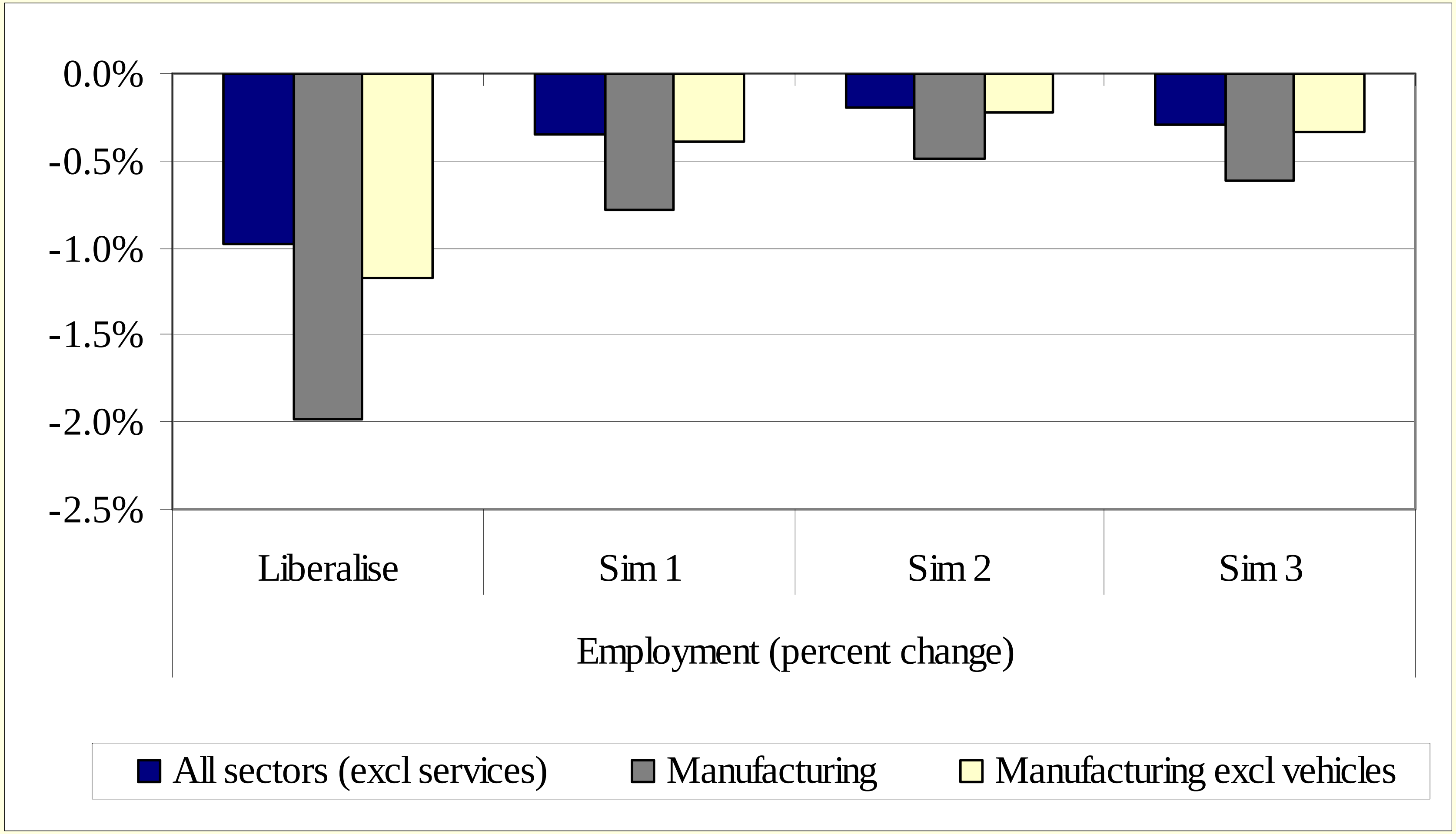
- **Scenario 1 (Sim 1): Single Band Final goods**
  - *Input liberalisation with a 15 % tariff on final goods with current tariffs in excess or equal to 10%. Zero tariff otherwise*.
- **Scenario 2 (Sim 2): Dual Band Final goods**
  - *Input liberalisation with a 20, 10 or zero percent tariff on final consumption goods.*
- **Scenario 3 (Sim 3)**: **Dual Band All goods**
  - *Partial liberalisation of inputs (10 or zero percent) and a 20, 10 or zero percent tariff on final goods*.

