

# **US Trade Strategy after Cancun: Prospects and Implications for the SACU–US FTA**

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# US Trade Strategy after Cancun: Prospects and Implications for the SACU–US FTA

Peter Draper and Mills Soko<sup>1</sup>

## Executive summary

The United States (US) and the five member states of Southern African Customs Union (SACU) — Botswana, Lesotho, Namibia, South Africa and Swaziland — have embarked upon negotiations aimed at concluding a free trade agreement (FTA) by December 2004. These negotiations form a vital part of the broader US competitive liberalisation strategy of opening key foreign markets through bilateral and regional free trade accords. They extend beyond the conventional trade negotiating agenda (market access for industrial and agricultural goods) and encompass the so-called ‘new generation’ trade policy issues such as trade in services, investment, competition policy, intellectual property rights as well as labour and environmental standards.

The purpose of this report is to highlight the contours of US trade strategy, as well as its prospects and implications for the SACU–US FTA negotiations. It is pointed out that the US–SACU FTA — the first of its kind in sub-Saharan Africa — constitutes a turning point in the growing trade and investment relationship between the US and SACU. It would enable the US to gain guaranteed preferential access to its largest export market in sub-Saharan Africa and allow it to

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'level the playing field' in sectors where its exporters feel that they have been disadvantaged by the South Africa–EU FTA.

For SACU countries the mooted FTA represents not only an opportunity to shore up their bilateral trade with the US, but also to build on the success of the African Growth and Opportunity Act (AGOA) while redressing some of its deficiencies. The SACU nations are the leading suppliers of non-fuel goods to the US under AGOA, accounting for more than a third of US non-fuel goods imports from eligible sub-Saharan African countries.

Yet, drawing on lessons learnt from the experiences of other US-inspired bilateral and regional FTAs, the report warns that the proposed US–SACU FTA raises an array of complex challenges that must be tackled if the FTA is to yield balanced and mutually beneficial outcomes. These challenges concern:

- the different levels of development and size of economies among the SACU countries;
- the issue of trade negotiating capacity given SACU's limited negotiating resources;
- the effect these negotiations will have on SACU institutions considering that SACU is embarking on this exercise in a context where its own institutions are in a major state of flux;
- the possible ramifications of a US–SACU FTA for the SADC regional integration process;
- the potential loss of revenue arising from the proposed FTA;
- the question of whether the US–SACU FTA can be seen as a panacea for regional development problems, especially in light of the fact that the region's comparative advantage lies in natural resources, which in their extraction are capital, not labour, intensive;
- the forthcoming US election and its likely impact on the imperative to extend 'trade promotion authority'; and

- the extent to which the proliferation of FTAs can be reconciled with the multilateral liberalisation agenda within the context of the WTO.

## Introduction

On 2 June 2003, the US and the five member states of SACU — Botswana, Lesotho, Namibia, South Africa and Swaziland — initiated negotiations in Pretoria designed to conclude an FTA by December 2004.<sup>2</sup> Not only did this event represent a watershed in the burgeoning trade and investment relationship between the US and SACU, it also heralded a new set of complex challenges that must be addressed if the FTA is to yield balanced and mutually beneficial outcomes.

This report examines contemporary US trade strategy; its prospects; and implications for the proposed SACU–US FTA negotiations. To this end, it deals with six issues. First, the report traces the historical origins of US trade policy. Second, it explains the shifts which US trade policy underwent in the 1970s and 1980s, laying the foundations for contemporary US trade strategy. Third, it discusses American trade strategy under the present Bush administration. Fourth, it analyses the motivations of both the US and SACU for the mooted FTA negotiations. Fifth, it outlines potential negotiating options and associated consequences for SACU of the FTA negotiations, drawing on lessons learnt from the experiences of the North American Free Trade Area (NAFTA), the Central American Free Trade Area (CAFTA), the Free Trade Area of the Americas (FTAA), and the US–Australia FTA. It concludes by reflecting on some future challenges stemming from the envisaged SACU–US trade deal.

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<sup>2</sup> Originally set up in 1910, SACU is the oldest customs union in the world.

## **US trade policy in historical context**

US trade policy has gone through two distinct historical epochs. The first, roughly spanning the period covering the emergence of the unified nation at the end of the Civil War until the Second World War, was characterised by increasing protectionism in which the Republican party played a dominant role. In this period the Republican-controlled Congress was firmly in charge of US trade policy, and viewed tariffs as their primary instrument of protection. Thus tariffs were generally high and arbitrarily imposed according to the whims of individual constituencies.<sup>3</sup> The result was a steadily declining share of trade in gross domestic product as business concentrated on the domestic market. In contrast, the domestic market was highly competitive, fuelled by a massive influx of migrants and capital from the old world. The domestic regulatory environment, underpinned by liberal philosophies, was designed to maintain this vigorous competition.

In the interregnum between the two great wars, the trade policy paradigm shifted in important respects. The Democrat Roosevelt Administration, led by Secretary of State Cordell Hull, sought and obtained limited authority from Congress to negotiate reciprocal tariff liberalisation agreements. This came in the form of the Reciprocal Trade Agreements Act (RTAA) of 1934, which empowered the State Department to conduct bilateral tariff negotiations. It also constituted the essential departure for subsequent Trade Negotiating Authority granted to the President. The RTAA was to comprise a key pillar of the General Agreement on Tariffs and Trade (GATT) system

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<sup>3</sup> See Chang Ha-Joon, *Kicking Away the Ladder? Policies and Institutions for Economic Development in Historical Perspective*. London: Anthem Press, 2002; Schlesinger AM, *The Cycles of American History*. London: Penguin Books, 1986, pp.132–135 offers a particularly illuminating account of this period. Also see Irwin DA, 'The aftermath of Hamilton's report on manufactures', *National Bureau of Economic Research, Working Paper 9943*, 2003.

that emerged after the Second World War.<sup>4</sup> Underlying this, the breakdown of the international economic order, partly owing to tariff wars between the major industrialised nations, persuaded US elites that a return to such forms of protection would be disastrous. However, this was only grudgingly acknowledged, and recognised by the Republican representatives in Congress as the price to be paid for sustaining a liberal international economic order.<sup>5</sup> The quid pro quo was the establishment of procedures for domestic industry to obtain relief from import competition.<sup>6</sup> This reticence was reflected in the early GATT rounds: it wasn't until the conclusion of the Kennedy Round in 1967 that major reductions were made to US tariffs, this time on a multilateral basis.<sup>7</sup>

Nonetheless the RTAA ushered in the second period in US trade policy history: that of US leadership in championing international trade liberalisation in the post-war period. At the end of the Second World War, most industrialised countries still pursued trade policies characterised by high tariffs, quantitative restrictions, exchange controls and bilateral trading arrangements. In part, this was a legacy of the Smoot-Hawley tariff and the virulent economic nationalism of the 1930s. Yet it was also a result of these countries' considerable demand for foreign exchange, which was essential to their securing the necessary materials for reconstruction.<sup>8</sup> However,

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<sup>4</sup> See Irwin DE, 'From Smoot-Hawley to reciprocal trade agreements: Changing the course of US trade policy in the 1930s', *National Bureau of Economic Research, Working Paper 5895*, 1997.

<sup>5</sup> So whilst Congress was prepared to tolerate the GATT, it would not countenance the formation of the proposed International Trade Organisation, as proposed by Keynes. That had to wait until 1994, and the formation of the World Trade Organisation.

<sup>6</sup> This became Article XIX of the GATT: the safeguards clause.

<sup>7</sup> Irwin DE, *op.cit.* p.33. Interestingly, he notes that the major source of effective tariff reductions in the post-war period was inflation, via relatively declining specific duties.

<sup>8</sup> Krueger AO, *American Trade Policy — A Tragedy in the Making*. Washington DC: The AEI Press, 1995, p.26.

recognising that they also required access to foreign markets to derive export earnings they too were prepared to acquiesce in the formation of the GATT.

In contrast, the US came out of the war with its productive capacity unharmed. Through the liberalisation of international merchandise trade, it sought to remodel the global economy in its own (internally) liberal image. Increasingly this was underpinned by a domestic bipartisan consensus in which new export interests were increasingly apparent. The latter recognised the opportunities available in reconstructing the shattered European and Japanese economies. And old protectionist interests, notably labour, did not feel threatened by import competition during this reconstruction phase.

