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South African Trade Policy and the Future Global Trading Environment

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ABSTRACT

This paper puts forward a strategic view of what South African trade policy should be doing in relation to the future global trading environment. The future is uncertain, but if the past is prologue, South African trade policy needs to be positioned for a continuation of the commodity cycle, and to exploit markets in emerging economies, including Africa, more fully. Simultaneously, it needs policies to spur labour-intensive services and manufacturing exports, both because these will be needed if commodity markets are less robust and because of their employment creating potential. South Africa's current strategy, however, is inflexible, heavily focused on domestic concerns and has the danger of placing South African exporters at a disadvantage in accessing the growing emerging economies. It also gives rise to an inherent tension between the interests of South Africa and the African region in trade negotiations. Having as the central tenet of trade policy a commitment to deal with tariffs on a case-by-case basis will not serve South Africa well in the global economy that is likely to emerge over the next fifteen years. A simpler tariff structure would facilitate the conclusion of free trade agreements and actually make industrial policy more effective.

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ABBREVIATIONS AND ACRONYMS

APTA	Asia–Pacific Trade Agreement
ASEAN	Association of Southeast Asian Nations
BRIC	Brazil, Russia, India and China
BRICS	Brazil, Russia, India, China and South Africa
COMESA	Common Market for Eastern and Southern Africa
CU	Customs Union
EAC	East African Community
EFTA	European Free Trade Association
FDI	foreign direct investment
FTA	free trade agreement
G-20	Group of Twenty
GDP	gross domestic product
GSP	Generalised System of Preferences
GSTP	Global System of Trade Preferences among Developing Countries
IMF	International Monetary Fund
Mercosur	Southern Common Market (Mercado Común del sur)
MFN	most favoured nation
OECD	Organisation for Economic Co-operation and Development
PSA	Partial Scope Agreement.
RTA	regional trade agreement
SACU	South African Customs Union
SADC	Southern African Development Community
SSA	sub-Saharan Africa
TFTA	Tripartite Free Trade Agreement
the dti	Department of Trade and Industry
TPSF	Trade Policy and Strategy Framework
TRAINS	Trade Analysis and Information System
UNCTAD	UN Conference on Trade and Development
WTO	World Trade Organization

INTRODUCTION

Trade policy has a key role to play in South Africa's growth strategy. If it is to meet the aspirations of its people for higher incomes and increased employment opportunities, the South African economy needs to expand at an average rate of at least 6% a year. If this happens, the demand for imports of intermediate inputs, capital equipment and finished goods is likely to grow at double-digit levels.¹ In the short run, increased foreign borrowing may be able to finance this demand but there are limits to the size of the resulting current account deficit that can be sustained. Over the long run, therefore, the growth in exports will have to accelerate.² Achieving the required export expansion poses a considerable challenge. Growth in the volume of goods and services exported prior to the start of the financial crisis in 2008 averaged only 3.9% per year (2000–07), which is why, despite booming commodity prices, the current account deficit rose strongly over the period.

Trade is also especially important in creating jobs for unskilled and semi-skilled workers – the central goal of the South African Economic Development Department's New Growth Path policy framework.³ Tradable sectors such as agriculture, mining, manufacturing and tourism employ such workers more intensively than most services sectors.⁴ Growth in the tradable sectors is therefore likely to play an important role in meeting the New Growth Path's objective of raising the employment-intensity of output growth.

In addition to helping meet the external constraint and providing jobs, trade can also raise living standards and promote growth. South African firms and consumers gain from imports through lower prices and a greater variety of goods and services. Exporters achieve economies of scale and the increased competition due to trade can spur innovation and productivity growth.

At the same time, however, there may be reasons to constrain some imports: trade protection may be warranted to provide safeguard protection, especially for vulnerable labour-intensive domestic industries and to provide targeted infant industry protection for industries to achieve long-run competitiveness. In addition, selective government procurement might be used to leverage domestic production capabilities.

Given trade's importance, it is appropriate to consider if South Africa's current trade policy strategy is well crafted for the external environment and the domestic economic challenges it is likely to face. Trade policy has external and internal dimensions that are interrelated. The external dimension provides opportunities for promoting the market access of South African exports of goods and services, and the domestic dimension opportunities for implementing policies that complement domestic industrial and other policies to promote growth and job creation. Since foreign barriers are often reduced reciprocally in trade negotiations there are, at times, trade-offs between these dimensions. One key challenge is to find the correct balance between preserving adequate space for domestic policy while at the same time obtaining reciprocal market opening. A second is enhancing export opportunities that can assist in achieving domestic goals – especially, in South Africa's case, employment creation.

This paper puts forward a strategic view of what South Africa should be doing in relation to the trade agenda. The approach followed is to first outline some important features of the global trading environment and how these may evolve in the future. We

then consider whether South Africa's current trade strategy is positioned to take advantage of the features of this environment and propose alternative strategies.

THE FUTURE GLOBAL TRADING ENVIRONMENT

The future is uncertain. It is tempting to assume the past is prologue and to extrapolate the trends that have dominated the past decade. Indeed, that is precisely what many of the forecasts by the multilateral institutions are prone to do. But the one thing we can be sure of is that although these trends are bound to be influential, we will also be surprised.

The 'consensus' view of the future suggests an environment for trade policy that has six distinguishing features.

Global growth divergence

The first feature of the global trading environment has been the shift in the locus of global growth and the expansion in trade and investment from industrialised to emerging economies that occurred over the past decade. Whereas in the 1980s and 1990s developing and industrialised countries on average grew at the same pace, from 2000 developing economy growth increased strongly, led by the BRIC (Brazil, Russia, India and China) economies. By contrast, performance of the developed countries from 2000 was quite tepid – less than 2% per year. Consequently, the share of emerging economies in world gross domestic product (GDP) on a purchasing power parity basis rose from 20% in 2000 to 35% in 2011 and predictions are that this share will reach close to 60% by 2020.⁵

Global patterns of investment and trade flows are expected to mimic these shifts in the composition of global GDP. For example, the BRICs share in global outbound foreign direct investment (FDI) increased from 1–2% in the late 1990s to over 5% by the late 2000s.⁶ The composition of this investment is also changing. Although much of the outbound FDI has been destined for relatively advanced countries (for example, the purchase of the UK's Jaguar by the Indian company, TATA; China's Lenovo acquisition of IBM), South–South investment has also increased.

Lesser-developed countries, including Africa, have been among the beneficiaries of this surge in FDI.⁷ FDI flows from the BRICs to least-developed countries reached about \$2.2 billion in 2009 (2–3% of total FDI flows from BRICs), with countries from sub-Saharan Africa (SSA) receiving \$0.9 billion (41% of total). Chinese FDI to least-developed countries rose from 5.7% of its total outbound FDI in 2003 to close to 10% in 2009.⁸

The share of emerging economies in international trade grew even faster reflecting the trade-intensive growth path of the dominant emerging economies. In 2000 the BRICs accounted for 7.2% of world exports. By the third quarter of 2010, this share had risen to 18%.⁹ These trends are predicted to continue.

Global imbalances

The second feature that will shape the future global trading environment is the unwinding of global trade imbalances. Global economic growth over the past decade was associated with the emergence of large and unsustainable trade imbalances. Boosted by buoyant

equity and property markets, low interest rates, and 'creative' financing practices – that turned out to be disastrous – consumers in the US borrowed and spent more than their incomes. This led the US to generate very large current account deficits financed heavily by foreign central banks that accumulated large holdings of dollar reserves. By 2008 the US deficit on goods and services had reached 4.9% of US GDP (see Table 1). Although the EU as a whole has been in surplus, similar divisions remain between the surplus countries such as Germany, the Netherlands and deficit countries mainly in Eastern and Southern Europe and the UK.

Table 1: External balance on goods and services (% of GDP)

	1980	1990	2000	2008
External balance goods & services				
High income: OECD^a	-1.3	-0.6	-0.8	-1.3
US	-0.5	-1.3	-3.9	-4.9
EU	-2.3	-0.5	0.3	0.7
Japan	-0.9	0.9	1.5	0.1
Low & middle income	-2.2	-0.3	1.5	1.1
Brazil	-2.3	1.2	-1.8	0.2
China	-0.4	3.0	2.4	7.7
India	-3.1	-1.4	-0.9	-5.4
Russian Federation		0.2	20.0	9.2
South Africa	8.0	5.5	3.0	-3.0
sub-Saharan Africa (developing only)	1.2	0.9	1.6	-2.8

a OECD denotes Organisation for Economic Cooperation and Development.

Source: World Bank, 'World Development Indicators', <http://data.worldbank.org/data-catalog/world-development-indicators>, accessed 18 January 2011.

Developing countries in Asia and elsewhere represented the other side of the coin. Asians kept their exchange rates weak and accumulated reserves. In China, extremely high domestic saving rates by both households and corporations supported investment and an export-led dynamic that featured high profit shares, and declining shares of wages and consumption in GDP. The outcome was rapid growth in exports of goods and services as a share of GDP (16% to 35% from 1990–2008), combined with slower growth in imports (13% to 27% of GDP from 1990–2008) and a rising trade surplus that reached 7.7% of its GDP in 2008 (from 3% in 1990).¹⁰

The rebalancing of global trade flows will require shifts in global production and expenditure by both developed and emerging economies. In the medium term the need for fiscal consolidation in numerous developed countries will constrain both public and private expenditures. This implies that the advanced economies are unlikely to provide markets for developing countries that are expanding as rapidly as they did in the past. This

will represent a major change from the experience of the past decade in which developing country growth, especially in Asia, was based on servicing developed country markets. These markets will still be large, but developing countries that seek to increase their exports to developed countries will have to do so by displacing other importers rather than domestic firms. By contrast, population growth, urbanisation and income growth in emerging markets will generate a growing number of middle-class consumers with substantial aggregate buying power.

On the production side, the focus of global competition in manufacturing will shift in Asian markets from production to serve consumers in advanced economies to production for supplying the growing middle class in their own economies and in other emerging economies. The re-orientation in the largest player, China, from export and investment led growth to domestic consumption led growth, should be eased by a gradual real appreciation of the Chinese yuan and rising wages.¹¹

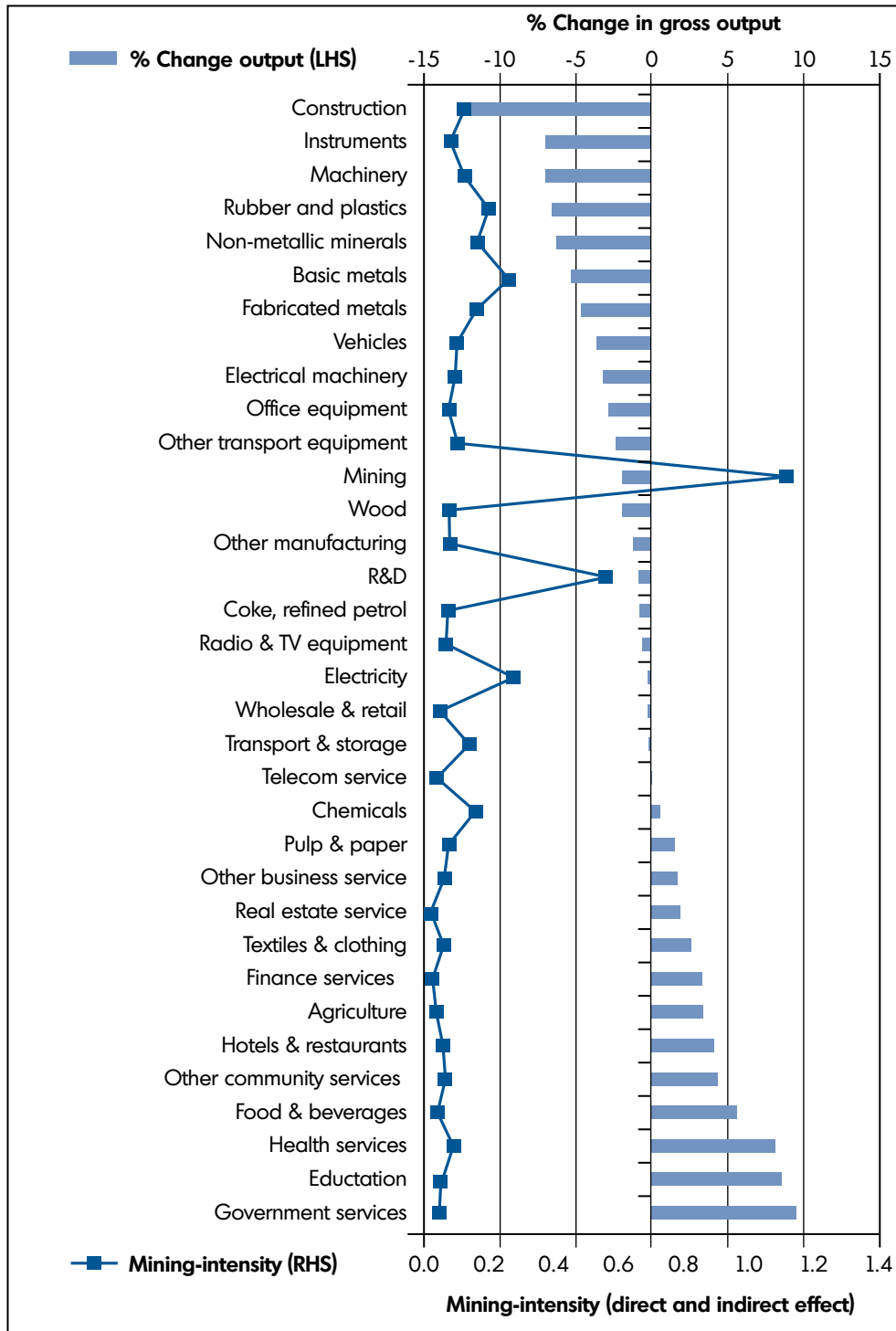
The composition of Chinese GDP is also expected to change, leading to new opportunities and challenges for other emerging economies such as South Africa. As Chinese consumption increases and savings fall, investment expenditure will decline relative to consumption expenditure. Chinese consumption patterns are far more oriented towards agricultural and food products (21% of consumption) and services (63% including government services), whereas investment expenditure is made up predominantly of construction (53%) and machinery and equipment, including electrical machinery (27%).¹²

