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Free Trade Agreements

1. Introduction

International trade is a vast mesh that affects almost every human being on the planet. A smart phone may be designed in South Korea and assembled in a factory in China from raw materials that were mined in Africa, before being shipped half way around the world to a shop in California.

Despite 'globalization' being a prominent buzz word, this is not a new phenomenon. Global trade reached very high levels in the late 19th and early 20th centuries, before the Great Depression, subsequent protectionist politics, and two world wars sent international trade levels plummeting again.

Free Trade Agreements are part of the matrix of international law and economic ties that link economies around the world. The details are not commonly understood by lay people, but they can have very real impacts on the lives of everyone, including the poor.

This paper goes over some of the concepts involved in Free Trade Agreements, and then addresses some topical issues relating to South Africa and these agreements. It then briefly discusses the various issues involving the African Growth and Opportunities Act, before finishing with a brief word about the importance, and pitfalls, of trade deals.

2. Free Trade Agreements

A Free Trade Agreement (FTA) is a binding treaty between two or more countries that commits them to allow a greater flow of goods and services between them, usually by lowering barriers to trade such as a tariffs and import quotas. Many countries limit the importation of certain goods, either by charging special taxes on them at the border (tariffs), or by simply limiting the amount of a certain type of good that can be imported into the country. Ideologically, preventing imports is a major element of protectionist thinking – the notion that domestic producers, industries and businesses need to be protected from external competition in order to safeguard jobs and economic opportunities for citizens.

By contrast, advocates of free trade often promote it as a means of increasing wealth and prosperity. This is not simply an abstraction, or something that benefits only large corporations. Small businesses can gain access to much larger markets through free trade. Moribund local markets can be shaken up and revitalised by the introduction of fresh external competition. Furthermore, people can often gain access to much cheaper goods than they were able to previously – for example, imported clothing or food can be much cheaper than local products.

However, FTAs can often have very visible negative effects on people's livelihoods. Local industries may not be able to compete with cheap imports. Entire sectors can vanish without a trace, taking thousands of jobs with them. The SA textile industry is a good example of how cheap imports (in this case, Chinese) have done enormous damage to local industries.

3. Non-tariff Barriers

It is important not to be lulled into thinking that a bilateral removal of trade barriers such as import tariffs is all that is needed for fair competition to take place. The European Union, for example, subsidizes its farmers with billions of Euros in aid every year, whereas farmers in South Africa do not have this luxury. Farmers in South Africa who wish to trade into the Eurozone may have advantages (cheaper labour, land and weather),

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but they cannot compete equally with farmers who enjoy massive European Union subsidies.

Aside from subsidies, regulations and standards can create serious barriers to trade. These can include issues such as phytosanitary[1] and food safety regulations. Countries may from time to time ban imports of certain foodstuffs due to food safety issues. For example, an outbreak of Bovine Spongiform Encephalopathy (BSE or 'mad cow' disease) may result in countries banning beef imports from the affected region. Obviously, food safety is an important issue, and countries ought to protect consumers from dangerous imports. However, disagreements over whether food safety regulations are reasonable, or undertaken in good faith, can become very serious. For example, South Africa has until recently banned chicken imports from the US, due to an outbreak of avian flu; but the US contends that banning all its chicken is unreasonable, given that the outbreak is confined only to parts of the US. Is South Africa acting reasonably by banning Californian chickens, given that the outbreak is thousands of miles away in New Jersey?

Another example of this kind of debate is the 'black spot' issue. Black spot is a type of fungus that infects citrus plants, and has been found on South African citrus exports destined for the EU. Our trade authorities argue that black spot is not a serious problem. The EU insists that keeping black spot out is vital, and justifies sweeping restrictions on South African citrus imports. South African farmers and trade authorities argue that this constitutes unfair protectionism, designed to keep South African farmers from competing with EU citrus farmers[2].

Unfortunately, there is rarely an easy or quick way of settling disputes such as these. Different countries may have different standards and levels of acceptable risk, and it is not always readily apparent whether a restriction is being applied out of a bona fide concern for health and safety, or as a way of stealing a march on a competitor.