However, in keeping with US trade policy's protectionist roots, and notwithstanding its support for free trade, the US maintained a protectionist trade regime in agriculture, clothing and textiles. This inconsistency can be traced to the agreement made by the major economic powers, mainly the US and Europe, at the inception of the GATT system that its rules would not apply to the agricultural sector. Thus the restrictions imposed by the GATT agreement on import quotas and export subsidies were waived in recognition of the 'specificity of the agricultural sector'; and price support programmes were preserved — a key EU requirement central to building the common agricultural policy.<sup>9</sup> Likewise the GATT created the Multifibre Agreement, which permitted industrialised nations to control textile imports either through the negotiation of bilateral quotas or through the application of flexible safeguard measures.

Apart from a determination to avert a repeat of the devastation wrought by the economic mercantilism of the 1930s, foreign policy concerns also played a central part in the endorsement of a liberal international trade system by successive US administrations. By

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<sup>9</sup> We are indebted to Geza Fekatekuty for this insight.



assuming the leadership of the open multilateral trading system, the US signalled that it was able and willing to underwrite the costs of providing international public goods to other states in return for their support and co-operation.

This played a crucial role in securing Europe's acquiescence in the GATT system. European countries needed access to the US security umbrella, in return for which GATT participation was required. The US sponsored trade liberalisation across Western Europe in two ways: through the Marshall Plan and through its leadership of consecutive rounds of tariff reductions under the GATT. The Marshall Plan was an essential part of the US strategy to multilateralise the bilateral trade and payments system that underpinned European reconstruction efforts.<sup>10</sup> Furthermore, Cold War rivalry between the US and the Soviet Union led the former to prioritise the economic advancement of its allies and pledge to guarantee their security. The US-Japan relationship during this period is illustrative of this policy. In a quest to 'contain' the spread of Soviet communism, the US backed Japan in a number of ways, including: supporting Japanese economic growth and paying for its defence requirements; providing Japan with cheap technology transfers; and opening its markets to Japanese exports without demanding reciprocity.<sup>11</sup>

### **The shift to aggressive unilateralism**

In the early 1970s US leadership of the open multilateral trading system underwent a fundamental reorientation. This was triggered principally by the declining relative position of the US in the global economy. The weakening of US hegemony stemmed partly from the enormous structural changes the global economy had undergone by the 1970s, characterised mainly by the internationalisation of

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<sup>10</sup> *Ibid.*, pp.29–30.

<sup>11</sup> See Dobson AP & S Marsh, *US Foreign Policy Since 1945*. London: Routledge, 2001.

production processes and the realignment of the industrial hierarchies of the world. These changes were driven by the resurgence of Europe, the emergence of Japan as a great economic power, and the ascendancy of the 'tiger economies' of East Asia. Japan's rapid technological progress and the emergence of the newly industrialising economies (NICs), in particular, considerably increased the number of manufacturing exporters at the same time as the volume of world trade was decreasing and world markets were closing. Significantly, these emergent economic powers were combining highly sophisticated productive techniques with the customary low-wage advantage of developing nations. Ironically their success could at least in part be explained by prior US efforts to build their economies, utilising trade preferences and unconditional aid flows, as part of the broader construction of an anti-communist bloc.

This intensification of competition led to increased US protectionism against Japanese and NIC exports in particular. As such, the decline of American leadership was accompanied by the erosion of support on the part of the US for the qualified ideal of free trade, especially the principles and norms — enshrined in GATT — that had guided the international trading regime since 1945.<sup>12</sup> However, it still bears emphasising that the decline in American support for the global trade system did not imply a complete abdication of its multilateral obligations. To be sure, the US played a key role in initiating the Tokyo and Uruguay Rounds of trade negotiations.<sup>13</sup> And in recent years the US also played a leading part in the creation of the WTO and the launch of the Doha Round. Yet these actions took place in a context where the US was no longer willing to use its power and resources unconditionally, in a spirit of enlightened self-interest, to maintain collective goods for the

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<sup>12</sup> Reich R, 'Beyond free trade', *Foreign Affairs*, 61, 4, Spring 1983, pp.780–781.

<sup>13</sup> Spero JE & JA Hart, *The Politics of International Economic Relations*. London: Routledge, 1997, pp.49–95.

international community and underwrite the costs of the liberal international economic order.<sup>14</sup>

Furthermore, the post-war period marked a turning point in the institutional management of US trade policy. In order to curtail the State Department's powers and increase the executive's accountability in trade matters Congress created the office of the Special Trade Representative in the Presidency in the early 1960s. Following the conclusion of the Kennedy Round, in which for the first time non-tariff issues had come to the fore,<sup>15</sup> Congress had refused to implement key agreements. This process culminated in the passage of the 1974 Trade Act. That dramatically boosted the powers of the Executive in negotiating trade agreements subject to 'fast track' negotiating authority, now extending beyond tariffs. The quid pro quo was the establishment of structured consultative processes in the form of the private-sector advisory committee system and increased Congressional oversight of trade negotiations.

However, as Stokes and Choate argue,<sup>16</sup> this had the unintended effect of greatly complicating the trade policy process as it opened up to a host of new interested parties.<sup>17</sup> Thus new, previously 'non-trade' issues, appeared on the trade policy agenda. And as Bergsten notes<sup>18</sup>, these interests have to be assuaged to some extent if the

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<sup>14</sup> See Ikenberry JG, 'State power and the institutional bargain: America's ambivalent economic and security multilateralism', in Foot R, MacFarlane N & M Mastanduno (eds), *US Hegemony and International Organisations*. Oxford: Oxford University Press, 2003.

<sup>15</sup> Notably customs valuation and anti-dumping.

<sup>16</sup> Stokes B & P Choate, 'Democratising US trade policy', a Council on Foreign Relations Paper, 2001, pp.15–17.

<sup>17</sup> Mitigated by the fact that by tying congress down to single votes on trade agreements, and trading partners being able to negotiate with a single office in the Executive rather than 535 Senators and Representatives, processes have become correspondingly less complex. We are indebted to Alan Tousseignant for this insight.

<sup>18</sup> Bergsten FC, 'A renaissance for United States trade policy?', *Foreign Affairs*, November/December 2002.

broader process of US-led trade liberalisation is to advance. Furthermore, Stokes and Choate note that these processes were conducted within a relatively small circle of participants, sowing seeds of future distrust and battles to come over the direction and control of US trade policy. In the 1980s and 1990s these concerns fused with growing discontent over the perceived costs associated with trade liberalisation, manifested in the growing anti-globalisation lobby.

Consequently, at a time when international competition was escalating dramatically, domestic consensus on trade policy matters was becoming far more difficult to achieve. Internationally, the increasing complexities and ever-expanding terrain of trade negotiations translated into multilateral rounds taking far longer to conclude. Nonetheless, the Nixon Administration initiated negotiations in the Tokyo Round, ultimately extending the ambit of the GATT into new areas in the form of plurilateral agreements.<sup>19</sup> For the first time developing countries' interests were reflected in various special and differential treatment provisions (SDT).<sup>20</sup> The Uruguay Round subsequently expanded the scope still wider and converted most of these plurilateral codes to all members.

US concerns over the increasing complexities of launching and concluding multilateral agreements were partly addressed through recourse to bilateralism. This culminated in the North American Free Trade Agreement in 1992 (NAFTA). To some extent this was a response to growing US frustrations over the length of time taken to

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<sup>19</sup> Notably product standards and government procurement. For a useful overview of the issues covered in various rounds see Hoekman BM & MM Kostecki, *The Political Economy of the World Trading System — The WTO and Beyond*. Oxford: Oxford University Press, 2001, pp.100–108.

<sup>20</sup> Many of them were former colonies which the US and Europe were reluctant to see residing in the Soviet orbit. Hence the generosity, contrasted with the Uruguay Round strictness in the application of SDT principles. For an analysis of SDT in the context of the current Doha Round, see Draper P & N Khumalo, 'Smoke and mirrors: Africa, special and differential treatment, and the Doha Development Agenda', *SAILA Trade Policy Briefing No. 2*, September 2003.

secure sufficient consensus to launch the Uruguay Round, itself a reflection of the ever-widening agenda and increasing number of participants. Nonetheless it represents a partial return to the RTAA framework, a tendency that may be gathering pace. But it also reflected a broader United States Trade Representative (USTR) strategy to put pressure on the multilateral process through 'competitive liberalisation',<sup>21</sup> a strategy much in evidence today.<sup>22</sup> However, it is important to note that NAFTA was also driven by the Canadian and Mexican governments' desire to lock in preferential access to the US market. US responsiveness to such concerns from key trading partners also partly characterises their trade policy today.