Consequently, increases in the consumption-intensity of Chinese expenditure can be expected to raise relative demand for services (health, education, government services), agriculture, and food and beverages and reduce the relative demand for construction, machinery and equipment, and various mining- and resource-intensive products including basic metals, fabricated metal products and non-metallic minerals. These structural shifts are illustrated in Figure 1, which shows estimated changes in Chinese output (final and intermediate demand including imports) by sector, arising from a re-orientation of current final expenditure from investment towards consumption. The simulation assumes a ZAR¹³ 120 billion increase in domestic consumption (just under a 10% increase) combined with an equivalent reduction in investment expenditure – total GDP therefore does not change.

The re-orientation of export production towards supplying the domestic market is also expected to have profound effects on the composition of Chinese production. The export and import profiles are far more oriented towards heavy industry than household consumption patterns. Re-orientation of the export sector towards supplying the domestic market can therefore be expected to reduce the industry-intensity of Chinese GDP.

The re-orientation of the Chinese economy towards increased domestic consumption is also expected to have an impact on commodity prices and the geographic location of manufacturing production.

Figure 1: Structural shifts in output associated with re-orientation of Chinese demand towards domestic consumption



Note: The percent change in demand includes direct and indirect effects as well as imports.

Source: Authors' own calculations using Input–Output for China (late 2000s) obtained from OECD, 'Structural Analysis Database', <http://www.oecd.org/sti/industryandglobalisation/stanstructuralanalysis-database.htm>.

Commodity prices

The third feature deals with future growth in commodity prices. Emerging economy growth is highly commodity-intensive.¹⁴ The effect of high investment rates and industry-intensive production, both of which are commodity- and energy-intensive, in developing countries can be seen in their voracious demand for metals and other primary commodities. China, for example, contributed one-third of global growth over the past few years, but accounted for almost 60% of the increased demand for metals and other primary commodities and 20-40% of the increase in oil.¹⁵ The consequence of this increased demand was strong increases in the price of commodities from 2000–07: threefold increases in metal prices, a doubling of food and beverage prices and increases in coal prices and iron-ore prices, both major South African exports, by multiples of five to seven.¹⁶ Commodity prices plummeted during the financial crisis of 2008, but prices have recovered and in many cases now exceed pre-crisis levels. The increases in iron-ore prices, for example, have been exceptional: nearly a threefold increase from 2008 to March 2011.

Looking to the future, supply constraints will contribute towards sustained price pressure. The challenge of supply meeting demand for some commodities is a result of the depletion of current reserves at a time when replenishment is becoming increasingly difficult. For most commodities, primary reserves are not located in the same places that generate most of the demand. Additionally, many known reserves slated for future exploration are located in developing regions where the political climate may be unstable and a lack of infrastructure may pose challenges for extraction, processing and transportation.

On the demand side, continued high economic growth together with the increased population growth, urbanisation and industrialisation of emerging economies is expected to sustain high levels of demand for commodities. Chinese growth, for example, is expected to decline moderately from the very high levels of the mid-2000s, but is still predicted to remain above 8% in the near future, which will sustain demand pressures on commodities. In the long run, however, the demand for commodities will attenuate as Chinese growth moderates further and the commodity-intensity of its growth path declines as it pursues a more consumption-intensive growth path. For example, our estimates in Figure 1 suggest that a 10% re-orientation of Chinese final expenditure from investment towards consumption reduces the mining intensity of GDP by 4%.¹⁷ Demand for other mining- and resource-intensive products (basic metals, fabricated metal products and non-metallic minerals) also decline substantially. Finally, emerging countries are increasingly seeking to retain more commodity value-addition at home, which will further reduce the industrial and pollution intensity of Chinese growth.

Global supply chains

The fourth feature is the centrality in manufacturing trade of global supply chains in which developed and developing countries occupy different parts of the production process. Lower transport costs, rapid improvements in information and communication technology and the proliferation of trade agreements have enabled the splitting up of industry's value chains into smaller components that can be performed by foreign subsidiaries or independent suppliers located in different countries across the globe. Multinational firms and their FDIs have been central to the emergence of these production networks.¹⁸ China's

exports provide a vivid example: The most dynamic component of their exports consists of the processing and assembly of imported components by foreign-owned firms in export processing zones – these firms account for almost 60% of Chinese exports. The import content of these exports typically ranges from 40–50%, but exceeds 80% for the high-technology electronic products.¹⁹

An iconic example of this is the iPod.²⁰ Although the full value is counted as an import from China, only \$4 of the landed US price of \$180 is attributed to China where the assembly takes place (by a Taiwanese-owned firm). The hard drive, display assembly and battery pack are sourced from Japan, the SDRAM from Korea and the video processor, flash memory and controller chip from the US. The emergence of production networks therefore enables firms to specialise in a limited part of the production chain.

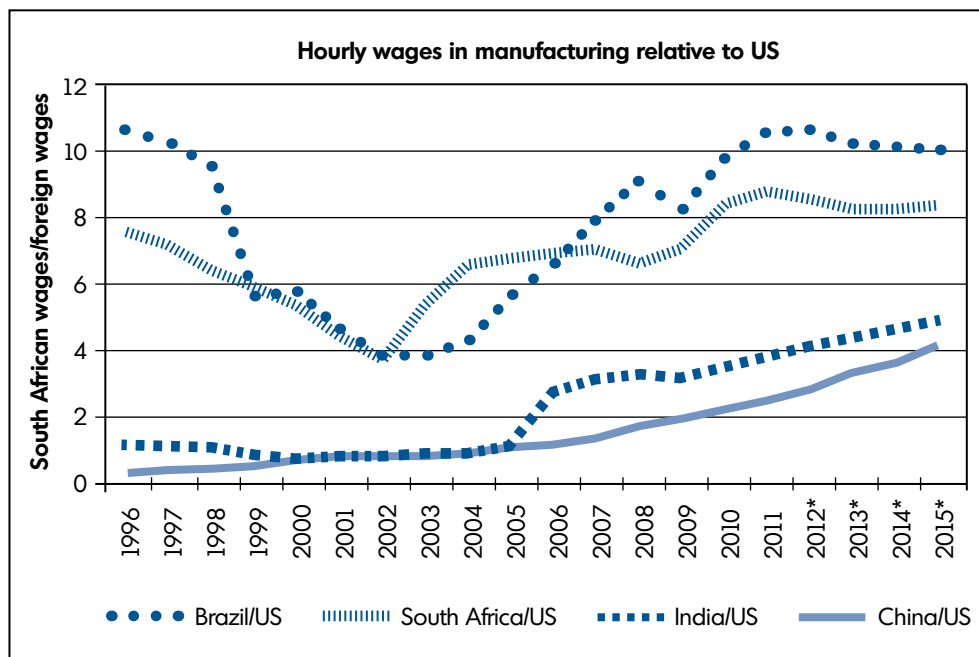
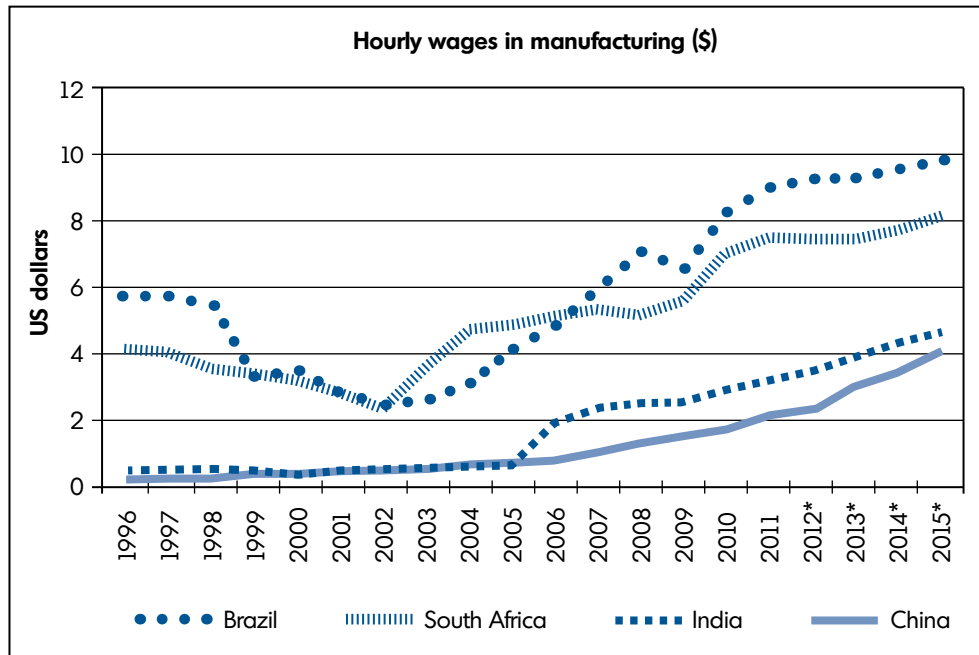
Technological change combined with increased global integration has also increased the scope for product differentiation in global markets, even in the same detailed product categories. This has enabled firms from both developed and developing countries to differentiate their products and occupy different market niches.²¹ The scope for product differentiation is actually greatest in the so-called sophisticated or higher value-added products.²² This helps explain the phenomenal emerging economy growth in exports of these 'traditionally' developed-country products – emerging economies specialised in the export of low-priced, low-quality varieties.

These developments in manufacturing have two important implications for trade and industrial policy. Firstly, the target for intervention is no longer the product – it is the production process or stage of the value chain. Secondly, differences in the scope for quality variation, production techniques including technology requirements, and market demand characteristics are often greater for varieties within a particular product (or sector) category than between products (or sectors). These developments pose challenges to policymakers who wish to engage in sectoral-level targeting of policy.

The global fragmentation of production is set to continue and affect new products. For example, lower transport costs and improvements in telecommunications have opened up the traditionally 'non-traded' services sector to international trade in the form of outsourcing. India epitomises this development with its rapid growth in exports of services.²³ The low end has seen the explosion of business process outsourcing services such as call centres and data entry. At the high end, India has become increasingly involved in software. By 2008 ICT services exports made up slightly over 50% of all India's services exports.²⁴

Further, the rebalancing of global trade discussed earlier will require a re-orientation of Asian supply from export markets towards supplying the local market. An important component of the shift towards increasing domestic consumption involves reversing the astounding decline in wages. For example, in the 2011–15 five-year plan issued by the National People's Congress of China in 2011 it was announced that minimum wages would *increase* by 13% yearly. Chinese wages have already been rising quite rapidly – the average hourly wage in manufacturing more than doubled in the four years from 2006 from \$0.9 per hour to \$1.9 per hour (see Figure 2). Indian manufacturing wages have also increased dramatically over the past decade. These trends are expected to continue – the Economist Intelligence Unit, for example, predicts that Chinese and Indian manufacturing wages will double further to over \$4 per hour by 2015. These expected increases far exceed those in developed countries (the US) as well as in Brazil and South Africa (Figure 2).

