Workshop on EU-SA Agreement on Trade, Development and Co-operation
July 22 – 23, 1999

Boipuso Hall, Gaborone, Botswana

OPENING STATEMENT BY THE HONOURABLE K.G. KGOROBA, MINISTER OF COMMERCE AND INDUSTRY AT THE WORKSHOP ON THE EUROPEAN UNION/REPUBLIC OF SOUTH AGREEMENT ON TRADE, DEVELOPMENT AND COOPERATION

CHAIRPERSON
MEMBERS OF THE DIPLOMATIC CORPS
DISTINDUISHED DELEGATES
LADIES AND GENTLEMEN

1. I feel greatly honoured to have been invited by the Management of Botswana Institute of Development Policy Analysis (BIDPA) to officially open this Workshop on the EU/RSA Agreement on Trade, Development and Cooperation. I would like to extend a special welcome to those delegates who have come from outside Botswana to participate in the Workshop. I wish them a pleasant stay in Gaborone. I also wish to express my sincere gratitude to the Frederick Ebert Foundation and the European Union for providing the necessary support for the Workshop.

2. I am informed that the Workshop aims to provide an in-depth analysis of the EU/RSA Agreement, to assess its implications on the BLNS and SADC industries, to identify the necessary restructuring programmes and to make proposals on how the BLNS countries can access technical, material and financial assistance to address the negative impact of the Agreement. These are pertinent questions to which the BLNS governments and the business community need answers. I am confident that the Workshop will address itself to these questions.

3. This Workshop is taking place at an appropriate time when the RSA is seeking concurrence from the BLNS as a pre-requisite to the implementation of the Agreement. The BLNS on the other hand, would like to fully understand the provisions of the Agreement and be assured that their interests will be accommodated before such concurrence could be granted.

The Workshop will provide an opportunity for the RSA, the EU and other experts to fully outline the implications of the Agreement to the BLNS countries to enable them to make informed decisions about the Agreement.

4. Mr Chairman, the Agreement provides for development cooperation as well as the formation of a free trade area (FTA) between the EU and RSA. The formation of FTA is of immediate and material interest to the BLNS as these countries belong to the Southern African Customs Union (SACU) together with the RSA. As a Customs Union, SACU countries apply a common external tariff on goods from third countries.

5. Needless to say, the economies of the SACU member states have become intertwined as a result of this common external tariff.

Therefore an agreement such as the EU/RSA Agreement which offers concessions on duties will bring about major changes in the trade environment and may even be dubbed a de facto EU/~~RSA~~ SACU Agreement.

6. South Africa's partners in the Customs Union would like to derive as much benefit from the Agreement as the contracting parties will. The BLNS would therefore like to see the Agreement implemented in such a manner that their benefits will be enhanced. The BLNS have always advocated for full cumulation with RSA for purposes of exporting to the EU under of the Lome Convention. I am informed that this request has only partially been granted in the final Agreement under the provisions partial cumulation. The BLNS would like to re-affirm their request for full cumulation with RSA as this would enable them to derive maximum benefits from the Agreement.

7. Distinguished delegates, while the EU/RSA Agreement is expected to have positive long-term effects on the whole region, the BLNS fear that it could have negative economic effects in the short-term. These fears have been confirmed by a number of studies, the most comprehensive of which was the one commissioned by the EU and undertaken by BIDPA in collaboration with the IDS of the University of Sussex. These studies generally concluded that the Agreement could lead to, among others, a dramatic reduction in Customs Union Revenues. These revenues are of material importance to all SACU member states, including the RSA as they account for a significant proportion of Government revenues. The studies cited earlier also recommended that the BLNS should consider options for restructuring and reform of their revenue sources.

8. In addition, the introduction of duty free EU goods into the RSA market is expected to increase competition for BLNS goods in the SACU market. The increased competition may result in injury to fledgling BLNS industries which will definitely be accompanied by job losses and heavy adjustment costs.

9. The implementation of the Agreement will, in particular, erode the advantages that are currently being enjoyed by the BLNS as ACP states under the Lome Convention. The Agreement will effectively change trade relations between the BLNS and the EU from a non-reciprocal market access arrangement to a reciprocal one. There is also the possibility of investment diversion from the BLNS to RSA to take advantage of the improved access to the EU market through the Agreement. The BLNS may therefore have to review their investment promotion strategies in order to retain existing investors and to attract new ones.

10. We are, however, grateful, ladies and gentlemen, that the Agreement has provisions for supporting regional adjustment programmes made necessary by the implementation of the Agreement. It is of utmost importance that this restructuring assistance be adequate and as comprehensive as possible to counteract the resultant negative impact. It is my hope that this Workshop will discuss modalities of how the regional restructuring programme should be implemented.

11. Distinguished delegates, the EU/RSA Agreement is but one of the many major developments that have ushered in changes in the regional trading environment. The effects of the general trade liberalization process brought about by the implementation of the World Trade Organization (WTO) agreements are already being felt in the region. Policies and legislations are being reviewed to allow for liberalisation and globalisation of trade. The review exercise required both human and financial resources commodities that are rare in this part of the world. Member states

will also be aware that the EU/RSA Agreement may be implemented simultaneously with the SADC Protocol on Trade Cooperation which requires SACU to liberalize at a faster pace than other SADC member states and that the EU is proposing to start phasing out the preferential market access for goods originating from ACP states, by the year 2005. The impact of the EU/RSA Agreement in the SACU will therefore be additional to all these effects, thus requiring SACU member states to undertake restructuring programmes on a scale much larger than would otherwise be necessary if the EU/RSA Agreement was implemented on its own. The restructuring programmes for the BLNS within the context of the EU/RSA Agreement should therefore take into consideration the impact of all these changes.

12. Before I conclude my remarks, Chairperson, please allow me once again to commend the organisers of this important and timely Workshop. I am confident that the participants will come up with concrete recommendations on how the BLNS can derive

maximum benefits from the EU/RSA Agreement on Trade, Development and Co-operation.

13. It is now my pleasure to declare this Workshop officially open.

I thank you for your attention.

KEY ASPECTS OF THE

EU - SOUTH AFRICA AGREEMENT ON TRADE, DEVELOPMENT AND CO-OPERATION

Botswana Institute for Development Policy Analysis
Private Bag BR-29
Gaborone
Botswana

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1. INTRODUCTION

On March 24, 1999 after 42 months of negotiations, the European Union (EU) Heads of State and Governments approved the "Trade, Development and Co-operation Agreement" with South Africa. The Agreement covers a wide range of economic and social issues and forms the basis for a long-term relationship between the EU and RSA. The agreement amongst other things provides for the establishment of a bilateral free trade area (FTA) between the EU and RSA; the strengthening of European development assistance to South Africa and a series of undertakings which open the way for intensified co-operation in the political and social fields.

The FTA is expected to contribute towards the restructuring of the South African economy by securing preferential market access for its products in the EU market and attracting EU investment into its economy. The resulting economic growth in South Africa is expected to facilitate intra-regional economic trade and investment flows which will spill over to the rest of Southern African. South Africa also believes that regional economic co-operation will advance a broad and integrated process of industrialization and modernization in Southern Africa.

The EU-SA Agreement is expected to promote a business environment that stimulates domestic and foreign investment, thereby increasing capacity growth (in addition to accelerating the transfer of technology). High hopes have been based on the experience of the integration of Spain and Portugal in the EU following their membership and the closer links established between the EU and Central European countries and between the United States and Mexico after NAFTA, all cases of substantial increase in inward foreign direct investment.

The following channels have been distinguished.
First, the agreement is expected to reduce uncertainty for investors in several ways:

- it provides contractual assurances of access for South African exports to European markets;
- it also enhances the credibility of the South African authorities' economic reform commitment through the perceived locking in of reforms as a result of the agreement itself, and
- more generally the acceleration of the move toward a fully market-based and open economy.

Second, the dynamic increases in productivity, for example through the adoption of EU standards and regulation, can be expected to raise the return on capital.

The Agreement provides for the protection of South Africa's sensitive sectors and commits the EU to provide support for the SACU adjustment efforts resulting from the establishment of the FTA. Increased aid and technical assistance from the EU will support the needed structural reforms. The financial assistance will be aimed at helping to alleviate short-term costs of implementing the Agreement. The Agreement also contains several important protective provisions for SADC countries, particularly BLNS countries.

The agreement will be valid for unlimited period, however, either party may denounce the agreement by notifying the other party in writing and the agreement shall cease to apply six months after the date of notification. In the event of any dispute relating to the application or interpretation of the Agreement each party may refer to the Co-operation Council.[1] The Agreement also has an Amendment Clause in the event that any party wants to amend the agreement.

This paper outlines key issues in the Agreement. The paper is organized as follows: Section 2 provides a brief outline of the whole agreement; Section 3 analyses the key features of the trade agreement; Section 4 analyses the key features of the trade related issues; Section 5 analyses the sectoral agreements; and, Section 7 provides an outline issues of concern to the BLNS countries.

2. TRADE, DEVELOPMENT AND CO-OPERATION AGREEMENT

The EU-SA Agreement seeks to attain the following objectives:

- Progressive elimination of all tariffs on industrial goods over 12 years;
- Gradual and limited trade liberalization for agricultural products, some over 12 years and others to be reviewed periodically;
- Measures to liberalize services;
- Measures to liberalize the right of establishment; and
- Harmonization of rules and regulations of a wide range of trade-related regulations (i.e., competition policy, intellectual property rights, standardization, customs and statistics).

[1] The Co-operation Council will be responsible, among others, for ensuring the proper functioning and implementation of the Agreement and the dialogue between the Parties, and studying the development of trade and co-operation between the Parties.

Other than the Provisions for a Free Trade Agreement (FTA) and Trade Related Issues, the "Trade, Development and Co-operation Agreement" between the EU and South Africa covers a wide range of components. It includes:

- Joint Declaration on Political Dialogue;
- Economic Co-operation;
- Financial Assistance and Development Co-operation; and
- Social and Cultural Co-operation.

In this section we will briefly outline some of the components of the agreement relevant to BLNS while the Provisions for a Free Trade Agreement (FTA) and Trade Related Issues are covered in sections 3 and 4. The outline will highlight co-operations that include BLNS and/or SADC countries.

2.1 *Joint Declaration on Political Dialogue*

As essential element of the Agreement, the parties agreed to the principle of good governance that is the respect for democratic principles, fundamental human rights, and the rule of law. Any violation of the principles by one party would lead to the other party taking appropriate measures, including withdrawing some concessions (Article 2).

2.2 *Economic Co-operation*

The agreement provides for economic co-operation between the EU and South Africa. The co-operation includes:

(i) Industrial restructuring and modernization of the South African industry to foster its competitiveness and growth (Article 50).

(ii) Investment promotion and protection. The co-operation, among others, will also aim at **encouraging investment in Southern Africa** (Article 51).[2]

[2] The EU-SA Agreement is expected to promote a business environment that stimulates domestic and foreign investment, thereby increasing capacity growth (in addition to accelerating the transfer of technology). High hopes have been based on the experience of the integration of Spain and Portugal in the EU following their membership and the closer links established between the EU and Central European countries and between the United States and Mexico after NAFTA, all cases of substantial increase in inward foreign direct investment. The following channels have been distinguished: First, the agreement is expected to reduce uncertainty for investors in several ways: it provides contractual assurances of access for South African exports to European markets; it also enhances the credibility of the South African authorities' economic reform commitment through the perceived locking in of reforms as a result of the agreement itself, and more generally the acceleration of the move toward a fully market-based and open economy. Second, the dynamic increases in productivity, for example through the adoption of EU standards and regulation, can be expected to raise the return on capital.

(iii) Development, diversification and increase of trade between the EU and South Africa and improvement of the competitiveness of South African products on domestic, regional and international markets. **The co-operation will focus on, among others, regional co-operation for the development of trade and trade related infrastructure and services in Southern Africa** (Article 52).

(iv) Development and strengthening of micro enterprises and small and medium sized enterprises in South Africa and Southern Africa. **The co-operation will also facilitate links between South Africa, Southern Africa and EU private sector operators** (Article 53).

(v) Promotion of telecommunication and information technology. **The co-operation will, among others, support co-operation between the countries of Southern Africa, in particular, in the context of satelite technology** (Article 54).

(vi) Energy - **the co-operation will, among others, support co-operation between countries in Southern Africa to exploit locally available energy resources in an efficient and environmentally friendly manner and promote energy co-operation in Southern Africa** (Article 56).

(vii) Mining and minerals - technology research and development. **The co-operation will include, among others, South African activities undertaken within the framework of the SADC Mining Co-ordination Unit** (Article 57).

(viii) Restructuring and modernization of road, rail, port and airport infrastructure. **The co-operation includes, among others, supporting the co-operation between the countries in Southern Africa in order to create a sustainable transport network for regional needs** (Article 58).

(ix) Strengthening the development of a competitive tourism industry. **The co-operation will, among others, promote regional co-operation in Southern Africa** (Article 59).

(x) Modernization and restructuring of the agriculture sector through modernization of infrastructure and equipment, the development of packaging and storage techniques and the improvement of private distribution and marketing chains (Article 60).

(xi) Promotion of sustainable management and use of fisheries resources. **The agreement will be set out in a separate fisheries agreement** (Article 61).

(xii) Co-operation in services sector, particularly in the area of banking, insurance and other financial services (Article 62).

(xiii) Consumer protection and protection of consumer's health (Article 63).

2.3 *Development Co-operation*

The Development Co-operation Agreement aims at contributing to South Africa's integration into the world economy and trade, expansion of employment, for development of sustainable private enterprises and regional co-operation and integration. This is the most important component of the agreement for the Southern African countries, especially the BLNS countries. The BLNS countries can utilize the proposed technical, material and financial assistance to assist them in adjustment efforts occasioned by the establishment of the free-trade area. The assistance could be directed towards industrial and agricultural restructuring, and fiscal adjustment. (Annex 1 outlines the criteria for qualification for assistance).

2.4 *Co-operation in other Areas*

The agreement (Title VI) also covers co-operation in the following areas:

- Science and technology,
- Environment
- Culture, Social issues,
- Information,
- Press and audio-visual media,
- Human resources,
- Fight against drugs and money laundering,
- Data protection, and
- Health.

2.5 *Financial Aspects of Co-operation*

South Africa and the other SACU countries will benefit from financial and technical assistance from the EU in the form of grants and loans to support its social-economic development needs (Title V). The financial assistance may be used to fund projects or programs of national or local interest in South Africa as well as the participation of South Africa in regional co-operation activities which it undertakes together with other developing countries.

3. PROVISION FOR FREE TRADE AREA

The popular component of the agreement is the provision for a Free Trade Area (FTA). Its popularity has led the public to believe that the agreement is all about trade. In this section we look at the Free Trade Area Agreement.

3.1 General Features

The EU and RSA agreed to establish a Free Trade Area in conformity with Article XXIV of GATT 1994.[3] The FTA negotiated share the following objectives:

- Progressive elimination of all tariffs on industrial goods over 12 years, and
- Gradual and limited trade liberalization for agriculture products.

The coverage of the FTA will free around 90 percent of all trade exchanges between the EU and RSA in 12 years. The agreement is asymmetrical both in timing and content. The EU will liberalize faster and with a larger coverage of products than South Africa.

The Agreement provides for the protection of South Africa's sensitive sectors and commits the EU to provision of support for the SACU adjustment efforts resulting from the establishment of the FTA. It also contains several elements that assure a positive regional impact on the other SADC countries.

3.2 Industrial Sector Tariff Elimination

This sector covers 86 percent of South Africa's total exports to the EU. The EU will fully liberalize 95 percent of its imports from South Africa within a 10-year transitional period. South Africa will fully liberalize 86 percent of its imports from the EU within a 12-year transitional period.

South Africa will present proposals for further liberalization of automotive products (including components) from the EU. This will be based on the outcome of the South African Motor Industry Development Program (MIDP) review.[4]

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[3]Article XXIV of GATT 1994 allows signatory countries to form customs unions and FTAs with the view that a removal of trade restrictions represents an important step toward free trade, similar to the process of integrating different provinces within a single country. The article provides two main conditions governing such arrangements: a "substantial-all-trade" requirement and a "not-on-the-whole-higher-or-more-restrictive" requirement.

[4] The MIDP combines phased tariff reduction with duty free allowances and tariff rebates (contingent on exports). The objective is to create a transitional incentive system to redirect production toward competitive sectors. Until 1994 auto manufacturers in South Africa enjoyed the protection of 155 percent import duties on assembled vehicles. The rate has since fallen to 54 percent, and will drop further to the WTO allowed rate of 40 percent by 2002, when the MIDP program is scheduled to end. Under the program component makers have a 40 percent import duty protection, which is scheduled to fall to 30 percent by year 2002.

3.3 *Agricultural Sector Tariff Elimination*

The agricultural sector is the most protected sector in the EU and has generally been excluded by the EU in other free trade agreements. The provisions apply to products covered by the WTO definition of agricultural products as well as fish and fisheries products.

Given the sensitivity of agricultural markets, an **agricultural safeguard clause** gives either party the right to challenge the other if there is proof that increased imports of agricultural products are causing harm or threaten to cause harm to the domestic industry.

The EU will fully liberalize its imports from South Africa within a 10-year transitional period. The EU list of exclusions has been significantly reduced to 38 percent (based on 1997 trade statistics). The reserve list is subject to regular reviews with a view to further opening of the market.

South Africa will fully liberalize its agricultural imports from the EU within a 12-year transitional period. South Africa's reserve list as with the EU is subject to regular reviews.

The fisheries agreement should enter into force, and the appropriate EU concessions on fisheries should be fully implemented within a transitional period of 10 years from the entry into force of the Agreement.

4. TRADE RELATED ISSUES

4.1 *Customs Union and Free Trade Agreements*

The agreement provides for consultation between the parties concerning agreements establishing or adjusting customs unions of free trade areas and other major issues related to their respective trade policy with third countries. In particular, in the event of a third country acceding to the EU, such consultation shall take place so as to ensure that account can be taken of the mutual interests of the EU and RSA.

4.2 Anti-dumping and Countervailing Measures

Before definitive countervailing duties are imposed the agreement provides for parties to consider the constructive remedies as provided for in the agreement on implementation of Article VI of the GATT 1994 (Anti-dumping and Countervailing Duties) and the Agreement on Subsidies and Countervailing Measures.

4.3 Safeguard Clause

The Agreement has comprehensive safeguard provisions to ensure that South Africa and the BLNS countries can temporarily protect themselves or slowdown the pace of liberalization if the effects of increased imports cause serious difficulties. It provides for appropriate measures to be taken by either Party in the case of increased imports which cause or threaten to cause serious injury to domestic producers of like or directly competitive producers. The measures will be taken under conditions provided for in the WTO Agreement on safeguards or the Agreement on Agriculture annexed to the Marrakech Agreement establishing the WTO. The measures shall also be applied to increased imports which cause or threaten to cause serious deterioration in the economic situation of the EU's outmost region or in any of the SACU member countries (Article 23).

The safeguard clause is supplemented by non-reciprocal provision for South Africa to take measures to protect infant industries or sectors facing difficulties caused by increased imports during the transitional period, particularly where the difficulties produce major social problems (Article 24).

The measures shall be applied for a period not exceeding 4 years and shall cease to apply at the latest on the expiry of the maximum transitional period of 12 years. The time limit may exceptionally be extended by decision of the Co-operation Council. No such measures can be introduced in respect of a product after more than 3 years of elimination of all duties and quantitative restriction or changes or measures having an equivalent effect concerning that product.

The Agreement has an exception clause that provides for the protection of domestic producers against the importation of used goods.

3.4 Rules of Origin

The rules are applicable in general to enforce anti-dumping and countervailing duties as well as other trade protectionist measures. They also limit the ability of

exporters in other countries to exploit these preferences. The rules prescribe what would count as local content.