Scenarios achieve 60 – 70 percent of National Welfare Gains from Liberalisation

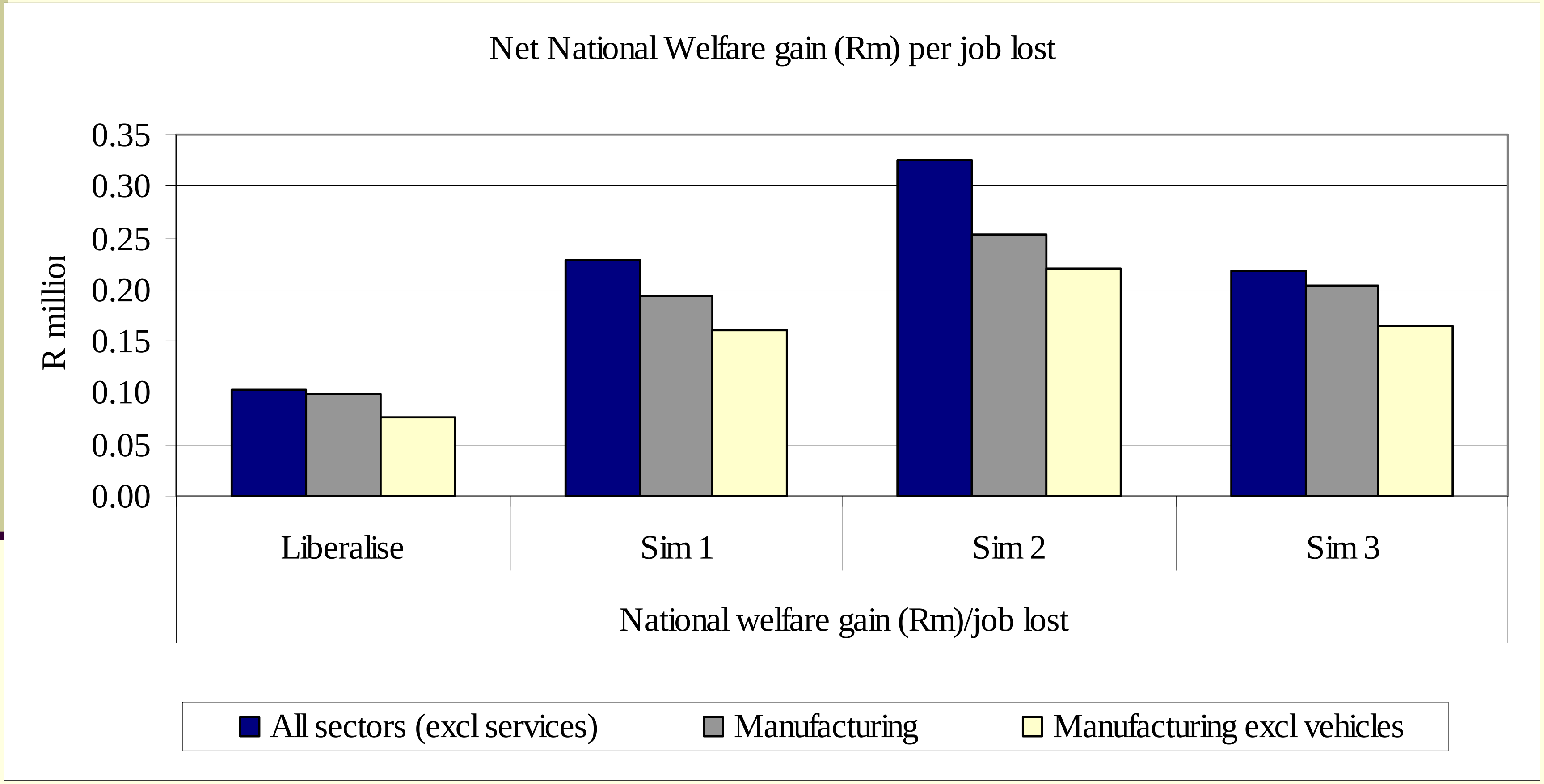


With only 20 to 35 percent of the Employment Losses from Liberalisation

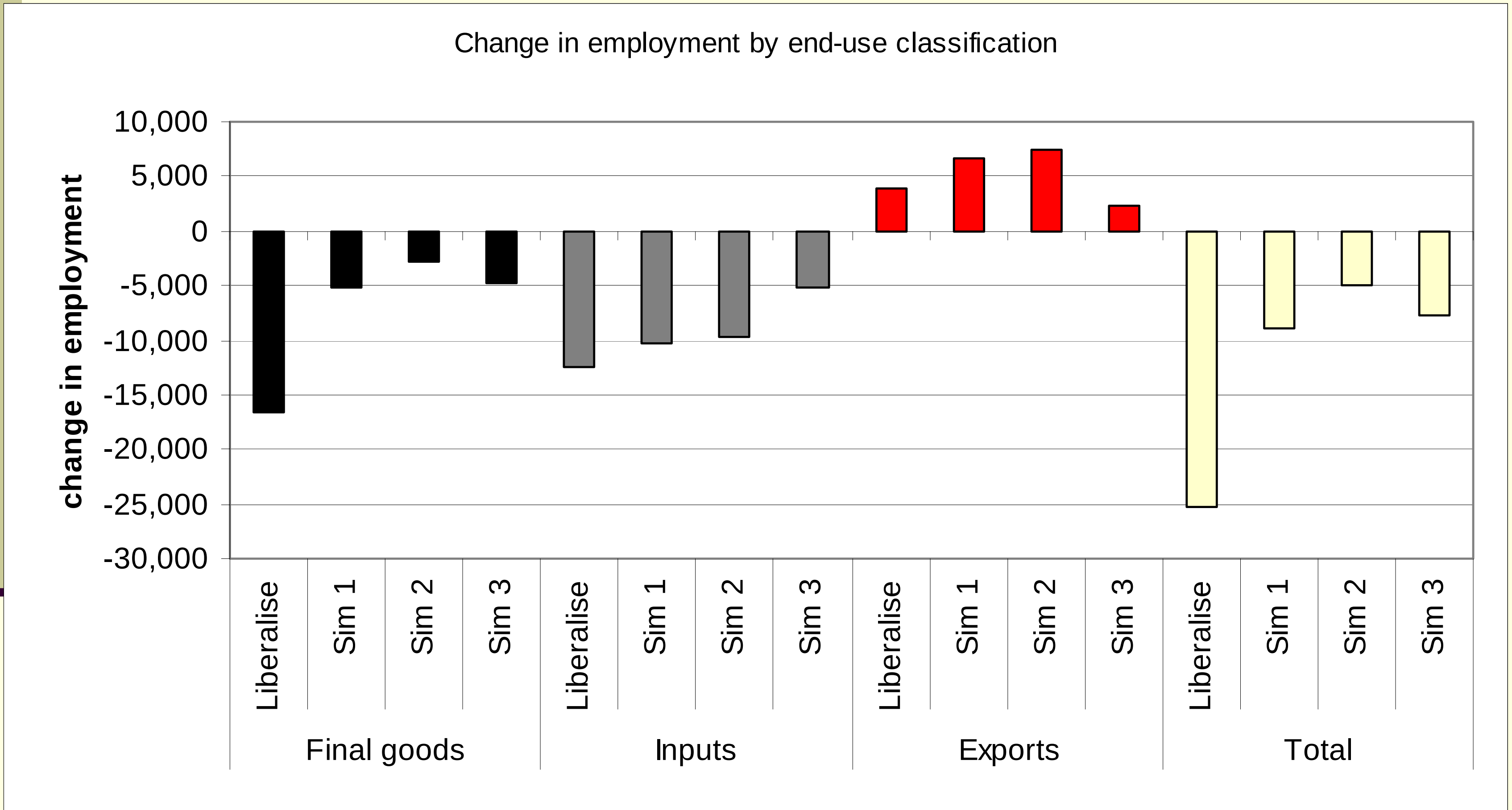
Figure: Employment changes



Leading to Higher Welfare Gains per Job Lost than Liberalisation



Employment is Re-oriented Towards Exports



Conclusion

- Simplification of tariff structures, combined with liberalisation of tariffs on inputs and outputs simultaneously:
  - Provides benefits to consumers,
  - Limits employment dislocation,
  - Promotes exports,
  - and provides a norm against which industrial priorities can be set.
  - Facilitates multilateral trade negotiations

C. SA Regional Trade Arrangements

- Fundamental interests:
  - Enhance export and investment opportunities. (Role as hub)
  - Promote regional economic development.
  - Deepen political relationships.
- Current Focus: SACU and SADC.

SACU Revenue Sharing Formula: Show me the money!

- After 15 percent deduction for development fund, distribution of customs revenue on basis of intra-SACU trade shares. This results in redistribution far in excess of costs imposed on BLNS by SA tariffs.