Figure 2: Comparison of hourly wages in manufacturing, including forecasts to 2015



Source: Economist Intelligence Unit, <http://www.eiu.com>, accessed 18 January 2011.

If China can reduce domestic saving, it will be in a better position to allow the yuan to strengthen without causing unemployment and/or deflation. Thus in addition to higher wages in terms of domestic currency, additional changes in global competitiveness will occur as a result of currency appreciation. Those firms that seek to remain in China will

have to respond by increasing production for the domestic market and/or by upgrading and moving into higher-unit value products. This will create new opportunities for other countries to enter into the assembly stage of global supply chains. The upgrading of products, however, will also increase competitive pressures in medium-tech manufactured goods.

Global trading system

The fifth feature of the consensus view is that the multilateral trading system will remain open, but regional and bilateral arrangements will play a major role in driving trade flows. Economic growth has changed the global balance of power in trade negotiations. At Cancun in 2003, it became clear that the developed countries (the US and the EU) could no longer dictate the terms of the agreement – indeed the World Trade Organization (WTO) has been at the frontier of multipolar governance later apparent by the Group of Twenty (G-20). This has given rise to two important developments: an impasse in Doha, and the rise of regionalism.

The impasse in the Doha Round is, in part, because the negotiations were overtaken by the events described above. The Round's focus has been on establishing a system that better meets the needs of developing countries, especially in agriculture. Yet high food prices and shortages heightened concerns about food security and made liberalisation more difficult. Developing countries such as India have placed a special emphasis on safeguards. The climate for liberalisation soured especially in the US, in which polls revealed a widespread scepticism about the benefits of trade agreements that the US had signed in the past.²⁵ At the multilateral level, the dispute settlement system has nonetheless flourished and has been used increasingly to deal with disputes by developing countries, both between one another and with developed countries.

Yet regionalism has flourished (see Box 1). As countries have competed to attract the foreign investors that will integrate them into global supply chains, they have sought to improve market access for their goods and services by obtaining better than most favoured nation (MFN) treatment through free trade agreements (FTAs). Consequently, regional trade agreements (RTAs) have proliferated since the Uruguay Round was concluded, rising from around 10 in 1992 to over 200 by 2009 (120 agreements covering goods, one agreement covering services and 81 agreements covering goods and services).²⁶

Box 1: Regional Trade Agreements

China and India have been active participants in concluding FTAs. India has been a tough negotiator in the Doha Round, holding up agreement to preserve special safeguards in agriculture, for example. But it has been moving decisively to reduce its tariffs unilaterally far below their WTO bound rates as well as signing extensive FTAs with Korea, Japan, and the Association of Southeast Asian Nations (ASEAN), all of which will remove 90% of all tariffs on goods within 10 years (Table 2).²⁷

Table 2: RTAs for BRICS

List of notified RTAs in force	Details of agreement	Type of agreement	List of RTAs for which an early announcement has been made
China			
ASEAN ^a -China	Goods (January 2005), Services (July 2007)	PSA ^b	Costa Rica-China
Asia-Pacific Trade Agreement (APTA)	Goods (June 1976)	PSA	Australia-China
APTA-Accession of China	Goods (January 2002)	PSA	China-Norway
Chile-China	Goods (October 2006), Services (August 2010)	FTA	
China-Hong Kong, China	Goods & Services (1 January 2004)	FTA	
China-Macau, China	Goods & Services (1 January 2004)	FTA	
China-New Zealand	Goods & Services (1 October 2008)	FTA	
China-Singapore	Goods & Services (1 January 2009)	FTA	
Pakistan-China	Goods (1 July 2007), Services (10 October 2009)	FTA	
Peru-China	Goods & Services (1 March 2010)	FTA	
India	Date of entry into force		
ASEAN-India	Goods (1 January 2010)	FTA	BIMSTEC ^c
APTA	Goods (17 June 1976)	PSA	EC-India
APTA-Accession of China		PSA	EFTA ^d -India
Chile-India	Goods (17 August 2007)	PSA	India-SACU
Global System of Trade Preferences among Developing Countries (GSTP)	Goods (19 April 1989)	PSA	Japan-India
India-Afghanistan	Goods (13 May 2003)	PSA	
India-Bhutan	Goods (29 July 2006)	FTA	
India-Nepal	Goods (27 October 2009)	PSA	
India-Singapore	Goods & Services (1 August 2005)	FTA	
India-Sri Lanka	Goods (15 December 2001)	FTA	
Korea-Republic of India	Goods & Services (1 January 2010)	FTA	

List of notified RTAs in force	Details of agreement	Type of agreement	List of RTAs for which an early announcement has been made
Southern Common Market (Mercosur) –India	Goods (1 June 2009)	PSA	
South Asian FTA	Goods (1 January 2006)	FTA	
South Asian Preferential Trade Arrangement	Goods (7 December 1995)	PSA	
Brazil			
GSTP	Goods (19 April 1989)	PSA	
Latin American Integration Association	Goods (18 March 1981)	PSA	
Mercosur–India	Goods (1 June 2009)	PSA	
Protocol on Trade Negotiations	Goods (11 February 1973)	PSA	
Mercosur	Goods (29 November 1991), Services (7 December 2005)	CU ^e	
South Africa			
EC–South Africa	Goods (1 January 2000)	FTA	India–SACU
EFTA–SACU	Goods (1 May 2008)	FTA	
Southern African Customs Union (SACU)		CU	
Southern African Development Community (SADC)	Goods (1 September 2000)	FTA	

- a ASEAN includes Indonesia, Thailand, Malaysia, Singapore, Brunei, the Philippines, Cambodia, Laos, Myanmar and Vietnam.
- b PSA denotes Partial Scope Agreement.
- c BIMSTEC: Bay of Bengal Initiative on Multi-Sectoral Technical and Economic Cooperation.
- d EFTA denotes European Free Trade Association.
- e CU denotes Customs Union.

Source: Author's own construction using data obtained from WTO, <http://www.wto.org>, accessed 8 February 2011.

China's approach to FTAs has been very pragmatic. It has shown a willingness to negotiate with countries individually and in groups (eg ASEAN and recent discussions between South Korea, China and Japan) with developed (New Zealand and Australia) and developing countries and with those that are heavily specialised in agriculture (New Zealand and Australia), manufactured goods (ASEAN and South

Korea) and services (Hong Kong). It has been focused on East Asia but also quite willing to deal with countries in Latin America, South Asia, and Africa. It has sought to signal that its interests are global.

Chinese agreements have not followed a single template. Some have included goods, services, investment and co-operation (eg Hong Kong, Macau); others cover only goods (eg Chile); while some have started with goods liberalisation, adding services later (eg FTA with ASEAN on goods in January 2005 and services in July 2007). The deepest agreements thus far are with Hong Kong and Macau, although even these do not cover issues that are part and parcel of agreements that are typically signed by the US (eg intellectual property, labour and environment, government procurement, dispute settlement by panels) or the EU (eg competition policy).

Brazil has generally not followed the same FTA approach as its two Asian BRIC counterparts. With major concerns about farm subsidies they have been especially interested in a successful Doha Round, but their regional agreements and those they have concluded thus far with India have tended to follow a more selective approach.²⁸ They have tended to be more aspirational and political. Brazil's trade agreements with China are similar and are aimed at boosting trade and energy co-operation between the two states. Typically these agreements are confined to sectors in which each side feels comfortable, combined with expressions of goodwill and pledges of enhanced co-operation rather than extensive liberalisation. Brazil's agreement with China, for example, includes a pact to build a Chinese steel plant in Brazil.²⁹

Asian economies are using trade agreements to eliminate regional barriers and enhance production networks. A strategic priority of Asian economies has been the elimination of trade and other barriers between them. The objective of these agreements is to facilitate the development of regional production networks, but also improve market access into those countries that impose relatively high tariff barriers compared with developed economies.

Singapore, for example, is intent on becoming a hub that can provide firms that locate there with preferential access to almost every global market and hence has negotiated an extensive range of trade agreements across the globe. In the recently enacted FTA between China and ASEAN (which came into force on 1 January 2010), the six richest ASEAN members (Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore and Thailand) eliminated remaining tariffs and barriers to investment on 90% of products. The poorest four ASEAN members, Vietnam, Cambodia, Laos and Myanmar, will not need to cut tariffs to the same levels till 2015. By 2015 duties must also be cut to no more than 50% on the hitherto 'highly sensitive' items, including ambulances in Brunei, popcorn in Indonesia, snowboard boots in Thailand and toilet paper in China.³⁰

Japan, a major source of FDI into the region, was a latecomer to this process, but has been signing FTAs with abandon.³¹ It has concluded separate agreements with Malaysia, Indonesia, the Philippines, Singapore, Thailand, Vietnam, Mexico, Chile and Switzerland and is currently negotiating agreements with the Republic of Korea, Australia and India. With the noteworthy exception of agriculture in which

Japan still protects its rice farmers, these agreements are also typically deep, covering investment and services.

There is no question that these agreements have many exceptions. In addition they do not necessarily take care effectively of numerous non-tariff barriers, but they are a striking reflection of the major efforts that governments in Asia are taking to eliminate the trade barriers between them.

Given the length of time the current Doha negotiations have taken, it seems certain that any agreement will set the rules of the game for the multilateral system for the foreseeable future. If concluded, this agreement is likely to achieve significant reductions in developed country farm subsidies and market barriers. It will also require some reductions in the current applied rates of developing countries because the use of the Swiss formula could eliminate 'water' – ie limit the leeway between the applied tariff rates and the bound or maximum tariff rates negotiated under the WTO – in some peak rates.³²

Developing countries have over time found their domestic policy space increasingly constrained as a condition for improved access to developed country markets. In particular, they have been required to adopt intellectual property protection, and to eliminate export subsidies and requirements to use domestic products rather than imported products. Further, they have had to accept disciplines and restrictions on trade-related investment measures. However, they have not signed the Government Procurement Agreement, and thus remain free to use this as an industrial policy tool. In addition, they retain discretion on a range of tariffs and some water in their tariffs, and as long as industrial subsidies are not trade distorting, they could be used provided they do not cause injury or 'serious prejudice' in foreign markets or nullify concessions made in other agreements. This suggests considerable scope for domestic policies will remain.

Africa

The final distinguishing feature of particular relevance for South Africa is the continued growth in Africa. The past decade has been especially favourable for African economies and the continent has experienced a renaissance. Driven by rising commodity prices and domestic reforms, Africa became the world's third-fastest growing region from 2000.³³ Africa's collective GDP (\$1.6 trillion in 2008) is now roughly equal to that of Brazil or Russia.

The future environment provides great opportunities for Africa. Strong commodity demand encourages foreign investment in mining and minerals and the necessary complementary infrastructure. African countries have opportunities to use their leverage to increasingly participate in beneficiation of resources. Increased demand for food products provides opportunities for enhanced agricultural production and exports from African agricultural producers. This in turn brings improvements to rural areas and raises rural purchasing power.

This optimism is reflected in the various growth forecasts. According to the 2010 International Monetary Fund (IMF) World Economic Outlook, the share of SSA, excluding

South Africa, in world GDP is expected to rise to 1.2% by 2015; double its share in the first half of the 2000s.³⁴ Other estimates place Africa's (including South Africa) share of world income at 3.5% by 2020.³⁵ Future growth in Africa will clearly be influenced by what happens to commodity prices, but improvements in the macroeconomic environments within these countries and various regulatory improvements suggest that growth will continue even if the resource boom moderates.

The future may also bring opportunities for Africa to integrate into global supply chains.³⁶ The migration of foreign investors with assembly operations is based on wages, which are relatively low in Africa. Rising wages in China will provide further impetus for the relocation of assembly operations. Poor productivity levels and high trade costs impede the emergence of African-based production networks, but positive moves have been made in reducing these costs. The East African Community (EAC), for example, has made good progress in negotiating a simplified common external tariff, reducing transit costs and developing telecommunications networks that cover the region.