The protocol provides for diagonal cumulation between South Africa and the EU as well as with materials originating in ACP countries. It therefore allows for trade flowing from BLNS to South Africa to the EU to be treated as originating from a single customs territory. ACP countries including SACU will be able to cumulate with materials which have originating status in South Africa.

These are specific rules for specific products, based on the tariff nomenclature. The list which is contained in Annex II of the protocol describes the working or processing to be carried out on non-originating materials in order that the final product obtain originating status.

3.5 Right of Establishment and Supply of Services

The parties reaffirmed their commitments as annexed to the fourth protocol to the GATS concerning basic telecommunications and the fifth protocol concerning services (Article 28). The parties agreed to extend the scope of the agreement such that the liberalization process provide for the absence or elimination of substantially all discrimination between the Parties in the services sectors covered and should cover all models of supply including the supply of services (Article 29).

By liberalizing the right of establishment, South Africa signals that it is open to foreign investment (FDI) and willing to bind this pledge, thus increasing the incentive to EU firms to establish themselves with the ensuring concomitant financial and technology transfers.

3.6 Current Payments and Movements of Capital

The Parties undertook to allow all payments for current transactions between their respective residents to be made in freely convertible currency (Article 31). The Agreement also calls for facilitating and eventually achieving full liberalization of the movement of capital between the EU and South Africa (Article 32). However, in cases where one or more Member States of the Community, or South Africa, is in serious balance of payments difficulties or under threat thereof, the EU or RSA, as the case may be may in accordance with the conditions established under the GATT Articles VIII and XIV of the Articles of Agreement of the International Monetary Fund adopt restrictions on current

transactions which shall be of limited duration and may go beyond what is necessary to remedy the balance of payments situation.

4.7 Competition Policy

The parties agreed that whenever there is reason to believe that there are anti-competitive practices the other Party's competition authority may be requested to take appropriate remedial action in terms of that authority's rules governing competition (Title III, Section D-A).

The EU will provide technical assistance to RSA to assist in restructuring of its competition law and policy. This may include the exchange of experts, organization of seminars, and training activities (Article 38).

4.8 Public Aid

The Agreement calls for a fair, equitable and transparent granting of public aid. It prohibits the granting of public aid favoring certain firms or the production of certain goods, which distorts or threatens to distort competition, and which does not support a specific public objective or objectives (Article 40).[5]

4.9 Other Trade Related Provisions

4.9.1 Intellectual Property

The Agreement requires South Africa to implement the provision of assurance of adequate and effective protection and enforcement of intellectual property rights

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[5] While the South African government refrains from competing with the private entities in the private sector some firms enjoy some form of protection through direct or indirect allowances from the government which give them a financial advantage vis-à-vis the private entities. Some of the well known ones are: ADE (diesel engines), SASOL (synthetic fuels and petrochemicals), Industrial Development Corporation, the strategic Fuel Fund, TELKOM (enjoys a 5 year monopoly on providing basic telecommunications services), TRANSNET (enjoys a monopoly on most transport and port services), and ESKOM (the state electricity monopoly operates as a non-taxed company).

Even though South Africa's objectives in providing public aid to some firms is to develop the previously disadvantaged communities, it is more likely that with this Agreement South Africa may be required to provide a time table for phasing out the subsidies. At the same time South Africa may also request the phasing out of state subsidies in some of the EU industries.

under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs) (Article 45).

In order to facilitate the implementation the EU may provide, on request and on mutually agreed terms and conditions, technical assistance to the South Africa in, amongst other things, the preparation of laws and regulations for the protection and enforcement of intellectual property rights, the prevention of the abuse of such rights, the establishment and reinforcement of domestic offices and other agencies involved in enforcement and protection, including the training of personnel.[6]

4.9.2 Standardization, Customs and Statistics

The Parties will co-operate in the filed of standardization, metrology certification and quality assurance in order to reduce differences between the Parties in the areas, remove technical barriers and facilitate bilateral trade. The co-operation shall include, among others, facilitation of technical assistance for Southern African capacity building initiatives in the fields of accreditation, metrology and standardization (Article 46).

The Agreement also calls for co-operation between the respective **customs services** in order ensure that the provisions on trade are observed and to guarantee fair-trading (Article 47) and co-operation to the **harmonization of statistical methods** and practice to enable processing of data (Article 48).

5. SECTORAL AGREEMENTS

[6] In South Africa property rights, including intellectual property, are protected under a variety of laws and regulations. South Africa is a member of the Paris Union and acceded to the Stockholm text of the Paris Convention for the protection of industrial property. South Africa is also a member of the World Intellectual Property Organization (WIPO). South Africa passed two IPR-related bills (the Counterfeit Goods Bill and the Intellectual Property Laws Amendment Bill) at the end of 1997 bringing South Africa's laws largely into conformity with its international trade obligation under the related TRIPS agreement of the WTO and enhanced enforcement of its trademarks act.

Although South Africa's intellectual property laws and practices are generally in conformity with those of the industrialized nations as of May 1998 the U.S. Trade Representative put South Africa on the special 301 watch list as a result of a law which appears to grant the Minister of Health the power to abrogate patent rights for pharmaceuticals. The aim of the law is to enable South Africans acquire non-generic medications at affordable prices.

5.1 *Fisheries Co-operation*

The Parties agreed to negotiate and conclude a co-operation agreement by the end of the year 2000. South Africa will abolish its tariffs on fisheries products in parallel to the elimination of duties of the corresponding tariff positions by the EU.

6.2 *Wine and Spirits*

A Wines and Sprits Agreement will be concluded no later than September 1999 to ensure that entry into force takes place by January 2000. The political comprise on port and sherry contains the following main elements:

(a) South Africa will phase out the use of the names "port" and "sherry" in third markets over 5 years, except in the case of non-SACU SADC countries where a 8 year phase out period would apply.

(b) South Africa will continue to use the names "port" and "sherry" on its domestic market throughout the transitional period of 12 years.[7]

(c) The use of names will be reviewed within the transitional period to decide on the names to use beyond the 12 years.

(d) The EU will provide duty free quota for South Africa wine covering the current level of trade of 32 million litres with allowance for the future growth in the quota.

The EU will also provide 15m euro for the restructuring of the South Africa wines and spirits sector and for the strengthening of marketing and distributions of RSA wines and spirits and spirits products.[8]

[7] Domestic include all of SACU

[8] It is emerging clearly that the EU has bigger objectives beyond the Agreement with South Africa. Its strategy is to make the terms exclusive geographic denominations under TRIPS at the WTO. Since there is no acceptance by all the WTO members that certain terms are multilaterally agreed geographical denominations the EU would like to establish a de facto strength in this debate at the WTO. The question is: If the EU are unsuccessful in their objectives in the WTO will South Africa after having agreed to surrender its rights to use the terms "sherry" and "port" resume using them working contravening the agreement.

Annex 1: Qualification for Assistance

(i) Eligible Beneficiaries

Co-operation partners eligible for financial and technical assistance shall be national, provincial and local authorities and public bodies, non-governmental organizations and community-based organizations, regional and international organizations, institutions and public or private operators. Any other body could be made eligible if so designated by both parties.

(ii) Programming

Detailed operational procedures and provisions for implementation and monitoring of the development co-operation shall be attached to a Multi-annual Indicative Program. The Program will be based on specific objectives derived from the priorities as stated in the Development Co-operation and indicating modalities for the preparation, implementation and monitoring of the Development Co-operation and resulting operations. The Program will be an outcome from programming discussions carried out between the EU and RSA with the contribution of the European Investment Bank.

(iii) Project Identification

The identification and preparation of development operations shall be the responsibility of the Government of South Africa, or any other eligible beneficiary. Project or program dossiers submitted for financing by the EU will be required to contain all the information necessary for their appraisal. Such dossiers shall be officially transmitted to the Head of Delegation by the eligible beneficiaries.

(iv) Financing Proposal and Decision

The conclusions of the appraisal shall be summarized by the Head of delegation in a financing proposal prepared in close collaboration with the National Authorizing Officer and/or the requesting partner.

(vi) Financing Agreements

Any project or program approved by the Community shall be covered by:

(a) either a financing agreement drawn up between the Commission acting for the community, and the national Authorizing Officer acting for the government of South, or eligible beneficiary,

(b) or a contract with international organizations or legal bodies, physical persons or any other operator defined in the [eligible beneficiaries} Article responsible for carrying out the project or program.

All financing agreements or contracts shall provide for on the spot checks by the Commission and the European Court of Auditors.

EU-SA Agreement on Trade, Development and Co-operation:

Options for Fiscal Restructuring

Ndaba Gaolathe
BIDPA

July 1999

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1. Introduction

1.1 The European Union Agreement on Trade, Development and Cooperation with South Africa intends to foster greater economic integration not only between the European Union and South Africa but also between the SACU members and Europe. The agreement will have far reaching implications on investment, trade and on government revenue in South Africa and among the BNLS countries.

1.2 The elimination of tariffs on SACU's trade with the EU will have a negative impact on revenues. The severity of the revenue impact will depend on:

- The initial share of import taxes in total tax revenue;
- The import demand response to tariff reductions;
- The share of imports from the EU in total imports;
- The elasticities of substitution between imports from the EU and other countries (trade diversion) as well as between imports and import competing goods and services produced domestically (potential for erosion of domestic tax base).

1.3 The elimination of tariffs on EU imports to SACU will have numerous costs to the BNLS countries. Some firms will close, and workers laid off, in the face of increased competition from potentially cheaper goods from the EU. The effect will be the erosion of both the company and personal tax bases. In the event that EU goods become considerably cheaper, importers will divert to EU sources thus further eroding the tariff base. There is also the possibility that consumers will divert away from domestic products in favour of EU goods and services thus further eroding the domestic tax base. These and other shifts in trade patterns and prices will affect even government expenditures depending on how expenditures are distributed across the different categories of products and services.

1.4 Results of a comparative static CGE model used in a BIDPA-IDS study estimate that the real growth in South African's contribution to the duty revenue pool be between 17 and 22 % lower (than without the agreement) over the full period of the FTA agreement. It is expected that during FTA's implementation period of twelve years, the average growth rate of South Africa's contribution to the duty revenue pool shall fall by between 1.3 % and 1.7%.

1.5 The envisaged impact of the EU-SA agreement varies across the BNLS countries. A commodity flow model anticipates that the revenue pool shall be reduced by 31%. Botswana's customs revenue will fall by about 5.3%, which may not be severe given that customs revenue accounts for 17% of revenues. Customs revenue declines are expected to range around 8.6 %, 13.9 % and 12.9 % for Namibia, Swaziland and Lesotho respectively. These figures raise serious concerns for Swaziland and Lesotho where customs revenues account for more than 40 percent of revenues. Namibia will also find course for worry since customs revenues constitute about 27.6 percent of revenues.

2. Options for fiscal adjustment

2.1 In the face of the compelling evidence that BNLS countries are likely to suffer revenue losses as a result of the EU-SA trade agreement it is important to take stock

of the various options that are available to mitigate the negative effects associated with revenue losses. These options may entail either cutting government expenditures or finding new avenues for additional revenues:

- Decrease in government expenditure: This might not be a feasible option for various reasons. In many if not all of the BNLS countries, politicians argue that government expenditures, as it is, fall short of catering for the many national needs. In addition, the recommendation that government expenditures be reduced is not new; if anything, it is a recommendation that has proven most difficult to pursue even when the case for such a measure was most compelling;
- Privatisation of public enterprises: Public enterprises continue to be significant features of the BNLS economies. Botswana, South Africa and Namibia made efforts over the past few years to privatize even the "strategic" public sector enterprises. In the process, governments received revenues from equity sales and gained from new tax receipts which came about as a result of private sector involvement in previously public sectors. However, any remaining privatization efforts are not likely to be significant;
- Expansion of tax base: The tax base may not be sufficiently broad in many of the BNLS countries. For instance, Botswana's tax base is concentrated towards receipts from mineral sales; there is no value-added tax and the threshold for personal income taxation is fairly high. This is a stark contrast to experiences among developed countries particularly in the US where the personal income tax is the largest revenue source for government. Over the past one or two decades, many countries have adopted the value added tax as a way of broadening the tax base and minimizing economic distortions associated with the traditional taxation;
- Strengthening of tax administration: It is often the case especially among developing countries to find that tax administration is inefficient, de-motivated and even corrupt. Consequently, tax collection is poor resulting is huge "tax gaps".

2.2 Of the various fiscal options for restructuring presented above, the paper concerns itself with the question of tax reform. For various reasons, tax reform appears to be the most promising area for revenue improvement. Many countries are plagued by poor tax administration and collection so that it is a simple matter to recognize the potential effects of improved tax collection systems. Also, unlike deficit reduction, tax reform in many ways is a relatively new debate and those countries that have embraced the idea have largely been successful. Finally, there are relatively little political costs associated with the overhaul of tax systems.

3. Programmes for fiscal reform

3.1 Many governments will have to restructure their tax collection agencies along modern and functional lines; and concentrate efforts on the most important taxes and the largest taxpayers. Often, in developing countries, issues of policy attract significantly more attention than questions of institutional development. Yet it is institutional deficiencies that hinder economic development. Tax administration institutions in developing countries are no exception in this light. In fact, most developing countries are characterized by incidences of high "tax gaps" reflecting that these countries are collecting significantly less taxes than would be expected under prevailing tax statutes.

3.2 In designing strategies for tax administration reform it is important to diagnose specific country deficiencies and needs. One step towards this diagnosis is to evaluate the "tax gap" which essentially is the difference between actual tax collection and expected tax revenues given the tax statutes and laws. Thus the tax gap comprises of taxes not paid due to tax evasion, tax arrears and taxes not paid due to misunderstanding of tax laws.

3.3 Some of the specific tax administration reform programmes that countries would wish to consider are:

- Best ways to restructure existing organizations along modern and functional lines and giving emphasis to the most productive taxes and the largest tax payers;
- Application of modern information technology (computerization) to manage tax payer databases and other information processing;
- Introduction of VAT and in some cases introduce best audit strategies and targeted interventions;
- Consider the feasibility of establishing independent revenue authority.

3.4 The following paragraph discusses several of many programmes that countries could conduct as part of tax administration reform:

- Management and organization of tax collection agency: Depending on the specific deficiencies of a country and on the needs, governments need to consider the possibility of independent tax agencies. This provides flexibility for these agencies in terms of their ability to attract skilled expertise, capacity to introduce modern information systems and possibly propensity to be transparent;
- Political commitment of reform process: It is essential that the top civil servants and politicians be in agreement that there is a need for reform in tax administration. The reform process may require legislative amendments in the tax code. It may also be necessary to establish tax collection agencies that are independent of government structures. Such measures can not be achieved without the input of key players in the political process;
- Identify tax and accounting laws that require amendment;
- Simplify the tax system to aid administration and reduce compliance costs: Policy makers and governments are slowly finding that there is little merit to high personal income taxes, multiple exemptions or deductions and many tax brackets. Instead there is a new and winning wave towards marginal taxation that is in line with corporate tax rates, elaborate use of withholding, lower tax rates and fewer tax brackets or exemptions;
- Improve voluntary compliance: As discussed above, voluntary compliance will depend on the extent to which tax administration is able to create the impression that defaulters will be detected and punished. Obstacles to voluntary compliance include complexity of tax laws, fairness of punishment system, perceived inequity of the tax system, integrity and professionalism of tax administration, audit programmes and the appeal process. Recently in more developed countries there has been a trend towards a system of "self assessment" where taxpayers determine their own tax liability. Essential elements for successful implementation of "self assessment" include (a) good taxpayers services to ensure that tax payers are knowledgeable about their liabilities and entitlements (b) simple procedures (c) a strict but fair penalty system (d) effective verification and enforcement

programmes. Thus self assessment and voluntary compliance are at the heart of modern tax administration;

- Pursue an integrated approach to the tax collection process: In reforming tax administration, tax collection must be viewed as a chain process entailing registration, collection, collection enforcement, audit, legal affairs and services. Each of these steps must be improved in order to achieve effective tax collection;
- Initiate reform with pilot projects: many of the countries that have been successful in reforming their tax system started off the process with pilot projects. A pilot project may involve computerizing and monitoring only the largest tax-payers and using this experience for extension to the rest of the tax-payers;
- Introduce or refine a broad-based tax: The lesson for the conduct of tax policy is that tax policy be made simple, transparent and enticing for its participants. This accounts for the advent of the VAT over the past two decades. A broad-based VAT, with a single rate, a few exemptions and possibly a thresh-hold to exclude small business carries many advantages over and above those of other tax systems.

3.5 Various studies document trends in countries world-wide and find that, in general, bottlenecks in tax administration can be identified in the areas of: (a) Tax payer registration; (b) Returns and payments processing; (c) Computer operations; (d) Detection and Stop-filers; (e) Delinquent Taxpayers; (f) Audit; (g) Sanctions and the Penalty System; (h) Taxpayer Services and Publicity; (i) Management and Organization; and Personnel. The tax administration reform programmes as discussed above must address these bottlenecks. Some of these bottlenecks are discussed below:

- Taxpayer registration: One way of assessing the appropriateness of the taxpayer registration is to consider questions such as: what measures are in place to register businesses in both the private and public sectors? What percentage of the registered taxpayers actually files tax returns? Who issues tax-registration numbers and to what extent are TINs enforced?
- Processing of returns filings: Evidence in developing countries is that delays often occur in the tax-filing process as a result of poor return forms which often pose irrelevant questions. Experiences in Latin America suggests that simplification of forms and the use of electronic filing systems can improve the tax returns filing systems;
- Application of modern information technology: In a modern information intensive world, it is difficult to be efficient, accurate and fast without the use of computers. This is so even in tax administration where there is a compelling need to coordinate information from taxpayers and reconcile it with that from banks. Computers are also essential for purposes of forecasting future tax receipts, filing and processing data. Computerization has to be pursued in tandem with other tax reform processes and is not to be viewed as an independent process;
- Delinquent taxpayers: The questions to ask are: What percentage of reported taxes are actually collected? How long does it take to detect delinquent taxpayers? Once a delinquent is discovered, how long does it take recover the overdue amount? How expensive is it to pursue delinquent taxpayers? These are some of the central questions that any government should be in a position to answer. In one or two Latin American countries, it was revealed, for instance, that 3.6% of delinquent tax payers accounted for 90% of the delinquent taxes;

- Audit: Studies reveal that the perception of the likelihood of being audited determines the degree of compliance. In Denmark where auditing is taken most seriously, taxpayer compliance is more than 95% and is higher than in most countries. Tax auditing is not taken seriously in many countries as it is common to find that only about 10% of tax administration is dedicated to auditing;
- Penalty legislation: The are serious deficiencies in the penalty systems of most developing countries. A guideline to an appropriate system is to ensure that penalties (a) are exercised promptly after a liability has been established (b) are not excessive and (c) must take into account prevailing interest rates and spreads. For example, Columbia recently adopted new rules to encourage quicker settlement including the reduction of penalty fees;
- Taxpayer services and publicity: for taxpayers to be compliant, it is essential for tax administration to provide consistent, fair and prompt service. Key elements about tax issues must also be disseminated to the general public;
- Management and organization: Many tax revenue collection agencies are small departments with government's Ministry of Finance. These agencies often lack skilled personnel and the necessary autonomy to effect modern management practices. In some cases, taxes are not collected by the same agency. However, it is an absolute requirement, for tax reform to succeed, that tax collection agencies be managed professionally.

4. Conclusion

4.1 There seems to be a consensus about the impact of Trade Agreements on Government budgets and therefore on the need for fiscal reform aimed at macroeconomic stability and the revamping of tax structures and administration in order to enable more efficient, faster and less distortionary tax collection. Although policy-makers are often inclined towards issues pertaining only towards policy, the case can be made that the most serious issues facing developing countries are institutional in nature.