So by the 1980s the stage had been set for US trade policy to assume a double-pronged character. On the one hand, it embraced a more cautious commitment to multilateralism. On the other hand, it exhibited a growing penchant for 'aggressive unilateralism'. This was required in order to convince Congress that the USTR was achieving its stated objectives of opening foreign markets to US goods. It entailed the use of retaliatory measures against countries deemed to be engaging in 'unfair' and 'unreasonable' trade practices. These actions are authorised in terms of the Super 301 and Special 301 provisions of Section 301 of the Trade and Tariff Act. Super 301 requires the USTR to compile a list of external trade barriers, identify a priority list of countries and their unfair trading practices, and set a deadline for progress in rectifying these practices. If the designated countries fail to comply, the US institutes retaliatory actions against them. Special 301 operates in a more or less similar manner to Super 301, except that it is specifically targeted at infringements of intellectual property rights. Although these

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<sup>21</sup> The term is attributed to the current USTR, Ambassador Zoellick. See Zoellick R, 'Unleashing the trade winds', *The Economist*, 7 December 2002.

<sup>22</sup> See Feinberg RE, 'The political economy of United States' free trade agreements', Blackwell Publishing Ltd, mimeo, 2003.

provisions were originally directed at Japan, they have been used widely in recent years.<sup>23</sup>

## **US trade policy and the Bush administration**

Contemporary American trade policy is predicated on two pillars. The first is, in some quarters, a visceral distrust of economic multilateralism, reinforced by the failed Seattle and Cancun ministerial meetings in 1999 and 2003 respectively. The second pillar is a resurgence of the aggressive unilateralism that epitomised US trade policy in the 1970s and 1980s.<sup>24</sup> Under the current Bush administration the unilateralist and associated bilateralist streak has without doubt predominated.

The past few years have witnessed a significant increase in US interest in bilateral and regional trading arrangements. These form an integral part of the broader 'competitive liberalisation' strategy of opening key foreign markets through bilateral and regional free trade accords. And they extend beyond the traditional trade negotiating agenda — market access for industrial and agricultural goods — to cover the so-called 'new generation' trade policy issues such as trade in services, investment, competition policy, intellectual property rights as well as labour and environmental standards. The USTR views current US trade policy as essential to forcing other countries, especially those whose actions are considered to be wayward, to return to the multilateral trade arena. The US has concluded bilateral FTA negotiations with an array of countries, including Singapore, Chile, Australia, Israel, Jordan and Morocco. These have been complemented by an expanding number of

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<sup>23</sup> For a detailed discussion of the policy of 'aggressive unilateralism' see Bhagwati J & PT Hugh, *Aggressive Unilateralism — America's 301 Trade Policy and the World Trading System*. Michigan: The University of Michigan Press, 1990, pp.1–48.

<sup>24</sup> Higgott R, 'The limits to multilateral economic governance'. A paper presented before the Council for Asia–Europe Co-operation Task Force on Global Governance, Seoul, 26–28 September 2003, p.18.

regional FTA arrangements, including the recently concluded pact between the US and the Central American Free Trade Agreement (CAFTA).

The US has not been alone in its drive to push for comprehensive trade liberalisation. Although in its rhetoric the EU extols the virtues of multilateral trade, it is equally determined to use bilateral deals in order to attain its goal of opening up developing country markets. Japan has recently followed suit by concluding a free trade deal with Singapore and is exploring several others. And China is in the process of establishing its own frameworks.

Although bilateral and regional FTAs are permitted under Article 24 of the General Agreement on Tariffs and Trade (GATT), such trade arrangements have been criticised for undermining multilateral trade and distorting the global trade system. FTAs have been condemned for offering free trade to countries that participate in them and excluding those which do not. They have also been blamed for encumbering trade with discrimination, creating a web of trade duties and barriers that vary according to source. Furthermore, they have been condemned for weakening the bargaining strength of poor countries in the WTO system and for preventing the emergence of developing country coalitions as they ditch principle in favour of wringing small concessions from the powerful negotiating partner.<sup>25</sup> Some commentators regard the acceleration of this tendency as alarming, with the Bush Administration being the primary culprit.<sup>26</sup>

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<sup>25</sup> Bhagwati J, *Free Trade Today*. Princeton: Princeton University Press, 2002.

<sup>26</sup> Gordon BK, 'A high risk trade policy', *Foreign Affairs*, July/August, 2003. He is primarily concerned with the implications of the possible emergence of an East Asian economic bloc, potentially encompassing China and Japan, for US exports to that part of the world. He sees such a bloc as potentially threatening US security interests in East Asia. Furthermore, he makes the interesting observation that US exports are divided roughly evenly between the Americas, Europe, and North East Asia based on which he concludes that multilateralism is the best route for pursuing US interests.

There is some concern that the failure of the Cancun ministerial summit may strengthen the unilateralist and bilateral impulses in US trade policy. In the aftermath of Cancun the US made it clear that failure to achieve progress in the Doha Round could result in it accelerating its efforts to conclude bilateral and regional free trade agreements. Tied to this has been a propensity to subsume trade policy within the wider imperatives of the US-led war against global terrorism. In the wake of the 11 September 2001 terrorist attacks, the Bush administration has argued that free trade is the best means to improve global economic development and foster peaceful co-existence among different nations. Indeed, the launch of the Doha Round in 2001 was justified on the grounds that it would contribute to the war against terrorism in the same way as trade was viewed as an antidote to communism at the height of the Cold War.<sup>27</sup> In this respect political and security calculations are as important as economic ones in the determination of US bilateral trading arrangements.

The cases of Singapore and Australia have shown that countries that have supported the Bush administration's foreign economic and security policies, and have co-operated with the US in their implementation, have been duly rewarded. On the contrary, countries that have challenged US policies (such as New Zealand and Egypt which respectively opposed the Iraq war and failed to support the US case against the EU on the issue of genetically modified products) have been either excluded from free trade negotiations or had them delayed.<sup>28</sup> Thanks to American pressure and arm-twisting, several Central and South American countries (notably Costa Rica, Guatemala, Colombia and Peru) pulled out from the G20+ coalition, citing the politicisation of this group as the reason for their withdrawal. On 17 December 2003, the CAFTA

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<sup>27</sup> See Zoellick R, 'The WTO and new global trade negotiations: What's at stake'. A speech presented before the Council on Foreign Relations, Washington, D.C., 30 October 2001.

<sup>28</sup> Higgott, *op. cit.*, p.20.



countries completed FTA negotiations with the US, signalling that their long-term economic interests are tied to those of the US.<sup>29</sup> It was only recently that the Bush administration announced that Canadian firms would now be allowed to bid for US-financed reconstruction projects in Iraq: Canada had previously been barred from bidding for such contracts because it had not supported the US-led invasion of Iraq. These examples provide a graphic illustration of how a dominant state such as the US can employ trade as a weapon to alter the behaviour of other states and to advance particular strategic goals in the international system.

If the current trajectory of US trade policy persists, it is likely that future US engagement with its trade partners will be conditional more than ever before upon the willingness of these countries to support American national security or foreign policy interests. This raises questions about how this US policy will affect South Africa, given the latter's anti-Iraq war stance and its prominent role within the G20+ in Cancun. Indeed, Charles Grassley, chairman of the US Senate committee on finance, warned after the Cancun fiasco that the US would in future determine the suitability of countries seeking bilateral trade pacts with it by the way they conducted themselves in Cancun.<sup>30</sup>

## **Motivations for the proposed US–SACU FTA negotiations**

The US regards an FTA with SACU countries — its first FTA in sub-Saharan Africa — as essential to realising its objective to prise open

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<sup>29</sup> The CAFTA is made up of El Salvador, Guatemala, Honduras, Nicaragua and Costa Rica. It is worth noting that the Costa Rican government temporarily pulled out of the US–CAFTA negotiations — it only joined on 25 January 2004 — in response to domestic protests against US demands to open the country's telecommunication and insurance sectors to foreign competition. The US has begun negotiations with the Dominican Republic, which it seeks to bring into the CAFTA negotiations in 2005 in a process known as 'docking', before Congress ratifies the agreement.