These developments are particularly important for South Africa. Sub-Saharan Africa plays a disproportionate role in South Africa's trade flows relative to its contribution in world income. For example, exports to SSA currently make up close to 20% of South Africa's total merchandise exports (excluding gold). These exports make up a very high share of total imports within many of the SSA countries – 50% of Zimbabwe imports, 41% of Mozambique imports and between 20–30% of total imports in Zambia, Malawi and the Democratic Republic of Congo. South Africa is also an important export destination for many African countries – 28% of Zimbabwean exports and between 6% and 10% of exports from Malawi, Zambia, Botswana and Namibia are destined for South Africa.³⁷

The complementarity between South African exports and the rest of SSA imports is arguably greatest in services. South African services trade is very poorly measured.³⁸ Nevertheless, anecdotal evidence indicates extensive involvement by South African retail, communications, construction, financial and tourism sectors in trade with the region. An important determinant of South African manufacturing firms' comparative advantage in selling to the region is that they also provide services related to the assembly, maintenance and repair of facilities.

There are also strong African–Asian trade complementarities that have important spill-over effects for South Africa. The last decade has seen a boom in trade between Africa and Asian countries. For example, exports from Africa to Asia grew at 20% per year from 2000–05.³⁹ South Africa's linkages with the rest of Africa therefore provide it with an opportunity to benefit from the strong economic growth in the Asian economies.

Finally, the region is an important destination for South African FDI, particularly the neighbouring countries. Compared with investment from outside of Africa, where the deals are concentrated in the primary sector, intra-African investment (mainly from South Africa) is relatively oriented towards services and manufacturing.⁴⁰

FUTURE UNCERTAIN

None of the outcomes in the consensus view is assured. Growth in developed countries is already expected to be sluggish, but it could be even slower than expected if fiscal difficulties in the US and financial problems in Europe are not overcome. Growth in

emerging economies could also prove slower than is now expected, especially if China confronts economic problems in shifting its demand patterns in a new direction and if it experiences political upheavals. Oil price fluctuations in particular have the ability to destabilise growth, and the Middle East too is a highly unstable region. In response to unexpectedly slow demand, commodity markets could experience gluts and instability. Indeed, if China is successful in moving to a domestically oriented growth path, its growth will become much less commodity-intensive. African growth could also stall if the environment deteriorates. Finally, if the Doha Round fails, and unemployment rates remain high in developed countries, the global trading system could also face new protectionist measures. Another threat could be 'eco-protectionism' if developed countries impose climate 'border adjustment taxes' on imports from countries they deem to have inadequate climate change policies.

As with most risky decisions that have the potential for high pay-offs, the correct response to these opportunities and risks is to diversify. A multi-pronged trade strategy is thus required. This entails trade policies that have both global and regional dimensions and promote a range of exports (commodities, manufactured goods and services). In the following section we consider whether South Africa's current trade strategy is positioned to take full advantage of the changing global trading environment. We also offer suggestions for changes in that strategy that offer the promise of better results.

IMPLICATIONS FOR SOUTH AFRICAN TRADE POLICIES

The implications entailed by the risks in the consensus forecast point to the importance of a diversification strategy that is multi-pronged. South Africa needs to be positioned for a continuation of the commodity cycle, and to exploit emerging economies more fully. But simultaneously it needs policies to spur labour-intensive services and manufacturing exports, both because these will be needed if commodity markets are less robust and because of their employment-creating potential.

This discussion of the economic outlook therefore suggests that South Africa's trade policies should prioritise four key goals.

- Capitalise on the growth in emerging economies by improving market access for South African exports.
- Increase South Africa's participation in global manufacturing supply chains to increase exports of goods and services to both developed and emerging countries.
- Capitalise on the strong global markets for primary commodities through enhancing minerals development by domestic and foreign investors and, where appropriate, moving higher along the value chain.
- Take advantage of Africa's improved growth prospects by (a) increasing exports of goods and services to the region; (b) deepening African integration; (c) positioning South Africa as a hub for African regional and global engagement; and (d) leading Africa in negotiations to reduce barriers to African exports in developed and developing markets.

Before exploring whether South Africa's current trade policy is appropriate for achieving these goals, we should emphasise that these goals cannot be achieved through trade policies, narrowly construed. Complementary measures to facilitate trade both domestically and regionally need to be undertaken (eg improved transportation, regulation, customs, etc.) In addition, as well recognised in the New Growth Path, a multi-faceted complementary approach which allies other microeconomic (industrial) and macroeconomic (real exchange rate) policies will be required. In particular, macroeconomic policy has an important role to play in keeping the economy diversified. This requires preventing excessive appreciation of the rand to maintain a healthy industrial base and accumulating fiscal surpluses during good times, in order to be able to tide the economy over when times are bad.

In what follows these issues are dealt with in turn. Our aim is to discuss whether the current trade policy strategy is well positioned to take advantage of these four goals. We begin with an appraisal of South African tariff policies, and argue that the current strategy is heavily focused on domestic concerns and has the danger of placing South Africa at a disadvantage as its exporters seek access to the growing emerging economies. We then offer some suggestions for alternative approaches that might assist in entering manufacturing export supply chains. We then briefly discuss policies towards developing minerals and beneficiation, emphasising the need for an improved regulatory regime and providing some caveats about an approach emphasising commodities. Finally, we turn to regional policies and emphasise the inherent tensions between South Africa's desire for domestic policy space in the setting of tariffs and the need to operate within the proposed SADC CU with a common external tariff.

Trade policy to enhance market access into emerging economies

The New Growth Path states that 'South Africa's trade policy should become more focussed, identifying opportunities for exports in external markets and using trade agreements and facilitation to achieve these.'⁴¹ Our assessment is that the current approach as outlined in the *Trade Policy and Strategy Framework* (TPSF) by the Department of Trade and Industry (the dti) does not really provide a convincing strategy for increasing South Africa's entry into emerging economies or enhancing participation in global supply chains. This is evident both in South Africa's position in the Doha Round, as well as its neglect of bilateral and regional FTAs.

In the Doha Round, aside from what are surely justifiable demands for reductions in developed country agricultural subsidies and protection, South Africa's approach is heavily defensive. South Africa's explicit negotiating objectives in the WTO are given as:⁴²

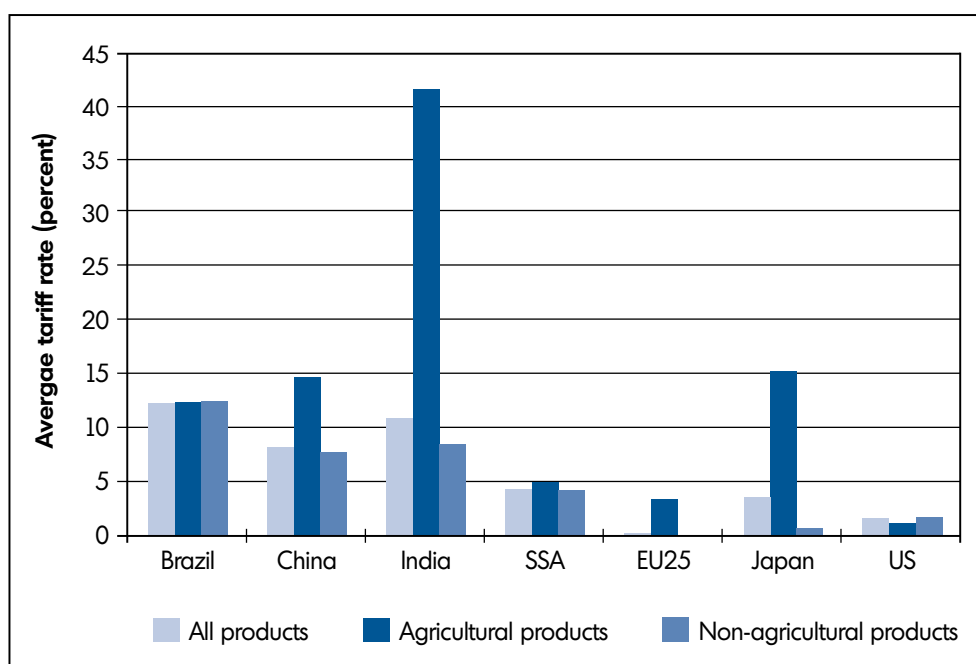
- i) enhance market access to developed countries; ii) eliminate industrial countries' subsidies and support to agriculture; iii) re-negotiate rules that perpetuate imbalances in the international trade regime; and iv) ensure appropriate policy space for developing countries to pursue developmental objectives through meaningful implementation of the principle of special and differential treatment.

Conspicuous by its absence in this statement of goals is the objective of improving market access to developing countries, particularly the dynamic fast-growing economies. South

Africa has strong interests in lower tariffs in the large emerging economies, yet it has avoided asking for these in Doha. It has essentially viewed the negotiations in North–South terms and positioned itself strongly on the side of the South. Yet South Africa's interests are not necessarily aligned with those of other developing countries in all cases. During the Uruguay Round, South Africa participated as a developed country and was required to make more extensive cuts in its maximum (bound) tariff rates than other emerging economies (although tariff protection in many developing economies fell substantially through unilateral liberalisation).

Tariff barriers on South African exports to developing countries far exceed those to developed countries. This is clearly illustrated in Figure 3, which presents the 2008 average applied tariff rate on South African exports to Brazil, India, China, Japan, the US and the EU. The average applied tariff imposed on South African exports to BRICs (excluding Russia which only joined the WTO in 2012) ranges from 8.37% in China to 12.4% in Brazil. In contrast, the average applied tariff rate by developed economies is substantially lower: 0.26% by EU countries, 1.66% by the US and 3.62% by Japan.

Figure 3: Simple average applied tariff rates on South African exports, 2008



Source: Author's own calculations using UNCTAD (UN Conference on Trade and Development), TRAINS (Trade Analysis and Information System), database, <http://wits.worldbank.org/wits>.

The tariff barriers on South African exports to emerging economies are particularly high on agricultural goods: 41.7% in India, 14.7% in China and 12.4% in Brazil. Japan also has a highly protected agricultural market with average applied rates of 15%. The agricultural sector is prioritised for development in Pretoria's TPSE, yet South Africa has not focused on the lowering of these market barriers.

South Africa's emphasis on enhancing market access into developed country markets, for all developing countries in all products, is also not necessarily in its interest. Analytically, the key issue is whether South African exports to developed countries compete more strongly with domestic producers in these markets (eg against US producers when selling in the US market) – in which case lower MFN tariffs *are* in its interest, or with other countries, (eg Brazilian producers selling in the US) in which case preferential access could be better. Through its FTAs with the EU and EFTA, the US African Growth and Opportunity Act preferences and the Generalised System of Preferences (GSP) (used to export to Japan), South Africa actually has preferential access into the developed economies. As shown in Table 3, South Africa's preference margins on average tariff rates applied by developed economies range from 3 percentage points (into EU) to 0.4 percentage points (into Japan). Reductions in developed economy barriers will erode these preference margins. In contrast, South Africa faces negative preference margins into the BRICs as a consequence of the various regional trade agreements entered into by these economies.

Table 3: Comparison of average tariffs and preference margins on South African exports to selected destinations, (simple average), 2008

	Brazil	China	India	SSA	EU25	Japan	US
All products							
Applied rate	12.48	8.37	11.06	4.40	0.26	3.62	1.66
Preference over applied	-1.31	-0.42	-0.19	4.12	3.17	0.40	0.95
Agricultural products							
Applied rate	12.42	14.67	41.72	4.95	3.38	15.30	1.17
Preference over applied	-3.94	-1.13	-0.46	3.87	2.50	0.17	1.26
Non-agricultural products							
Applied rate	12.49	7.77	8.46	4.31	0.00	0.63	1.72
Preference over applied	-1.12	-0.35	-0.16	4.17	3.04	0.46	0.92

Note: The HS6-digit tariffs for SSA are weighted averages. South Africa gets preferential access to Japan under the GSP. In calculations including the Mercosur–SACU agreement, the SACU MFN preference margin is estimated at 0.4%, the SACU Applied preference margin equals -0.4% (calculated using South African exports to Brazil in 2007 and 2008).

