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Anyone wishing to respond to or contribute articles should contact:

Peter Draper
Research Fellow
Development Through Trade
South African Institute of International Affairs (SAIIA)
Ph: +27-(0)11-339 2021 (General)
Cell: +27-(0)82 786 7983 (Preferred)
Fax: +27-(0)12-998 3491
Email: draperp@mweb.co.za

DR MILLS SOKO is a founding director of Mthente Research and Consulting Services, and a research associate of SAIIA.

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SACU and India: Towards a PTA

By Mills Soko

The governments of the Southern African Customs Union (SACU) member states (South Africa, Botswana, Lesotho, Swaziland and Namibia) and India have proclaimed a mutual interest to conclude a preferential trade agreement (PTA) before the end of 2006.[1] The mooted PTA is aimed at cementing and expanding the burgeoning trade relations between SACU (predominantly South Africa) and India. Following in the wake of the signing in December 2004 of a PTA between the SACU and the Mercado Común del Sur (Southern Common Market — Mercosur) countries — and the conclusion of the India–Mercosur PTA in January 2004 — the trade deal promises to inject further momentum into the India–Brazil–South Africa (IBSA) Dialogue process.

What is the rationale for the proposed SACU–India PTA? How will negotiation modalities be determined? What are likely to be the respective SACU and Indian negotiating interests? What are the potential challenges and constraints? How will the outcome of the negotiations dovetail with the touted plan to create a trilateral free trade agreement (FTA) including the other IBSA partner, Brazil?

Background to PTA negotiations

The impetus for negotiating a bilateral PTA between SACU and India grew out of a meeting between India's commerce and industry minister and South Africa's trade and industry minister in New Delhi in January 2000. In 2002, they agreed to initiate negotiations to conclude a PTA designed to strengthen bilateral trade and investment.[2]

An understanding was subsequently reached that such a trade deal would include South Africa's four SACU partners. Subsequent to the third meeting in Namibia in 2004 of the Joint Working Group established to commence negotiations, a Framework Agreement was hammered out providing for the implementation of limited tariff liberalisation in the initial stage, with a view to broadening the scope and coverage of the agreement into a full-blown FTA later.[3]

Rationale for negotiations

A combination of factors explains the two trade partners' desire to conclude a PTA. From the SACU perspective, it makes sense to negotiate a PTA with India, given the latter's rapidly expanding economy and consumer market, as well as steadily falling Indian tariff barriers within the context of the World Trade Organisation (WTO).[4]

In particular, South Africa is eager to exploit a trade deal with India to reduce protectionist barriers that have hampered its potential exports to the Indian market.[5] Research conducted by the Indian Institute of Foreign Trade found that in excess of 50% of India's exports faced a tariff of less than 10% in South Africa, while only 33% were subjected to a tariff rate of over 20%. Conversely, 55% of imports from South Africa faced tariffs of over 20% in India, with merely 34% of imports from South Africa attracting a tariff rate of 10% and less. According to the study, the weighted average tariffs in India and South Africa amounted to 22.89% and 16.35%, respectively.[6]

SACU has a trade and development agreement with the EU and PTAs with Mercosur and the European Free

Trade Association, which is made up of Switzerland, Norway, Iceland and Liechtenstein. It is currently engaged in (stalled) FTA talks with the United States and processes are under way to explore FTA discussions with China. And it is keen to conclude a trade deal with an African country, possibly Nigeria. Several other countries have declared an interest in signing FTAs with SACU, including Singapore, Japan, Thailand, Sri Lanka and Turkey.

India's intention to forge a PTA with South Africa is a vital element of the country's policy to continue the reforms initiated by its government in 1991 to liberalise the Indian economy.[7]

Bilateral and regional FTAs are pivotal to India's strategy to bolster its exports and increase its share of global trade, which currently stands at 1%.[8] India has concluded, or is exploring, regional and bilateral FTAs, PTAs and other economic co-operation agreements with scores of countries, including Sri Lanka, Mercosur, the Association of South East Asian Nations (ASEAN), Mauritius, the Gulf Co-operation Council, Chile, China, Japan, Australia, the US and the EU.[9]