<sup>30</sup> 'Crushed at Cancun', *Financial Times*, 15 September 2003.

these countries' economies to its commercial interests. This forms a vital part of American 'commercial diplomacy' — the intersection of foreign policy, government power and business transactions — in terms of which the US deploys its official weight to help firms gain access to foreign markets.<sup>31</sup> An FTA would enable the US to gain guaranteed preferential access to its largest export market in sub-Saharan Africa, which accounted for nearly \$3.1 billion and \$2.5 billion of US exports in 2001 and 2002 respectively. Leading US exports in the SACU region include machinery, vehicles, aircraft, medical instruments, plastics, chemicals, cereals, pharmaceuticals, and wood and paper products. Total bilateral trade between the US and SACU amounted to approximately \$7 billion and \$7.3 billion in 2001 and 2002 respectively. US foreign direct investment in the SACU region totalled \$2.8 billion in 2000, mainly in the manufacturing, wholesale and services sectors. The SACU nations are the most important suppliers of non-fuel goods to the US under AGOA, accounting for more than a third of US non-fuel goods imports from eligible sub-Saharan African countries.<sup>32</sup>

Through an FTA, the US also seeks to level the playing field in sectors where US exporters feel that they have been disadvantaged by the South Africa–EU free trade accord. In this regard the US is likely to focus its efforts on sectors where its domestic industries compete for market share with the EU. The US has also argued that bilateral and regional FTAs provide an impetus for competitive liberalisation at the multilateral level and contribute towards advancing common objectives in the WTO. Furthermore, in the same way as the North American Free Trade Agreement (NAFTA) was viewed as a catalyst for political and economic reforms in Mexico after 71 years of unbroken Institutional Revolutionary Party rule, the mooted FTA between the US and SACU has been touted by

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<sup>31</sup> See Guyatt N, *Another American Century? The United States and the World after 2000*. London: Zed Books, 2000, p.185.

<sup>32</sup> Office of the USTR, 'US and Southern African nations plan for upcoming FTA negotiations'. Press Release, 13 January 2003.

some commentators in the US, and in SACU countries, as essential to fostering political and economic reform in the SACU member countries.

On the trade front the most important piece of reform was the signing of the re-negotiated SACU Agreement by the five member states in October 2002. Not only does this Agreement provide for a new democratic institutional structure, it enables the member countries to carry out future trade relations and negotiations with third parties as a single entity. It also provides for the harmonisation of policies on competition, industrial development, agriculture, and unfair trade practices within the wider common SACU economy. In addition, the SACU Agreement substantially revised the revenue-sharing formula and provides for the creation of a dispute settlement mechanism. Along with supporting these institutional reforms,<sup>33</sup> it is envisaged that a free trade zone with the US would improve the commercial competitiveness of SACU nations, help them attract much-needed foreign direct investment, and consolidate regional integration in Southern Africa.<sup>34</sup>

For SACU members the proposed FTA accord represents not only an opportunity to bolster their bilateral trade with the US, but also to build on the success of AGOA while redressing some of its shortcomings. Introduced in October 2000, AGOA is a crucial part of the American trade and investment policy toward sub-Saharan Africa, designed to promote free markets and expand US–African trade and investment. With 38 beneficiaries, AGOA designates over 1,800 products from sub-Saharan Africa for duty-free access to the

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<sup>33</sup> The negotiations will present considerable challenges too, notably pressure to harmonise policies in the broad range of areas not covered by the agreement. For an interesting analysis of the institutional status of the SACU agreement see Kirk R & M Stern, 'The new Southern African customs union agreement', *World Bank Africa Region Working Paper Series*, 57, June 2003.

<sup>34</sup> Notwithstanding these notable achievements the SACU agreement does not cover services, an obvious shortcoming. Thus the services negotiations in the SACU–US FTA will be complex.

US — in addition to the 4,650 products already eligible under the Generalised System of Preferences (GSP). This is in line with the policy of ‘trade not aid’ initiated by the Clinton administration in the late 1990s in terms of which the US undertook to spearhead a trade and investment drive in Africa that would compensate for reductions in its aid to the continent.

By most accounts SACU countries have scored relative gains from their participation in AGOA. They are the leading AGOA beneficiaries in sub-Saharan Africa. Thanks to its relatively diversified economy, South Africa has been the biggest provider of these non-fuel exports to the US. Lesotho is the leading exporter of clothing goods, while Botswana, Namibia and Swaziland recorded a 40%–75% increase in their total exports to the US in 2002.<sup>35</sup> Furthermore, an FTA will provide an opportunity to lock in market access to the US market in apparel products, in the context of the impending expiration of the WTO’s multi-fibre arrangement. US imports of apparel products from SACU countries are highly quota constrained.<sup>36</sup> Once these quotas are lifted competition from China in particular will escalate, requiring a degree of privileged market access for SACU exporters if their industries are to be sustained.

Yet critics of AGOA have argued that its key shortcoming is that it is a unilateral trade initiative that can be withdrawn arbitrarily by the US administration.<sup>37</sup> Furthermore, as South Africa’s trade minister, Alec Erwin, pointed out in his post-Cancun address to South Africa’s Parliament, preferences are pernicious: not only do they create dependencies, but those dependencies are used as

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<sup>35</sup> Office of the USTR, January, *op.cit.*

<sup>36</sup> US International Trade Commission, *Textiles and Apparel: Assessment of the Competitiveness of Certain Foreign Suppliers to the US Market*, Investigation No. 332–448, 2004.

<sup>37</sup> There is precedence for this. For example, recently renewal of the Andean Community Initiative was held up in the US Congress for six months; and India’s challenge to the EU’s GSP scheme in the WTO has generated substantial fears in preference-receiving developing countries. AGOA is subject to annual reviews.

bargaining chips in trade negotiations.<sup>38</sup> Therefore, critics of AGOA have pointed out that a free trade treaty is more preferable as not only would it be more difficult to rescind but it would also include goods not covered by AGOA. Hopefully this would include key agricultural commodities such as sugar and tobacco, which are currently excluded.

These views have been echoed by a study that has cast doubts on whether AGOA will create new export opportunities for South African products. This, the study argues, is due to the fact that before the advent of AGOA, US tariffs on South African exports were already low. It points out, however, that some South African agricultural exports (such as pears, avocados, oranges, pimientos, citrus juice and grape juice) have benefited enormously from AGOA, recording exponential growth over the last few years. These products could benefit further from a two-way trade agreement with the US. Furthermore, the study argues that although some clothing exports have gained from AGOA, a considerable share of clothing products does not qualify for AGOA preferences. This is because the rules of origin — which favour the least developed nations and not South Africa — have prevented South African clothing producers from accessing AGOA benefits.<sup>39</sup>

Proponents of a US–SACU FTA have alluded to the special status a free trade area will bestow upon SACU. However, as the experience of Mexico has shown, an FTA does not necessarily translate into a special trade status. Since its accession to the WTO in 2001, China has displaced Mexico as the second biggest exporter (after Canada) to the US. Even though Chinese manufactures are subject to duties, they are generally far cheaper than Mexican products. China has also replaced Mexico as the favoured destination for multinational

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<sup>38</sup> Alec Erwin, Minister of Trade and Industry, address to the South African National Assembly, 'Statement on the 5<sup>th</sup> Ministerial Meeting of the World Trade Organisation held at Cancun, Mexico, in September 2003', 26 September 2003.

<sup>39</sup> See Stern M & N Netshitomboni, 'AGOA, Africa and agriculture — A case study of South Africa', *SAIIA Trade Policy Report No. 3*, 2004.

companies seeking cheap labour. Moreover, several other countries, including most Caribbean nations, now enjoy the same trade status with the US as Mexico. In recent years a growing number of clothing and textile companies have moved from Mexico to lower-cost destinations such as Honduras and Costa Rica.<sup>40</sup> Furthermore, in the admittedly unlikely event that the Doha Development Agenda concludes an ambitious tariff liberalisation deal, the value of preferential access into the US market will decline accordingly.<sup>41</sup>

Offsetting this is the strategic opportunity to lock in access to the US market in the context of a secular decline in support for trade liberalisation there. This is reflected in the enormous difficulties modern US Presidents have in obtaining trade promotion authority. Thus in the current presidential election cycle trade has returned to centre stage and is increasingly divisive. According to this argument, the FTA represents an 'insurance strategy' against a possible US retreat into protectionism.