Global Implications of the EU–South Africa FTA

Dr Christopher Stevens

IDS

Institute of Development Studies
University of Sussex

Paper prepared for a Workshop on EU–SA Agreement on Trade, Development and Co-operation

bidpa

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Introduction

The EU–South Africa free trade agreement (EU–SAFTA) may turn out to have implications for a much broader area of trade policy negotiations. It has contributed already to the evolution of the EU's thinking both in respect of a successor to the Lomé Convention and in relation to other proposed trade pacts (such as the Mercosur–Chile FTA). The reception that the agreement receives in the multilateral arena may also influence:

- the demands made on SACU in the next broad WTO Round;
- precedents on the meaning of WTO Article XXIV;
- the attitude of the EU to future trade policy.

The influence on the EU may be greater than would be supposed from a narrow reading of the FTA text since the negotiations came at a time when both the economic and the institutional foundations of policy were undergoing change. Policy-making on European-level trade and aid towards developing countries used to be a relatively simple affair. It was focused on one major instrument and one Directorate-General (DG) of the Commission. Whilst they remained the ultimate decision-makers, the member states were not heavily involved except at five-year intervals.

During the 1980s and, especially, the 1990s things became a lot more complex. By 1999 four DGs, five Commissioners and the European Parliament were all closely and directly involved in the formulation and implementation of policy (if transition economies are included), and the member states were also deeply enmeshed in the process. Moreover, decisions had to be framed in response to pressures in Geneva (from the WTO) as well as Brussels and the national capitals.

One result has been for trade policy to evolve away from non-reciprocal trade preferences for developing countries within a multilateral framework towards a hub-and-spoke system of reciprocal trade accords. Whilst portrayed by its supporters as a move towards liberal trade and WTO compatibility, critics can point to evidence in the opposite direction.

If the WTO banana dispute was an important catalyst for this change, the negotiation of the EU–SAFTA was its first major manifestation. The proposed replacement of Lomé with a set of regional economic partnership agreements (REPAs) is the second. And the possible enhancement of the Generalised System of Preferences (GSP) as an alternative to REPAs might well turn out to be the third.

The WTO Dimension of the EU–South Africa FTA

The characteristics of the agreement

The EU–SAFTA will be one of the most important to be subject to WTO (as opposed to GATT) scrutiny and may set precedents for subsequent accords, including REPAs. The EU–South Africa accord includes effective definitions of the two salient WTO requirements that an FTA should cover 'substantially all' trade, and that it should be completed within a 'reasonable length of time'. It has interpreted 'substantially all' as meaning an *average* of *90 percent* of the *items currently traded* between the two partners. All three italicised elements

could be challenged: the figure of 90 percent, its relationship to the items currently traded, and the averaging between partners.

The 90 percent figure is, perhaps, the least controversial. Evidently, the phrase 'substantially all' implies that less than 100 percent of trade is liberalised. The EU claims to have canvassed in Geneva the 90 percent figure, and to have received assurances from trade partners on its acceptability.

But this begs the question: 90 percent of what? Should the calculation be made in relation to the goods actually traded between the two partners, or should it be in relation to all possible traded goods? The difference is important. The effect of heavy protectionism (such as is provided by the Common Agricultural Policy (CAP)) is either to eliminate trade or to keep it at very low levels. If trade does not occur, or is slight, a calculation based upon current flows will show the excluded items to be a very small proportion of the total. Ironically, therefore, the more polarised a country's trading regime (between unsensitive goods and exceptionally sensitive ones) the easier it will be to meet the 90 percent target, since the latter group can easily be excluded without upsetting the arithmetic.

The alternative would be to make the calculation in relation to every item in the tariff nomenclature (which describes all possible traded goods and allocates them a unique numeric code). This in turn would have its problems. The trade nomenclature is particularly detailed on products which are sensitive, in order to allow import regimes to target precisely the goods that are to be kept out. Hence, the exclusion from an agreement of a small number of very sensitive products would have a disproportionate effect on the arithmetic compared with the inclusion of non-sensitive items. This would make the 90 percent threshold more difficult to achieve.

As part of its commitment to an asymmetrical agreement, the parties have agreed that a larger proportion of EU imports must be made duty free than is necessary for South African imports. Hence, while 96 percent of the goods imported into the EU will be covered by the FTA, only 86 percent of those imported into South Africa will be covered.

The agreement also includes a definition of the term 'a reasonable length of time'. The new WTO agreement indicates that this should 'normally' be not more than ten years, which implies that abnormally it could be longer. But how much longer? Most products referred to in the EU–SAFTA will be liberalised over a period of 12 years. The EU will liberalise over ten years, but South Africa has an additional two. This might not, of itself, cause problems, but in addition South Africa has put into what are called protocols a range of goods on which it is not willing, at the moment, to agree liberalisation but which could come on to the agenda at a later stage (particularly if the EU is willing to extend its offers). Such products are therefore covered by the FTA, but will not be liberalised within 12 years or, indeed, any specified finite period.

Obtaining WTO approval

The formal procedure for WTO scrutiny of the new accord (and its interpretation of Article XXIV) is for it to be submitted to the Committee on Regional Agreements (CRA). This committee has a large backlog of agreements: it is still assessing accords notified before the completion of the Uruguay Round (and hence subject to GATT rules), and so has not yet

begun to establish any guidance for the interpretation of the regulations under the WTO. On past form, it is unlikely to give a straightforward approval or disapproval of any agreement.

In the absence of a CRA decision, appeal to the WTO's dispute settlement provisions might fulfil this task instead. For example, if one of SACU's trade partners considered that an EU–SAFTA disadvantaged its exporters, it might post a complaint. But this would be risky. There is very little guidance available on how the weasel words of Article XXIV are to be interpreted. As the banana dispute has shown, the WTO has given birth to a strong dispute settlement mechanism. Any country launching a complaint would have to weigh up the possible consequences of multilateral trade policy being established in a quasi judicial framework rather than through inter-governmental negotiation. There could be far-reaching implications from this 'case law', and some of these might rebound on the complainant in unexpected ways.

It is reported that the USA has indicated it will not challenge the agreement — possibly for this reason. But the USA is not the only country that could lodge a complaint — any WTO member might do so. And not all countries facing trade diversion in either the South African or the EU market will necessarily attach much weight to the danger of a precedent being established. So the accord could be vulnerable to challenge.

Precedents for a new Round

Even if the agreement is not challenged within the WTO, it is likely that it will be taken into account when the participants in multilateral trade negotiations prepare their initial demands. The WTO agenda is unclear: there have to be negotiations on agriculture, services and trade-related aspects of intellectual property rights, but whether or not these will be expanded to a full-blown Round remains to be seen. Even if the negotiations remain sectorally limited, the EU preferences to South Africa on CAP products will be noted by its less-preferred trade partners.

The EU–SAFTA has illustrated in a stark way a more general problem that continues to bedevil EU efforts to negotiate trade accords with developing countries. This is that the most attractive part of any package for the trade partner is precisely that which the EU finds most difficult to concede: improved access on CAP products. One of the effects of the CAP is to maintain prices in the European market at an artificially high level. If foreign suppliers can capture part of this market they have the possibility of achieving much higher profits than they would on sales to other countries. But DG VI sees its duty as defending the interests of the group for which the artificially high prices have been created: European farmers.

A realisation of the central importance of agriculture and the need not to establish unwelcome precedents for the WTO agricultural negotiations contributed powerfully to the abandonment of the proposed EU–Mercosur FTA. It has also contributed to the ruling out by the EU (at least for the time being) of any improvement in African, Caribbean and Pacific (ACP) access for *merchandise exports* under post-Lomé accords.

SACU is likely to come under similar pressure in WTO negotiations, with the breadth of the demands made being determined by the scope of the Round. It would be prudent, therefore, to begin now to anticipate the likely sources of demands for improved access in order to:

- assess the adjustment costs (and economic gains) of accepting such demands;

- identify reciprocal demands that SACU would wish to present as the 'price' of acceding to such requests for preference generalisation.

Applying the New Approach to Lomé

The EU's drive to abandon the Lomé Convention and replace it with a new approach stems from:

- the WTO banana dispute, which brought the Lomé concept into question;
- the EU–SAFTA, which illustrated a possible new way;
- the much reduced economic importance of the ACP, which reduced the EU's willingness to 'take risks' at the WTO on its behalf.

Nonetheless, the EU's position has evolved since Autumn 1997, when the Commission's proposal for a negotiating mandate opted for a two-stage approach. Initial negotiations would be for a Framework Agreement setting out the principles for trade and aid co-operation following the expiry of Lomé IV (and its WTO waiver) in February 2000. It would also seek a further WTO waiver (under Article IX) for the continuation of Lomé preferences to 2005.

During this second stage ACP states would be invited to negotiate REPAs. Least developed states that failed to agree REPAs would continue their current access to the EU market, but under an improved GSP provision open to all least developed states. Other ACP members not in REPAs would be downgraded to the Standard GSP. The choice of the year 2005 for the end of the waiver was not unrelated to the fact that it was the target date for the inauguration of the FTAA. When and if this occurs it will leave the EU as the only OECD state requiring an Article IX waiver for trade agreements with developing countries.

Although its status as leader of the post-Lomé negotiations was unchallenged (following its successful leadership of the EU–SAFTA), DG VIII found that in formulating its proposals it had to accept limitations imposed by DGs I and VI. In a formulation in mid-1997, DG VIII had sought to dissipate some of the tension that its 'REPA or GSP' choice would provoke by offering a third way — a vague 'Regional Economic Co-operation Agreement' that would not require ACP reciprocity. But this was shot down by DG I as being WTO incompatible.

DG VIII's attempts to produce an offer that would appeal to the ACP were also restricted by limits to what could be said in relation to CAP products. Since Lomé preferences already provide virtually unrestricted access on manufactures, agriculture is the only product area in which the EU could offer improvements for the exports of REPA members. But this was ruled out, at least until the final negotiating rounds, by DG VI's insistence that improvements on CAP products could not be contemplated. DG VIII was left, therefore, with the less-than-easy task of selling to the ACP an offer in which they would be required to open up their markets to EU exports simply in order to retain the *status quo* for their exports.

In fact, the task of selling the new approach was even more difficult because considerations of the CAP and WTO required DG VIII to underplay the costs of being downgraded to the GSP and, hence, the relative attractiveness of the REPA alternative. DGs I and VI insisted that nothing be said that would undermine the EU's claim that its Sugar and Beef Protocols were WTO compliant (by virtue of their inclusion in the EU's Uruguay Round tariff schedules). To do so would weaken the EU's credibility in the WTO not only in respect of the Protocols but also in relation to other elements of trade policy that are justified by the

specifics of the Uruguay Round schedules. The implication was that these Protocols (which for their beneficiaries are the most valuable part of their preferences) could continue after Lomé even if countries failed to enter a REPA.

During the first half of 1998 there was intensive negotiation between the member states on the mandate proposal. Two clear viewpoints emerged. One was to support the Commission's proposals as a way of fostering a liberal trade policy in ACP states and integrating the Lomé Convention into the 'mainline' provisions of the WTO. The other was to reduce the contrast between the post-2005 options by improving the Standard GSP. This was seen both as a method of reducing friction in the negotiations with the ACP and of promoting a wider liberalism in EU trade policy (since enhancements to the GSP would tend to benefit all developing countries).

The result was a mandate agreed in the dying hours of the UK Presidency at the end of June 1998 that combined both approaches. On the one hand, it committed the Community to 'offer a process to establish free trade areas ... [to] be negotiated during the five years following the expiry of the current convention (2000–2005)'. On the other hand, a footnote provides that:

> Notwithstanding the primary objective set out in the mandate with regard to FTAs, the Council and the Commission agree to assess, in 2004, the situation of the non-LDC ACPs who are *for objective reasons* not in a position to join such FTAs with the EU.
>
> They will examine all alternative possibilities ... to provide ... a new framework for trade between them and the European Union which is equivalent to their existing situation under the Lomé Convention and in conformity with WTO rules. In particular the Council and the Commission will take into account their interests in the review of the GSP in 2004, making use of the differentiation permitted by WTO rules (EU Council 1998: 18, footnote 1 (emphasis added)).

Potential Areas for Policy Evolution

The EU–SAFTA, together with the banana dispute, have contributed both to the EU's proposals for a post-Lomé regime and to the characteristics of its offer to the ACP that make it unlikely that this will receive an easy passage. On the one hand, the EU is seeking improved access to ACP markets; on the other, it is unable to offer improved *merchandise access* to its own market, and the record of the South African negotiations speaks eloquently to the impracticality of expecting the process to be completed by 2005.

One consequence may be to provide a stimulus to movement in one or both of two directions:

- to introduce preferences on non-merchandise trade into Lomé;
- to generalise Lomé preferences.

If the EU cannot afford to offer more on agriculture, could REPAs be made attractive to the ACP by covering the 'new' trade issues? What could ACP states gain through a North–South regional agreement that could not be obtained as well or better through the multilateral system or via a South–South accord? If Lomé's discrimination against other developing countries makes it WTO incompatible, could the GSP be enhanced sufficiently to make it an adequate alternative for the ACP without running into insuperable opposition from European protectionist interests?

The 'new' trade issues

It is widely held that as tariffs fall, so the relative importance of other policy influences on trade increases. But the trend goes further than this: 'new trade-related policy instruments' are growing in absolute as well as relative importance. The primary reason for this has nothing to do with traditional protectionism: it is an outgrowth of trends in the nature of national and global markets. These trends are likely to have differential effects on both countries and communities which are not yet well understood.

Among the new areas are:

- a search for tariff substitutes such as 'chain' anti-dumping complaints;
- a generalisation of standards between, previously separate, markets resulting in *altered* (although not necessarily more restricted or open) competitive environments;
- new methods of implementing trade policy, such as the requirement for in-country testing by exporters, that effectively restrict access to those states with the required testing infrastructure;
- changing consumer demands, whether or not backed by law — for example to favour products for which evidence exists on paper concerning the mode of production;
- the extension of process criteria to trade policy;
- new types of trade, notably in services;
- and the uneven development of international law, notably the weakness of international competition law.

The 'new' trade areas could give rise to 'new' trade preferences to replace the old ones that are being eroded by the liberalisation of merchandise trade. There are possibilities, for example, of having preferences on services trade such as bilateral air transport agreements and agreements on taxation of tourism and travel. At present, there are effectively reverse preferences against developing countries since any special deals tend to be bilateral (or restricted) ones between industrialised countries.

Multilateral disciplines on these new issues are still in their infancy: the General Agreement on Trade in Services is little more than a set of lists, and much the same could be said of the provisions on trade-related investment measures. But there will be pressure for subsequent negotiations to tighten up on the multilateral rules. This poses particularly strong problems for relatively small trading countries. They may well have strong interests at stake, and the WTO consensus approach to decision making gives them the opportunity to defend these interests. But what are their interests? Effective defence assumes prior knowledge, and these are such new areas that many countries have only the haziest notion of where their interests lie at a detailed level.

This conundrum illustrates both the potential danger and opportunities of broaching the issues within a post-Lomé accord. The EU has indicated a willingness to broaden the scope of REPAs beyond merchandise trade, but it would be unwise to accept this invitation without some prior understanding of the areas in which ACP interests could be enhanced through an accord with the EU and those in which such a geographically restricted agreement would be undesirable.

If such issues could be elaborated sufficiently well to give the ACP confidence to enter into negotiations with the EU, the benefit could be considerable. This is because a side effect is likely to be the influencing of any subsequent WTO agenda. Precisely because multilateral disciplines are so limited, their future development will have to take into account pre-existing sub-multilateral accords. In that sense, the provisions of post-Lomé agreements would form part of the existing architecture around which WTO accords would need to be fashioned.

The generalisation of preferences

The Lomé preferences have already been substantially generalised. Whereas in 1975 the ACP were at the pinnacle of a sharp 'pyramid of privilege', that pyramid now approximates to the shape of Table Mountain. There are three broad bands of preference: a higher level, which the 70 ACP share with over 50 others; a middle level, from which 47 developing countries benefit; and the bottom level, comprising the mis-named most-favoured-nation provision. If the middle band — the standard GSP — could be enhanced in some way, it would let the EU off the WTO hook whilst avoiding the political fallout from a downgrading of non-REPA ACP members. And, if the WTO verdict on the EU–SAFTA is negative, it would provide a way to side-step REPAs.

The principal difficulty in extending the GSP is that a relatively small number of large and competitive states are eligible and can be expected to take strong advantage of any improvements. Given the relatively high income of the Caribbean states, it would not be possible to exclude from standard GSP enhancements on income grounds alone a swathe of countries in Latin America and South East Asia, not to mention India. But unless the GSP enhancement were to be available to all ACP, it would not be an adequate substitute for Lomé.

It is possible, in fact, to identify a set of criteria that would allow Lomé equivalence to be extended via the GSP to most non-Protocol products without at the same time opening the floodgates to imports from middle-income non-ACP states. It would require political initiative from the EU, and would result in further complexity to the GSP which might, or might not, provoke problems in the WTO.

The purpose of this paper is not to speculate on whether such initiative and multilateral acceptability would be forthcoming, but to point to the implications for the ACP of a move in such a direction. The implication is that the competitive advantage that ACP states currently derive would disappear except in the, very, limited number of cases in which their main competitors are those OECD states outside the EU/EEA/EFTA bloc.

Unless there is a sharp reversal in the trend towards liberalisation of merchandise trade, the current pattern of the EU's trade policy towards developing countries will fade rapidly over the next decade. Hence, even if the post-Lomé regime turns out to have strong similarities to the current policy *vis-à-vis* the ACP, the practical value of the agreement will decline.

To a certain extent, this will facilitate a change in the direction of European policy. Old agreements will not need to be torn up and the costs of abandoning them in the face of external pressure from the WTO will decline. The 'new' trade hierarchy will be created in the 'new areas' of trade policy: agreements on services, intellectual property, standards harmonisation, investment measures, etc. These are all in their infancy. It remains to be seen whether or not it is either desirable or politically feasible to negotiate agreements in these

areas at a sub-multilateral level. If it does prove to be desirable and feasible, it remains to be seen with which countries the EU forges such accords. But it is reasonable to surmise that the most likely candidates for such pacts will be the states (developed or developing) which have the greatest economic or political importance for the EU. And it is also reasonable to speculate that these countries will not be identical to those that were at the pinnacle of the EU's old trade policy regime, based as it was on preferences for merchandise trade.

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Development Assistance in the EU-SA Agreement on Trade, Development and Co-operation

Kennedy Mbekeani
BIDPA

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1. Introduction

Other than the Provisions for a Free Trade Agreement (FTA) and Trade Related Issues, the "Trade, Development and Co-operation Agreement" between the EU and South Africa covers a wide range of components. It includes:

- Joint Declaration on Political Dialogue;
- Economic Co-operation;
- Financial Assistance and Development Co-operation; and
- Social and Cultural Co-operation.

In this paper we will briefly analyze the Development Co-operation aspect of the Agreement.

The Development Co-operation Agreement aims at contributing to South Africa's integration into the world economy and trade, expansion of employment, for development of sustainable private enterprises and regional co-operation and integration.

This is the most important component of the agreement for the Southern African countries, especially the BLNS countries. The BLNS countries can utilize the proposed technical, material and financial assistance to assist them in adjustment efforts occasioned by the establishment of the free-trade area. The assistance could be directed towards industrial and agricultural restructuring, and fiscal adjustment.

2. Assistance from the EU

The EU has indicated that it will provide assistance to the BLNS countries, partly to compensate for the loss of revenue and restructuring in the industries. It is not, however, clear whether the assistance from the EU will be provided specifically under Article 65 of the EU-SA Agreement on Trade, Development and Co-operation or Article 12 of the Lome IV convention.