Source: Author's own calculations using trade and tariff data at the 6-digit level of the Harmonized System obtained from UNCTAD, TRAINS, database, <http://wits.worldbank.org/wits>. Rates only cover products exported by South Africa to that region in 2008.

Therefore, in addition to defending its legitimate needs for policy space, South Africa's goals in the Doha Round should in part be about reducing these disadvantages in accessing the growing emerging economies.

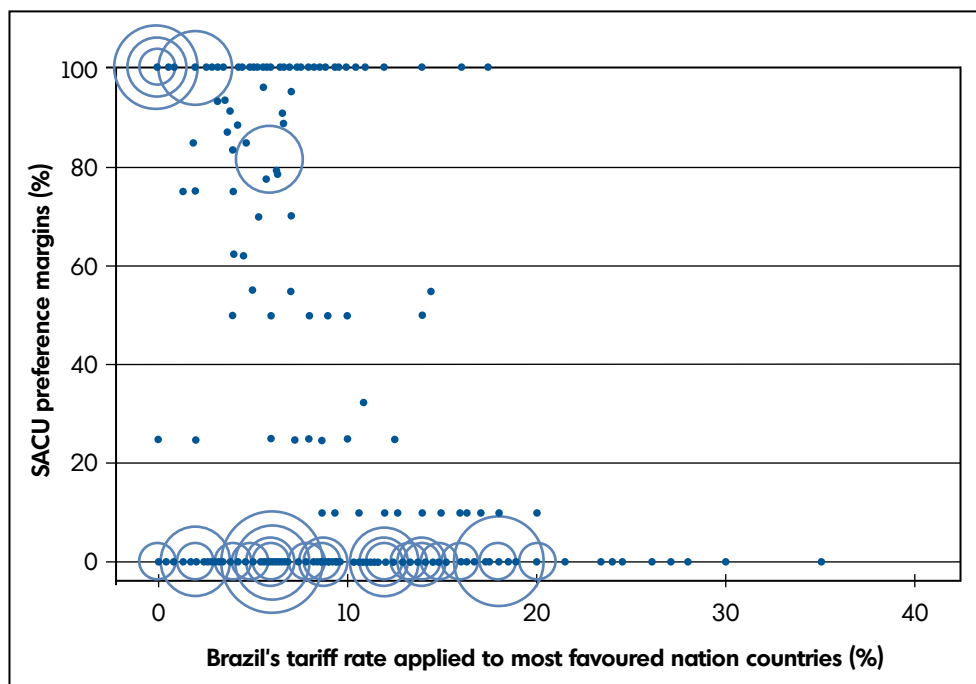
South Africa's position in the Doha Round would not be problematic if, as both China and India have done, it complemented its hard-nosed position in the Doha Round with an active pursuit of FTAs with emerging economies. But with the exception of the SACU–EFTA agreement, South Africa has not been an active participant in the global trend towards FTAs after 2000. The co-operation agreements that have been signed – for example, with India, China and Brazil – have had a high symbolic and hortatory character emphasising desires to increase trade and investment rather than establishing systems based on binding rules and tariff preferences. The same applies to the India–Brazil–South Africa Forum (established in 2003) and the SACU Trade, Investment and Development Cooperation Agreement (in 2008) with the US that was the final outcome of the failed negotiations of a SACU–US FTA.

South Africa did (as part of SACU) conclude a preferential trade agreement with Mercosur in 2008, and a similar agreement is in prospect with India. In addition, there is a Comprehensive Strategic Partnership Agreement with China (Partnership for Growth and Development).⁴³ These agreements have been justified as useful but they do not give South Africa the same access benefits as those given to countries that have signed more comprehensive FTAs.

The future objective, as outlined in the TPSF, is not to engage in deep and comprehensive FTAs, but rather more focused preferential trade agreements that allow for a more strategic integration process. The intention is to simultaneously ensure that policy space is preserved to 'pursue national objectives' while (at the same time) 'leveraging the benefits of more integrated regional and global markets'.⁴⁴ Partial trade agreements, however, have limitations with regard to promoting trade. They do not necessarily give South Africa the market access it desires – 'you get what you give'.⁴⁵ High preference margins tend to be granted on products with low tariff rates. 'Preferential access' may be less valuable because tariff reductions are given on products where preferential access has already been granted to other countries.

The SACU–Mercosur agreement has gone the furthest in the direction of a binding agreement and it demonstrates the inherent problems associated with partial trade agreements. Figure 4 presents a scatter plot of the relationship between the tariff preference margins granted by Mercosur countries on products exported by SACU members (on the vertical axis) and the average tariff rate applied by Brazil (a Mercosur member) on imports of these products from other countries (horizontal axis). The preference margin reflects the percentage reduction in the MFN tariff rate applied by the importing country, ie a value of 100 indicates that the product can be imported duty free under the trade agreement. The size of the circle in the scatter plot is made proportional to the value of the product in total SACU exports to Brazil.

Three key features are evident in the agreement. Firstly, only one-sixth of all product lines are covered, reflecting the narrow scope of the agreement. Secondly, high preference margins tend to be granted on products facing relatively low applied rates: for example, duty-free access (a 100% preference margin) has been granted on coal and unsaturated acyclic hydrocarbons. These are important export products for SACU, but the MFN tariff rate applied by Brazil on these products is 2% or less.

Figure 4: SACU applied preference margins on exports to Brazil

Note: The figure is constructed using export and tariff data at the 6-digit level of the Harmonized System. On the vertical axis, a value of 100 implies that SACU exports can enter the Brazilian market without paying tariff duty. A value of zero implies that no preference is granted, and the full MFN tariff rate is applied. The horizontal axis denotes the MFN tariff rate applied by Brazil on imports from all countries with which it has no preferential trade agreement.

Source: The tariff and trade data are obtained from UNCTAD, TRAINS, database, <http://wits.worldbank.org/wits>. The SACU preferences are obtained from Annex 1 of the Preferential Trade Agreement between Mercosur and SACU, http://www.sice.oas.org/tpd/mer_sacu/negotiations/viiround_annexi_e.xls.

Finally, very low preference margins were granted on the products that made up a large share of South African exports – see the large circles along the bottom axis denoting large export products with no preference margins. For example, no preferences have been granted on the two most important products exported by South Africa (ferro-manganese and spark-ignition engines over 1 000 cc), yet these products face tariff rates of between 6% and 18%.⁴⁶

There is little evidence, therefore, that the partial trade agreements emphasised by the South African government will be effective in enhancing access into the growing emerging economies.

To be fair, the SACU–Mercosur agreement *has* established a legal framework for negotiating future tariff reductions. However, unless the focus is on negotiating comprehensive trade agreements that match those signed by other developing countries, South African exporters will remain relatively disadvantaged in these markets.

The justification for South Africa's defensive stance in these trade negotiations is that it is necessary to provide the maximum leeway for domestic industrial policy.⁴⁷ The trade strategy is designed to follow industrial policy imperatives. This involves a detailed sector-by-sector approach which seeks to upgrade South Africa's industrial base and to encourage the production and export of more sophisticated value-added products, 'through purposeful intervention in the industrial economy aimed at achieving dynamic competitive advantages'.⁴⁸ Although South Africa may have engagements both multilaterally and bilaterally, the central desire is to retain the maximum policy space to implement its approaches unilaterally.

This approach does have the advantage of providing the maximum room for 'domestic policy space', but not only does it result in an excessively complex tariff structure, it also places South Africa in a disadvantageous position when seeking market access for its exporters.⁴⁹ It is ironic that the current policy is justified as avoiding the consequences of specialisation along the lines of 'static comparative advantage,' but in fact by considering only the requirements of each sector and keeping tariffs high for all sectors that seem at all vulnerable, the policy actually leads to resource allocation along the lines of static comparative disadvantage. In making decisions to retain resources on a sector-by-sector basis, the policy neglects the opportunity costs of putting resources to alternative uses.

An alternative approach would be to simplify the tariff structure with much fewer tariff rates, but still maintain barriers in a few sectors – both to preserve jobs and nurture infant industries. In addition, more emphasis would be given to offensive interests by seeking greater multilateral liberalisation from the large emerging economies and/or by negotiating more comprehensive bilateral agreements in which greater liberalisation is exchanged by granting preferential market access while still retaining some protection for sensitive sectors.

Enhance labour-intensive manufacturing exports

Part of the reason for this cautious and defensive approach to trade policy is that, with a few exceptions, South Africa has not yet developed manufacturing exports that can realistically be expected to compete in and with emerging markets. With a few exceptions, South Africa has also not been able to participate effectively in global supply chains that export manufactured goods to the developed countries – especially when the rand stands at below eight to the dollar. Thus, in addition to striving for better market access for exports, trade policy needs to be complemented by other policies that enhance export diversification by fostering competitive manufactured exports.

The New Growth Path recognises this not only by outlining a set of microeconomic policies but also an approach that involves reducing costs through a more competitive real exchange rate achieved through combining fiscal restraint with an incomes restraint policy. A real rand that is 20% weaker is equivalent to a 20% tariff on all imports and a 20% subsidy for all exports. One benefit from successfully implementing this New Growth Path approach is that it would create more room for a less defensive trade strategy. Indeed, with a real rand closer to nine to the dollar, a much broader range of South African manufacturing exports would become competitive. Contrary to the negative impressions given in some of the official trade policy strategy documents, South African non-resource

manufacturing firms have in the past generated impressive export growth in response to a competitive rand.⁵⁰

A complementary industrial policy strategy to this macroeconomic policy might involve a co-ordinated approach to attracting local and foreign investors to attractive special export zones in an explicit effort to become part of the global supply chains that are likely to move out of China over the next 15 years. Ideally, these would provide *additional* employment opportunities that would complement rather than compete with the domestic labour market.

The question remains as to how realistic a goal this is. A common critique is that South Africa cannot compete on the basis of labour costs. To evaluate this view, we compare labour costs across various countries in 2010. Table 4 presents hourly manufacturing wages as well as unit labour costs (relative to the US) where wages are adjusted for productivity differences. These are average wages and do not take into account the wage distribution or differences in skills. Nevertheless, the table provides some useful insights.

Table 4: Comparison of labour cost competitiveness in manufacturing, 2010

	Unit labour costs (US = 100)	Hourly wages (\$)
South Africa	105	7.1
India	118	3
China	85	1.9 (was 0.9 in 2006)
Brazil	95	8.2
Peru	84	4.5
US	100	33.7

Note: The unit labour costs are based on wage and productivity data for the overall economy. However, the relative wages for the overall economy are very similar to those for manufacturing alone.

Source: Economist Intelligence Unit, Website, <http://www.eiu.com>, accessed 18 January 2011.

Firstly, South Africa generally cannot compete against China and other emerging economies on the basis of average current manufacturing wages. South African firms face a wage cost disadvantage relative to China and India, but not Brazil. Average manufacturing wages in South Africa, for example (at \$7.1 an hour in 2010) were over three times those in China. Secondly, South Africa's labour cost competitiveness is far closer to that of China and India once productivity differences are accounted for.⁵¹ Thirdly, higher wage costs can also be offset through a *real* depreciation of the currency. According to the table, a real depreciation of 20% would be sufficient to improve South Africa's average labour cost competitiveness to a level close to that in China. Finally, China's average unit labour costs are expected to rise in response to the 13% per year increase in wages planned over the next five years.

Thus taking a five-year time horizon – even with its current labour costs, with a rand that is 20% lower – many South African manufacturers could be competitive in export markets. Indeed, empirical evidence suggests that South African exports are highly responsive to labour cost competitiveness, which can be achieved through real depreciation, wage moderation and/or productivity improvements.⁵²

In fact, the *average* manufacturing wage is a poor measure of what the average worker earns in the South African economy. This is illustrated most strikingly in the data given in the New Growth Path. It reports that half of all employed people in 2008 earned less than ZAR 2,500 a month (\$2.1/hour). A third earned under ZAR 1,000 a month (\$0.8/hour).⁵³ Most of these workers are found in the informal, agricultural and domestic work sectors. If we combine these shares with the fact that one-quarter of South African workers are unemployed, we conclude that 48% of all potential workers in South Africa earn less than \$0.80 an hour and 60% less than \$2 an hour.

South Africa, therefore, has the potential to compete on the basis of wage costs. The realisation of this potential will require complementary policies including development of trade infrastructure and a more flexible approach to labour legislation and the wage bargaining process. Yet infrastructure development is constrained by the budget and wholesale reform of labour legislation is regarded as not politically feasible.