- SA Auto boom resulted in explosive rise in payment from R9.7 bn in 2003/04 to R25.2 billion in 2006/2007.

- Now over half all government revenues for Namibia, Lesotho and Swaziland and a fifth of government revenues of Botswana

RSF: Deeply Flawed

- Inhibits trade. (Still need customs)
- Introduces payments volatility
- Payments unrelated to external revenues generated by trade
- Creates perverse incentives- BLNS to resist additional liberalization South Africa to use rebates as an industrial policy tool.
- Inhibits new accessions
- Development basis is unclear. Per-capita the largest transfers are going to Swaziland and Botswana and much smaller transfers are being allocated to Lesotho which is much poorer.
- South Africa receives little credit for its generosity as an international donor
- South Africa is unable to ensure that the funds are spent on development.
- Weakens BLNS incentives to develop adequate tax bases.

RSF Reform: How?

- De-link development assistance from tariff revenue
- Development Assistance Fund.
  - Allows planning.
  - Encourages BLNS to find alternative tax sources.
  - Allows for explicit development assistance.

- External Revenues shared on per capita basis.
  - Expresses SACU solidarity.
  - Eliminates internal customs controls

SA-SADC Options (Status Quo)

- Implement SADC Customs Union as planned
  - Free flow of goods
  - Allows for common negotiating positions
  - Induces institutional and political cooperation
  - Requires common policy approaches
  - Preserve current commitments.
- But:
  - Exposes inconsistencies in current commitments: overlapping membership problem.
  - Requires new RSF.
  - Requires CET.
  - Inhibits industrial policies.
  - Limits negotiations of S&D treatment.

SA Options (Alternative)

- Deepen and emphasize SADC FTA but postpone Customs Union.
  - Can still pursue deep integration and cooperation
    - Services liberalization.
  - Rules of Origin obstacles remedied by new tariff structure
  - Accommodates national differences in structure and strategy
  - Preserves independence of action vis-à-vis third parties
  - Avoids credibility problems.
  - Avoids revenue sharing issues.
- In addition: Propose Comesa-SADC FTA.

Conclusions

- **Tariff structure needs work.**
  - There are much better and simpler options. Emphasize input liberalization and a few bands
- **RSF needs revision.**
  - Keep revenue sharing and assistance separate.
- **Regional arrangements need rationalization.**
  - Stick to Free Trade Agreements.