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Botswana's Trade Agreements: Potential Benefits from non-SACU Bilateral and Multi-lateral Agreements

Johnson T. Maiketso
Research Fellow, BIDPA

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Introduction

Historically the most important component of Botswana's foreign trade regime has been the Southern African Customs Union (SACU) Agreement. Dating back to 1910, the SACU Agreement has been renegotiated twice, first in 1969, just a few years after Botswana, Lesotho and Swaziland (BLS) became independent, and second in 2002, after South Africa was democratized in 1994. As a Customs Union arrangement, the SACU Agreement forms the basis for Botswana's trade policy since it prescribes a common external tariff for member countries, which also include Lesotho, Namibia, South Africa and Swaziland, and free trade within the Union. The renegotiated agreement takes regional trade integration further by requiring SACU members to negotiate as a bloc in trade agreements with other countries, and largely prohibits member countries from negotiating new bilateral agreements or amending the existing ones unilaterally. The issue of whether SACU has on balance been a net benefit for Botswana is a controversial one, without general agreement on the outcome. Indeed, it is not an easy task to enumerate and weigh up the benefits of Botswana's membership of SACU vis-à-vis the costs. Nevertheless, the stable revenue contribution that government has received from the customs union has over the years stood out as a tangible benefit to the country.

While SACU is particularly important for Botswana, there are a number of other trade arrangements to which Botswana belongs. This policy brief attempts to highlight the benefits that Botswana enjoys or could enjoy from such arrangements. These trade arrangements include bilateral (such as Botswana-Malawi and Botswana-Zimbabwe bilateral agreements), regional (such as the SADC Trade Protocol) and

multilateral agreements (such as the World Trade Organisation (WTO)). Lately, there is a growing trend that involves trade negotiations between intercontinental regional blocs such as the recently concluded and signed SACU-Mercosur Agreement. SACU's negotiations with the USA for a free trade agreement have been suspended. SACU has also been in discussions regarding possible free trade agreements with China and India. At the multi-lateral level, the WTO is the custodian of the different international trade agreements and rules that govern the conduct of global trade, and all bilateral or regional trade agreements must be consistent with WTO rules.

This brief will focus on three of the most important non-SACU trade agreements that affect SACU, that is the SADC Trade Protocol, Economic Partnership Agreement negotiations with the European Union, and the US Africa Growth and Opportunity Act (AGOA). The policy brief is based on the study, "Diversifying Botswana Exports: An Overview", carried out by BIDPA and the World Bank in 2005.

Southern African Development Community (SADC) Trade Protocol

After SACU, the second major regional trade arrangement that Botswana belongs to is the Southern African Development Community (SADC). SADC was not originally created as an economic or trade arrangement but has over time embraced trade issues. To this end, the SADC Trade Protocol was ratified in 1996 and came into force in 2000.

The modus operandi of the protocol is to gradually liberalise trade in the SADC region. Therefore, the SADC member states have put forward tariff reduction commitments, which aim to eliminate tariffs over a maximum period of 12 years up to 2012, with most tariffs eliminated by 2008. The tariffs that are already low will be eliminated immediately, those for sensitive products will be eliminated over a period of 12 years and all the other tariffs will be eliminated in 8 years. The SADC Trade Protocol also covers regional regulatory cooperation, promotion of trade in services, cross-border investment and trade facilitation.

As a member of a customs union (SACU) that has brought with it tangible benefits in terms of tariff revenue, and free access to the largest economy in Africa for Botswana, the relative importance of SADC and its trade protocol might seem to be small, especially given that progress towards a more inclusive regional liberalisation through SADC is slow. Overall, it seems unlikely that the SADC free trade agreement, once finally implemented, will have much impact on Botswana's gross trade flows. Botswana already belongs to SACU and has a free-trade agreement with Zimbabwe. It has very little export trade with Malawi, Zambia and the other non-SACU SADC members.

Nevertheless, there are some potential benefits that might accrue. While most SADC economies (apart from South Africa) are small, some member states have recently registered improved economic growth and increases in per capita incomes, thus should in time be expected to become significant markets. Currently, SADC population is well over 200 million, suggesting a significant potential market for Botswana export products. Further, the SADC FTA is expected to provide Botswana firms with additional sources of cheap and proximate supply of inputs.

However, SADC's trade integration plans go further than just the FTA, and there is a stated intention to move towards a Customs Union by 2010. This timetable is highly ambitious and difficult to achieve. There are also significant problems resulting from the multiple memberships of SACU and SADC countries in different trade agreements, which risk eroding the influence of both organizations if it is allowed to continue. Of the members of SACU, South Africa, Botswana, Lesotho and Namibia

are members of SADC, while Swaziland is a member of both SADC and COMESA. One of the main costs of overlapping membership is that it undermines the harmonization agendas of competing organizations. It is ultimately counterproductive to have overlapping organizations, and unworkable if they are both customs unions. At some point, a choice has to be made, most acutely for countries in both SACU and COMESA. It should also be noted that if the SADC Customs Union does come to fruition, SACU will effectively cease to exist.