Bilateral trade relations

Over the past decade there has been a considerable rise in trade between India and South Africa, the most economically advanced and dominant SACU partner: on average, annual growth in total trade exceeded 31%.[10] This can be ascribed largely to the expansion of Indian gold imports from South Africa. In 2002, total bilateral trade amounted to $2.3 billion, up from $271 million in 1994.[11] During the period from 1998/99 to 2002/03, India's imports from South Africa increased by more than 54%, while exports increased by more than 22%.[12]

Even so, trade remains very low on both sides – just more than 1% of total trade. Partly, this has to do with the fact that SACU's and India's external trade is still dominated by the Organisation of Economic Co-operation and Development (OECD) and East Asian states.[13] Moreover, a key problem is the persistence of obstacles to the promotion of trade and investment between the two countries, including tariff and non-tariff barriers. The proposed PTA is expected to ease these hurdles and provide SACU and India with a platform to bolster two-way trade and investment.

Table 1: Some SACU imports from India
Rice
Leather of bovine or equine animals
Medicaments
Footwear
Stranded wire, cables, plaited bands of aluminium
Men's shirts
Women's outer wear
Original equipment components
Cotton yarn
Woven fabrics of cotton
Articles and equipment for general physical exercise
Soya bean oil cake and other solid residues
Vegetable products
Bed linen, table linen, toilet linen and kitchen linen
Diamonds
Petroleum oils
Women's shirts
Other woven fabrics of synthetic staple fibres
Machines, mechanical appliances
Unmanufactured tobacco, tobacco refuse
Bells, gongs, statuettes, picture frames, mirrors of base metal, etc.
Synthetic organic colouring matter
Records, tapes and other recorded media for sound
Goat or kid skin/leather
Source: Stern M & C Stevens, op. cit.; Alves P, *op. cit.*

Some SACU imports from and exports to India are indicated in Figures 1 and 2.

A detailed trade/tariff analysis carried out by the Trade and Industrial Policy Secretariat (TIPS) revealed principal areas in which trade could be stimulated between SACU and India through liberalisation. It identified a list of undertraded products for which market access barriers were 'sufficiently high' to hamper imports from SACU and India respectively (see Figures 3 and 4). For the purpose of this paper, it is important to stress that the findings of the TIPS analysis may be outdated – the study was published in 2000 – as high tariff barriers to some or all the undertraded SACU and Indian exports may have fallen over time.

From the SACU viewpoint, it has also been contended that trade liberalisation could benefit SACU by providing access to affordable medicines, competitive prices for motor vehicles and equipment for heavy industry. And it could also create fresh export markets for iron and steel, chemicals, aluminium and furniture.[14] In addition, considerable potential has been recognised for increased intra-industry trade in basic fabricated metals, precious stones and jewellery, and non-metallic minerals.[15]

Modalities

Preliminary negotiations between SACU and India were scheduled to commence in August 2005, but were postponed at the request of India following a change of government in that country. The first round of negotiations will begin by the middle of 2006.[16] It will finalise broad negotiating modalities with a view to agreeing to product lines that will be covered by the PTA.

Like the India–Mercosur and SACU–Mercosur negotiations, these discussions are expected to adopt a 'positive list' approach: only those sectors listed in the agreement will be liberalised. It is not clear at this stage what the total number of products covered by the PTA will be. Nonetheless, it bears mentioning that the India–Mercosur agreement contained more than 600 products in the agricultural, chemical, automobile and pharmaceutical sectors,[17] while the SACU–Mercosur trade deal designated 2,000 products for tariff liberalisation on a sector-by-sector basis.

Within SACU, the process of compiling product lists will take place at two levels: among the SACU member states and in South Africa's National Economic Development and Labour Council (Nedlac).[18] Some commentators have voiced a concern that formulating negotiating positions in Nedlac could allow protectionist interests to hold the negotiations to ransom.[19] This anxiety was dispelled on two grounds by a South African trade negotiator in an interview with the present author. Firstly, he argued that erstwhile experience had demonstrated that drawing up product lists for a PTA was relatively easier than doing it for a comprehensive FTA. Also, he asserted that there had been no 'significant' resistance within Nedlac and SACU to the planned SACU–India PTA.[20]

Table 2: Some SACU exports to India
Coal, briquettes, ovoids and similar fuels manufactured from coal
Semi-finished products of iron or non-alloy steel
Bombs, grenades, torpedoes, mines, missiles
Steel and non-ferrous metals
Chemical wood pulp
Ferro-alloys
Motor vehicle parts and accessories
Sugar
Mineral fuels and lubricants
Vegetable products
Beverages and tobacco
Food and live animals
Machinery and transport equipment
Phenols, phenol-alcohols
Animal and vegetable oils
Ketones and quinines
Uncoated paper and paperboard
Source: Stern M & C Stevens, op. cit.; Alves P, op. cit.