One approach is to reform at the margin. This could be through the establishment of a new set of duty-free processing zones that would concentrate on manufacturing for export markets. The aim would be to provide additional employment opportunities that would complement rather than compete with the domestic labour market. If duty-free zones in rural and coastal areas could combine competitive wages with tax incentives, high-quality infrastructure and preferential market access to both developed and developing markets, they could provide an environment in which manufacturing activities could thrive. Particular consideration could be placed on creating opportunities for workers in former Bantustan areas where unemployment is high and incomes are low.⁵⁴ These zones should be close to ports, offer excellent shipping and customs-clearance facilities and provide duty-free access to intermediate inputs.

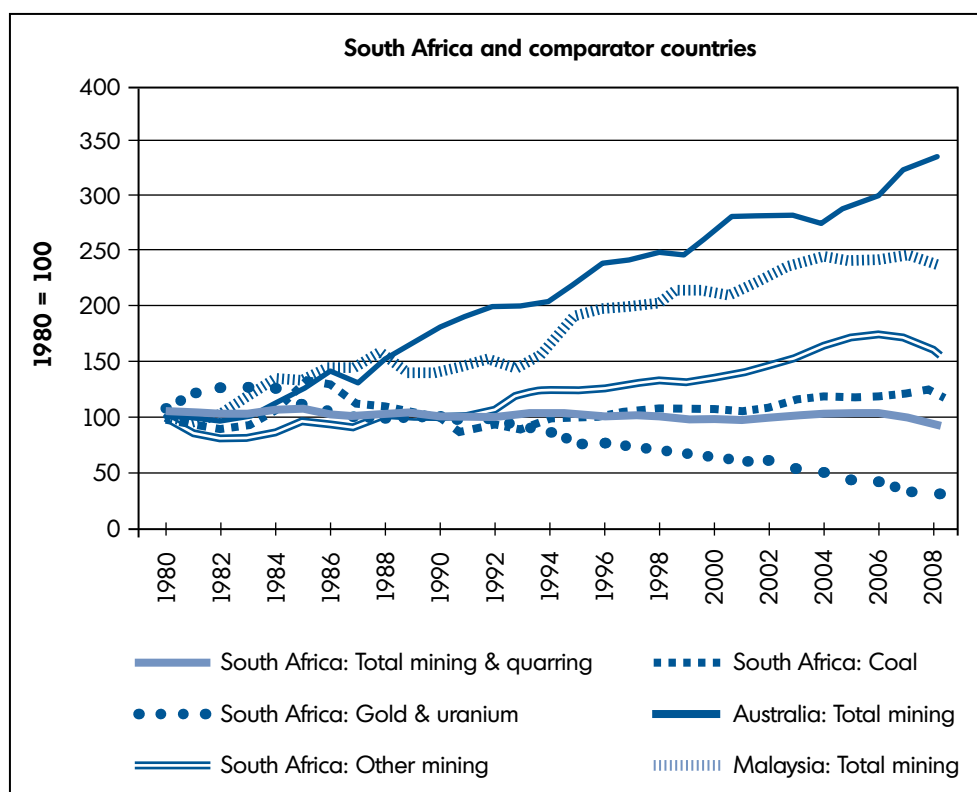
A key part of the strategy is attracting the right types of investors. This requires a sophisticated investment promotion agency that would identify and target the major players in global supply chains and seek to attract them to South Africa. Exporters and players in global supply chains are large and concentrated. These investors should be actively pursued and given the highest priority, indeed one-stop shopping with respect to obtaining the necessary permits and visas to set up their operations. A special emphasis could be placed on the electronics sector – a labour-intensive activity in which South African exports are conspicuous by their absence. Policymakers should also leverage off co-operative agreements (with BRIC countries) to facilitate investment in manufactures and not just in the beneficiation of raw materials.

Riding the commodity super-cycle

Although foreign market barriers are not high in minerals, the sector clearly deserves emphasis in both trade and foreign investment policies. The challenge lies in improving on the disappointing performance in the regulatory and infrastructure areas that have hindered exports over the past decade. Incredibly, as shown in Figure 5, the share of

minerals in South African output has stagnated for the past three decades. In real terms, mining value added was actually no different in 2009 to what it was in 1975. In contrast, real mining value added in Australia increased more than three fold. In Malaysia real mining value added rose by a factor of 2.5 over the period 1980 to 2009 – although this growth also reflects its discovery and production of oil and gas in the 1970s.

Figure 5: Index of real gross value added in mining, selected countries (1980=100)



Source: Quantec Research (Pty) Ltd, <http://www.quantec.co.za/>, accessed 19 January 2011; Australian Bureau of Statistics, 'Australian National Accounts: National Income, Expenditure and Product', 2011, <http://www.abs.gov.au/AUSSTATS>, accessed 8 February 2011; Malaysia, Department of Statistics, <http://www.statistics.gov.my>, accessed 8 February 2011.

The importance of rejuvenating mineral exports is broadly accepted and well recognised in policy circles. More contentious is the emphasis by government on the beneficiation of raw materials, which is also reflected in government's approach to international agreements. For example, an aim of the co-operative agreement with China – the Partnership for Growth and Development – is to 'promote value-added South African exports to China and increase inward investment by China in projects around mineral beneficiation'.⁵⁵

There is scope for South Africa to increase its value-added activities in commodities, but we would caution against the presumption made by many that because South Africa is a producer of raw materials it is automatically likely to be competitive in most beneficiation activities. There is little international evidence in support of the view that

production of raw materials automatically gives a country a competitive advantage in beneficiation activities.⁵⁶ South Africa, for example, faces significant disadvantages in the beneficiation of iron ore: It does not have sufficient local demand for scale, is not close to major foreign demand centres, the location of mills are not on the coast; and profitability is adversely affected by high costs of significant factors (capital, labour and energy) and high cost of imported pellets and coking coal.⁵⁷

Providing costly incentives for beneficiation could also draw on scarce resources that may be better used elsewhere. Our estimates (see Box 2) suggest that mineral beneficiation is often immensely capital-intensive, creates fewer jobs (particularly semiskilled and unskilled jobs) per dollar of output, has heavy demands for energy and is often highly polluting.

Box 2: Beneficiation

Mineral beneficiation is often immensely capital-intensive, creates fewer jobs (particularly semiskilled and unskilled jobs) per dollar of output, has heavy demands for energy and generates high levels of emissions. To illustrate the employment trade-offs, we estimate the *net* employment intensity of output growth for various industries in South Africa using input–output tables. The results are presented in Figure 6 and Table 5. These values are *net* values, as they exclude the employment creation associated with the upstream increases in production of primary commodities used as intermediate inputs. The reason is that with beneficiation the primary commodity is no longer exported directly, but is redirected for use in the downstream industry. The sectors are ranked according to net employment creation (from highest to lowest).

According to our estimates, the net employment intensity of output growth is lowest in the resource-intensive manufactured sectors where much of the beneficiation is occurring (net jobs per ZAR 1 million increase in domestic production in brackets):

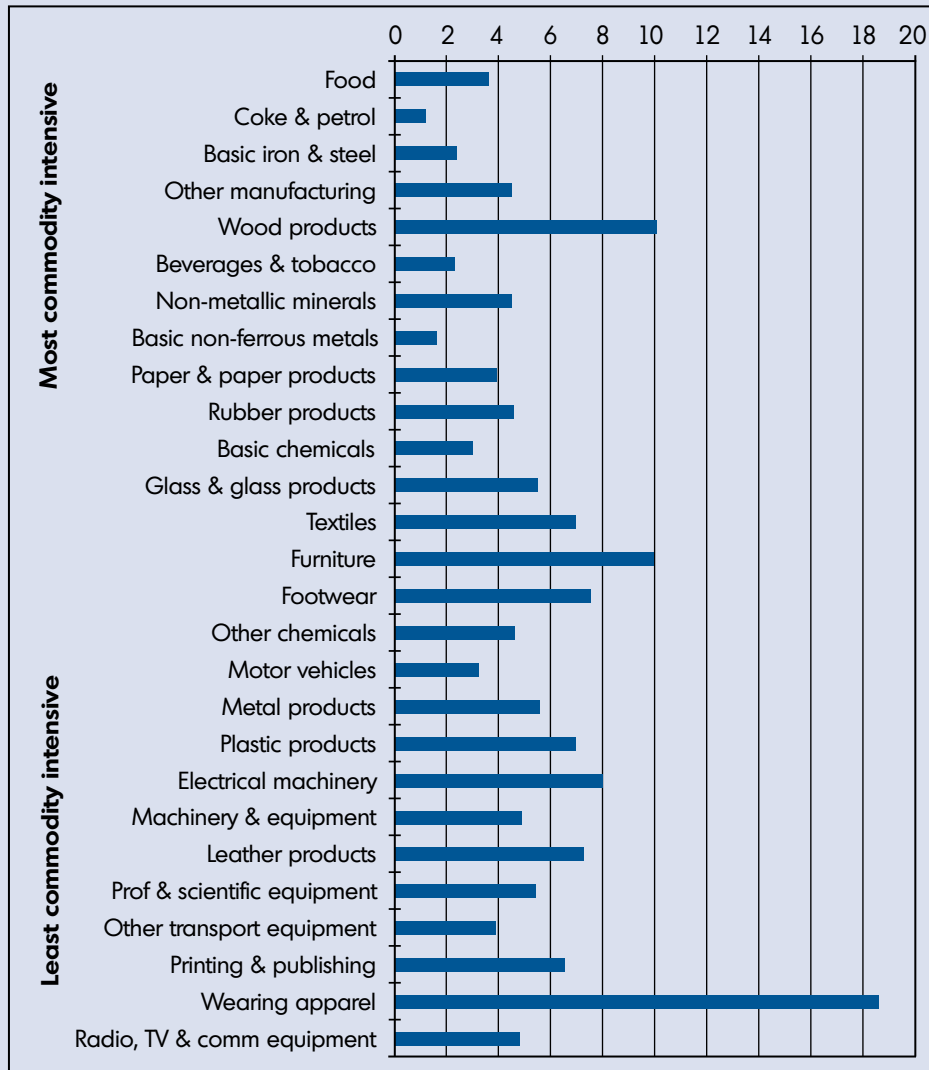
- coke & refined petroleum (1.2),
- basic non-ferrous metals (1.6),
- beverages and tobacco (2.3),
- iron & steel (2.4) and
- chemicals (2.9).

Roughly half of these jobs are of semi- and unskilled labour. The greatest employment effects are found in:

- wearing apparel (18.6),
- wood & wood products (10.1),
- furniture (9.9) and
- electrical machinery (8).

Semi & unskilled labour make up a relatively high share of these jobs – between 60 and 80%. Similar trade-offs with respect to the use of scarce electricity also need to be considered.

Figure 6: Net employment per ZAR million increase in output (ranked according to primary commodity intensity)



Note: Commodity intensity is measured as share of primary commodities in total costs. Jobs per million output reflect the direct and indirect employment opportunities associated with a ZAR 1 million increase (2 000 prices) in production. These values exclude the employment opportunities associated with the primary sector multipliers, as these products could be exported directly. This reduces the size of the multipliers, as primary sector production does not feed back into the system.

Source: Author's own calculations using Statistics South Africa, '2000 Supply-Use table', <http://www.statssa.gov.za/> and employment data from Quantec Research (Pty), <http://www.quantec.co.za>, accessed 18 January 2011.