2.1 Assistance under Article 65 (1a)

Article 65 (1a) of the EU-SA Agreement is less clear. The Article states that:

...special attention will be given to providing support to the adjustment efforts occasioned in the region by the establishment of the free-trade are under this Agreement, especially to the SACU.

Co-operation partners eligible for financial and technical assistance shall be national, provincial and local authorities and public bodies, non-governmental organizations and community-based organizations, regional and international organizations, institutions and public or private operators. Any other body could be made eligible if so designated by both parties.

The operational procedures will be an outcome from programming discussions carried out between the EU and RSA with the contribution of the European Investment Bank. Since BLNS states will not be party to the programming discussions the provision under Article 65 (1a) becomes less attractive and uncertain as to what the EU and South Africa will be able to provide. Elaboration of the Article and information regarding the operating mechanism and inclusion of the BLNS states may provide some comfort.

2.2 *Assistance under Article 12 of the Lome Convention*

Article 12 of the Lome Convention, which states that:

...where the Community intends, in the exercise of its powers, to take a measure which might affect the interest of the ACP states as far as this Convention's objectives are concerned, it shall inform in good time the said states of its intentions. Towards this end, the Commission shall communicate simultaneously to the Secretariat of the ACP States its proposals for such measures. Where necessary, a request for information may also take place on the initiative of the ACP States.

At their request, consultations shall be held promptly so that account may be taken of their concerns as to the impact of those measures before any final decision is made.

After such consultations have taken place, the ACP States may, in addition, transmit their concerns in writing to the Community and submit suggestions for amendments indicating the way their concerns should be met.

If the community does not accede to the ACP Sates' submissions, it shall advise them as soon as possible giving its reasons.

The ACP States shall also be provided with adequate information on the entry into force of such decisions, in advance whenever possible.

The EU seems to be following the procedure under Article 12 of the Lome IV convention. Based on the assistance provisions in the Agreement, Article 12 of

the Lome IV Convention would seem to be more attractive to the BLNS countries.

There are fears relating to the future of the Lome IV Convention, particularly because of the expiration of the Lome IV Convention. It is, however, unlikely that aid from the EU will cease with the expiration of the Lome IV Convention (this has to be verified with the EU). The BLNS countries can, however, request for the provisions under Article 12 to cover a specific time period that goes beyond the Lome IV Convention.

3. The Mediterranean Experience

To help mitigate the fiscal revenue and transitional adjustment costs and in exchange for the increased market access for European firms, the EU committed to provide financial assistance to the Mediterranean countries. Aid disbursements were conditional on the implementation of programs of structural reform between the authorities and the EU in close cooperation with the World Bank

Over the 15-month period through March 1998, Tunisia received financial aid from the EU amounting to ECU 130 million (about 0.5 percent of GDP on an annual basis), only slightly more than Tunisia received from the EU during 1992-96. For all Euro-Med countries combined, about ECU 1 billion has been assigned in grants on an annual basis during 1995-99.

Agreements with the EU were signed by Morocco in 1995, and Jordan in November 1997. To a large extent these agreements follow a similar outline. Nonetheless, country specific circumstances determined the type of assistance. For example, for Lebanon trade diversion is larger because the share of its imports originating from the EU is only about 50 percent. The fiscal revenue cost to Lebanon is also higher than in any of the other countries.

Lebanon's special situation added to the debate on the distribution among different Southern and Eastern Mediterranean countries of the total envelope of Euro-Mediterranean assistance. The Lebanese authorities feel that the three criteria for financial assistance proposed by the EU: population, per capita income, and willingness and ability to undertake economic reforms put them at a disadvantage. They stress the financial cost of reconstruction of their country, the cost of trade diversion, and their efforts in liberalizing services.

The cost of trade diversion is substantial in the case of Egypt and Jordan, mainly because the EU accounts for only 45 and 32 percent respectively of imports. To

raise welfare significantly, agreements with those countries need to have considerable leverage effects in improving the cost structure of doing business and thereby enhance prospects for inward FDI.

4. Recommendations

- It is important to consider country specific situations in requesting assistance.
- The success of the Agreement will depend on the quality and magnitude of economic and technical cooperation from the EU.
- Seek clarification on the operational procedures of the assistance program under Article 65(1a) of the EU-SA Agreement.
- Explore the benefits of utilizing Article 12 of the Lome simultaneously with Article 65 (1a) of the EU-SA Agreement.
- Seek clarification as to whether the development assistance will be conditional.

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NATIONAL COUNCIL OF TRADE UNIONS
PARLIAMENTARY AND RESEARCH OFFICE

THE EU-SA TRADE AGREEMENT:
AN EVALUATION OF TRIPARTITE CONSULTATION
(Draft presentation for BIDPA Workshop)

By

Henk Campher

July 1999

The South African Tripartite Process

On 18 February 1995, the National Economic Development and Labour Council (NEDLAC) was launched, ushering in a new era of inclusive decision-making and consensus-seeking in the economic arena.

NEDLAC's origins lie in the struggle against apartheid, against unilateral government decision-making, and in the calls from all sectors of society for decisions to be taken in a more inclusive and transparent manner.

It emerges out of recognition of the importance of seeking consensus on major economic, social and development policies to ensure their success, and out of awareness, as former President Mandela remarked at its launch, that "our democratic gains will be shallow and persistently threatened if they do not find expression in food and shelter, in well-paying jobs, and rising living standards".

NEDLAC has the unique feature of including not only the traditional social partners – government, business and labour –but also organisations which represent community interests in our country.

The social partners in NEDLAC have key roles to play in developing effective policies to promote urgently needed economic growth, increased participation in economic decision-making, and social equity in South Africa on a sustained basis. The form of multilateral decision-making created by NEDLAC provides an opportunity for the major stakeholders in South African society to meet these challenges, and to contribute to the journey to reconstruction and development.

In the NEDLAC structures government, organised business andorganised labour are represented in equal numbers in all NEDLAC's chambers and the Executive Council[1]. The government delegation in NEDLAC comprises ministers, deputy ministers, directors-general and other officials from several ministries and departments. Organised consists of Business South Africa (BSA) and the National African Federated Chamber of Commerce (NAFCOC). Organised labour is made up of the National Council of Trade Unions (NACTU), the Congress of South African Trade Unions (COSATU), and the Federation of Unions of South Africa (FEDUSA).

NEDLAC has four chambers that drive its work programme. These four chambers are:

- Public Finance and Monetary Policy Chamber;
- Labour Market Chamber;
- Development Chamber; and

[1] Organisations representing community interests are represented in the Development Chamber, Management Committee and Executive Council.

- Trade and Industry Chamber.

Background to EU-SA Trade Negotiations

Trade negotiations with the EU was considered by the Transitional Executive Council (TEC) before the Government of National Unity (GNU) was constituted. In April 1994, the EU offered assistance to South Africa in the form of an aid package and a limited General System of Preferences (GSP) package with some trade concessions. The EU further proposed negotiations which would lead to a comprehensive trade agreement with South Africa.

South African negotiators had argued for membership to the Lome Convention. South African membership to the general trade package of Lome was, however, rejected by the European Council. Instead, the European Council offered South Africa a negotiated free trade agreement (FTA) with reciprocity with regard to free trade.

South African negotiators had not rejected the possibility of an FTA, but argued for a set of preferential measures as close as possible to those enjoyed by the ACP countries. This could be accommodated by asymmetry with regard to reciprocity with a grace period of 10 years favouring South Africa. South Africa would be open to an FTA in the medium to long term subject to further detailed analyses.

The NEDLAC Process

The Technical Sectoral Liaison Committee (TESELICO) was set up by the Trade and Industry Chamber of NEDLAC to provide a consultative forum for government trade negotiators to liaise with business and labour over technical matters relating to the EU trade negotiations.

TESELICO focused on technical and detailed issues in response to the requirements of ongoing trade negotiations and made recommendations which assisted the SA trade negotiators. Government reported on developments in the ongoing EU-SA negotiations to TESELICO. Business and labour commented on and evaluated the proposals arising from the negotiations. TESELICO's inputs related to both the general principles informing the negotiations as well as specific issues.

The interrelationships between trade initiatives necessitated a holistic view of SA's trade strategy. TESELICO therefore also consider issues relating to other trade negotiations, in particular the South African Development Community (SADC) Trade protocol, the South African Customs Union (SACU) and multilateral negotiations in the World Trade Organisation (WTO).

Organised Labour's Mandate and Strategy

The basic principles of labour's position was:

- The protection of jobs;
- Promotion of labour standards; and
- The underpinned position that nothing can be agreed until all items are agreed to.

These principles set the agenda for labour's approach to tariffs and the trade agreement as a whole. This approach can best be described through an evaluation of some of the issues, problems and lessons to be learned from the EU-SA trade negotiations and the TESELICO tripartite process.

Some Issues, Problems and Lessons

The SA tariff phase-down offer

South Africa's initial offer to the EU was put together in collaboration with TESELICO. The committee had intensive discussions in a series of meetings in 1996 and 1997 to formulate the SA offer on a line-by-line basis with business and labour consulting extensively with their constituencies. Business and the Industrial Development Corporation (IDC) provided resources to undertake the technical analyses which eventually resulted in a comprehensive tariff reduction proposal over a period of 11 years by which time tariffs on virtually all industrial products and a large number of agricultural products would be eliminated.

The cooperation between the social partners became apparent during the drafting of the initial offer insofar as business and labour worked together to draft a joint line-by-line offer on manufacturing products. In a way this set the scene for future TESELICO consultations as business and labour continued to work closely together during the remaining period of consultation. This close cooperation between business and labour also lead to one of the most serious confrontations in TESELICO.

The eventual offer made by South Africa made a substantial number of changes to the joint business and labour line-by-line offer. Although a number of these changes were due to changes in tariffs and previous incorrect figures, the social partners still felt that these changes undermined their inputs and consultations. Further consultations, bilateral and sector specific meetings eventually ensured an amicable solution to the grievances.

Another problem experienced from a labour point of view was the consultation process dealing with agricultural products. The agricultural offer was drafted by

the Agricultural Trade Forum (ATF), where the dominant government department was the Department of Land Affairs and Agriculture. The level of commitment to consultation with all social partners was questioned as it was perceived by labour that the department did not show the necessary urgency to involve labour in these consultations. This problem was eventually dealt with after both business and the Department of Trade and Industry agreed that ATF discussions should also be included in the TESELICO process.

Sensitive products and protocols

Initially labour approached product protocols as areas of sensitive industries. These included textiles and clothing, motor vehicles and components and electronic industries. These exclusions were not based on tariff levels, but rather the nature of industries. In other words, a product could be included for protection if the industry was judged to be sensitive, even if the tariff was at a low level.

However, the tripartite consultation process brought a new dimension to labour's approach. The SA government supported the basic principle of protection of sensitive industries, but added that sensitive areas did not necessarily mean industries in danger of losing jobs. They argued that industries that show potential for growth should also be protected for a certain period in order for them to develop further.

This meant that product protocols was not only a job saving mechanism, but also a job creating mechanism. The reality is that uncompetitive industries will continue to shed jobs if they do not become more competitive in a free market. FTA's is a mechanism for competitive industries to exploit other weaker markets. By adding potential competitive industries to a list of protected industries, a short term job saving mechanism can turn into a long-term job creating mechanism.

Labour supported this approach and proposed a list of product protocols that included the traditional sensitive products as well as developing sectors and products. Labour's approach to these products was not to protect them indefinitely, but to review the progress made in these sectors every 2 years. Tariff phase-downs will also take place after every review.

However, the outcome of this approach did not necessarily have the expected result. The list of products that could have been included in the product protocol list did not, from a labour point of view, include enough of these developing sectors. This was mainly due to pressure from the EU and a lack of communication between and within government departments.

The Social Clause

In June 1996 the social partners at NEDLAC reached an agreement that the SA government will promote labour standards when engaging in trade negotiations. This will include promoting the ratification of core ILO Conventions (conventions 29, 87, 98, 100, 105, 111 and 138). Labour argued for all these conventions to be signed before the implementation of tariff phase-downs[2]. Labour stated clearly that it should not be seen as an instrument of trade protectionism, but rather an implementation of basic labour standards.

The Social Clause was of most importance to labour. In a world of globalisation and free trade, the only 'product' that labour can 'export' is labour standards and rights for workers in other regions. The identified ILO Conventions offers basic rights to workers, and are not by any means revolutionary. These rights are:

- Abolition of forced labour;
- Freedom of association and protection of the right to organize;
- Right to collective bargaining;
- Equal remuneration;
- The right not to be discriminated against; and
- Minimum age.

This was one area of much discussion between the social partners, with labour lobbying their EU counterparts to strengthen their position. After some initial problems the SA government undertook to push for the inclusion of the Social Clause.

The final version of the *Agreement on Trade, Development and Cooperation* between the EU and SA covers the Social Clause in Article 85. Although it is a somewhat watered-down version of the labour position, labour can still be pleased with the fact that it was included in the trade agreement and sets a precedent for future trade agreement negotiations.

General

A number of other general problems with the tripartite process were experienced These were:

Firstly, South Africa entered the trade negotiations believing that the EU will open its market at a much faster pace than SA. This was to accommodate the historic disadvantage (economic, level of development etc.) of SA. This, however, did not materialize. Any thoughts of SA benefiting from any goodwill from the EU side disappeared after it became clear that the EU was more interested in benefiting

[2] Labour also argued that if problems are experienced in ratifying certain conventions then a phase-in period could be implemented that coincides with certain tariff phase-downs.

their own market entry into SA, and protecting their market. It was naïve of SA to think otherwise. One of the shortcomings was a lack of understanding of the EU's political agenda, both in its internal politics (i.e. CAP) and external political considerations involving the renegotiation of the Lome Convention where the SA FTA was intended to be used as a model for similar FTA's for other developing countries. A lesson to be learned from this is that trade negotiations is not about favours, but about market access.

Secondly, in the early months of negotiations, there was a perception by the social partners that government representatives did not expect to obtain any benefits from TESELICO consultations and were merely going through the motions of consultation in order to satisfy a political imperative. As with most perceptions, it was found to be untrue. Even if it was true during the early part of consultation it was untrue during the later part of the process. The perception was that during the last rounds of negotiations, the consultation process was successful because of the commitment of government negotiators to consult with the social partners, even when they themselves had very little time other than try to save the EU-SA FTA. It made a strong argument that all tripartite structures need champions to ensure the process stay on course.

A third problem was the initial negotiating strategy of the SA government. The social partners felt that government showed too much of the own hand in the first round of information exchanges. The SA negotiators were up against seasoned negotiators from the EU and conceded too much too quickly. For example, the EU had a preliminary SA offer long before SA had any offer from the EU. This was double troublesome as the SA offer was close to what was planned to be the final offer. This enabled the EU to make a conservative offer and force SA's hand even further. It was a steep learning curve for the SA negotiators and where might have they started as the students at the beginning of the negotiations, they came ended the negotiations as equals – at the very least. A potential problematic situation was saved by what was seen by the social partners as skilled and hard negotiations during the later part of negotiations (especially the final Wine and Spirits proposals) by the SA negotiators.

Fourthly, it seemed for long periods as if the SA 'social partners' did not always trust each other enough to share all relevant information. All parties were guilty of this. A likely reason for this was that partied did not always have the mandates or resources to deal with all the problems. For example, labour had two people negotiating on behalf of organized labour, with very little research support other than what was supplied by the SA government. The SA government, on the other hand, must co-ordinate the activities between and inside all the different departments. It is therefore no surprise that information sharing was sometimes an issue of major concern. A lesson from this should be that parties should have greater co-ordination within themselves in order to ensure quality inputs.

Fifthly, labour was also concerned that on a number of occasions, TESELICO was expected to endorse concessions already (if tentatively) made to the EU by SA negotiators without prior consultation with the social partners. Even if proposed concessions are tentative and provisional, it is difficult to remove a proposed concession once it is tabled. The principle of 'nothing can be agreed until all items are agreed to' was used to solve these situations. It helped insofar as the stages of negotiations only made sense if a final overall cost-benefit assessment was made after concluding the negotiations.

Sixth, labour was also concerned that it frequently did not have sufficient time to obtain mandates from its principles. Obtaining mandates is generally time consuming, especially on tariff issues where there will always be a reluctance to concede lower tariff levels. Furthermore, the SA government also took their time in processing certain requests from labour. For instance, it was the labour and business position from the start that they should be included in the actual negotiations with the EU. This issue was approved by the Minister of Trade and Industry, Alec Erwin, but took two years to be implemented. Needless to say that labour did not participate when the offer eventually came.

A seventh, and last point, and it is especially relevant to labour and business deals with political responsibility. The TESELICO process was a consultative process, and any of the parties was free to walk out at any stage if they felt they did not benefit from the arrangement. However, the consultative process meant that if parties stay in the process they also have to acknowledge that the government will have to make the final decision as they are the people who will have to be accountable in the end. This is not wage negotiations where one should expect a final position supported by all parties. The social partners must be consulted with and the government should try and accommodate all the parties as much as possible, but a total agreement should not be expected.

Notwithstanding all these problems a greater degree of trust developed on all sides in the later months of the negotiations and consultations, and labour is satisfied and pleased that there was such a considerable degree of consultation on all aspects of the negotiation process as well as on all major issues. It was the first time since the GATT negotiations that social partners were involved in trade negotiations. The building of capacity in constituencies took time and in retrospect it would be difficult to determine whether more favourable outcomes would have been achieved if SA had greater experience and institutional experience. The lack of capacity and experience lead to some delays in the process, but assisted in asking questions that would not normally have been asked.

As with other trade related negotiations, the EU negotiations were a major capacity building experience for all participants, and showed the way forward towards future social partner consultations

EU - SA Agreement on Trade, Development and Co-operation

Presentation by: Bahle Sibisi
Chief Director, DTI, South Africa

July 1999

Workshop on EU-SA Agreement on Trade, Development and Co-operation

July 22 - July 23 1999

Boipuso Hall, Gaborone, Botswana

Briefing Document on the conclusion of the RSA - EU negotiations for a Trade, Development and Co-operation Agreement

1. BACKGROUND

This week marked the end of almost four years of negotiations with the European Union towards a Trade, Development and Co-operation Agreement. Minister Erwin and Commissioner Pinheiro **finalised this historic agreement** which has been endorsed by both the **South African Cabinet** and the **European Council of Ministers**. It means that the road has now been cleared for the signing and ratification of the agreement which is of **national and international importance**. The **expected implemenatation date is 1 January 2000** which will allow time for government structures as well as private sector operators to prepare for the **procedural implications** of a free trade area with our most important trading partner in the world.

1.1 The origins of the Agreement

The call for negotiations with SA was expressed **as part of the EU's desire to support SA's new democracy** and address the legacy of the past. The EU argued that a free trade area was the best and only way it could provide SA with better market access. The **EU's mandate tempered** SA's high expectations. **South Africa, however, chose to engage** and develop a strategic partnership with the EU which is SA's major trade and investment partner.

As part of economic transformation, the government has adopted policies which seek to **reposition and re-integrate the South African economy** within a rapidly changing global economy. This necessitates the establishment of globally competitive economic enterprises. The move toward global competitiveness has to be accompanied by **regional economic cooperation** that advances a broad and integrated process of **industrialisation and modernisation** in the economies of Southern Africa.

A growing South African economy that facilitates **intra-regional economic trade and investment flows** is a major opportunity for **development in Africa** and more particularly Southern Africa in the medium term. Not only will it source a wider range of products from its neighbours but it will also be able to invest in activities that will increase the region's exports. This can only happen if South Africa is able to expand its production base by strengthening and enhancing its competitive advantage in the beneficiation of its natural resources. This in turn requires that there is an increase in value added production and a larger manufacturing sector.