### **The SACU–US FTA: Prospects and implications**

On 4 November 2002, the USTR, Robert Zoellick, sent a letter to the US Congress notifying it of the US administration's intention to initiate FTA negotiations with SACU. The letter identified several areas that the US wanted the negotiations to focus on. The following discussion deals with some of the contentious items on the negotiating agenda, namely: trade in industrial goods; agricultural trade; rules of origin; intellectual property rights and enforcement co-operation; trade in services; investment; government

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<sup>40</sup> Kraul C, 'After initial boom, Mexico's economy goes bust', *Los Angeles Times*, 2 January 2004.

<sup>41</sup> The USTR has proposed that all tariffs be reduced to zero by 2015.

procurement; trade remedies; labour standards; environmental standards; and dispute settlement.<sup>42</sup>

### *Trade in industrial goods*

The US seeks to remove tariffs and other duties on trade between the US and the SACU countries on the broadest possible basis, subject to reasonable adjustment periods for import-sensitive products. It also wants to eliminate non-tariff barriers in the SACU countries to US exports, including licensing barriers, unjustified trade restrictions that affect new US technologies as well as other non-tariff measures identified by US exporters. This has important ramifications for the SACU trade regime, with its complex tariff system and its lack of common policies for certain non-tariff measures, such as quantitative restrictions, customs procedures, standards and technical regulations, and sanitary and phytosanitary measures.

The US–CAFTA FTA stipulates that textiles and apparel from Central America will immediately enter the US duty-free and quota-free if they meet the agreement’s rule of origin. A notable provision of the pact gives duty-free benefits to some apparel made in Central America as long as it contains certain fabrics from NAFTA partners, Mexico and Canada. This is designed to promote the integration of the North and Central American textile industries. Moreover, apparel containing certain fabrics and materials in ‘short supply’ in the US and Central America may also qualify for duty-free treatment. The list of these ‘short supply’ materials has been developed in consultation with the apparel and textile industry in the US and Central America. The US has concluded a virtually similar deal with Morocco, which provides for duty-free imports in textiles and apparel trade if these meet the agreement’s rule of origin

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<sup>42</sup> See letter sent by the USTR, Robert Zoellick, to the President of the Senate, Robert C Byrd, and the Speaker of the House of Representatives, Dennis J Hastert, 4 November 2002.

and which requires eligible apparel to contain either US or Moroccan yarn and fabric. It also contains a temporary 30 million square metre allowance for apparel that includes third country content (equal to 0.2% of imports into the US).<sup>43</sup> This has obvious relevance for SACU.

Already, the 'lesser developed beneficiary' status enjoyed by Lesotho and Swaziland allows them, in the short term, to source textile and clothing inputs from anywhere across the world. Botswana and Namibia also enjoy access to this provision through an AGOA amendment owing to the fact that they do not have domestic textiles industries. However, this provision expires at the end of 2004.<sup>44</sup> A case could be made by SACU for a flexible interpretation of the rules of origin to enable the small SACU members to bolster their domestic manufacturing capacity. In the longer term, once quotas have expired, such flexibility may be essential in order to deal with competition from more efficient Asian producers. How the region shapes up in the face of that challenge is a critical issue.<sup>45</sup>

But the SACU countries should brace themselves for tough political horse-trading in the negotiations. For the US-CAFTA agreement bears the hallmarks of a fragile political compromise. For example, the US textile industry pushed for rules to prevent the Central American nations from being used as a gateway for textiles and clothing produced elsewhere in the world for duty-free shipment to the US. And textile-producing states, particularly in the south, are likely to prove vital in the forthcoming US presidential

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<sup>43</sup> Office of the USTR, 'Free Trade with Morocco — A vital step toward Middle East free trade', 2 March 2004, p.1.

<sup>44</sup> Although it may be extended as part of an AGOA 3 package currently before Congress.

<sup>45</sup> It seems that US importers have identified two sub-Saharan African hubs for clothing and textiles sourcing: Senegal and Ghana in West Africa, and SACU. Confidential Washington Interview, August 2003. This would fit in with the International Trade Commission's depiction of non-Asian suppliers being downgraded to second-tier 'hub' status in the post ATC world. USITC, *op.cit.*



elections. It is also worth noting that both the US and the Central American countries succeeded in exempting their most sensitive goods from immediate competition. The US preserved protections for their sugar and textile industries in exchange for lengthy phase-out periods linked to tariff quotas of up to 20 years for tariffs on Central American corn, dairy and other farm products. And in the final analysis it should be asked how much additional market access SACU countries stand to gain: already 95% of goods exported to the US market are duty free.<sup>46</sup>

### *Agriculture*

Agriculture remains a key generator of rural income and employment as well as an important foreign exchange earner in all the SACU countries. For SACU the liberalisation of agricultural trade is imperative. But the US has indicated that it is not prepared to consider the problem of agricultural export subsidies outside the WTO framework. Rather, it has announced its intention to pursue a mechanism with the SACU countries that will support achieving the US objective in the WTO negotiations of eliminating all export subsidies on agricultural products. This implies that SACU will not be able to use the FTA negotiations to address comprehensively the three key pillars of agriculture at the heart of the Doha negotiations deadlock: bigger reduction in domestic support; a sound commitment on elimination of all export subsidies; and greater commitment to market access. Furthermore, the US has also argued that FTA members should not be permitted to exclude big sectors such as agriculture from their ambit. This may not be an insurmountable problem as apparently the only US products exported to sub-Saharan Africa that attract export subsidies are to be

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<sup>46</sup> Stern M & N Netshitomboni, *op.cit.*

found in the dairy sector.<sup>47</sup> Bigger problems are likely to derive from US domestic support systems.

In its other FTA negotiations, agricultural trade has generally been dealt with on an à la carte basis through a mixture of high tariffs, quotas, and tariff quotas. In the US–Morocco agreement, Morocco will provide immediate duty-free access on a range of US products, including pistachios, pecans, frozen potatoes, whey products, processed poultry products, pizza cheese and breakfast cereals. Tariffs on other products will be phased out in five years, including walnuts, grapes, pears, cherries and ground turkey. The US, for its part, has agreed to phase out all agricultural tariffs within fifteen years, although it will maintain an agricultural safeguard in cases where prices decrease considerably for certain horticultural products.<sup>48</sup> In the US–CAFTA pact, more than half of current US farm exports to Central America will become duty-free immediately, including beef, cotton, wheat, soybeans, fruits and vegetables, processed food products and wine. Tariffs on most US farm products will be phased out within 15 years. These products include pork, beef, poultry, rice, corn, processed products and dairy products.<sup>49</sup> On the other hand, CAFTA sugar quotas have been considerably expanded. However, the agreement met fierce opposition from sugar beet and sugar cane farmers in the US, who fear that competition would increase if sugar from Central America were allowed into the US without steep tariffs imposed on sugar imports from other countries. Notwithstanding the Australian sugar industry's fate, SACU should hold out for a similar deal.

This fear explains why there was a delay on the part of the US in finalising an FTA with Australia, a bigger economy with highly competitive farm products. The Australia–US (AUSTA) deal provides for the elimination of tariffs on more than 99% of US industrial

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<sup>47</sup> Confidential interview in Washington, D.C, August 2003.

<sup>48</sup> Office of the USTR, 'Free trade with Morocco', *op. cit.*, p.1.