4. Rules of Origin

Rules of origin are one of the issues that often emerge in trade discussions. At stake is the question of how to determine where a product was made. Due to complicated international supply chains, a finished product may pass through multiple jurisdictions. The cloth for a shirt may come from one country while the shirt itself may have been cut and sewn in another. Rules of origin are important so that both countries in a trade deal can be in clear agreement of what is and is not covered by the trade deal. This can also be necessary in order to avoid third party countries benefiting unduly from a trade agreement. For example, South Africa and the US might agree to a free trade deal, but find that entrepreneurs then begin importing almost-finished shirts from China, sewing on one button in South Africa, and selling them into the US market as 'South African' goods. This does not benefit either of the parties, and it would undermine the intention of the trade deal, which would be for free trade between the US and South Africa, as opposed to turning South Africa into a mere transhipment point for Chinese goods.

5. South Africa's situation

Following the elections of 1994, and the ending of sanctions, the first priority for South Africa was to re-enter the world trade system. South Africa joined the World Trade Organization (WTO) in 1995. Before 1994 the South African economy had been geared towards surviving in an era of sanctions and international hostility; post-1995 the challenge was to reintegrate into the world economy, and become competitive.

The South African economy has historically been underpinned by mining and agriculture, with manufacturing soaking up some additional labour. However, both agriculture and manufacturing have shown sustained and continuous declines as a percentage of GDP since the early 1990s. At the same time, services have swelled, to the point that they made up nearly 70% of the economy in 2012.[3]

In effect, the economy has de-industrialised. This process has been assisted by a rapid liberalization of tariff regimes following South Africa's entry into the WTO. This liberalization was not entirely forced – it was done voluntarily, in order to introduce competitiveness into local industries, but has resulted in them being hollowed out by cheap imports from abroad.

The Department of Trade and Industry has identified re-industrialization and beneficiation as key priorities in economic development and employment creation, but given South Africa's relative vulnerability to cheap imports, it is unclear how this will work.

Mining has also suffered. While the 2000s saw a massive commodity boom, driven by Chinese demand, this commodities 'super-cycle' has ended, with China's economy struggling to maintain high growth rates, and with many of its major build projects having been completed. Consequently, demand for commodities – such as platinum and steel – has plummeted, and our mining sector has suffered as a result.

6. South African Trade Deals

Enumerating the various trade deals that South Africa has acceded to would take far too long. However, some of the major agreements that South Africa is party to are the following:

6.1. The Southern African Customs Union

Not only a Free Trade Area (although it includes free trade provisions), the Southern African Customs Union incorporates SA, Botswana, Lesotho, Namibia and Swaziland. It is a revenue sharing agreement, in terms of which money collected in customs revenue from imports to the region is shared among the countries. The vast majority of trade into the region takes place via South Africa, so in effect this arrangement subsidises South Africa's neighbours, particularly Lesotho and Swaziland, which rely on SACU revenues for a very large sum of their core government income. However, South Africa derives an enormous amount of benefit from this arrangement. Its corporations benefit significantly from an extensive presence in South Africa's neighbours, and this is facilitated by the existence of SACU. Other projects linked to SACU include the Lesotho Highlands Water Project, where South Africa effectively buys large amounts of water from Lesotho, in order to feed mining and industry in water-scarce Gauteng.

6.2. The SA-EU Trade Development and Cooperation Agreement

One of the most significant FTAs that South Africa has signed up to is the TDCA, which came into effect in 2004. This gives South Africa free access to European markets (subject to the aforementioned non-tariff barriers), and vice versa.

The European Union is South Africa's largest trading partner, and trade with this region has boomed since the signing of the TDCA. Imports from the EU more than doubled in value between 2004 and 2014, from R124 billion to R300 billion, while exports went from R94 billion to R196 billion in 2014.[4]

It is worth noting that this agreement does not include the rest of SACU, and as a result South Africa's neighbours have expressed some disquiet over this arrangement. Due to SACU's common external tariff, the EU gets tariff free access to Botswana, Namibia, Lesotho and Swaziland, without the reciprocal being true.