The bold move toward a free trade agreement with the EU is intended to contribute towards **restructuring of the economy**. It is also aimed at consolidating the **strategic links with the economies of the member states of the EU, securing preferential market access** for South African products and **providing certainty and added leverage for foreign investment** into the South African economy.

2. OVERALL RESULTS

The Trade, Development and Co-operation Agreement with the EU covers a **wide range of issues** in a comprehensive field of co-operation. It includes, inter alia;

- Political dialogue
- Provisions for a Free Trade Area
- Trade related issues
- Economic co-operation
- Financial assistance and development co-operation
- Social and cultural co-operation

As part of establishing a comprehensive relationship with the EU, two other agreements have been concluded:

- Science and Technology Agreement (signed in December 1996)
- Partial Membership of the Lomé Convention (agreed in April 1997)

At the request of the EU, SA accepted to negotiate a Wines and Spirits Agreement and a Fisheries Agreement. SA insisted, however, that such agreements should be **mutually beneficial and that there should be no conditional linkage** with the main agreement. The main agreement contains a so-called hook-clause providing for future negotiations for a co-operation agreement on fisheries and there is also a side letter covering the political agreement on port and sherry.

3. KEY FEATURES OF THE AGREEMENT

3.1 Essential Element and Non-execution provisions

Respect for **democratic principles, fundamental human rights and the rule of law** is established as key elements of the agreement. Good governance is established as another important principle. Any violation of these principles by one party would lead to the other party taking appropriate measures, including withdrawing some concessions. SA insisted on the formulation of these provisions such that there is **objectivity in the test for breach** of the essential element of the agreement without the **risk of unilateral action** nor the balance of economic or political interests becoming the determining factor. The agreed text has a better definition of good governance and circumstances under which the non-execution

provision can be invoked.

3.2 Free Trade Area (FTA) Provisions

3.2.1 General Features

When SA presented its trade offer to the EU in June 1997, it called for free trade with **asymmetrical coverage** of all trade and sectors and **special protocols** to cover sensitive products. It also called for development and financial measures to **support further regional integration** and to **facilitate the adjustment process in Southern Africa**. The outcome of the negotiations meets the WTO requirements of Art. XXIV GATT 1994. The coverage of the FTA will be around *90%* of current trade between the Parties with the following elements:

- Community: full liberalisation of *95%* of imports from SA at the end of the transitional period of *10* years.
- South Africa: full liberalisation of *86%* of imports from EU at the end of the transitional period of *12* years.
- Includes both traded and non-traded products.
- Provides for the protection of SA's sensitive sectors (automobiles and components, textiles and clothing, red meat, sugar, winter grains, and dairy).
- Includes the agricultural sector, alongside all other sectors with **partial liberalisation** and provision for **regular reviews** on products on the **reserve lists.**
- Commits the EU to provision of **support for SACU** for adjustment efforts resulting from the establishment of the FTA.
- Contains several elements that assure a positive regional impact on the other countries of SADC.

3.2.2 Industrial Sector

Approximately **86% of SA's total exports** to the EU consists of industrial products. While the EU's average tariff levels for industrial products is low, the removal of tariffs will nevertheless give SA's exporters **a relative advantage against some of their competitors** in the EU market. The EU will eliminate its industrial tariffs **either immediately or within three years after** the entry into force of the agreement. This includes most of the sensitive products of textiles and clothing (only about 20% of SA's textile exports to the EU will be phased out over a longer period. i.e. 6 years from the entry into force of the agreement). At entry into force of the agreement tariffs on auto-components will be reduced to

50% of the MFN rates[1] applied by the EU. Other products like **ferro-chromium** with tariff elimination starting in the 4th year will continue to have a **global duty free quota**. Only six lines of aluminium will remain on the reserve list. The products on the reserve list will nevertheless be subject to reviews.

As indicated the transitional period for the phasing out of tariffs by SA **is twelve years to allow for adjustment** by firms. Sensitive products like **automobiles and parts** will remain on **the reserve list** without any tariff elimination or reduction schedules at this point. This will be reviewed in the light of the outcome of the mid-term review of the Motor Industry Development Programme. With regard to other sensitive products, South Africa persuaded the EU to moderate its initial expectations. This will enable SA to have a slower phase-down. In the case of **clothing and textile** there is a commitment to reduce the tariffs applicable to imports from the EU. Depending on the **segment of the market**, by the end of the 8th year the tariffs will **vary between 5% and 20%. Between the 8th year and the end of the transition** period, EU products will enjoy a preference over the **MFN rate of around 40%**. The agreement therefore takes into account the changes in these industries at a pace far beyond what was conceivable a few years ago.

3.2.3 Agricultural sector

The agricultural sector is traditionally the most protected sector in the EU and has generally been excluded by the EU in other free trade agreements. In its mandate the EU *a priori* excluded about 46% of agriculture from the FTA with SA.

- **Agricultural safeguard clause**

While the EU's Common Agricultural Policy (CAP) is still a matter of concern, the agreement provides **(with regard to agricultural policies) for consultation and compensatory adjustments** for any changes which may affect the balance of concessions. The Agricultural policies provision is supplemented by an Agricultural safeguard clause which gives SA **the right to challenge the EU should there be proof that increased imports of agricultural products are causing harm or threatening to cause harm to the domestic industry**. The onus is on South Africa, especially the industry, to put in place an effective monitoring system that will serve as an early warning signal in this regard.

- **EU export subsidies**

Although SA did not succeed in eliminating EU export subsidies completely, there are some important breakthroughs. Firstly, the EU has committed itself not to pay export refunds on cheese exported to South Africa under the tariff quota of 5000

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[1]The MFN rate is the rate applicable to all other contracting parties of the World Trade Organisation (WTO).

ton. Secondly, the EU is willing to eliminate export refunds on products South Africa might want to offer for front-loading during the implementation period. Refunds will be eliminated in full once tariff liberalization starts. This is an important aspect of the agreement, as most of the EU agricultural products will not be competitive on the domestic market without refunds. South Africa will take up this challenge. Should the EU be unwilling or unable to eliminate export refunds, South Africa can simply retract its offer of front-loading.

- **Tariff quotas**

The introduction of **tariff quotas** is important in that it makes **inroads into the EU reserve list**. Especially the tariff quotas for **canned fruit (60 000 ton), fruit juices (5 000 ton) and cut-flowers, in particular proteas (900 ton)** are of interest to the industry in SA. The quotas for **wines and sparkling wines**, as well as for **cheese** are also significant.

- **Reserve list**

The EU list of exclusions has been reduced, i.e. from **46% to 38%** (based on 1997 trade statistics). If one takes into account tariff quotas, it has been reduced even further to 26%. This is an important development. In addition, it is now called a **reserve list subject to regular reviews** with a view to further opening of the market. South Africa will therefore be continuously pressing for a review of this list in the light of changing circumstances on EU and/or world markets.

3.3 Trade-related issues

While the SA law on the regulation of economic activities is consistent with international practices, SA took a view that provisions on trade-related issues in the bilateral agreement with the EU **should not go beyond the current multilateral** conventions and disciplines agreed in bodies like the WTO, WIPO etc. This is particularly important given SA's commitment on playing an active role in advancing the interests of the developing countries in the multilateral fora. A number of the trade-related issues put on the table by the EU are still subject to intense debates and examination in the multilateral fora. **On issues like government procurement and intellectual property rights** the agreement provides for mechanisms for **further dialogue with the EU.** Generally speaking, commitments that were made were regarded as necessary for the proper functioning of the free trade area. These include:

- **Customs Unions and FTAs**

The agreement provides for consultations to take into account the mutual interests in the event that the maintenance or establishment of CUs or FTAs affect each other's interests. For SA, this provision was regarded as essential for the protection of domestic interests against the change in the balance of rights which may arise from the future enlargement of the EU.

- **Anti-dumping and Countervailing Measures**

The agreement provides for parties to **consider alternatives (constructive remedies)** before imposing definitive anti-dumping duties and counter-vailing duties. This creates an opportunity for the relevant firms to put options for undertaking on price, volume and/or combination of that rather than to face prohibitive duties.

- **Safeguards**

There is a comprehensive provision covering regular, regional and transitional safeguard measures. The **regular safeguard** provides for measures to be taken in the case of **import surges** which threaten or cause injury to domestic producers. This is supplemented by the **non-reciprocal provision** in terms of which **SA will be able to take exceptional measures** to protect infant industries or sectors facing serious difficulties caused by increased imports during the transitional period. There is also provision for measures to be taken to **safeguard any of the other SACU[2] members** against increased imports which threaten or cause serious deterioration in that member's economic situation. The comprehensive safeguard provision is important to ensure that SA and other SACU members can temporarily **protect themselves or slow down the pace** of liberalisation if the impact proves to be more than what SA or the respective SACU member can handle.

- **Used goods**

The exceptions clause provides for the protection of domestic producers against the importation of used goods.

- **Competition Policy**

SA sought to ensure that the provisions do not go beyond those of the new competition policy and law. It provides for consultative mechanisms to attempt to accommodate the interests of each Party with the application of domestic law. It does not regulate the provision of state aid, nor deals with services and government procurement as was proposed by the EU.

- **Public Aid**

The agreed text recognises that it is in both parties' interest to ensure that public aid is granted in a **fair and transparent manner**. It also takes into account the **facilitating role that can be played by state support and involvement in the restructuring** of the SA industry and economy. It thus provides for consultation between the parties to find a satisfactory solution to situations where public aid

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[2] SACU (Southern Africa Customs Union) consists of Botswana, Lesotho, Namibia, South Africa and Swaziland.

distorts fair competition.

♦ **Dispute Settlement**

To ensure that there are **no unnecessary delays** in the resolution of disputes, the agreement sets out **clear disciplines** for the trade chapter. Other disputes on the general provisions of the agreement or for those arising in areas such as Development Cooperation and Economic Cooperation will be governed by a less tight procedure.

4. ECONOMIC COOPERATION

The agreement provides for co-operation in a variety of fields including **industrial restructuring and modernisation, investment promotion and protection, trade development, development of SMMEs, information and communication technology, energy, mining and minerals, transport, tourism, services and consumer protection.**

5. PROTOCOL ON RULES OF ORIGIN

Rules of origin form the backbone of a preferential trade agreement like the one SA is about to sign with the EU. These rules prohibit the deflection of trade and thereby protect the integrity of the agreement. **The protocol will therefore determine the administrative framework of the agreement between SA and the EU.** It prescribes what would count as local content and has the same function as a passport for a human being. The rules determine the ability of economic operators in the contracting parties to reap the rewards of duty-free access to one another's markets. Important features of the protocol include:

♦ **Cumulation**

Cumulation of the rules of origin is an instrument[3] enabling the parties to a free trade area to **use material originating in certain other countries**, i.e. without violating the rules of origin. The protocol provides for **diagonal (or partial) cumulation** between SA and the EU as well as with materials originating in non-SACU ACP countries. As far as SACU is concerned it allows for full cumulation with materials originating in BLNS..

As far as cumulation within the context of the Lomé Convention is concerned - i.e.

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[3] There are basically two types of cumulation, i.e. a) partial or diagonal cumulation; and b) full cumulation. In terms of the former imported material has to meet the rules of origin applicable to that specific intermediate product. In the case of the latter the countries which are allowed to cumulate are treated as a single customs territory which means that whatever value is added in whatever part of the territory will count towards meeting the rules.

trade in the direction SA to all ACP countries to the EU - the EU has undertaken to remove the current ad hoc provision with regard to SA and to replace it with **diagonal cumulation** with SA. This means that ACP countries including BLNS will be able to cumulate with materials which have acquired originating status in SA.

- **List rules**

These are **specific rules for specific products**, based on the tariff nomenclature. This list which is contained in Annex II of the protocol describes the working or processing to be carried out on non-originating materials in order that the final product can obtain originating status. SA's view was that some of these rules did not reflect the level of productive capacity in South Africa. These are 04.03 (cream yoghurt); 09.02 9 (tea); 20.08 (peanut butter); 20.09 (fruit juices); 22.02 (beverages); and 25.25 (mica). This matter is still under consideration by the EU.

- **General value tolerance rule**

Art. 5 allows a certain percentage of the value of the final product to be imported from other countries, notwithstanding the conditions set out in the list rule. The protocol makes provision for a general tolerance of 15%, with the exception of textiles (which will be covered by explanatory notes 5.1 and 6.1), fish, tobacco and alcohol.

- **Prohibition of drawback of, or exemption from, customs duties**

The Commission's proposal contained in Art.14 of their draft protocol specified that non-originating materials used in the manufacture of products destined for the EU or SA market shall not be subject to drawback of or exemption from customs duties. However, it did not preclude the application of the export refund system for agricultural products applicable in the EU.

This proposal was not acceptable to SA and the prohibition on draw-back has therefore been deleted from the protocol.

- **Definition of fishing vessels**

As far as the definition of fishing vessels is concerned, a paragraph has been added at the end of article 4.2 to reflect SA's position on the requirement for officers and masters, subject to the entry into force of tariff concessions on fishery products (which in reality will only be granted if SA is willing to grant the EU access to its fishing waters).

6. Sectoral Agreements

6.1 Fisheries Co-operation

The EU put SA under lot of pressure for a Fisheries Agreement with provision for **access to SA's fishing resources**. It thus made **a linkage** between the Fisheries agreement and the market access concessions as well as the overall agreement.

From the outset SA explained its new fisheries policy and its efforts towards the restructuring of the industry and conservation of fisheries. It emphasised that **access to fishing resources would not be possible**. An agreement regarding the future fisheries co-operation was reached in December 1998. This includes:

- Both sides declared that they will make their **best endeavours** to negotiate and conclude a co-operation agreement no later than the end of the year 2000.

- The EU wants to **hold back** the implementation of tariff concessions to SA on fisheries products. The most sensitive of these concessions are only envisaged in the light of the **content and continuity** of the future fisheries agreement.

- SA will **abolish its tariffs** on fisheries products **in parallel to the elimination** of duties of the corresponding tariff positions by the Community.

6.2 Wines & Spirits

The political compromise on port and sherry which was reached in Davos on 29 January by Minister Erwin and Professor Pinheiro contains the following main elements:

- **Phase out clause** for SA use of names port and sherry in exports to third countries.

- **Definition** of SA domestic market to include all of SACU.

- **SA to continue the use** of names port and sherry on its domestic market throughout the transitional period of 12 years.

- **Review of the use** of names within the transition to decide on the names to use beyond the 12 years.

- SA wine sector to enjoy a **duty free quota** and **financial assistance** for restructuring of the industry.

7. CONCLUSION

The agreement with the EU will, among other things, establish for the next 12 to 15 years SA's trade relationship with its major trading partner and important trading block. The agreement establishes as **good concessions** as each party can get at this point. There is room for improvement within the reviews as set in the

agreement. The agreement reached between Minister Erwin and Commissioner Pinheiro is **the basis** for both Parties to move forward after almost four years of protracted negotiations. It still has to be **formally signed** after which it will be submitted for **ratification by Parliament.** The venue for the signature of the agreement is more than likely to be in SA which would mark the historical agreement between SA and Europe.

25 March 1999

C:\WORK\OFFICIAL\BRIEFING.3

COMPROMISE PACKAGE ON WINES AND SPIRITS

(1) *South Africa reconfirms that the names "port" and "sherry" are not and will not be used for its exports to the EU*

(2) South Africa will phase out the use of the "port" and "sherry" names on all export markets within 5 years, except in the case of non-SACU SADC countries, where an 8 years phase out period would apply.

(3) For the purpose of the Wines and Spirits Agreement, the South African domestic market is defined to cover SACU (*South Africa*, Botswana, Lesotho and Swaziland).

(4) South African products may be marketed as « port » and « sherry » on the South African domestic market during a 12 years transitional period. Beyond that period the new denominations of these products which shall be used on the South African domestic market will be jointly agreed between South Africa and the EU.

(5) From entry into force of the agreement, the EU will provide a duty free quota for wines covering the current level of trade of 32 million litres of South African exports to the EU, with allowance for the future growth of this quota.

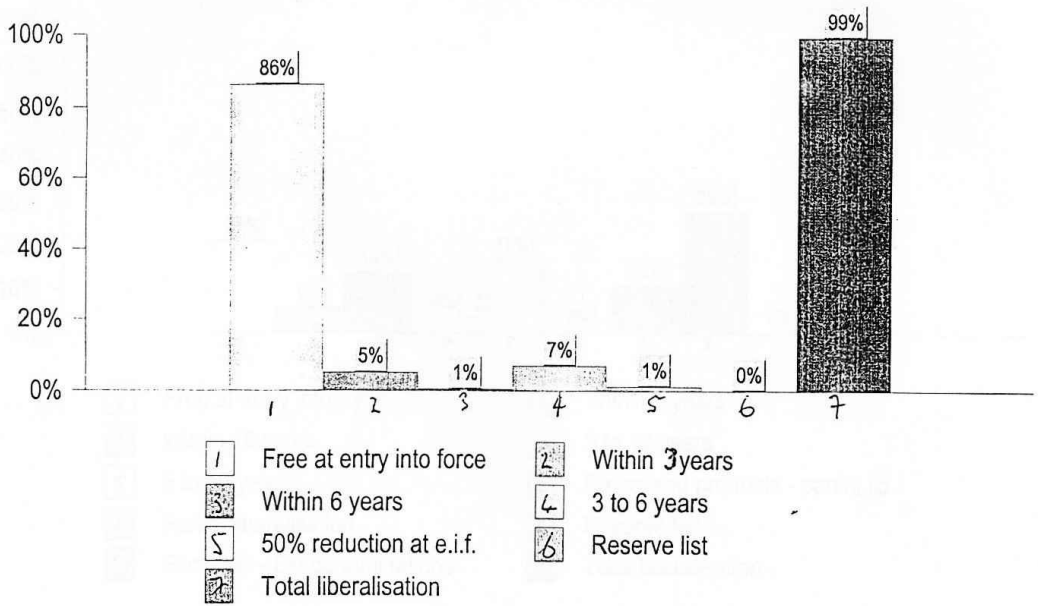
(6) As an additional effort to the main objectives agreed for the Development programme for South Africa to be funded by the EU, the EU will provide assistance of 15 million euro for the restructuring of the SA wines and spirits sector and for the marketing and distribution of SA wines and spirits products. *Such assistance will commence at entry into force of the Wines and Spirits Agreement.*

(7) A Wines and Spirits Agreement between South Africa and the EU will be concluded as soon as possible and no later than in September 1999, in order to ensure that the entry into force of the Wines and Spirits will take place before or in January 2000.

Berlin, 24 March 1999.