SADC-EU Negotiations on EPAs

The European Union has for many years offered non-reciprocal market access to the African, Caribbean and Pacific (ACP) nations[1]. Currently, this dispensation is governed by the Cotonou Agreement, which was preceded by the Lome Conventions I through IV. However, the Cotonou Agreement is incompatible with WTO rules, which do not generally permit non-reciprocal trade agreements[2]. It therefore has had to operate under a WTO waiver, which expires at the end of 2007 and is unlikely to be extended. Therefore, negotiations are ongoing between the EU and ACP states to develop trade relations into reciprocal trade arrangement, termed Economic Partnership Agreements (EPAs).

Expected Outlook of the EPAs and Potential Benefits and Costs

When completed the EU/ACP negotiations are expected to yield new Free Trade Agreements (FTA) between the EU and ACP negotiating groups (6 in number)[3]. Botswana falls under the SADC negotiating group, which also includes Lesotho, Namibia and Swaziland plus Angola, Mozambique and Tanzania. However, several SADC members are (confusingly) members of a different negotiating group, for Eastern and Southern Africa. In essence, the EPAs will replace the non-reciprocal preferential market access that the ACP states have enjoyed under the Lome Conventions and the current Cotonou Agreement, and will be more akin to the existing Trade and Development Co-operation Agreement (TDCA) between the EU and South Africa.

The replacement of the preferential market access to the EU market will open up the ACP states to more competition in their home markets from the EU countries, and possibly more competition from other countries for their exports to the EU market. For Botswana, this may mean more competition for beef exports that has over the years enjoyed the preferential EU market access. The status of beef under the EPA (sensitive products) is still being negotiated, although it is unlikely that other ACP states (apart from Namibia) would be able to provide significant competition for Botswana in the EU market[4]. Nevertheless, the existing beef protocol will change, and other ACP states will find that the markets for products like sugar, coffee, rice, bananas etc will also change.

Preferential (duty-free and quota-free) access to the EU market has historically been important for apparel and textiles exports from Botswana. However, it would seem that the introduction of AGOA by the United States made a significant mark in terms of shifting Botswana's textile exports from the EU to the US. Under the current dispensation that classifies Botswana as an LDC, the US market is more accessible than the EU market, thus the shift to the US market. The table on the next page shows the different trade arrangements that affect apparel and textiles exports from Botswana.

1 The agreement is non-reciprocal in that the ACP countries do not have to offer concessions to the EU in return for gaining concessions from the EU.

2 The provisions of GATT Article XXIV of 1994 require that countries that enter free trade agreement should meet two key conditions. The first condition is that such regional trade agreement should liberalise "substantially all trade." Secondly, such liberalization should be implemented within a "reasonable time." Since the Cotonou agreement is incompatible with these provisions, it is scheduled to be replaced by a reciprocal trade agreement by end of December, 2007.

3 The regional negotiating groupings include West Africa, Central Africa, East and Southern Africa, SADC, Caribbean and Pacific regions.

4 However, longer term reforms to EU trade and agricultural policy may make the EU beef market less attractive for Botswana exporters, especially if the market is opened up to highly efficient South American producers. But this is not an EPA issue.

Principal Trade Agreements Affecting Apparel and Textiles

Trade Agreement	Duties	Rules of Origin	Time Limit	Comments
EU-ACP (Cotonou)	Apparel- 0 percent Textiles- 0 percent	Double Transformation Change of HS heading	2008	Currently being renegotiated into EPAs
SACU	Apparel and textiles- 0 percent	None- SACU duty paid on imported inputs	None	
Zim-Bots	Apparel and Textiles- 0 percent	Apparel- 20 percent local value added	None	
SADC	Garments-40 percent	Double Transformation	Duties will be gradually reduced to zero by 2008	
AGOA	Garments –0 percent Textiles-Various	-None -Yarn Forward Various-see note 2	- Sept 2007 (2012) - Sept 2015 None	See note 1. See note 2.

Notes:

1. The LDC waiver has been extended to 2012. Following this time, Botswana garments will have to meet the AGOA rule of origin, which is yarn-forward, to qualify for duty-free status.
2. AGOA makes no provision for duty-free imports of textiles, except for handmade and folkloric items. Manufacturers in other African countries, however, can use Botswana textiles to produce garments that qualify for the yarn-forward rule of origin.