Table 6: Net employment creation from beneficiation

	Net employment creation from beneficiation (jobs per ZAR million output)				Share	Primary resource intensity	
	Semi & unskilled	Skilled	Total employment		Semi & unskilled	(Primary resource cost share)	
Manufacturing				rank/27			rank/27
Wearing apparel [313–315]	14.9	3.7	18.6	1	0.80	0.00	26
Wood and wood products [321–322]	6.1	4.0	10.1	2	0.61	0.26	5
Furniture [391]	6.6	3.3	9.9	3	0.66	0.03	14
Electrical machinery and apparatus [361–366]	4.7	3.3	8.0	4	0.59	0.01	20
Footwear [317]	6.2	1.3	7.5	5	0.83	0.02	15
Leather and leather products [316]	5.3	2.0	7.2	6	0.73	0.00	22
Plastic products [338]	4.6	2.4	7.0	7	0.66	0.01	19
Textiles [311–312]	5.1	1.9	7.0	8	0.73	0.07	13
Printing, publishing and recorded media [324–326]	2.1	4.4	6.6	9	0.33	0.00	25
Metal products excluding machinery [353–355]	3.4	2.2	5.6	10	0.61	0.01	18
Glass and glass products [341]	3.7	1.8	5.5	11	0.67	0.08	12
Professional and scientific equipment [374–376]	3.1	2.3	5.4	12	0.58	0.00	23
Machinery and equipment [356–359]	2.5	2.4	4.9	13	0.51	0.01	21
TV, radio & communication equipment [371–373]	2.9	2.0	4.9	14	0.59	0.00	27
Other chemicals and man-made fibres [335–336]	2.3	2.3	4.6	15	0.49	0.02	16
Rubber products [337]	2.9	1.7	4.6	16	0.63	0.10	10

	Net employment creation from beneficiation (jobs per ZAR million output)				Share	Primary resource intensity	
	Semi & unskilled	Skilled	Total employment		Semi & unskilled	(Primary resource cost share)	
Non-metallic minerals [342]	3.0	1.5	4.5	17	0.66	0.18	7
Other manufacturing [392–393]	2.3	2.2	4.5	18	0.52	0.31	4
Paper and paper products [323]	2.3	1.6	3.9	19	0.59	0.10	9
Other transport equipment [384–387]	2.0	1.8	3.9	20	0.52	0.00	24
Food [301–304]	2.0	1.6	3.6	21	0.55	0.40	1
Motor vehicles, parts and accessories [381–383]	1.8	1.4	3.2	22	0.56	0.02	17
Basic chemicals [334]	1.5	1.4	2.9	23	0.52	0.09	11
Basic iron and steel [351]	1.3	1.1	2.4	24	0.53	0.33	3
Beverages and tobacco [305, 306]	1.3	1.0	2.3	25	0.56	0.21	6
Basic non-ferrous metals [352]	0.8	0.8	1.6	26	0.51	0.11	8
Coke & refined petroleum products [331–333]	0.6	0.6	1.2	27	0.48	0.40	2
Average manufacturing	3.5	2.1	5.6	-	0.59	-	-

Note: See notes to Figure 6.

Source: Author's own calculations using Statistics South Africa, '2000 Supply-Use table', <http://www.statssa.gov.za/>; Employment data from Quantec Research (Pty), <http://www.quantec.co.za>, accessed 18 January 2011.

Nonetheless, in some cases, beneficiation could make sense and trade policies can play a role in encouraging these activities. In the face of booming markets, projects that refine and smelt minerals can contribute to foreign exchange earnings and employment growth. A strategic use of export taxes (as advocated in the New Growth Path plan) could in principle encourage beneficiation, although there are delicate trade-offs, especially since such measures could actually reduce the attractiveness of more labour-intensive mining. Attention should also be focused on the tariff escalation present in South African

trading partners that have the impact of protecting value-addition in these partners and discouraging these activities in South Africa and other African countries.

Taking care of the neighbourhood

South Africa's regional trade engagement is extremely important, especially in regard to its diversification strategy, since these are major export markets for its non-commodity manufactured goods and its services. SACU and the SADC Free Trade Area and the proposed new Tripartite FTA (TFTA) between the EAC, the Common Market for SADC all reflect this vital strategic interest.

South Africa has a strong interest in these groups for several reasons. *First*, to enable local firms to export goods and services; *second*, to assist in South Africa's role as a hub for foreign firms seeking to enter African markets; and *third*, deeper African integration can help Africans compete more effectively in global markets in ways that could provide opportunities for South Africans.

Separately, many countries are still too small to realistically achieve the scale economies required to develop the capacity to make significant contributions to value added in global supply chains. Standing alone, for example, even Lesotho, Africa's largest clothing exporter to the US, is too small to support a textiles industry that produces the variety of fabrics it requires. But by combining forces, these countries can more easily offset their scale deficiencies. In addition, as the Asian experience has indicated, there is immense scope for firms from countries at different incomes levels (eg China and Hong Kong) to combine forces with each contributing the value added in which they have comparative advantage.

For South Africa an expansion of African supply chains would offer opportunities not only to engage directly by providing inputs and equipment but also indirectly through providing services such as finance, transportation, and logistical co-ordination and so on. Similarly, African minerals development, and infrastructure and construction projects to support their exports, offer opportunities for South African service providers.

But the challenges involve the specific nature of the co-operation. There are inherent tensions between South Africa's desire to make its entire tariff structure subservient to its industrial policy and the need to operate that tariff structure within the proposed SADC CU with a common external tariff. Structuring CU agreements around regional industrial policy objectives adds further complexity. This would require members with vastly different development needs to not only agree on the common external tariff, but also to co-ordinate their industrial policies. It is difficult enough to determine an interventionist industrial policy strategy at the national level. It is even more difficult to operate at the regional level and determine such a policy by consensus. It is not impossible – the Europeans have responded to these tensions by banning state aids at the national level and carrying out the industrial policies at the European level. However, this involves giving up a degree of national sovereignty and control over crucial policy areas that the diverse set of African countries are unlikely to be ready for.

There is recognition of these tensions and South Africa has tried to shift attention from the schemes for grand CUs and emphasised the many other actions that need to be undertaken to deal with the non-tariff barriers, such as standards and technical barriers that impede regional integration. In addition, the trade policy documents have correctly emphasised working on trade facilitation that can deepen integration. We also believe that

the adoption of a common, simple, African rule of origin should be developed and adopted in all African FTAs.⁵⁸ This would allow for cumulation across countries and would ideally be used in the preferences granted to African countries by the rest of the world. And finally, South Africa has a strong interest in including services in these agreements.⁵⁹ Services are a key input in determining the competitiveness of firms and are already an integral part of South Africa's trade with the region.⁶⁰ Entering into rule-based agreements on services can enhance South Africa's integration in the region.

CONCLUSION

In this paper we identify some major patterns of the future global trading environment that serve as the context for trade policy. We highlight continued shifts in global growth from developed to developing economies, the growing share of emerging markets in trade and investment and the continued upward pressure these are expected to place on commodity prices. We also note the shifts in consumption and production patterns required for the unwinding of global current account imbalances and how these may give rise to a re-orientation of global supply chains, facilitated through use of regional trade arrangements. Finally, we describe Africa's strong growth performance and how this has been driven by commodity prices and domestic reforms.

None of these outcomes is assured. Fiscal difficulties in the US and financial problems in Europe may constrain global growth. Growth in China may slow, especially if it confronts economic and political problems in re-orienting its economy from export and investment led growth to domestic consumption led growth. Instability in the Middle East has the potential to destabilise global growth through its impact on oil prices. Unexpectedly slow demand could depress commodity markets, which would slow African growth. Finally, if the Doha Round fails, and unemployment rates remain high in developed countries, the global trading system could also face new protectionist measures. The implications entailed by the risks to the future global trading environment point to the importance of a diversification strategy that is multi-pronged.

South Africa's current trade strategy, however, does not position the economy to take full advantage of the features of the future global trading environment. South African tariff policies are heavily focused on domestic concerns and run the risk of placing South Africa at a disadvantage as its exporters seek access to the growing emerging economies. We offer some suggestions for alternative approaches that might assist in entering manufacturing export supply chains. In particular, we promote the idea of establishing duty-free export zones where exporters are able to compete in low-wage manufacturing industries.

The paper has discussed policies towards developing minerals and beneficiation, emphasising the need for an improved regulatory regime and providing some caveats about the current government approach that emphasises the beneficiation of commodities. Finally, we have emphasised the inherent tensions between South Africa's desire for domestic policy space in the setting of tariffs and the need to operate within the proposed SADC CU with a common external tariff.

In this paper we have accentuated our differences with the current trade policy to stimulate discussion. Our differences should not be couched as a debate between free trade versus protection. There is a role for industrial policies and indeed, in some instances,

trade policy needs to be subordinate to industrial policy. However, we do not believe that industrial policy should prevent comprehensive improvements in the tariff regime or the conclusion of FTAs when these will be beneficial to South Africa.

Having as the central tenet of trade policy a commitment to deal with tariffs on a case-by-case basis will not serve South Africa well in the global economy that is likely to emerge over the next 15 years. A simpler tariff structure would facilitate the conclusion of FTAs and actually make industrial policy more effective. In our view, you cannot have exceptions for industrial policy if you do not have rules.

ENDNOTES

- 1 These values are based on import and export equations for the South African economy estimated by Edwards L & R Lawrence, 'South African Trade Policy Matters: Trade Performance & Trade Policy', *Economics of Transition*, 16, 4, 2008, pp. 585–608.
- 2 South African history is replete with examples of collapses in growth in response to the lack of foreign exchange. For example, the economic stagnation of the 1980s – with annual growth at just 1.5% – was in no small measure due to an externally imposed constraint that also made clear the degree to which the economy depended on trade. For a detailed review of the external constraint on South Africa's growth see Bell T, Farrell G & R Cassim, 'Competitiveness, International Trade and Finance in a Minerals-Rich Economy: The Case of South Africa,' in Fanelli JM & R Medhora (eds), *Finance and Competitiveness in Developing Countries*. London: Routledge, 2002, pp. 181–221.
- 3 South Africa, Department of Economic Development, *The New Growth Path: The Framework*. Pretoria: Government Printers, 2010.
- 4 See Rodrik D, 'Understanding South Africa's economic puzzles', *The Economics of Transition*, The European Bank for Reconstruction and Development, 16, 4, 2008, pp. 769–97.
- 5 See The Conference Board, 'Global Economic Outlook 2011', 2010, <http://www.conference-board.org/data/globaloutlookresults.cfm>. See also the IMF (International Monetary Fund), 'World Economic Outlook', October 2010, <http://www.imf.org/external/pubs/ft/weo/2010/02/pdf/text.pdf>.
- 6 The share of exports of FDI originating from non-OECD countries increased from about 20% to 25% from 2003–07, with the BRIC countries accounting for about a half of this growth. See Mattoo A & A Subramanian, 'Criss-crossing globalization: uphill flows of skill-intensive goods and foreign direct investment', World Bank Policy Research Working Paper Series 5047. Washington: Peterson Institute for International Economics, 2009. Lesser-developed countries, including Africa, have been amongst the beneficiaries of this surge in FDI. FDI flows from the BRICs to least-developed countries reached about \$2.2 billion in 2009 (2–3% of total FDI flows from the BRICS), with SSA countries receiving 0.9% (41% of total). Chinese FDI to least-developed countries rose from 5.7% of its total outbound FDI in 2003 to close to 10% in 2009. See Broadman HG, *Africa's Silk Road: China and India's New Economic Frontier*. Washington: World Bank, 2008; IMF, *New Growth Drivers for Low-Income Countries: The Role of BRICs*. Washington: IMF, 2011.
- 7 South–South investment in Africa has been driven mostly by state-owned companies and has been destined for natural resource industries (including oil). Over time, however, South–South investment is spreading to agriculture, manufacturing, and service industries

(eg telecommunications). The type of investor has also changed, at least in the case of Chinese investment in SSA where small and medium sized, predominantly private-sector, enterprises are emerging as important investors. See Kaplinksy R & M Morris, 'Do the Asian Drivers Undermine Export-Oriented Industrialisation in SSA?', *World Development*, 36, 2, 2008, pp. 254–73.