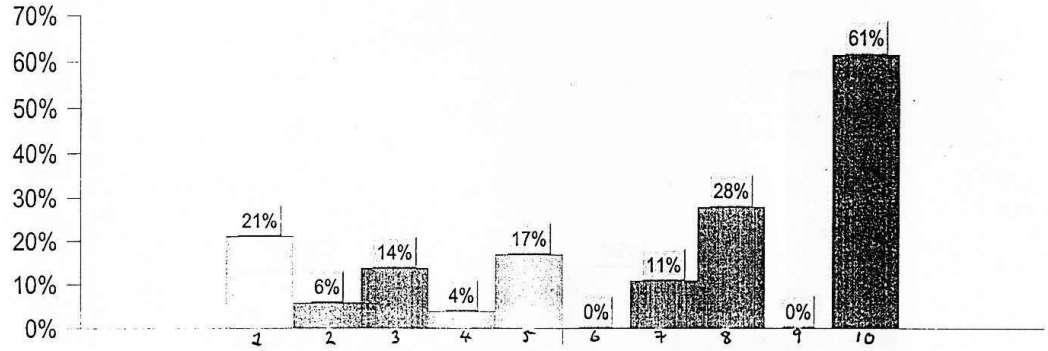
EU LIBERALISATION SCHEDULE

SUMMARY : INDUSTRIAL PRODUCTS



EU LIBERALISATION SCHEDULE

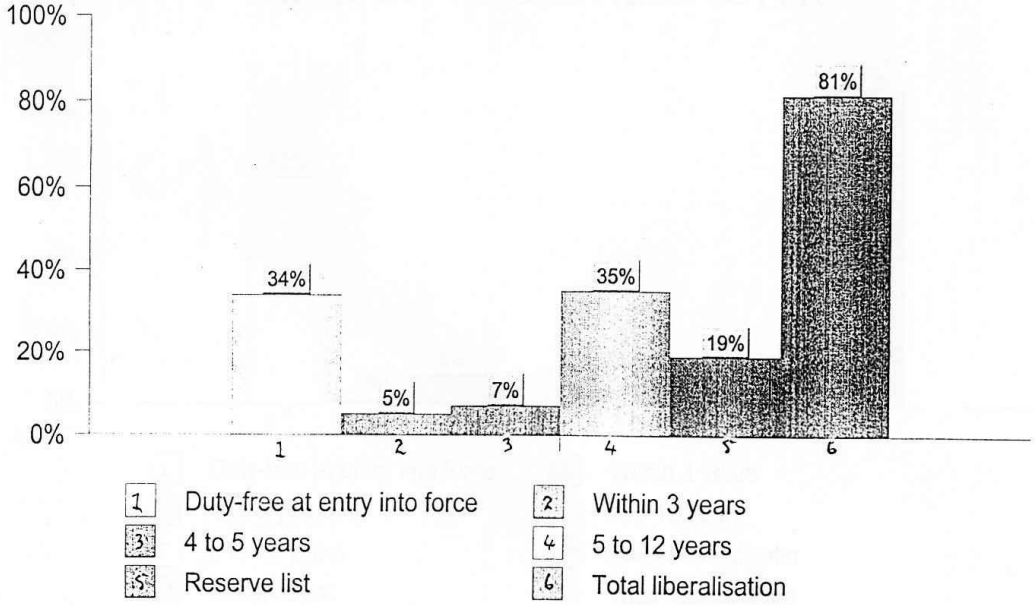
SUMMARY : AGRICULTURAL OFFER



1	Free at entry into force	2	Within 3 years
3	Within 10 years	4	3 to 10 years
5	5 to 10 years	6	Processed products - partial lib.
7	Partial liberalisation	8	Reserve list
9	Excluded - EU denominations	10	Total liberalisation

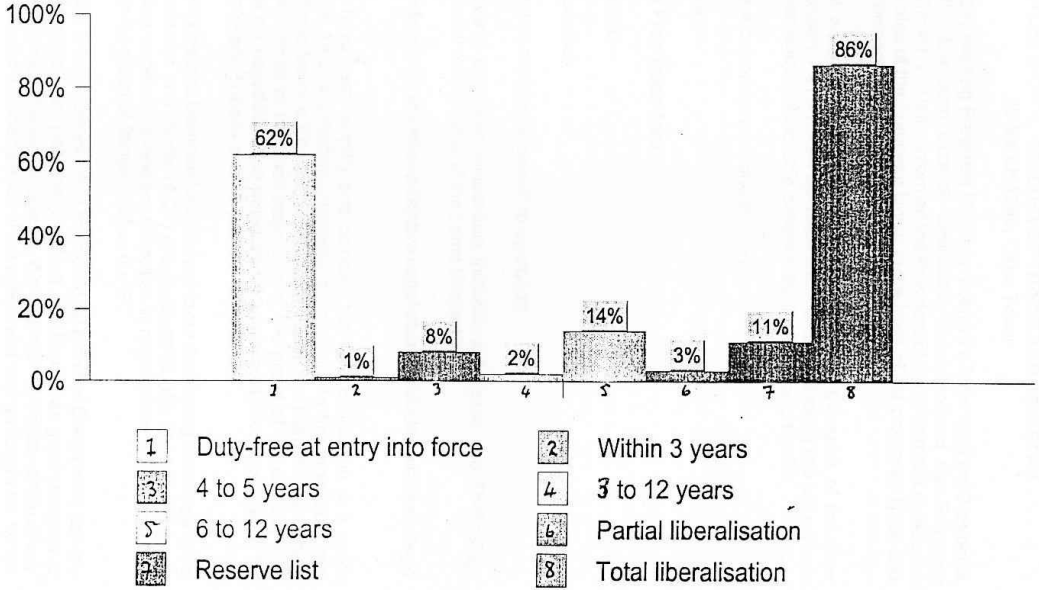
SA LIBERALISATION SCHEDULE

SUMMARY : AGRICULTURAL OFFER



SA LIBERALISATION SCHEDULE

SUMMARY - INDUSTRIAL OFFER



STATEMENT ON THE TRADE, DEVELOPMENT AND CO-OPERATION AGREEMENT BETWEEN SOUTH AFRICA AND THE EUROPEAN UNION BY MR ALEC ERWIN, MINISTER OF TRADE AND INDUSTRY
25 March 1999, Cape Town

Late on Wednesday evening President Mandela received a letter from the Presidents respectively of the European Council, Chancellor Schroder, and the European Commission, Mr Santer. The letter informed the President of the unanimous agreement of the Member States of the European Union to the texts of the proposed Trade and Co-operation Agreement [full text of letter attached].

The Government welcomes this decision and in particular the spirit of the letter conveying the decision. As had been our hope and intention all along this will serve to cement a lasting economic relationship between South Africa and the EU.

The agreement is a comprehensive one covering:

➡Political dialogue

➡Provisions for a Free Trade Area

➡Trade related issues

➡Economic co-operation

➡Financial assistance and development co-operation

In addition the overall economic relationship includes a Science and Technology Agreement and partial membership of the Lome Convention.

The decision therefore ends the most extensive negotiation conducted with a strategic partner to date.

The negotiations have been lengthy and complex but their conclusion is a major milestone in South Africa's unfolding international relations. In the process of the negotiations we have learnt a tremendous amount about the international trading system and the intricacies of the trade negotiations. We proud of the capacity and professionalism of our negotiators and would also like to express our appreciation for the conduct of Professor Pinheiro and his team of negotiators.

Some of the complex lessons learnt will be conveyed to our developing country partners in the African, Carribean and Pacific (ACP) group countries. We hope that this will assist in overcoming some of the inherent difficulties in negotiations with a large and economically powerful group of States such as the EU.

In the final stages of the agreement when the individual Member States were actively involved the negotiations were particularly difficult and there was great pressure to accommodate a wide range of specific interests. We approached this as constructively as possible but in the end it is the balance of the agreement that we fought for. Whilst we made a qualitative concession on the port and sherry issue we retained the intended

degree of openness on the future denominations in the South African markets. In addition we are satisfied that by removing the excessive number of additional interests from the final negotiations we were able to reach a balance that is protective of our objectives.

We welcome the decision as it concludes a very strategic negotiation for South Africa. South Africa took a strategic decision some years ago to bring about major structural changes in its economy. We consciously entered into a free trade agreement negotiation with the EU because we are convinced that it is in our best long term interests to carry out our structural changes in a partnership with our major international trading and investment partner.

There is still much to do to ensure rapid implementation. However, the unanimous decision of the Council should allow us to begin implementation from the beginning of 2000. We will also work to complete a Wine and Spirit agreement before that time. It is a matter of some regret that it will not be this first Parliament that will have the occasion to ratify the agreement. They have done so much to support the negotiations that it would have been appropriate for them to complete the process.

The end of this long negotiation marks a very real achievement for the Government. The hard work of implementation now lies ahead and in this there are challenges for our economy. However, if we meet those challenges with the confidence and tenacity with which we have negotiated the agreement then there is an immense opportunity lying ahead through the world's largest market opening to us.

It is also a real achievement to have gained the extent of access in the agricultural sector. Further access in this sector will now be pursued in the multilateral context as the current EU agricultural policies are an obstacle to development in Africa.

This is an important day for our relations with Europe and we look forward to deepening that relationship. We would like to register our appreciation for the goodwill shown and the support given by countries, peoples and parliaments for South Africa's cause. This played a crucial role in the realisation of this historic agreement.

The member States of the South African Customs Union and of SADC are being fully updated as to the final outcome of the agreement which contains important protective provisions for intra SACU AND SADC trade.

SOME LEGAL ASPECTS OF THE EU-SA AGREEMENT ON TRADE, DEVELOPMENT AND COOPERATION

Clement Ng'ong'ola, LL.M., PhD
Associate Professor
Department of Law
University of Botswana
Private Bag 0022
Gaborone

Workshop on EU-SA Agreement on Trade, Development and Co-operation

July 22 - July 23, 1999

Boipuso Hall, Gaborone, Botswana

SOME LEGAL ASPECTS OF THE AGREEMENT ON TRADE, DEVELOPMENT AND COOPERATION BETWEEN THE EUROPEAN UNION AND SOUTH AFRICA

INTRODUCTION

The EU-SA Agreement is a multi-sided agreement. It covers trade and trade related matters, and cooperation in various fields related to economics, development, finance, science and technology, information technology, human resources, culture and other social issues. Interesting legal questions could be raised and explored on most of these topics, but this brief exploration will be confined to the trade and trade related matters. These aspects of the agreement will be reviewed from the perspective of international trade law, encoded in the Agreement Establishing the World Trade Organisation (WTO) and related instruments. The WTO provides the most likely arena in which the EU-SA Agreement will be exposed to legal challenge and scrutiny. The European Community and South Africa are among the leading members of the WTO. All of South Africa's neighbours likely to be affected by the Agreement are also members of the WTO. WTO law requires the notification and the conduct of conformity assessments for agreements of this nature. Thus, while noting legal and other implications of the Agreement for trade relations within Southern Africa, it must also be evaluated for compliance with WTO rules and disciplines.

WTO RULES ON PREFERENTIAL TRADING ARRANGEMENTS

As is well known, the WTO provides the legal and institutional framework for the conduct of multilateral trade relations amongst its members. It provides the framework for the conduct trade negotiations leading towards liberalisation of trade in goods and services, for the observance of certain disciplines on trade-related intellectual property rights, and for the resolution of trade disputes.[1] One of the cardinal principles of WTO law on trade liberalisation is the requirement for non-discrimination in international commerce. This principle is most evident in the Most-Favoured-Nation (MFN) treatment rule, under which all WTO Members are entitled to equal or non-discriminatory treatment in the application of trade barriers or restrictions in a particular country [.2] Regional or preferential trading arrangements such as that proposed under the EU-SA Agreement inherently contradict the MFN rule and the principle of non-discrimination. They are permitted by way of exception to the rule and principle, if they have the potential for facilitating multilateral trade liberalisation and other objectives of the multilateral trading system.

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1 Art II and II of the Marrakesh Agreement Establishing the WTO

2 Article I:1 of GATT 1947.

The rules or yardsticks by which to assess admissible preferential trading arrangements are better developed or have been applied for a longer period in respect of the regulation of trade in goods. They were elaborated in Article XXIV of the General Agreement on Tariff and Trade (GATT), the main treaty on multilateral trade liberalisation before the establishment of the WTO in 1995, and amplified in one of the WTO texts called GATT 1994. The rules set three main requirements. It must be shown that an agreement proposes the removal of trade barriers in respect of "substantially all trade" between the parties; this must be achieved within a reasonable period; and the agreement must also not have the effect of raising barriers to trade with non-participating countries. The Understanding on the Interpretation of Article XXIV, included in WTO instruments as part of GATT 1994, has suggested that the reasonable period for the elimination of trade barriers should exceed 10 years in exceptional cases calling for special justification. It has also suggested that the likely impact of an agreement on internal and external trade flows must be rigorously assessed in reference actual trade statistics. Beyond these trade liberalisation requirements, emerging WTO practice suggests that other important elements to consider in the conduct of conformity assessments should include the countries involved as parties to the arrangement; the nature or type of trade arrangement proposed; and aspects of the arrangement concerning relations with third parties, rules of origin, dispute settlement and other institutional mechanisms.[3]

ASSESSMENT OF THE EU-SA AGREEMENT

Parties

Some of the intriguing legal questions can be raised in respect of what otherwise would appear to be the most obvious aspects of EU-SA Agreement, such as the parties to the Agreement. The Agreement may have been concluded between the European Union and South Africa, but it directly affects other countries. The European Union is one member of the WTO for some purposes, and as many members as are states within the Union for other purposes.[4] After the completion of the establishment of a common or single European market in 1992,[5] the Union is likely to enter into trade agreements as one entity, but, still, the individual states have sovereign powers to enter into trade related agreements of their own. An added complication is that the size of the European market changes periodically through the admission of new members. This has obvious implications on the extent of legal obligations of parties to trading arrangements with the Union.

Several provisions in the EU-SA Agreement attempt to deal with the complications arising from the nature of the EU as a party to international trade agreements, but perhaps not in a manner that is legally certain. Article 104, for example, indicates that the Agreement shall not affect rights contained in existing agreements between South Africa and Member states of the EC, "except in so far as it creates equivalent or greater rights for the parties involved." This provision does not clarify whether existing Agreements or the newer EU Agreement must prevail in this situation. On accession of new members to the Union, Article 21(2) gives South Africa the right to seek

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3 WTO, Committee on Regional Trading Agreements, Reporting on Regional Trade agreements, WT/REG/6, 11 March 1998.

4 See, for example, Art IX of the WTO Agreement on Decision Making.

5 This was in compliance with two well known legal instruments: the Single European Act of 1985, and the Maastricht Treaty of European Union.

consultations "so as to ensure that account can be taken of the mutual interests of the Community and the Republic of South Africa." But consultations after the event might not lead to proper accommodation of rights and obligations of a party not directly represented during the accession negotiations.

On South Africa's side, the countries directly affected by the conclusion of Agreement are its partners in the Southern African Customs Union (SACU). Because of the adoption in SACU of South Africa's common external tariff (CET) and South African laws and procedures on customs and excise duties,[6] South Africa has effectively renegotiated the external trade relations of all its partners. South Africa under the SACU agreement is required to give its partners "adequate opportunity for consultations" before amending or abrogating its CET and relevant laws.[7] Every member of SACU is also required to seek "the prior concurrence of the other contracting parties" before entering into a trade agreement with a third country that affects SACU rights and obligations.[8] It is a moot point whether these requirements have been observed in the negotiation of the EU-SA Agreement. It is not insignificant that the Final Provisions of the Agreement do not suggest that it is a provisional agreement that will enter into force only after indication of concurrence by South Africa's SACU partners.

The other legal conundrum to be considered in reference to the parties to this Agreement is related to the classification of both South Africa and the EU, or all of its Member states, as developed countries for the WTO purposes.[9] Developing countries and, especially, the least developed among them, are entitled to special and differential treatment in the assumption of WTO obligations. They are entitled to concessions and dispensations that will ensure their integration into the multilateral trading system in a gradual manner, commensurate their capabilities and development needs.[10] Three of South Africa's partners in SACU, Botswana, Namibia and Swaziland, are developing countries. Lesotho, is a least developed country. South Africa as a developed country is generally required to observe and comply fully with WTO rules and disciplines. But can special and differential treatment be claimed for the EU-SA Agreement on the ground that it directly affects the external trade relations of countries entitled to such treatment? If the answer to this question is negative, the EU-SA Agreement could have the incidental effect of abridging some of the legal rights and entitlements of South Africa's SACU partners under the WTO legal framework, and of accelerating their integration into the multilateral trading system.

Nature of the Trading Arrangement and Trade Liberalisation

The Agreement, according to Article 4, proposes the establishment of a Free Trade Area (FTA)

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6 Arts 4 and 8 of the SACU Agreement, 1969.

7 Art 5

8 Art 19(1)

9 The WTO adopts the classification of countries under the UN system for these purposes. South Africa and members of the European Community were classified as developed market economies under the 1997 UN classification.

10 Art XI of the WTO Agreement, and the WTO Ministerial Decision on Measures in Favour of the Least-Developed Countries, 15 December 1993.

between the EU and South Africa. A FTA in WTO terms does not involve the evolution of a CET or common legal position as regards trade with non-participating countries. The extent of liberalisation of trade with non-participating countries is not as critical to the assessment of the arrangement as is trade liberalisation between the constituents. The EU-SA Agreement proposes liberalisation of trade between the constituents in respect of goods and services, as well as free movement of capital. But the commitments on liberalisation of services are tepid and threadbare. The parties have essentially acknowledged the importance of applying the GATS, the main WTO text on services, and agreed to consider further liberalisation of trade between them.[11] These tepid obligations to some extent mirror the nature and manner of multilateral liberalisation of trade in this sector.

The liberalisation of trade in goods is, by way of contrast, more comprehensive. The FTA is supposed to cover goods in all sectors, and to be completed, on part of the EU, within a maximum period of 10 years, and, on South Africa's part, within a maximum period of 12 years.[12] The establishment of the FTA will involve immediate abolition of quantitative restrictions and the phased reduction of tariffs, customs duties of a fiscal nature, and charges having an equivalent effect to customs duties.[13] The Agreement is strangely mute on the identification of the quantitative restrictions to be eliminated upon its entry into force, and more elaborate on the processes for the reduction of tariffs. It lays down different time frames for the elimination of tariffs by the EU and by South Africa, in respect of industrial goods and agricultural products.[14] The basic, broad pattern is that the EU will liberalise trade in industrial goods faster and proceed more cautiously in respect of agricultural products, keeping the most sensitive products out of the arrangement. South Africa will conversely delay the process for most of its industrial products and keep some of the most sensitive sectors for future liberalisation. Through this differentiation South Africa gained more time for its hitherto sheltered industrial sectors to adjust, and the EU will continue to procrastinate in the dismantling of its notorious common agricultural policy and the application of liberal trade disciplines to agricultural trade.[15]

The time frames for the liberalisation of trade in goods were obviously drawn taking into consideration WTO requirements in Article XXIV of GATT 1994. The Agreement, however, has not entirely succeeded in obviating or pre-empting awkward legal questions or queries. First, the differentiation of the time frames for the EU and South Africa invites the comment that this is not a reciprocal process of trade liberalisation. The second cardinal principle of the multilateral trading system, in addition to non-discrimination in international commerce, is reciprocity in the conduct of trade negotiations and the allocation of trade concessions. This is especially required of developed Member states like South Africa. The second query is that the maximum period of 12 years suggested for South Africa is longer than the period of 10 years recommended in the WTO Understanding on the interpretation of Article XXIV as reasonable for the completion trade

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11 Arts 28 to 30

12 Art 4

13 Arts 6 to 8 and 18

14 Articles 9 to 11 for Industrial Goods, and 12 to 17 for Agricultural Products

15 This is supposed to be one of the objectives and achievements of the Uruguay Round of multilateral trade negotiations which concluded belatedly in April 1994 with the addition of an Agreement on Agriculture to the WTO texts and instruments.

liberalisation within regional or preferential trading arrangements. The period of 12 years will require special justification in the assessment of the Agreement by relevant WTO organs. Giving additional time to South African industries more vulnerable to international competition, I dare say, might not be the sufficient justification required for these purposes. Where applicable, relief must be sought under WTO rules and disciplines on Safeguards or Infant Industry Protection for these purposes.