Table 3: Undertraded Indian exports facing tariff barriers in SACU
Fish (frozen, excl. fillets)
Crustaceans (frozen)
Edible nuts (fresh, dried)
Oil cake, oilseed residue
Tobacco (not stripped)
Cotton (not carded, combed)
Tyres (pneumatic, new, bus)
Cotton yarn (excl. thread)
Cotton fabric (woven, unbleached)
Curtains, other furnishings
Passenger transport vehicles
Source: Stern M & S Stevens, op. cit.

Table 4: Undertraded SACU exports facing tariff barriers in India
Other ferrous waste, scrap
Other inorganic bases, oxides
Nitrogenous chemical fertiliser
Fertilisers
Silver
Machine appliances (special industrial)
Parts (data processing, etc.)
Parts (telecommunication equipment)
Gold (non-monetary, excl. ores)
Source: Stern M & S Stevens, op. cit.

Negotiating interests

Previous FTA negotiations involving SACU and India provide general pointers to what the offensive and defensive negotiating interests of both parties might be.

In the field of services, India has a clear offensive interest in the expansion of cross-border work opportunities and flexible movement for its technical personnel, especially software and IT workers (Mode 4 of the General Agreement on Trade in Services).[21] Undoubtedly, India's strength lies in its software and IT sector. But, as a trade analyst avers, considering that the South African IT sector is almost totally open to external competition, 'SACU cannot offer anything that is not already available to Indian IT firms.'[22]

Notwithstanding the difficulties SACU governments have had in rallying their services sectors, which explains their defensive postures, they have advocated liberalisation in specific sectors.[23] South Africa, in particular, has a dynamic and very competitive financial services industry that has begun to make inroads into the protected Indian market. It is conceivable that South African negotiators will push for more liberalisation of laws governing foreign ownership in this sector.

Given that SACU and India have opposed the inclusion of the Singapore issues in the WTO — bar trade facilitation, which was agreed multilaterally as part of the 'July Package' — they are unlikely to consider substantial liberalisation in these areas in a bilateral setting. Nonetheless, transparency in government procurement and investment might emerge as discussion items on account of their contentiousness. One of the concerns raised by South African firms in an IBSA perception survey conducted by the present author was the 'discriminatory' awarding of Indian government contracts in favour of local Indian companies. (Government procurement in India constitutes about 20% of gross domestic product.)[24] For their part, Indian investors might take issue with the South African government's black economic empowerment policy, which requires investors to sell equity stakes to black partners as a condition for public tender eligibility.

Regarding investment, SACU and India might exploit their discussions to accelerate the process of negotiating a bilateral investment treaty, which currently does not exist. SACU is also likely to argue for a further relaxation of restrictions on foreign direct investment in India.

Another issue poised to come up for deliberation is the rules of origin. This has been a major point of contention in both parties' FTA negotiations. It has featured in SACU FTA talks, most conspicuously in the deadlock with the US. And it has dominated India's negotiations with trade partners, notably Thailand and ASEAN.[25] Mainly, concerns have revolved around preventing third countries from taking advantage of FTAs negotiated by India with other countries. In the case of the Indo–Thai FTA, India produced a 'sensitive list' of items that would be exempted from tariff reduction under the trade deal.

India's offensive interests are likely to coalesce around textiles and, perhaps, certain categories of motor vehicles. The WTO has identified India, along with China, as a winner from the elimination of quotas in clothing and textile trade in 2005. Naturally, the country will harness this strong competitive advantage to its benefit. SACU countries, losers from the globalisation of trade in clothing and textiles, might be inclined to adopt a defensive posture, especially in light of the relentless competition from Chinese imports that has seriously threatened the viability of the domestic garment sector. However, South Africa has a competitive automotive industry and this remains an essential competitive advantage.