- 8 Broadman HG, *op. cit.* and IMF, *op. cit.*
- 9 The BRIC share of world imports rose by equivalent amounts (5.8–16%). Values are drawn from the UN Monthly Bulletin of Statistics.
- 10 Authors' own calculations using World Bank 'World Development Indicators', <http://data.worldbank.org/indicator>, accessed 8 February 2011.
- 11 These trends are already reflected in the gradual appreciation of the yuan as well as strong wage growth in manufacturing. The goal of shifting the economy towards a more consumption-led growth path is also reflected in the objectives of the Twelfth Five-Year Guideline approved by National People's Congress in 2011.
- 12 Authors' own calculations using Input–Output for China (late 2000s) obtained from OECD (Organisation for Economic Cooperation and Development), 'STAN Structural Analysis Database', <http://www.oecd.org/sti/industryandglobalisation/stanstructuralanalysisdatabase.htm>, accessed 8 February 2011.
- 13 ZAR is the three-letter currency code for the South African Rand.
- 14 Economies that grow at 7%, will generally invest around 30% of their output. In China, the investment share of GDP reached close to 50% in 2009. Investment expenditure is concentrated on infrastructure, construction and equipment, all of which are metals and minerals intensive. Industrial production is also commodity and energy (and pollution) intensive. On average, industrial production makes up 37% of GDP in emerging economies compared with 25% in high-income OECD countries. In China, the share of industrial production in GDP is exceptionally large – 47% of GDP in 2008. World Bank 'World Development Indicators', <http://data.worldbank.org/indicator>, accessed 8 February 2011.
- 15 The metals intensity of China's GDP is far higher than comparable developing countries. For example, China's copper and aluminium intensity was 1.8 and 4.1 kilograms per \$1,000 of real GDP for 2007–09, compared with world averages of 0.4 and 0.7 kilograms, respectively. World Bank, 'Global Economic Prospects', January 2011, p. 58.
- 16 Data sourced from IMF 'IMF Primary Commodity Prices', database, <http://www.imf.org/external/np/res/commod/index.aspx>, accessed 8 February 2011.
- 17 GDP remains constant in the simulation. Hence, a 4% decline in mining output implies a 4% decline in the mining-intensity of GDP.
- 18 Bordo M, Eichengreen B & D Irwin, 'Is Globalization Today Really Different from Globalization a Hundred Years Ago?', in Rodrik D & S Collins (eds), *Brookings Trade Forum: 1999*. Washington: Brookings Institution Press, 1999, p. 150.
- 19 The domestic content of selected Chinese electronic exports is 4.6% for computers and accessories, 14.9% for telecommunications equipment, 19.7% for other computer peripheral equipment and 22% for electronic element and devices. See Koopman R, Wang Z & SJ Wei, 'How Much of Chinese Exports is Really Made In China? Assessing Domestic Value-Added When Processing Trade is Pervasive', National Bureau of Economic Research Working Paper, 14109. Cambridge, MA: National Bureau of Economic Research, 2008.
- 20 See Linden G, Kraemer KL & J Dedrick, 'Who Captures Value in a Global Innovation Network? The Case of Apple's iPod,' *Communications of the ACM*, 52, 3, 2009, pp. 140–44.

- 21 The niche, however, mostly reflects a country's endowments and income level. In general, the price or quality of the product reflects the productivity and income of the country – richer countries export higher-priced varieties. See Schott PK, 'Across-product Versus Within-product Specialization in International Trade', *The Quarterly Journal of Economics*, 119, 2, 2004, pp. 646–677.
- 22 Edwards L & RZ Lawrence, 'Do Developed and Developing Countries Compete Head to Head in High-tech?' National Bureau of Economic Research Working Paper, 16105. Cambridge, MA: National Bureau of Economic Research, 2010.
- 23 Improvements in information and communication technology have led to an even finer degree of fragmentation. International competition increasingly plays out at the level of individual tasks and not only at the level of the firm or industry. See Grossman G & E Rossi-Hansberg, 'Trading Tasks: A Simple Theory of Offshoring,' *American Economic Review*, 98, 5, 2008, pp. 1978–97.
- 24 Authors' own calculations using World Bank 'World Development Indicators', <http://data.worldbank.org/indicator>, accessed 8 February 2011.
- 25 A January 2008 poll by Fortune magazine found that 63% of US respondents indicated that 'trade had made matters worse for the United States as a whole.' In turn, 78% felt it 'made things worse for US workers' and 55% felt it 'made things worse for US business.'
- 26 WTO, 'Regional trade agreements: facts and figures', http://www.wto.org/english/tratop_e/region_e/regfac_e.htm.
- 27 The ASEAN–India FTA will see tariff liberalisation of over 90% of products traded between the two regions, including the so-called 'special products', such as palm oil (crude and refined), coffee, black tea and pepper. Tariffs on over 4 000 product lines will be eliminated by 2016.
- 28 The PTA offer list of Mercosur for tariff concessions for India contains 452 products. The PTA offer list of India for tariff concessions for Mercosur's exports to India contains 450 products (obtained from the WTO).
- 29 *BBC News*, 'China and Brazil sign trade deals at Bric summit', 15 April 2010, <http://news.bbc.co.uk/2/hi/business/8624052.stm>.
- 30 Kate DT, 'China–Asean Trade Pact Takes Hold, Sparer, Popcorn, Toilet Paper,' *Bloomberg*, 31 December 2009, <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aYYX6TLe2mjg>.
- 31 Japan's Ministry of Foreign Affairs is explicit in its recognition of the strategic importance of creating trade agreements with its Asian partners to overcome high tariff barriers and enhance the development of regional production networks. 'FTAs with East Asia will produce the greatest additional benefits through further liberalization. As is apparent from the simple average figures for tariff rates [...] East Asia, the region where Japanese products account for the highest percentage of trade, has the highest tariffs. Liberalization of trade with East Asia will help facilitate the activities of Japanese businesses, which are facing competition from ASEAN and China and which, in many cases, have shifted their production bases to locations in East Asia.' (Japan, Ministry of Foreign Affairs 'Japan's FTA Strategy (Summary)', 2002, <http://www.mofa.go.jp/policy/economy/fta/strategy0210.html>).
- 32 The Swiss formula is a mathematical formula designed to reduce and harmonise tariff rates. The formula narrows the gap between high and low tariffs and sets a maximum tariff, irrespective of how high the original tariff was.
- 33 McKinsey Global Institute, *Lions on the Move: The Progress and Potential of African Economies*. Chicago: McKinsey Global Institute, 2010.

- 34 IMF, 2010, *op.cit.*
- 35 The Conference Board, 'Global Economic Outlook 2011 – Key Results', <http://www.conference-board.org/data/globaloutlookresults.cfm>.
- 36 See Broadman HG, *op. cit.*
- 37 South Africa, the dti (Department of Trade and Industry), 'Economic Database', <http://www.thedti.gov.za/econdb/raportt/SATradeinWorld.html>, accessed 25 January 2011.
- 38 'South Africa's trade in services data is inadequate for the purpose of monitoring trade in services. It comprises only 3 components: travel, transport and "other" and is not decomposed either by country of origin or destination or by mode of trade. In addition, mode 3 trade (commercial presence) is not captured and most mode 4 trade (temporary movement of natural persons) is either not captured or conflated with "travel"'. See Mayer M, *Trade in Services: Synthesis of Research Findings*. Johannesburg: Human Science Research Council, 2005, p. 10.
- 39 Broadman HG, *op. cit.*
- 40 UNCTAD, *Economic Development in Africa Report 2009: Strengthening Regional Integration for Africa's Development*. Geneva: UNCTAD, 2009.
- 41 South Africa, Department of Economic Development, *op. cit.*, p. 24.
- 42 South Africa, the dti, A South African Trade Policy and Strategy Framework. Pretoria: Government Printers, May 2010, p. 42.
- 43 The aim, the co-operative agreement with China – the Partnership for Growth and Development – is to 'promote value-added South African exports to China and increase inward investment by China in projects around mineral beneficiation'. See South Africa, the dti, *op. cit.*, p. 40.
- 44 *Ibid.*, p. 12.
- 45 This is clearly reflected in the failure of South Africa to obtain duty-free access into China during discussions as part of the South Africa–China Partnership for Growth and Development. See South Africa, the dti, 'China Country Briefing, Part 1 and Part 2', http://www.dti.gov.za/parliamentary/052610_Briefing_2_china.pdf, accessed 1 May 2011.
- 46 A bizarre outcome for South Africa is that 43 of the 196 lines granted 100% preference margins face zero MFN rates. A simple regression explaining the preference margin reveals a highly significant and negative coefficient on the Brazil applied rate (ie high preferences granted on goods with low protection rates) and insignificant coefficients on the size of South African exports (no relationship between size of South African exports and preference margin) and the preference margin for the rest of the world (ie it does not appear that Brazil granted high preference margins to South Africa on products that already faced high preference margins).
- 47 South Africa's industrial policy objectives are outlined in South Africa, the dti, National Industrial Policy Framework. Pretoria: Government Printers, 2007.
- 48 *Ibid.*, p. 11.
- 49 For a critique of the current tariff structure see Edwards L & R Lawrence, 'SACU Tariff Policies: Where should they go from here?' Centre for International Development, Working Paper, 169. Boston, MA: Kennedy School of Government, Harvard University, 2007.
- 50 See Alves P & L Edwards, 'South Africa's export performance: Determinants of export supply', *South African Journal of Economics*, 74, 3, 2006, pp. 473–500.
- 51 Productivity levels are on average greater in South Africa than in these countries and this offsets some of the wage cost disadvantage. South Africa's productivity adjusted wages (unit labour costs) are only 24% greater than those in China. Unit labour costs in South Africa are actually lower than in India reflecting that economy's low productivity rates. In contrast, South

- Africa faces a productivity disadvantage with respect to Brazil that more than offsets the relative wage advantage of South African workers.
- 52 Sector-level estimates for South Africa reveal that a 1% improvement in South African labour-cost competitiveness is associated with a 2.7% increase in labour-intensive manufacturing exports in the long run. The export response in other sectors is lower (1.29% for resource-intensive manufacturing, 1.5% for machinery and metal products), but still highly responsive. See Edwards L & S Golub, 'South Africa's International Cost Competitiveness and Productivity in Manufacturing', *World Development*, 32, 8, 2004, pp. 1323–39.
- 53 At ZAR 7.5 to the dollar, and a 40-hour work week, ZAR 1,000 a month is ZAR 6 per hour or 80 US cents.
- 54 Bantustans were the homelands (territories) set aside for black inhabitants of South Africa as part of the policy of apartheid.
- 55 See South Africa, the dti, 2010, *op. cit.*, p. 40.
- 56 See Hausmann R, Klinger B & R Lawrence, 'Examining Beneficiation', Centre for International Development Working Paper, 162. Boston, MA: Harvard University, 2008. This view is supported by the final recommendations of the International Growth Advisory Panel that advised South Africa on economic growth policies: 'Greater processing of natural resource exports does not constitute an easy or natural next step in the process of structural transformation, especially in South Africa [...] Privileging beneficiation is unwarranted and it takes Government's attention from other opportunities that may have more potential to create export jobs in South Africa.' See Hausmann R, 'Final Recommendations of the International Panel on ASGISA', Centre for International Development Working Paper, 161. Boston, MA: Harvard University, May 2008.
- 57 Anglo American Kumba Iron Ore, *Creating a Growing and Sustainable Iron & Steel Value Chain in South Africa*. Johannesburg: Anglo American, 2011.
- 58 SADC has the most complex rules of origin of the TFTA group. It uses a line-by-line approach and uses a combination of specific processing requirements, changes in tariff classification and material content percentage tests. COMESA and the EAC follow an across-the-board basis for determining origin. See Naumann R, 'Tripartite FTA State of Play on Preferential Rules of Origin', Tralac (Trade Law Centre for Southern Africa) Trade Brief. Stellenbosch: Tralac, March 2011.
- 59 For example, cabotage laws segment and distort the market for transport services by preventing transporters from operating outside the country in which they are registered. A Namibian registered truck with a shipment for Gaborone (Botswana) cannot pick up a load in Gaborone to take to Durban (South Africa). Similarly, a South African truck delivering goods to Oshkati (Namibia) cannot accept a consignment for delivery in Windhoek (Namibia). This is an area where services agreements are required for further integration. COMESA, for example, has a 'common carriers licence which registers transporters in all COMESA countries, allowing carriers to carry backloads and thus significantly reducing the costs of transport.' See Charalambides N, 'The Private Sector's Perspective, Priorities and Role in Regional Integration and Implications for Regional Trade Arrangements', European Centre for Development Policy Management Discussion Paper, 66. Maastricht: European Centre for Development Policy Management, 2005.
- 60 The need to liberalise trade in services is already recognised in SADC Trade Protocol (Article 23) and a draft Protocol on Trade and Services was developed in 2007. This covered the communication, construction, energy, financial, tourism and transport sectors. This protocol

was adopted in August 2012. See Cronjé JB, 'Trade in services and the regional integration process in southern Africa,' in McCarthy C *et al.* (eds), *Supporting Regional Integration in East and Southern Africa: Review of Select Issues*. Pretoria: Tralac, Stellenbosch and the Royal Danish Embassy (Danida), 2010.

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