The third issue of concern is whether there will be elimination of trade barriers with respect to "substantially all trade" between the parties at the end of the given periods. This is admittedly a vague parameter, capable of genuinely varying interpretations. The elimination of tariffs in respect of 80 per cent of trade between the parties to an arrangement is suggested by some as the applicable threshold. The parties to this agreement will probably regard this requirement as satisfied by the projected liberalisation of 95 per cent of imports from South Africa to the EC, and by the projected liberalisation of 86 per cent of imports from the EC to South Africa, by the end of the transitional periods.[16] A proper legal assessment will however involve a disaggregation of these percentages, and an assessment of the relative importance to trade between the parties of the products and sectors placed under the derogations and exceptions. On South Africa's side, the shielding of sensitive sectors like automobiles and components, textiles and clothing, red meat, sugar, winter grains and dairy products will be critical. On the side of the EU, the proportion of agricultural trade excluded from the FTA, (46 per cent?), may be far too large. On both sides it should also be appreciated that liberalisation of fisheries and wines and spirits will be completed under separate arrangements. It is thus not a foregone conclusion that the Agreement will satisfy the main requirement for admission of FTAs under WTO rules.

Relations with Third Parties and other Arrangements

This aspect would ordinarily be of critical importance to the assessment of an arrangement with a CET such as a Customs Union. In the case of the FTA under consideration, some brief comments are in order because of the position of the parties to the arrangement. Article 21, partly considered above, indicates that the Agreement shall not preclude "the maintenance or establishment" of CUs, FTAs or other arrangements "except in so far as they alter rights and obligations provided for" in the Agreement. There is some ambiguity here on what should be the fate of existing, contradictory arrangements. What follows in paragraph 2 is merely an obligation to consult on future agreements "establishing or adjusting" CUs or FTAs. Perhaps it is just as well that the revision of SACU and the finalisation of the SADC protocol were not completed before the conclusion of the Agreement. South Africa will in due course be able to comply with this provision and to consult properly on restoration of the balance under the Agreement if this will be necessary.

The second notable provision on trade related issues reflecting on relations with third parties is Article 23, the Safeguard Clause. Paragraph 3 of this Clause empowers South Africa to "exceptionally take surveillance or safeguard measures" at the request a member of SACU where any product is being imported in such quantities and under such conditions as to cause or threaten serious deterioration of the economic situation of that member. This seems to be the only provision

16 Department of Trade and Industry (DTI), RSA, "SA/EU Negotiations, Trade Development and Cooperation Agreement", Briefing Document, 20 February 1999, p 3.

on trade liberalisation that directly addresses the concerns of SACU. If South Africa took proper account of the needs and interests of its SACU partners in the negotiation of the tariff concessions, this was not regarded warranting specific mention in most of the provisions.

The Safeguard Clause in this Agreement will otherwise probably attract attention during WTO conformity assessment because of the "Transitional Safeguard Measures" in Article 24. These are not the regular or standard measures, or the "provisional measures," to be taken in strict compliance with the WTO Agreement on Safeguards. They are special, non-reciprocal measures for the protection of South African infant industries or sectors against import surges from the Union, particularly where trade liberalisation is likely to cause major social problems. The accommodation of social factors in the determination of injury for safeguard purposes is a novelty in trade law. The suggested application of remedial measures with an element of preference for products from the Union is also an innovation that arguably contradicts multilateral trade disciplines.

The Rules of Origin in Protocol 1 provide yet another indication of the relationship between the FTA an another relevant trade arrangement. The Rules in the Agreement generally resemble Rules under the Revised Lome IV trade arrangement between the EU and some African, Caribbean and Pacific (ACP) States. The Rules more specifically emulate the concept of cumulation in the Lome Rules, so that a product made in one of the ACP states with inputs from the EU or from any of the other ACP states may not be denied origin status upon importation into the Union. The rules in the EU-SA Agreement expand on this on this concept. Cumulation is allowed for inputs obtained from South Africa, the EU, SACU countries and from the other ACP States not party to SACU. The main concern here is that the Lome Convention is under review. Partly because of legal challenges in the WTO related to its discriminatory and preferential treatment of some, but not all, developing countries, and the concept of non-reciprocity in trade relations it espouses, its trade provisions are likely to be substantially revised. It is surprising that the EU-SA Agreement refers to aspects of an arrangement that the EU is otherwise seeking to transform.

The third arrangement relevant to the EU-SA Agreement is the Southern African Development Community (SADC) whose trade protocol is awaiting ratification by South Africa, some members of SACU, and other SADC states. The SADC is referred to in the EU-SA Agreement mainly in the provisions on cooperation in economic and other fields. It is not mentioned under trade liberalisation. The SADC Protocol proposes the creation of a FTA for SADC. This is not likely to abridge concessions under the EU- SA Agreement and to trigger the consultative mechanism referred to above. The SADC protocol is moreover tolerant and permissive of existing and future trade arrangements involving parties to it. They will not even be required to apply the MFN rule to concessions secured under pre-existing arrangements.[17]

Institutional Mechanisms

Institutional arrangements, especially on dispute settlement, also contribute to the legal profile of a trading arrangement. Dispute settlement mechanisms that encourage legal certainty and, and at same time, do not pre-empt recourse to the WTO dispute settlement mechanisms, contribute to a more positive rating. The EU-SA Agreement proposes novel institutional arrangements with both

17 Arts 27 and 28 of the SADC Trade Protocol.

negative and positive attributes. It proposes a Cooperation Council, to be constituted and composed, and to operate in a manner to be agreed upon by the parties.[18] This will be the main forum for consultations between the parties on the operation of the Agreement. It will also be the forum to which disputes relating to the interpretation and application the Agreement may be referred for settlement by means of a decision.[19] If the dispute cannot be settled through the implementation of the decision, reference shall be made to a panel of three arbitrators appointed by the parties to the dispute and by the Council. The Agreement does not state that the decision of the arbitrators, to be taken by majority vote, if necessary, shall be binding and enforceable. It prescribes time limits within which the affected party must indicate its intentions as regards implementation of any findings or decisions. It also provides that the party concerned may be afforded a reasonable time to implement the findings or decisions if it is impracticable to do so immediately. We are left to presume that failure to implement findings or decisions could lead to imposition of retaliatory measures or withdrawal of concessions. On the positive side, the Agreement also indicates that this dispute resolution process shall be without prejudice to the right of the parties to have recourse to WTO dispute settlement procedures on pertinent trade and trade related issues. It provides that issues concerning each party's WTO rights and obligations shall not be considered under the arbitration process unless the parties agree to such reference. Other Agreements on regional trading arrangements in Africa could do well to emulate this deference to the WTO process in their dispute settlement arrangements.

CONCLUDING REMARKS

There are many more issues that could be discussed to develop a full legal profile of the EU-SA Agreement. On trade and trade related matters, this brief presentation has not considered provisions on general and specific exceptions to the trade disciplines; standards and technical barriers to trade; sanitary and phytosanitary measures; subsidies, public aid, anti-dumping and countervailing measures; intellectual property rights; public procurement; movement of capital; and competition policy. The basic elements referred to are nevertheless sufficient to indicate that the great care taken to accommodate WTO rules and disciplines in the framing of the Agreement may not pre-empt legal disputes during or after WTO conformity assessment procedures. The Agreement incorporates some elements of doubtful legality on critical issues such as the elimination of tariffs in trade between the parties. In the context of trade relations within Southern Africa, some of its provisions may be vague, but the Agreement would otherwise appear to be legally compatible with arrangements such as SACU and SADC.

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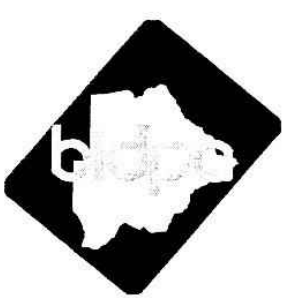
18 Art 96
19 Art 103

16641/1/bulpw

Measures to Protect BLNS industries in the EU-SA Agreement on Trade, Development and Co-operation

Robert Kirk*
Adviser/Consultant
Ministry of Finance
Swaziland

July, 1999



Workshop on EU-SA Agreement on Trade, Development and Co-operation

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* This paper is written in a personal capacity and should not be interpreted as representing the views of the Government of Swaziland.

Introduction

Botswana, Lesotho, Namibia and Swaziland (BLNS) are full members of the Lome Convention, which amongst other things determines their market access to the European Union. They are also members, with South Africa, of the Southern African Customs Union (SACU). They are also all classified as developing countries in terms of both the Lome Convention and the World Trade Organisation (WTO). These three characteristics have played an important role in determining the format of the agreement between South Africa and the European Union.

South Africa approached the EU after the first democratic elections in 1994 and requested improved market access. The EU indicated that it could not offer 'full Lome' access because South Africa's status as a 'developed market economy' within the WTO would require any preferences to be extended on a Most Favoured Nation (MFN) basis. The EU argued that any improved market access for South Africa would have to be compatible with Article XXIV of the GATT (1994)-essentially either a Free Trade Area (FTA) or a Customs Union.

The existence of the SACU, which allows free trade between all the members behind a common external tariff was a major complication for the proposed bilateral between the EU and South Africa. At the beginning of the negotiations there was some talk within SACU of involving the BLNS in the actual negotiations. However, the EU stated that they only had a mandate to negotiate with South Africa. Further, if the BLNS were to participate in the negotiations as individual sovereign states this would raise serious problems regarding their membership obligations under the Lome Convention. It was agreed that both parties (South Africa and the EU) would brief the BLNS before and after each round of negotiations. This process of consultation was followed throughout.

During the negotiations the BLNS raised a number of concerns. These included:

- Possible increased competition within SACU for products produced by the BLNS arising from increased imports from the EU.

- The need for rules of origin within a Free Trade Area to prevent countries from importing through the country with the lowest duty.

- The likely decline in tariff revenue to the SACU and the consequent reduction in SACU revenues to the BLNS.

In the remainder of the paper I focus on the safeguard provisions for the BLNS and the significance of the rules of origin for the BLNS.

Safeguard Provisions

Almost every international trade agreement contains safeguard provisions. The EU-SA agreement is no exception. The term 'safeguard protection' refers to a provision in a trade agreement permitting governments under specified circumstances to withdraw - or cease to apply- their normal obligations under the agreement in order to protect (safeguard) certain overriding interests. Safeguard provisions are critical to the existence and operation of trade liberalisation agreements as they function as both insurance mechanisms and safety valves. The GATT contains a series of safeguard provisions that allow for the temporary suspension of duties and provides the framework for the specific safeguards within the EU-SA agreement.

The safeguard provisions in the EU-SA agreement are contained in Articles 22 – 25. Article 22 makes explicit reference to Article VI of the GATT 1994, which sets down the conditions for taking anti-dumping or countervailing measures. Under the EU-SA Agreement both parties can take action in terms the GATT 1994. However, in the strict sense these measures would only apply to the contracting parties, namely South Africa and the EU, however the BLNS through their membership of the SACU share a common market with South Africa.

Article 23 paragraph 3 explicitly addresses this issue

Where any product is being imported in such quantities and under such conditions as to cause or threaten to cause serious deterioration in the economic situation of one or more of the other Members of the Southern African Customs Union, South Africa, at the request of the country or countries concerned, and after having examined alternative solutions, may exceptionally take surveillance or safeguard measures in accordance with the procedures laid down in Article 25.

Thus in terms of the EU-SA agreement the BLNS will be able to request that action is taken if they experience a sudden 'loss of market share' for their industries in the SACU as a consequence of increased imports from the EU. This safeguard is necessary because under the existing agreement (i.e. Lome) market access is non-reciprocal and South Africa is excluded from the trade provisions, so the machinery for addressing these problems is not present, and under the EU-SA agreement the BLNS are non contracting parties. It is also important to recognise the disparity in size and economic development within SACU. By allowing for each country to specify 'serious deterioration' the small size of the BLNS compared to South Africa is taken into account. Put another way, a small decline in market share to South Africa arising from increased imports from the EU would be unlikely to qualify as grounds for action on the basis of 'causing a serious deterioration in the economic situation'. However, a decline of the same absolute amount affecting BLNS would have a much larger impact because of the different relative size of the industrial sectors.

Article 23 allows South Africa to take action and implement Safeguards at the request of the BLNS. Any action must be taken in terms of the Safeguard Procedures set down in Article 25. These procedures apply to all Safeguard actions taken in terms of the EU-SA Agreement. Requests for safeguards are referred to the Co-operation Council –a joint body charged with managing the agreement (Article 96)- and if no agreement is reached within 30 days the importing country may impose safeguard measures for up to 3 years. Provision is made for immediate action to be taken in 'exceptional circumstances' (Article 25 5(b)).

Some commentators have argued that the safeguards for the BLNS are not adequate. They consider the BLNS should have the automatic right to impose safeguards. It would be very unusual to grant non-signatories to an agreement automatic rights to suspend certain aspects of the agreement. The BLNS have to request safeguards through South Africa-this would seem logical given the existence of the SACU and any requests for safeguards have to originate from a contracting party, however, it could create a potential problem if South Africa disagreed with the request from the BLNS. In such a situation the disagreement would become an internal SACU issue. This would seem to be correct although, the mechanisms for addressing such disputes within SACU are still under review. The conclusion of the SACU re-negotiations should be a priority for all the parties since improved co-ordination and a more efficient institutional structure within SACU will minimise disputes between the parties.

Rules of Origin

Rules of Origin are necessary within FTAs since member countries retain their own outside tariffs. Ignoring internal transport costs, this feature opens the possibility that a product destined to a high tariff member country will first be imported into the lowest tariff member country and then re-exported to the former. Or put another way, if inputs imported from outside countries (i.e. Rest of the World) constitute a large part of the value added of a product, producers on the member country with the lowest tariffs on inputs can undercut producers in other countries. Rules of origin are necessary to prevent these possibilities from being realised.

The key issue on the Rules of Origin for the BLNS relates to the principle of cumulation and the determination of whether an export to the EU is eligible for Lome preferences or EU-SAFTA terms.

The Rules of Origin under the EU-SA Agreement are based on the Lome Rules however, there is a substantial difference (in principle). Under the Lome Rules origin is essentially defined through Change of Tariff Heading (CTH) which is supplemented in a number of cases with processing requirements, However, under the EU-SA Agreement originating status is met through meeting the processing requirements under each tariff heading. In many cases the processing requirements listed under the EU-SA Agreement are identical to a CTH, however, in some cases they appear to be more onerous. On balance the Rules of Origin under the EU-SA Agreement are certainly no less onerous than under Lome.

The rules of origin for the application of tariff preferences in terms of the EU-SA Agreement are set down in Protocol 1.

Cumulation allows for processes carried out in a number of countries to be added together in the final processing country for the purposes of meeting the Rules of Origin. Thus under the Lome Convention the ACP are treated as a single unit. This means that it is not necessary for intra-ACP exports to have been sufficiently processed to merit originating status. An ACP state can imports inputs from other ACP states, (none of which by themselves have achieved originating status) providing that when the good is exported to the EU the combined processing undertaken in all of the ACP states is sufficient to justify originating status. This combined processing is referred to as cumulation.

In terms of the EU-SA Agreement **diagonal cumulation** is permitted. This allows for full cumulation on BLNS inputs into South African exports to the EU (Protocol 1 Article 3 paragraph 4). This provision states

Any working or processing carried out within SACU shall be considered as having been carried out in South Africa, when further worked or processed there.

This is satisfactory since it is to be expected that South Africa, as the more developed economy, will more frequently utilise BLNS components as inputs into a final product, rather than the vice versa. This full cumulation reduces the administrative costs of complying with the rules of origin.

BLNS exports to the EU are governed by the rules of origin under the Lome Convention which, as noted above allow for full cumulation within the ACP. With the accession of South Africa to the Lome Agreement provision was made for ad hoc cumulation with South African inputs. The ad hoc provision creates uncertainty for investors in the BLNS and has been a cause of complaint by SACU members. During the final stages of the negotiations between SA and the EU the EU agreed to modify this requirement under the Lome to permit full cumulation between South Africa and the BLNS (and other ACP states). This amendment provides for full cumulation within the SACU.

The new rules of origin will have an impact on the BLNS vis a vis South Africa. On the one hand, the improved market access of South Africa will reduce the incentive for investors to locate in the BLNS to obtain Lome preferences. However, this is mitigated by the fact that the BLNS are likely to retain better market access to the EU than will be available to South Africa, although on the vast majority of tariff lines access will be the same. On the other hand, the provision for full cumulation within SACU on exports from South Africa could stimulate BLNS production for inputs to South Africa for export to the EU under the EU-SA Agreement.

The agreement on the rules of origin will tend to favour intra-regional processing since it permits both BLNS inputs into South African exports and South African inputs into BLNS exports. In so far as the rules of origin under Lome are more generous by requiring less processing this would tend to give the BLNS a competitive advantage over South

Africa as a location for production. However, the differences identified by the consultants (IDS BIPDA, Impact Study, p.29) appear to be marginal and would therefore be unlikely to have a significant impact.

Summary and Conclusion

The agreement to establish a Free Trade Area between South Africa and the European Union will have a major impact on the BLNS as members of the SACU. It will create additional opportunities for the region as well as creating adjustment costs. The paper has a very narrow focus on the specific safeguard measures contained within the EU-SA Agreement for the BLNS.

The safeguard provisions are considered to be satisfactory since they make explicit reference to the BLNS. The rules of origin also recognise the position of the BLNS as part of an internal SACU market including South Africa and permit full cumulation.

The existence of adequate safeguards represents a positive starting point for implementing the agreement. The next step is for the BLNS as partners within SACU to co-operate in ensuring the successful implementation of the agreement. To this end the BLNS, in partnership with both South Africa and the EU, are developing a research agenda to anticipate the likely adjustment costs. This will result in the development of a programme aimed at enabling the BLNS to maximize the benefits arising from the new trading regime.

EU-SA Agreement on Trade, Development and Co-operation:

Options for Industry Restructuring

Keith R. Jefferis
Senior Research Fellow
BIDPA

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Introduction

1. The implementation of the EU-SA FTA will lead to significant changes in the competitive environment in Southern Africa, affecting both the South Africa and the BLNS countries. This is an unavoidable consequence of economic interdependence in southern Africa, and will apply despite the fact that only South Africa is a signatory to the agreement, while the BLNS countries are not.

2. The main changes in the competitive environment will be:

   - greater competition within SACU, due to imports from the EU that were previously subject to tariffs now coming in duty-free; this will affect BLNS firms exporting to South Africa (now faced with EU competition), as well as BLNS firms selling into their domestic markets, where it will in practice be impossible to keep out EU products imported duty-free into SA, even though this is not technically allowed under the EU-SAFTA and SACU agreements;
   - greater competition within Europe for export products of BLNS firms, which will now potentially be subject to greater competition from similar SA export products that can now enter the EU duty free (BLNS products have had duty-free access to the EU under Lome)

3. The impact will be quite uneven across industrial sectors. Some products already enter SACU duty-free from the EU, and for these there will effectively be no change in the competitive environment. Similarly for BLNS exports to the EU where similar SA exports are not at present subject to tariffs. Obviously, the industry sectors that will be most seriously affected are those that are at present subject to the highest levels of tariff protection.

4. The IDS/BIDPA study of the effects of the EU-SAFTA agreement showed that overall, there was unlikely to be a substantial negative impact on the BLNS industrial sectors – by far the largest potentially negative impact would be through reduced revenue sharing under SACU. However, as the overall impact would not be evenly spread, some sectors would suffer adverse consequences. These included the following:

(i) Products that are currently exported to the EU by both BLNS and SA, where the former currently have superior access terms that will be eroded as a result of the EU-SAFTA. Trade and tariff analysis indicates that these are:

   - preserved fish
   - grapefruit
   - grapes
   - processed pineapples
   - clothing

   Company interviews indicate that problems are not expected in all of these sectors, as in some cases the SA and BLNS firms sell to different sub-sectors within the trade categories.