6.3. The African Growth and Opportunities Act (AGOA)

While this is not a trade deal, it is worth briefly discussing since it is highly topical. AGOA is a unilateral piece of US legislation which was enacted in order to support Africa's development and economic growth. AGOA allows African countries, subject to certain conditions, to sell roughly 7 000 different products to the US without paying import levies. It brings significant benefits to its beneficiaries. For example, Lesotho has managed to develop a fledgling footwear industry. Chinese investors, drawn by the prospect of being able to sell easily into the enormous US market, have set up factories in Lesotho which make shoes for export to the US.

In terms of trade numbers South Africa is the largest beneficiary of AGOA on the continent. South African agricultural exporters and car manufacturers manage to make large amounts of money through this eased access to US markets. According to one set of statistics, approximately 62 000 jobs in South Africa are supported by AGOA.

However, the US has threatened to revoke access to their markets due to a couple of issues. The first, and probably the central one, is poultry. South Africa has levied duties on US chicken imports since 2000 on the grounds of anti-dumping protection, arguing that US producers were selling their chicken at lower prices in South Africa than in the US. They have also cited phytosanitary concerns (specifically, bird flu). This has incensed US chicken producers and South Africa has recently gone through an out-of-cycle AGOA review. In effect, South Africa is being checked for eligibility to remain in AGOA. South African chicken producers have pushed back and accused the US of "dumping" cheap chicken onto South African markets, an accusation that the US government vehemently denies. As things stand, South Africa has relented on this topic and has promised to allow imports of US chicken. However, the imports have not arrived yet.

The other issue looming over AGOA is the question of the Private Security Industry Regulation Amendment Bill, which, if enacted, will prohibit majority foreign ownership of security companies in South Africa. Significant US capital is invested in these security companies[5], and should it pass in its current form, it is quite possible that the US will revoke South Africa's eligibility for staying in AGOA.

6. Conclusion

South Africa's economic position is difficult, but few of the difficulties are externally imposed. When it comes to international trade, there is both opportunity and danger.

First, South Africa needs to maintain its trade relations with African countries, and expand these where possible. Leaving SACU, for example, would be a highly problematic decision. While it costs the fiscus a fair amount annually to maintain this revenue sharing, there are significant benefits to South Africa from both regional stability and integration. Having our neighbours turn to other sources of trade and goods would be highly undesirable.

Looking further abroad, South African policymakers ought to maintain a balanced, long term perspective on trade deals. Hastily accepting deals with BRICS formations, without interrogating their long-term effects, should be avoided. There are undoubtedly huge opportunities within BRICS, and these should definitely be pursued, but not at the cost of local jobs or manufacturing enterprises. Similarly, ties to the European Union and the US should not be neglected. Despite China's rise, a staggering amount of wealth is still tied up within the West, and these ties ought to be maintained. On balance, South African policymakers should seek new deals wherever the benefits can be clearly shown, without allowing themselves to be dazzled by promises of wealth, or unduly strong armed by powerful states. Our economic issues are largely internal, and panaceas cannot be found abroad – however, the power of international trade and investment must not be ignored, provided it can be harnessed in service of generating prosperity and a better life for all South Africans.

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1 Related to plant health and disease.
2 The black spot controversy seems to have been settled, for now – the EU has allowed imports of South African citrus, after an audit by the EU found that South African measures to detect and contain black spot affected citrus were adequate.
3 These figures come from a presentation by Mark Schoeman of the South African Institute for International Affairs, made on the 21 August 2015 in Cape Town, at a Round Table organized by the CPLO.
4 These figures were extracted from the DTI's trade statistics, available from http://tradestats.thedti.gov.za. Values were Annual HS8 import (and exports), given annually, with the region set as European Union.
5 ADT security is an American company, based in Florida.