Source: Adapted from BIDPA and World Bank in "Diversifying Botswana's Exports: An Overview", March 2005

US African Growth and Opportunity Act (AGOA)

The clothing and apparel sector has been the major beneficiary of the US AGOA dispensation, even though there are more than 6,000 product lines that qualify for duty-free and quota-free market access into the US. However, Botswana started benefiting from the AGOA dispensation at a later stage as the original arrangement had very restrictive rules of origin. Being a middle income country, Botswana could not source her raw materials from non-AGOA beneficiaries such as Zimbabwe and proceed to export the finished products to the US. This meant that Botswana had to source raw materials from sources that are less efficient, probably more costly and less reliable, a factor that would erase some or all of the intended benefits of AGOA. Further, the AGOA-eligible sources of raw materials (generally blended synthetic yarns) in sub-Saharan Africa do not provide a great variety, leaving the producers with no choice but to source from East Asia, mainly China and Taiwan.

Botswana had to be given a least developed country status in order to remove the restrictiveness of AGOA rules of origin. The LDC status accorded Botswana and other countries was originally scheduled to expire in late 2007; however, it has recently been extended to 2012. After that time, assuming no further extension, producers are unlikely to meet the AGOA rules of origin and thus will not be able to compete with the giants from Asia and Latin America. In order to minimise this impact and keep the industry growing, the following options should be considered:

- Shift market focus away from the USA to other markets, such as Europe or SADC, where the rules of origin are not as restrictive.
- Shift market focus to SACU, where duties on fibre, yarn and fabric is still lower than on garments.
- Shift the sourcing of raw material to AGOA eligible countries. Even if the materials cost

more, Botswana apparel may still be price competitive if the additional cost does not exceed the advantage from being duty-free. There is a residue of trained operators in the country from previous cycles of investment and industries which could potentially use Zambian yarn, which qualifies for export preferences under AGOA, and is currently in plentiful supply.

- Reduce manufacturing costs through improved labour and material efficiency.
- Reduce manufacturing costs by investing in more automated equipment. The best opportunity for this is converting from hand-flat to automated flat knitting.
- Shift market focus to less price sensitive markets, such as niche markets, and concentrate on competing on product response and quality.
- Shift production to apparel made from fabric and yarn that is considered in short-supply in the USA and, therefore, still duty-free to the USA under AGOA[5].

The future of AGOA is quite similar to the Cotonou Agreement, in that AGOA is not a permanent trade arrangement. SACU has had some negotiations with the US regarding the establishment of a free trade agreement. Should this be implemented, the AGOA benefits would be superseded by a set of permanent trade arrangements. However, negotiations on the proposed SACU-US FTA are currently suspended due to the limited progress that has been made and some fundamental disagreements between the parties.

Challenges Facing Exports from Botswana

With the current trading regimes through which Botswana trades and the developments relating to the ongoing negotiations at regional and international levels, there are a number of challenges that face exports from Botswana to all the markets all over the world and especially to the existing lucrative markets such as the EU, US and South Africa. These challenges include among others, the MFA Phase-out, the non-tariff barriers, rules of origin and SPS requirements in the EU market.

Textiles and the MFA Phase-Out

The apparel (clothing) sector contributes immensely to industrial development in Botswana. Textiles are Botswana's third largest goods export (after diamonds and copper-nickel), and a significant source of employment. The good performance of this sector reflects both trade preferences and the financial and tax incentives provided under schemes such as the Financial Assistance Policy and Development Approval Orders. As a result, this sector has a reasonable supply of adequately trained labour and a sizeable capital stock. The AGOA dispensation and the preferential market access into the EU through the Cotonou Agreement are added advantages that have enhanced the performance of this sector.

However, one important change in the international trade arrangements affecting textile and clothing exports has been the expiry of the Multi-Fibre Arrangement (MFA) at the end of 2004. Under the terms of the MFA, countries set quotas for imports of various apparel products from major apparel producing countries; since then, no quotas are now imposed on apparel imports, although duties can still be imposed. As a result, major low-cost apparel producing countries, notably China, have been taking a greater share of the apparel export market.

To date, unlike in countries like Lesotho, there have not been any major changes in the clothing and apparel sector in Botswana in response to the coming to an end of the MFA and it is argued that perhaps the Botswana producers still have a

5 Under AGOA, apparel made from yarn and fabric that is not available in commercial quantities in the United States can be exported duty-free to the USA from AGOA eligible countries without any limit. This is an important opportunity that has not received full attention from African garment manufacturers.

BOX 1: Effects of rules of origin on the car manufacrueing industry in Botswana

Disputes over rules of origin were a persistent source of disagreement between Botswana and South Africa in relation to the short-lived Hyundai motor vehicle assembly operation in Gaborone. The local Hyundai franchisee had initially imported semi-knocked down kits from South Korea, which were then assembled in Botswana and sold into the highly protected SACU auto market.