<sup>49</sup> Office of the USTR, 'Free trade with Central America — Summary of the US–Central America free trade agreement', Fact Sheet, 17 December 2003, p.1.

exports to Australia with immediate effect. It also provides for the dropping of tariffs on all US agricultural exports to Australia. However, the US declined to grant Australia additional market access for its sugar — even though most Australian goods were given duty-free access to the US market. It is believed that in return for maintaining the protection of its sugar industry, the US allowed Australia to keep restrictions on its wheat marketing, broadcasting, and pharmaceutical benefits schemes. Furthermore, the US government allayed its farmers' concerns about increases in Australian beef and dairy imports by negotiating lengthy (18 year) and slow market openings — less than a quarter of 1% — in these products.<sup>50</sup> The outcome of the Australia–US negotiations represents a political victory for US sugar producers, who had claimed that an expansion of Australian sugar quotas would wipe out the US sugar industry. The powerful sugar industry is a major campaign contributor, donating approximately \$20 million to US politicians since 1990. The Washington-based Centre for Responsive Politics has revealed that President Bush was the biggest recipient of the sugar lobby's largesse in 2000.<sup>51</sup>

Another issue on the US negotiating agenda is the matter of sanitary and phytosanitary (SPS) measures. The US wants to strengthen co-operation with SACU countries in implementing the WTO SPS Agreement. In the US–CAFTA agreement, the US and Central American countries resolved to work towards removing sanitary and phytosanitary barriers to agricultural trade, especially problems and delays in food inspection procedures for meat and poultry. Developing the technical and institutional capacity of SACU to implement SPS requirements is central to its objective of fostering further development and diversification of the agricultural sector with a view to improving access to global markets for farm products.

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<sup>50</sup> The AUSTA agreement authorises the US to use tariff-rate quotas in the beef and dairy sectors.

<sup>51</sup> 'Sweet deal', *Financial Times*, 12 February 2004.

### *Intellectual property rights*

The US seeks to establish standards that reflect a level of protection similar to that found in South African law and which build on the multilateral disciplines contained in the WTO Agreement on Trade-Related Aspects of Intellectual Property (TRIPS) and other international intellectual property agreements. It also wants to extract commitments from SACU countries that they will considerably strengthen their domestic enforcement procedures, such as by ensuring that government agencies may initiate criminal proceedings on their own initiative and confiscate suspected pirated and counterfeit goods.<sup>52</sup>

In addition, the US seeks to strengthen measures in SACU countries that provide for compensation of right holders for infringements of intellectual property rights and to provide for criminal penalties under the laws of SACU countries. The issue of intellectual property protection was raised frequently by various WTO member states during the SACU Trade Policy Review in 2003. Whilst South Africa complies fully with its WTO obligations in this regard, its SACU partners have been actively implementing measures to bring their law into compliance.

Enforcing intellectual property protection has posed many challenges for WTO members. For example, in its negotiations with Australia the US had pushed for higher prices on generic pharmaceuticals to reward the intellectual property of US drug makers. To this end, the USTR requested amendments to Australia's Pharmaceutical Benefits Scheme (PBS). The US–Australia agreement enjoins Australia to make several improvements in its PBS procedures in order to enhance transparency and accountability in its operation, including the setting up of an independent process to review determinations of product listings. Furthermore, the FTA sets up a medicines working group to promote the agreement's public

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<sup>52</sup> This is targeted partly at organised crime syndicates operating in the region, a concern shared by South African business.

health principles through dialogue between the US and Australia.<sup>53</sup> This has important implications for the US–SACU negotiations, especially in light of recent moves by South Africa’s Department of Health to regulate medicine prices. Furthermore, concerns have been expressed about the adverse impact the intellectual property protection regime might have on the ability of SACU countries to effectively tackle pandemics such as HIV/Aids, malaria and tuberculosis. The extent to which these anxieties can be addressed will partly depend on the degree of progress made in implementing the pre-Cancun WTO agreement permitting developing countries faced with public health emergencies to override patents and import copies of life-saving drugs.<sup>54</sup>

### *Trade in services*

The US intends to push vigorously for the elimination of market access barriers to trade in SACU countries’ services markets.<sup>55</sup> In the US–CAFTA agreement, the CAFTA countries agreed to accord substantial market access across their services regime, using the so-called ‘negative list’ approach in terms of which market access commitments apply across all sectors.<sup>56</sup> This has important implications for SACU countries, which have made the creation of an efficient services sector a key priority. Whilst the services sector is not part of the new SACU Agreement, there exists already a high degree of services integration in the SACU region. However, there is

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<sup>53</sup> Office of the USTR, ‘US and Australia complete free trade agreement’, 8 February 2004, p.4.

<sup>54</sup> There is cause for concern that the agreement will not deliver on its promises. See Pugatch M, ‘What Does the WTO Deal on Drugs Patents Achieve?’, in Draper P & S Gruzd (eds), ‘Africa after Cancun: Trade negotiations in uncertain times’, *SAIIA Trade Policy Report No. 2*, 2003.

<sup>55</sup> Analysis indicates that these barriers apply equally to domestic and foreign services providers. Thus liberalisation would benefit both. We are indebted to Matthew Stern for pointing this out.

<sup>56</sup> Office of the USTR, 8 February 2004, *op. cit.*, p.2.

recognition among policymakers that some problems — such as infrastructural deficiencies and financial constraints — ought to be addressed if economy-wide efficiency gains are to be realised.<sup>57</sup> The paramount challenge facing SACU trade negotiators in this regard is to strike a balance between the imperatives of services reform with the necessity to secure member countries' socio-economic objectives.

If the US's tariff offer, viewed in combination with the rules of origin that regulate industrial location, is not sufficiently attractive to SACU countries, then the latter are likely to be commensurately less ambitious in the services negotiations. Unfortunately the US–Chile FTA does not seem to provide a good precedent in this regard. According to Whalley and Leith,<sup>58</sup> that agreement could be characterised as 'primarily an asymmetric package for the liberalisation of non-manufactures trade barriers'. They argue further that 'if a US–SACU negotiation takes this same direction, its evaluation on the SACU side may be influenced by this perception'. The result would be less liberalisation in the services sector.

It is interesting that SACU's approach has been to opt for a 'positive list' negotiation, in terms of which only those commitments scheduled will apply and everything else is excluded. Clearly this is diametrically opposed to US objectives; consequently this negotiating area will be especially important. These considerations go to the heart of the furore over the decision by Costa Rica, Central America's most developed economy, to withdraw temporarily from the CAFTA negotiations in response to domestic disquiet about plans to privatise the country's telecommunications and insurance sectors. A similar sensitivity emerged in the negotiations between the US and Australia, with the latter successfully resisting the former's call

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<sup>57</sup> See Remarks by Nyamu J, Namibian Minister of Trade and Industry, on the occasion of the SACU Trade Policy Review, Geneva, 23 and 25 April 2003. See also Kirk R & M Stern, *op.cit.*

<sup>58</sup> Whalley J & JC Leith, 'Competitive liberalisation and a US–SACU FTA', *National Bureau of Economic Research, Working Paper 10168*, December 2003, p.29.

for local-content restrictions to be abolished on emerging media such as digital television.

### *Investment*

The US administration seeks to ensure that US investors receive treatment as favourable as that accorded to domestic or other foreign investors in the SACU region. Furthermore, the US wants to eliminate barriers to US investment in SACU countries, while guaranteeing that SACU investors in the US do not receive greater substantive rights concerning investment protections than US investors in the US. Investment is a contentious issue in the WTO, with many developing countries opposing negotiations on this subject. They have argued that trade negotiations on investment ought to take their concerns into account, including the need for: transparency; flexibility in allowing host governments 'policy space' in respect of the right of establishment, market access, and national treatment; and investor protection through intergovernmental dispute settlement procedures, not investor-state suits as contained in NAFTA's (in)famous Chapter 11.

A notable outcome of the FTAA negotiations has been a concession made by the US to allow Brazil, South America's biggest economy and perhaps the most restrictive on foreign investment, to opt out of regulations that would proscribe its ability to regulate foreign investors. This has been in keeping with a decision by the 34 member countries to create a two-tier approach to the FTAA — with one tier of mandatory obligations and a second, voluntary tier around more contentious issues, such as investment and intellectual property rights.<sup>59</sup> In essence, this so-called 'FTAA à la carte' approach

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<sup>59</sup> Ministerial Declaration, Free Trade Area of the Americas Eighth Ministerial Meeting, Miami, 20 November 2003. For a deeper analysis of contending Brazilian and US strategies in prosecuting the FTAA, see Zourabichvili A, 'Brazil's position in the Free Trade Area of the Americas negotiations process', *SAIIA Trade Policy Briefing No. 5*, 2004.

permits countries to cherry-pick aspects of the FTAA they will sign on to, in addition to some agreed mandatory obligations. This is not the first time that sensitivities about national sovereignty have impinged on trade negotiations. Concerns about national sovereignty in Mexico yielded one key concession in the NAFTA pact: the exclusion of Pemex, the Mexican national oil company, from its investment provisions. Pemex has opposed privatisation and continues to be shielded from foreign competition in some areas. The issue of national autonomy has also arisen frequently in US–Canada economic relations. For instance, anxieties about overwhelming US domination of the Canadian economy led to the inclusion of a provision — Article 2005 — in the Canada–United States Trade Agreement (CUSTA) of 1989 which states that ‘cultural industries are exempt from the provisions of this agreement.’ Moreover, during the Uruguay Round trade negotiations France successfully sought protection of its domestic movie industry from Hollywood film producers, citing fears of US cultural hegemony.