India's defensive interests are likely to blend around agriculture. Although agriculture does not play a central role in the South African economy (it does in the other SACU economies), there is a huge scope for growth of SACU exports of value-added food products into the Indian market, which SACU can provide.[26] Non-tariff barriers to agricultural trade, particularly sanitary and phyto-sanitary issues, might also feature in the discussions.

Issues about intellectual property rights (IPR) protection are likely to form part of the bilateral bargaining. South African businesses are eager to safeguard their intellectual property in foreign markets.[27] And the South African government might want to use an agreement with India to lock in IPR reforms in the SACU countries and improve the implementation of the domestic IPR regime. The Indian government has an interest in ensuring that IPR concerns do not unduly prevent the country's pharmaceutical firms from providing cheaper drugs to nations such as SACU, which are beset by public health emergencies, including HIV/Aids, tuberculosis and malaria.[28] This is underscored by the Indian government's decision to defer the introduction of a patent regime, although in 2005 it did implement — in line with a WTO directive — an amendment to the Patent Act of 1970 providing for the filing of product patent applications in the fields of chemicals, pharmaceuticals, agricultural chemicals and food products.[29]

Challenges

Firstly, the 'perception gap' between SACU and Indian business sectors must be bridged. This means changing the mindsets of businesses about the importance of South–South trade by creating awareness not only of opportunities in the respective commercial environments, but also of competitive advantages and trade complementarities among exporters.

Secondly, greater co-ordination and synchronisation between the various PTAs forged by the IBSA countries must be encouraged. International research has shown that multilevel negotiations, if not carried out in an integrated and coherent fashion by developing countries, could jeopardise their economic development.[30] Although the PTAs are distinct, there is a need to maximise synergies among them.

Thirdly, it is necessary to accord attention to both the Nedlac and SACU dynamics, which could impinge adversely on the negotiations. Striking a balance between domestic/regional pressures and external opportunities is a crucial imperative. Concerning SACU, it is vital to recognise that the new SACU Agreement enjoins member states to negotiate as a collective entity. Even though it is an overwhelmingly dominant regional actor, South Africa therefore cannot adopt positions and foist them upon its partners as it did in the past. Combined with the other parallel FTA (and multilateral) negotiations under way, which have exerted a strain on SACU's stretched negotiating resources, the quest to engender consensus among SACU partners could delay the pace of negotiations.

Fourthly, perceptions that the mooted SACU–India PTA is a political rather than an economic project ought to be allayed. Doubts have been expressed as to the economic import of the mooted bilateral trade pact. For instance, it has been suggested that India's interest in FTAs, including the one it seeks to conclude with SACU, is motivated less by a desire for market access than by political calculations.[31]

Fifthly, engagement in bilateral or regional FTAs should not detract from the over-riding goal of multilateral liberalisation. Understandably, the penchant for FTAs has been fuelled by disaffection with the pace of liberalisation in the WTO. Moreover, some countries find bilateral, rather than multilateral, liberalisation politically appealing, as it has lesser adjustment costs.[32] Still, the problem is that in the absence of multilateral liberalisation, countries will not be in a position to negotiate significant tariff reductions in the more shielded economic sectors. Importantly, studies have shown that in spite of the existence of commercial opportunities in the SACU and India markets, the economic impact of liberalisation will be diminished by the reality that the two negotiating parties' trade is still dependent on the OECD and East Asian states, and by the limited complementarities in their economies.[33]

The way ahead: A trilateral FTA?

According to South Africa's Department of Trade and Industry, there been 'talk' of forging a trilateral FTA among the IBSA countries in order to intensify economic co-operation.[34] Although attaining such a result is not impossible, it raises a number of questions. For example, how would such an FTA be conceptualised? What would be the scope of its product and sectoral coverage? Would the negotiations follow a negative or positive list approach? Would the FTA be a by-product of the three IBSA PTAs or would it be constructed as a separate arrangement? How would synchronisation and coherence be fostered among the trilateral FTA, the PTAs and multilateral trade agreements?

These issues require thorough research and analysis. Such analysis should also be extended to seeking to understand better how the undertraded sectors highlighted in studies on trade collaboration among the IBSA countries can undergird these trilateral negotiations.

Endnotes

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