(ii) Products made by BLNS where (potential) EU exports to SACU are suppressed by high SACU tariffs. These include items in the following broad product categories:

- Fish
- vegetable oils
- chemicals
- rubber articles
- textiles
- footwear
- glass
- vehicles
- fresh fruit and vegetables
- meat preparations
- plastics
- leather goods
- clothing
- ceramics
- iron and steel

5. It should be noted that these are broad commodity groups and not all products within each category will be affected in the same way. Furthermore, some of the above (textiles, clothing and vehicles) will be governed by special protocols which encompass much slower liberalisation (tariff reduction) schedules than will be generally applicable.

6. Products that were specifically mentioned during interviews with firms as likely to have major problems competing with duty-free EU imports in South Africa include the following:

Botswana: denim & polyester cloth, clothing, pasta & biscuits, cars
Swaziland: refrigerators
Lesotho: televisions, umbrellas
Namibia: wheat flour, meat

7. Although the overall impact on SACU industrial sectors is likely to be small, in those specific sectors where firms are vulnerable some major adjustments will be necessary. But even for firms that are not directly affected, to any great extent, the FTA does mark a potentially significant change in the overall competitive environment, especially in the medium to long term, to which they will have to respond.

8. In broad terms, firms will have to adjust by shifting production towards activities in which they are internationally competitive on the basis of price and quality, and away from those where they can only compete on the basis of protection and subsidies.

9. It is also important to note that the changes that will result from the implementation of the EU-SA FTA will not be taking place in isolation. At the beginning of the next decade, other important changes in the regional and international trade environments are likely to include the implementation of the SADC Trade Protocol (leading to a SADC FTA), the winding down of the Multi-Fibre Agreement governing world trade in textiles and garments (and which restricts competition from the very efficient Asian producers), the replacement of the Lome Convention, as well as any other trade agreements that may be negotiated under the tentative WTO "Millennium Round". For BLNS the most relevant of these is the SADC FTA, and the

discussion below covers industry restructuring that will be needed in the face of both the EU-SA FTA and the proposed SADC FTA.

10. One of the implications of the broader process of trade liberalisation in the region will be that a general relocation of industry within Southern Africa is likely. South Africa has some industries that, within the context of a region without trade barriers, probably should not be located there – obvious examples are labour intensive industries or ones that are intensive in their use of basic agricultural products. Without subsidies or protection, these industries can be more profitably located in other southern African countries.

11. Trade liberalisation in southern Africa will only work if this relocation is allowed to take place unhindered. One of the first effects of a SADC FTA will probably be a shift in regional trade balances in South Africa's favour – the smaller, protected, inefficient producers in some countries will not be able to compete with South Africa's larger firms once trade barriers come down (Zambia's experience over the past decade is a good example of this). If the smaller countries of SADC are to have gains from liberalisation that will offset these losses, it is essential that South Africa (in particular) does not restrict the relocation of its firms to other SADC countries.

Options for Industry Restructuring

12. We can therefore identify three processes that will be taking place within southern Africa as a result of trade liberalisation:

    (A) the relocation of some industries within southern Africa;

    (B) the opening up of new market opportunities within the EU (for SA firms) and within SADC (for firms of all SADC countries).

    (C) the exposure of many industries to greater regional and international competition;

13. In general, we note that it is possible to respond to these changes in both positive and negative ways; the former includes restructuring industries so as to be able to compete, while the latter includes resorting to unsustainable subsidies and protection.

14. What kind of policy measures will facilitate positive restructuring in response to the above, in a way that will work in the long term in the best interests of the region as a whole? Below, some suggestions are listed as to how firms and governments can respond.

15. Under (A) above, this relocation must be facilitated and not restricted. This means that trade liberalisation must also encompass capital market liberalisation, and South Africa must remove any exchange controls that inhibit capital movements within the region. Other countries should value inward investment, and support it with the necessary infrastructure – power supplies, transport links, communications etc.

16. Under (B), firms need to embrace new market opportunities as existing market opportunities change or disappear. This requires market research, gathering information about prices, quality standards, distribution channels, and securing

trading partners. While large firms may be in a position to go it alone in this area, small and medium sized firms may not. And because there are lots of externalities in information gathering and sharing, there is an argument for government involvement in meeting at least part of the costs of such efforts.

17. Under (C), restructuring for competitiveness, the challenges are greatest. The main problems that firms will face in meeting higher competitiveness standards include:

- low levels of labour skills and productivity;
- outdated technology and equipment;
- being too small – lacking economies of scale;
- regulatory burdens that impose unnecessary extra costs.

18. Possible responses to these problems include:

- investment in training, including on-the-job training
- investment in new technology
- consolidation of small firms into larger units, where economies of scale exist

19. It is also important to note that not all firms will be able to successfully adapt to the new environment. Almost inevitably, some will go under. This will add to the need for training, to improve the opportunities for retrenched workers to find new employment or self-employment.

20. An urgent priority is to identify which firms or industries do have good long term potential. The research for the BIDPA/IDS study did draw conclusions about the long-term prospects for some firms, but this was not based on a widespread survey. Much more broadly based surveys are therefore necessary in the BLNS countries to evaluate whether the relatively comforting conclusions of the BIDPA/IDS study are applicable to the productive sector as a whole.

21. Many firms will face the same kinds of problems – most obviously, firms in a particular industry will have common problems and hence a common approach to evaluating what the competitiveness problems are, and what kind of response can be made, makes sense. Here, industry groups or associations have a key role to play in identifying common problems facing firms in their sector.

22. We can therefore identify the following components of an industry restructuring programme:

- identification of the long-term prospects of a broad range of industries as the competitive environment changes;
- identification of the type of restructuring that is necessary to achieve this long term competitiveness;
- market research and development of marketing capacity
- skills training
- investment, upgrading of technology
- achieving competitive firm sizes

23. Besides being dependent upon their own efficiency, the long term potential of firms in SACU and SADC to compete with EU firms is also dependent upon policies within the EU. One area that has proved contentious is the extent to which EU firms are subsidised; research for the BIDPA/IDS study showed that several BLNS firms believe that they could compete with unsubsidised EU firms, but that in practice EU subsidies make it very difficult to compete. In general, the EU has made significant progress towards prohibiting subsidies that distort competition, but this does not apply to the area of agricultural products. Some SACU firms that operate in areas with agricultural products as inputs (meat, other foodstuffs) may have problems competing. SACU (and SADC) governments should therefore consider evaluating the extent to which EU subsidies (especially those under the Common Agricultural Policy) do distort competition. Perhaps the WTO would be an appropriate channel to take up grievances arising from this source.

24. Finally, it is worth noting that funds may be available from the EU under the EU-SAFTA, or from other sources, to address some of the issues that have been raised here. Article 65 of the Agreement states that:

> The areas of development co-operation will mainly concern the following:
>
> (a) support for . . . . regional co-operation and integration. In this context, special attention will be given to providing support to the adjustment efforts occasioned in the region by the establishment of the free-trade area under this Agreement, especially in the SACU.

25. Furthermore, Article 93 states that:

> Financial assistance in the form of grants shall be covered by:
>
> (a) a special financial facility established under the Community budget, in support of the development co-operation activities referred to in Articles 64 and 65.
>
> (b) other financial resources made available from other Community budget lines for development and international co-operation activities falling within the scope of those budget lines.

Under (b), financial assistance may be available under Article 12 of the Lome Convention.

26. It should therefore be possible to secure financial assistance from the EU from some of the restructuring activities listed under paragraph 22 above. However, it will be important for BLNS firms and governments to organise themselves in good time to secure these funds and ensure that they are spread around the region. South African firms will themselves be making use of these funds to help take advantage of their new opportunities for accessing the EU market; BLNS firms must do the same if they are not to get left behind.

Implication on BLNS based on the BIDPA-IDS study

(Excerpts from Executive Summary of IDS BIDPA study)

Jan Isaksen
Executive Director
BIDPA

July, 1999

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1. Purpose and approach of the study

In order to provide a comprehensive picture of the range of EU–SAFTA effects, and following the requirements of the ToR, the study utilised several different methodologies, making use of existing models and adapting them where necessary to the task in hand. The main potential effects investigated were:

- greater competition for BLNS exports to the EU from South African products;
- greater competition for BLNS products in the SACU market from EU products;
- a loss of customs revenue;
- indirect effects arising from changes to the South African economy;
- indirect effects on the flow of investment to BLNS.

Most of these effects were found to be small, with the exception of the large loss of customs revenue.

This range of effects were captured through four main methodologies:

- a detailed analysis of trade and tariff data;
- a survey of some of the BLNS firms that might be affected by the EU SAFTA, to identify their expectations of its likely impact;
- a commodity flow model designed to identify other effects on production and employment in BLNS, and the potential revenue implications of the EU-SAFTA;
- a set of simulations using a computable general equilibrium (CGE) model of the South African economy

The analysis was undertaken in the knowledge that concurrent events are moving BLNS in broadly the same direction as would an EU–SAFTA, i.e. towards lower levels of tariff protection resulting both in changes to competitive conditions in the SACU market and in lower levels of revenue from trade taxes. These concurrent events include the renegotiation of SACU, the negotiation of a post-Lomé relationship with the EU, the ratification and implementation of the SADC Trade Protocol, and the anticipated next Round of WTO negotiations. The combination of events considered most realistic in this study (a view supported during consultation on the Inception Report) is that progress will be made on all of these concurrent events. This would tend to minimise the marginal additional adjustment required as a result of the EU–SAFTA, although it also increases the absolute level of adjustment that will be required (to all of the changes) and, hence, the urgency with which BLNS governments need to address these issues. At the same time, the sections of the report describing the results of each set of analyses are presented in such a way as to enable the implications to be assessed of alternative assumptions concerning concurrent liberalisation.

2. The findings

2.1 Results of the trade and tariff analysis

BLNS exporters to the EU may face increased competition as a result of the EU–SAFTA since it will improve the access terms for South African exporters. In the short term, this change in competitive conditions will apply only to products which are exported by both BLNS and South Africa and for which the former currently have superior access terms that will be eroded as a result of the EU–SAFTA. From the trade statistics it appears that the product groups relevant to BLNS most likely to be affected by the EU–SAFTA are:

- preserved fish (especially frozen hake);
- grapefruit;
- grapes;
- processed pineapples;
- clothing.

The company interviews indicated that problems are not expected for all of these, partly because South African and BLNS firms sell to different sub-markets within the trade categories. This underlines the importance of assessing the results of the different methodologies in parallel.

A wide range of EU exports will face significantly reduced SACU tariffs as a result of the EU–SAFTA and, in addition, it is likely that Europe will begin to export some items in which it is internationally competitive but which have been suffocated by the existing high SACU protective barriers. This latter group includes items in the following broad product categories: fish, fresh fruit and vegetables, vegetable oils, meat preparations, chemicals, plastics, rubber articles, leather goods, textiles, clothing, footwear, ceramics, glass, iron and steel, and vehicles.
The rules of origin that the EU proposes to determine the eligibility of South African exports for EU–SAFTA tariff rates are substantially different from those incorporated into the Lomé Convention. However, the analysis of the study is that in relation to the products of current export interest to BLNS, the rules are broadly similar although those for South Africa appear to be somewhat less liberal in particular cases.
The EU's cumulation proposals appear to be unduly complex and potentially disruptive to trade. They act against the primary objective of a customs union by increasing cross-border formalities. They are also less favourable than those under Lomé.

2.2 Results from the commodity flow model

The direct EU–SAFTA impact is unlikely to be very significant for any of the BLNS countries except in the case of customs revenues and for a minority of companies that will be unable to compete. Any significant impact, including the revenue impact, is likely to work mainly through the South African economy. If the latter is boosted by the introduction of the EU–SAFTA the positive effect of this may be much greater than any direct negative impact on BLNS.
The severity of the revenue effect varies between BLNS states. Botswana, which depends least on SACU revenue and has the most comfortable budget position, will be affected the least. Swaziland, which also has a relatively comfortable budget situation, will be more severely affected and so will not be able to afford to ignore the loss of revenue arising from the EU–SAFTA. Both Lesotho and Namibia already have budget deficits that are large in relation to GDP, and will also tend to be strongly affected adversely by the fall in SACU revenue.
Increasing the rates for existing taxes does not appear to be a feasible solution to the revenue problem. Rather, the study indicates that a more far-reaching review of both revenue and expenditure will be necessary.

2.3 Results from the survey of firms

Only a minority of firms would be affected by the EU–SAFTA and, in most cases, only for some of their products. In other words, while there will be adjustment problems, and pain in particular cases, the BLNS states are not facing the prospect of substantial 'de-industrialisation'. However, this finding does depend critically upon the survey undertaken being representative of BLNS producers as a whole. It is strongly recommended that the BLNS governments undertake, as a matter of priority, more comprehensive surveys than were possible within the parameters of this study.
The survey has also found only a limited number of cases in which cheaper imported inputs would make BLNS firms more competitive. This is primarily because relatively few companies import recurrent inputs from the EU and a majority of those imports already enter SACU tariff free.
The survey also asked firms about their investment intentions. None stated that it would relocate to South Africa as a result of the EU–SAFTA

2.4 Country-specific results

For each country, the study gives results on the potential areas of direct trade competition, on the modelled effects of the EU-SAFTA on prices, the trade balance, key economic variables and main sectors.

More detailed information is given on the firm interviews. This identifies specific firms that may be adversely affected. Among the most notable cases are:

- In Botswana, a large company assembling cars stated that it would definitely not be able to compete in the SACU market without protection.
- In Lesotho, two companies expressed serious concern about the threat of EU competition: one produces high-quality television sets and the other umbrellas.
- In Namibia, two companies exporting to the EU expressed concern about increased competition in the European market: one in relation to its by-products (canned meat, ostrich and game meat) and the other in relation to its main product, frozen hake. Three companies would also have problems in competing on the SACU market for some, but not all, of their output. The products concerned are milk, meat and wheat flour.
- In Swaziland three companies stated that they would not be able to compete with tariff-free EU imports. The largest is a manufacturer of refrigerators. In addition, fears were expressed in relation to imports of beef and of glacé cherries.

2.5 Results of the CGE modelling

The set of five simulations undertaken using a CGE model of the South African economy has emphasised the importance of other macro-economic policies in determining the net impact of the EU–SAFTA. The simulated effects of the tariff changes *per se* are consistent with those of the commodity flow model in that the impact on both GDP and employment is positive. However, the model also takes into account the impact of other policies, which may produce effects operating in the opposite direction. Thus, for example, if the government of South Africa's fiscal policy stance requires it to reduce expenditure in line with the fall in trade taxes, this would tend to have a negative effect on growth in GDP and employment.

3. Recommendations

Recommendations have been made in three areas:

- those specifically concerning details of the EU–SAFTA negotiations;
- those for broader action by BLNS;
- and those concerning third parties.

3.1 The EU–SAFTA negotiations

3.1.1 Protocols

It is recommended that BLNS engage as a matter of urgency with South Africa to determine the latter's intentions with regard to the products it has proposed be placed in protocols under the EU–SAFTA.

3.1.2 Other items

BLNS governments should identify an optimum strategy for the adjustment of these sub-sectors and seek to give effect to this by influencing the details of the EU–SAFTA negotiations.

3.1.3 Rules of origin

It is recommended that BLNS seek to ensure that this subject is given due consideration, with their involvement. The most satisfactory arrangement is full cumulation, particularly given the uncertainty over the successor to Lomé.

3.2 Broader policy recommendations

3.2.1 Taxation

BLNS governments should undertake fundamental reviews of their tax systems, with an emphasis on establishing independent revenue authorities with salary structures and incentive systems designed to increase sharply the efficiency of revenue collection.

3.2.2 Public sector management and expenditure

Since the problems of adjustment to the decline in trade taxes are likely to be severe, it is recommended that the BLNS governments also review public sector management with particular emphasis to privatisation.

3.2.3 Uncompetitive firms

BLNS governments should undertake extensive company surveys to verify the likely impact but it is not recommended that governments offer assistance to firms with no prospect of becoming competitive but assists workers made redundant by the loss of protection, to train for other employment or to become self-employed.

3.2.4 Investment

BLNS governments should try to establish co-operation between the South African government and the investment promotion bodies that exist in each of the BLNS countries to alert potential investors to the possibilities of investing in all parts of SACU.

3.3 Recommendations concerning third parties

The EU–SAFTA will pose adjustment problems for BLNS that are additional to those addressed by current aid programmes. It is appropriate to raise with foreign donors the question of supplementary support for specific purposes. It is recommended that foreign assistance be considered for:

- a detailed survey of the revenue options available to BLNS in view of the likely decline in trade taxes;
- the design and implementation of new tax systems, and the design and setting up of independent tax authorities;
- technical assistance for the implementation of any new system and the associated training required;
- capital assistance (for example to establish information systems) in order to make a new system operational;
- a review of public sector management and the identification of possible areas for commercialisation and privatisation;
- detailed technical assistance for the privatisation of public enterprises and commercialisation of government services selected for this process by governments following the review;
- an extensive survey of firms in each BLNS country to confirm or reject the picture presented in this report that most of them will be either unaffected or able to compete as a result of the EU–SAFTA.

- technical assistance to design economically and socially desirable support packages to mitigate the adverse consequences of failure on the employees of a small number of firms if the surveys confirm the results of this study.
- capacity building in trade policy analysis in BLNS: this might start with meetings between BLNS at the technical level to consider improvement in the database and models to update the present study when final (or near final) negotiation results are available.

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Botswana Institute for Development Policy Analysis

Workshop on EU-SA Agreement on Trade, Development and Co-operation

July 22 - July 23, 1999: Boipuso Hall, Gaborone, Botswana

On March 24, 1999 the European Union (EU) Heads of State and Governments approved the "Trade, Development and Co-operation Agreement" between the EU and the Republic of South Africa (RSA). The agreement amongst other things. Provides for the establishment of a bilateral free trade area (FTA) between the EU and the RSA; the strengthening of European development assistance to South Africa and a series of undertakings which open the way for intensified co-operation in the political and social fields.

South Africa believes that the FTA with the EU will contribute towards restructuring of the South African economy by securing preferential market access for South African products in the EU market and attracting EU investment into the South African economy. This is expected to lead to economic growth and a growing South African economy will in turn facilitate intra-regional economic trade and investment flows which will spill over to the other southern African countries. South Africa believes that regional economic co-operation will advance a broad and integrated process of industrialization and modernization in the economy of southern Africa.

The Agreement has several implications to the other members of the Southern African Customs Union, the BLNS states (Botswana, Lesotho, Namibia and Swaziland) and the SADC region in general. Although the BLNS governments no doubt will have individually analyzed the effects of the Agreement, the discussion between government and private sectors as well as between the countries, are lagging behind. BIDPA's initiative of a regional workshop, with partial support from the **Friedrich Ebert Foundation** and the **EU**, aims at making a start at an in-depth analysis of the Agreement and its implications. The workshop should form a basis for exchange of viewpoints and ideas between governments of the BLNS as well as the private sectors. One particularly important task is to identify restructuring programs based on information on the sectors most likely to be affected.

Objectives

The workshop has the following objectives:

- To provide an in-depth analysis of the different components of the Agreement.
- To analyze the implications of the Agreement to the BLNS states and the SADC region.
- To identify the restructuring programs based on the sectors most likely to be effected.
- To get a better understanding of the different safeguard measures in the Agreement and how they are going to operate.
- To get a better understanding of the rules of origin.
- To get a better understanding of how the proposed technical, material and financial assistance can be accessed.

Topics to be covered

- A review of the Agreement
- A review of the scope for the FTA
- Implications of the agreement to BLNS
- Implications of the agreement to SADC
- Implications for the Lome Agreement
- Identifying the scope for restructuring

Faculty

The South African chief negotiator during the negotiations, senior researchers at BIDPA, regional trade experts, and EU experts will conduct the workshop.

Participants

The workshop will be of special interest to senior staff in Ministries responsible for Trade, Commerce, Finance and Agriculture, the private sector and state owned companies.