The relationship between investment and services constitutes an additional negotiating point. It seems that the USTR has proposed separating mode 3 (‘cross-border supply’) from the services chapter of the agreement with a view to incorporating it into a broader investment agreement. Given that mode 3 essentially deals with investment, albeit from a relatively narrow services viewpoint, this is a novel approach which appears to make sense. After all, why regulate goods and services investment separately and potentially differently?

### *Government procurement*

The US wants to institute rules requiring government procurement procedures and practices in SACU countries to be fair, transparent and predictable for suppliers of US goods who seek to do business with SACU governments. The US–CAFTA agreement grants non-discriminatory rights to US suppliers to bid on contracts from



Central American government ministries, agencies and departments — although it excludes low-value contracts. It covers the purchases of most Central American government entities. Additionally, it demands fair and transparent procurement procedures, including advance notice of purchases and timely and effective bid review procedures. And it criminalises bribery in government procurement under Central American and US laws.<sup>60</sup> Should they be replicated in South Africa, these stipulations would certainly have important consequences for black empowerment initiatives and other related national developmental objectives promoted by the South African government. This should not of course downplay the important role a procurement agreement could play in promoting transparency and accountability in government transactions.

### *Trade remedies*

The US has ruled out modifications to its anti-dumping and countervailing duty laws in the proposed FTA negotiations, deferring such discussions to the WTO. It is highly unlikely that they will reconsider this. However, they may show some flexibility in applying their rules. For example, in calculating *de minimis* thresholds their practice has been to cumulate South Africa steel exports with those of other developing countries. Perhaps one negotiated outcome could be for the ITC not to implement such cumulation. For South Africa this is a critical issue because South African steel exports to the US have been consistently hit with anti-dumping duties. Although South Africa has supported the use of these duties in genuine dumping cases, in the Doha negotiations it has sought to strengthen the anti-dumping agreement and reduce the abuse of anti-dumping duties by protectionist interests.

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<sup>60</sup> Office of the USTR, 17 December 2003, *op.cit.*, p.5.

### *Labour standards*

The US seeks to establish procedures for consultation and co-operation with SACU nations in order to strengthen their ability to promote respect for labour standards, including observance of International Labour Organisation (ILO) Convention 182 on child labour. It will also demand guarantees from SACU countries that they will not weaken the protections enshrined in their labour laws as an inducement to attract foreign trade and investment.

This negotiating posture represents an interesting dilemma for SACU. On the one hand, South Africa — the largest and most developed SACU member — already supports the promotion of core labour standards in line with ILO requirements, although it has cautioned against countries using them for protectionist ends. This reflects an important concession made by the African National Congress (ANC) government to the Congress of South African Trade Unions (COSATU), a key member of South Africa's ruling tripartite alliance, and other civil society groups. COSATU has lobbied for the inclusion of a social clause in all bilateral and multilateral trade agreements.

In particular, it has demanded that South Africa's trade partners observe and fully implement the four core sets of internationally agreed labour rights: freedom of association and collective bargaining; freedom from discrimination; prohibition of child labour; and prohibition of forced labour.<sup>61</sup> This is unlikely to constitute a problem for South Africa. However, sections of South Africa's labour movement are concerned that deeper integration with other southern African countries — whose labour laws are relatively lax when compared with those of South Africa — will result in South African factories relocating to other regional destinations in search of cheaper labour. And there is the problem

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<sup>61</sup> The Congress of South African Trade Unions, 'Cosatu Submission on Industrial Policy'. A presentation made to the Trade and Industry Portfolio Committee and the Select Committee on Economic Affairs, Cape Town, 30 April 2002, p.18.

posed by Swaziland, a perennial violator of ILO labour conventions to the extent that its AGOA preferences have almost been withdrawn several times.

If the US–CAFTA FTA is anything to go by, it can be surmised that the US will put considerable pressure on SACU countries to harmonise their labour laws and ensure that they meet not only ILO prescriptions, but also the labour objectives outlined by the US Congress in the Trade Promotion Act (TPA) of 2002. The US–CAFTA agreement extends beyond the Chile and Singapore FTAs in that it sets out a co-operative approach to improve working conditions by: ensuring effective enforcement of existing labour legislation; working with the ILO to upgrade existing laws and their enforcement; and enhancing local capacity to improve worker rights.<sup>62</sup> Yet in the final analysis, if Mexico's experience in enforcing labour and environmental codes is anything to go by, such provisions are unlikely to constitute serious problems.<sup>63</sup> This depends partly on the outcome of the forthcoming US presidential elections (see 'Future challenges').

### *Environmental standards*

The US seeks to extract a commitment from the SACU countries that they will not only enforce their environmental laws effectively, but also that they will not weaken the protections contained in their environmental laws as an incentive to attract foreign trade and investment. The US–CAFTA FTA provides an example of the kind of issues the US is likely to stress in its negotiations with SACU in its quest to achieve the environmental objectives set out by Congress in the TPA. The pact extends beyond the Chile and Singapore FTAs in seeking to develop provisions that would: develop a rigorous public

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<sup>62</sup> Office of the USTR, 17 December 2003, *op.cit.*, p.6.

<sup>63</sup> Schott JJ & GC Hufbauer, 'Prospects for North American economic integration: An American perspective post 9/11', Institute for International Economics, Draft for CDHowe Commentary, *The Border Papers*, 5 September, 2003. p.4.

submissions process to ensure that the views of civil society groups are incorporated; encourage the benchmarking of environmental cooperation activities and involve international organisations in evaluating progress; strengthen multilateral agreements and the FTA.<sup>64</sup>

### ***Dispute settlement***

The US wants to create fair, transparent and effective procedures for the settlement of disputes arising out of the proposed FTA agreement. The US–CAFTA regional trade deal provides for dispute panel procedures that are underpinned by such processes as open public hearings, public release of legal submissions by parties, special labour or environmental expertise for disputes in these areas, and opportunities for interested third parties to submit views. The most contentious aspect of the US proposals has been the determination to include dispute-resolution mechanisms similar to NAFTA's Chapter 11, which allows corporations to sue governments directly — a provision that was included in the FTA agreement with Singapore. Yet the US pushed vigorously, but ultimately unsuccessfully, for its companies to have the right to legally challenge the Australian government if it refuses US companies' investment plans. It agreed instead to a traditional state-to-state system.

### **Future challenges**

The first challenge facing the SACU–US FTA negotiations concerns the different levels of development and size of economies among the SACU countries. The SACU market is very small in relation to that of the US. Whilst very few of the SACU countries' products can take on the US market, American products and services can damage SACU

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<sup>64</sup> Office of the USTR, 17 December 2003, *op.cit.*

economies in that domestic producers may be dislocated by foreign competition — although domestic consumers are likely to benefit from gaining access to cheaper or better products. This calls for a very careful and calibrated approach to the negotiations on the part of SACU. SACU should strive to reach an agreement that enshrines a balanced set of obligations and rights, and which takes into account the imbalances and developmental needs of the region. Moreover, attempts must be made to accommodate the concerns of those countries that feel they have less to gain from an FTA than what they are already deriving from AGOA. As such, it is necessary that the SACU–US negotiations address the unique needs and economic circumstances of SACU economies, including possible internal dislocations and transition costs.

In this respect, the US and SACU can use the Trade, Development, and Co-operation agreement (TDCA) concluded a few years ago by the EU and South Africa as a model for their negotiations. A notable feature of the TDCA is that it provides for free trade with asymmetrical coverage of all trade and sectors. This entails an asymmetrical reduction of tariffs, with the EU making the speediest and deepest reductions to offset bilateral trade imbalances. The TDCA also provides for special protocols for the protection of South Africa's sensitive products (automobiles and components, textiles and clothing, red meat, sugar, winter grains and dairy products). Furthermore, it commits the EU to the provision of development and financial measures to strengthen further regional integration and support SACU's adjustment efforts. However, it should be borne in mind that the TDCA has some shortcomings, including its highly restrictive rules of origin and the fact that it excludes services and the new trade issues. Given America's own commercial objectives, it is questionable whether the USTR will be prepared to settle for this framework in lieu of deeper market access concessions.