South Africa challenged that there was insufficient value-added taking place and ruled that the products failed the rules of origin requirements as originating from within SACU. South Africa used SACU Article 11(5) to oblige Botswana to cooperate in the fulfilment of 'economic objectives' of its import control legislation for the auto sector. As a result a new plant was built, costing USD60 million, to assemble cars from completely knocked down kits which would meet the rules of origin requirements. The venture obtained BDC loan of $24 million and the same amount from two Dutch banks.

However, in 2000 the plant was closed due to heavy losses, which had a number of contributory factors, reportedly including a failure to reach the break even level of 15000 vehicles per year; the inimical attitude of the South African motor lobby, and fraud by the owners.

chance to compete in the lucrative markets.

This, however, does not rule out the additional competition that Botswana producers are likely to face in these markets and calls for increase of efficiency. This should involve improving production techniques and technology, reducing delivery times, lowering costs, and finding and adopting production to more specialised niche markets.

Non-Tariff Barriers

Non-tariff barriers (NTBs) pose a more significant constraint to Botswana's exports than applied tariff levels. While across the region the more obvious non-tariff barriers – foreign currency controls, import licensing, price controls and state marketing – have been removed, a number of more non-transparent and arbitrary NTBs remain. For exports outside of the region, complex rules of origin and onerous standards and SPS requirements act as a substantial barrier to exports. One possible reason for Botswana's lack of trade with its non-SACU neighbours is a plethora of arbitrary NTBs. Many of these are product-specific, sometimes of seasonal or limited duration. Of course, Botswana is not just a victim of such NTBs, as it uses such import restrictions (notably on agricultural products and foodstuffs) to restrict imports from its neighbours.

Rules of Origin

Rules of origin restrict trade with SADC, the EU, the US and other trading partners. Rules of origin are a central component of preference regimes, and are often the most important non-tariff barrier. One problem is the varying and complicated nature of such requirements.

The rules of origin in the SADC Trade Protocol, for instance, have proved to be the most contentious part of implementing the protocol. For countries like Botswana where almost all the raw materials in different sectors are imported, it makes exporting to the SADC market under the protocol quite difficult. Even the somewhat strategic export products like textile and clothing are affected.

During the initial years of AGOA, Botswana could not benefit until it was granted the LDC status because the rules of origin could not be

met. If in due course the LDC concession lapses, the same problems will recur and Botswana might have to look for other better markets outside the US.

SPS Requirements

Sanitary and phyto-sanitary (SPS) requirements are imposed by the EU, mainly affecting beef and ostrich meat exports. The requirements are very stringent and are increasingly becoming ever more costly to implement. The latest SPS-related requirement is the traceability system for cattle, which involves the placing of a bolus in each cow. The cost of the exercise to Government is estimated at P150 million. Still related to the same system, the BMC had to install new facilities in the abattoirs, both for its part in the Livestock Identification and Trace Back System (LITS) and for other SPS-related improvements.

Conclusions

This Policy Brief discussed a very fundamental question for Botswana at this point of global trade changes, namely, "Are there actual and/or potential benefits from non-SACU bilateral and multilateral trade agreements?" The discussion in this policy brief suggests that the answer to this question is inconclusive. There are both real benefits and costs of non-SACU trade agreements. While Botswana stands to benefit from increased market access from trade agreements such as the SADC trade protocol and SADC-EU trade agreement, it is likely that preferential market access will gradually be eliminated in all the major markets and this will expose Botswana to stiff competition. This therefore calls for concerted efforts to negotiate and renegotiate better market access in the existing markets and new ones. Botswana should pursue the following issues in an endeavour to achieve this objective:

- Botswana should launch a concerted lobbying effort to improve rules of origin in all preferential trading agreements, starting with a Government-initiated 'rules of origin' strategy paper. In particular, this could advocate for the Economic Partnership Agreement with the EU to allow for single transformation of goods such as found in the AGOA agreement with the United States. In addition, Botswana should lobby for simplified and liberalised SADC rules of origin in the SADC MTR follow-up discussions (quota restrictions should be removed and the derogation should become the general rule for all SADC Member States). Botswana should press within SACU for a concerted and more liberal approach to rules of origin – SACU has been resistant to relaxing rules of origin within SADC, insisting on higher local content to qualify for preferential treatment than other SADC members would like to accept.
- Botswana should lobby the EU to improve existing trade preferences for beef products to allow customs duty, quota and special duty free export of a wider range of beef and meat products, without excessive administrative and sanitary restrictions.
- Botswana should prepare detailed estimates of the costs of compliance in order to fully assess the costs and benefits of the current emphasis on sales to the European Union.
- Botswana should continue to lobby for the AGOA LDC provision to be made permanent in order to provide predictability for potential investors in a particularly unstable market.

References

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Botswana Institute for Development Policy Analysis (BIDPA) BIDPA House
Plot 134 Millennium Office Park
Private Bag BR -29
Gabrone, Botswana
Tel: +267 397 1750
Fax: +267 397 1748
Website: www.bidpa.bw