The second challenge relates to the issue of trade negotiating capacity. The new SACU Agreement enables the SACU countries to engage in trade negotiations as a single entity. Apart from the US–

SACU FTA negotiations, South Africa has been involved in exploratory work towards an FTA with the Mercosur, the European Free Trade Area, India, China and Nigeria. This has implications for SACU's limited negotiating resources. The formidable challenge facing SACU negotiators against the well-oiled US negotiating machinery in the coming months cannot be over-stated. Even so, SACU could use the lessons learnt by South Africa from its FTA negotiations with the EU to maximum negotiating effect with the US.

A third, and related, challenge is the effect these negotiations will have on SACU institutions. As has become clear in recent years, institutions matter for development. Yet SACU is embarking on this exercise in a context where its own institutions, to the extent that they exist, are in a major state of flux. Aside from future legal complications that may arise from this,<sup>65</sup> it is not clear how agreements concluded with the US in areas not covered by the SACU agreement will affect the regional integration project.

The fourth challenge then is the possible ramifications of a US-SACU FTA for the SADC regional integration process. Questions have been asked as to why the US has chosen to negotiate with SACU rather than with SADC. It would appear that America's decision to negotiate with SACU has been influenced by the fact that the latter is a customs union: it would be more difficult to negotiate an FTA with SADC, a somewhat incoherent and not yet fully integrated regional grouping. Furthermore, if the CAFTA experience is a guide, other countries in the region are likely to be eventually 'docked' into the US-SACU FTA in the same way as the Dominican Republic has been drafted into the US-CAFTA trade deal. Additional uncertainties include a lack of clarity on: what impact the FTA will have on SADC's ambitious plan to establish a region-wide customs

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<sup>65</sup> It is possible, for example, that the US will ultimately conclude 6 agreements as part of the overall package: one with each member state and one with 'SACU'. So at this stage it is not clear who the contracting parties will be, nor what they will be signing up to.

union; how this could affect Mozambique's interest in becoming a SACU member; and what the FTA's potential impact on the region's emerging Economic Partnership Agreement (EPA) negotiations with the EU will be.

Tied to this is the fifth challenge of how to deal with the potential loss of revenue arising from the proposed FTA. The Bank of Namibia has forecast a 35% decrease in state revenues (as a consequence of FTAs in general) over a period of 12 years, making a diversification of revenue sources a key priority. Part of the solution to this problem may lie in diversifying revenue sources towards indirect taxation, while another part may reside with the development component of the revenue-sharing formula. In addition, consideration should be given to the counter-balancing effects of increased trade stemming from the FTA.

The sixth challenge concerns the relationship between trade liberalisation and development. The experience of Mexico has demonstrated that although trade liberalisation can create conditions conducive to growth, it is not a panacea for development problems.<sup>66</sup> NAFTA played a crucial role in consolidating the reforms Mexico initiated in the early 1990s. It also opened the previously massively protected Mexican economy to foreign competition, forcing Mexican companies to become more efficient and focused. Furthermore, it bolstered the productive capacity of specific Mexican industrial sectors — notably the automobile sector — while it also exposed Mexicans to a wider choice of goods. However, commentators such as Joseph Stiglitz have argued that Mexico's economic boom in the 1990s was unsustainable in that it masked serious underlying weaknesses: a weak educational system with low investment in technology, a low tax base, low spending on research and development, high energy costs, and systemic corruption. They have also pointed out that although NAFTA enhanced Mexico's ability to

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<sup>66</sup> For an overview of this debate see White, L. 'Mexico's NAFTA: More pros than cons', *SAIIA Trade Policy Briefing No. 4*, February 2004.

supply American manufacturing firms with low-cost parts, it failed to transform the country into an independently productive economy.<sup>67</sup>

Furthermore, as Whalley and Leith note, it is by no means certain that this agreement (to the extent that it liberalises trade) will be poverty-reducing. They point out that the region's comparative advantage lies in natural resources, which in their extraction are capital, not labour, intensive. Further trade liberalisation may exacerbate this tendency and aggravate the unemployment problem. Therefore trade liberalisation must not be viewed in isolation from other policies such as those on investment, entrepreneurship development, training and development, technology, and research and development.

The seventh challenge is the forthcoming US election and its likely impact on the imperative to extend 'trade promotion authority.' Assuming that the Doha Round negotiations can be successfully concluded this year (a highly unlikely scenario), the President currently possesses all the authority required to enter into trade agreements and submit implementing legislation to Congress by 1 June 2005, the date on which the authority is scheduled to expire. However, if the Doha Round negotiations cannot be concluded this year (a highly likely scenario) the President may request a two-year extension of the authority by submitting a report outlining out what has been achieved under the current trade promotion authority and setting out clear reasons for the extension to Congress by 1 March 2005.

The joint decision by the President and Congress to arrange such an extension is likely to trigger yet another debate regarding US

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<sup>67</sup> Stiglitz JE, 'The broken promise of NAFTA', *The New York Times*, 6 January 2004; see also 'Free trade on trial', *The Economist*, 3-9 January 2004.



trade policy and may provide an opportunity for opponents of trade liberalisation to derail the negotiations.<sup>68</sup>

Given the parochial political dynamics that often characterise US presidential elections, a massive consensus-building effort will be required in the coming year, not only in the US but also at inter-governmental level, if the Doha Round negotiations are to be re-launched and completed by mid-2007. The paramount role of Congress in overseeing the process of ratifying FTAs cannot be ignored in this regard.<sup>69</sup> In recent years the passage of FTAs within Congress has become more difficult thanks to resistance to trade liberalisation by key US domestic constituencies such as labour and environmental lobbies. Therefore, a crucial test for the SACU countries will be not only whether they can deliver a technically sound trade agreement, but also whether they can ensure that the agreement successfully goes through Congress. This will require these countries to work closely with the US Executive Branch to engage members of Congress and enlist their support for the trade agreement. Tied to this is the need for the SACU nations to assiduously cultivate the influential Congressional Black Caucus and the mini 'Help Africa' industry, whose support could strengthen SACU's bargaining position in these FTA negotiations.<sup>70</sup>

More broadly, there are major questions regarding the degree to which the proliferation of FTAs can be reconciled with the multilateral liberalisation agenda within the context of the WTO. Regional and bilateral FTAs have come under attack for their propensity to fragment the global trade system. More significant, they have failed to tackle the most contentious and pressing issue in

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<sup>68</sup> See Rivers R, 'Note on the Doha Round and the deadlines imposed by US trade-negotiating authority', Washington DC, 30 October 2003.

<sup>69</sup> Not only can the US Congress annul trade agreements, it can also vote them down.

<sup>70</sup> Confidential interview in Washington DC, August 2003.

the WTO: agricultural trade liberalisation.<sup>71</sup> In this light it is encouraging that the USTR has urged that the Doha negotiations be restarted. His recent expression of support for the demand of the developing countries that discussion on investment and competition policy be shelved, augurs well for the resuscitation of the multilateral trade negotiating process. For all its imperfections, a rules-based world trade system provides a solid basis for ensuring that the trade interests of developing countries are taken into account. A reinvigorated global trade system could act as a catalyst for a breakthrough on some of the hurdles hobbling the WTO, including agricultural trade.

In conclusion, a different take on the dynamics underpinning these negotiations is provided by Stratfor, a Virginia-based US consulting firm. They argue a geo-political line. In their view, Australia was prepared to sacrifice its powerful sugar industry and afford major market access concessions to the US owing to its geopolitical reliance on Washington's East Asian security umbrella.<sup>72</sup> By contrast, Brazil is pursuing a hard line in its negotiations with the US in the Free Trade Area of the Americas. And Brazil occupies a much more independent geopolitical space than Australia. So in the final analysis, how important will South Africa's bilateral political relations with the US prove to be? That remains to be seen.

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<sup>71</sup> Bhagwati J, 'Don't cry for Cancun', *Foreign Affairs*, January/February, 2004, pp.62-63

<sup>72</sup> 'The geopolitics of alliance', *The Stratfor Weekly*, 6 February, 2004.