InBrief
No. 2B - September 2003

EPA Impact Studies

SADC and the regional coherence

Stefan Szepesi and Sanoussi Bilal

As part of the process of preparing for the negotiation of an economic partnership agreement (EPA) with the European Union (EU), the Secretariat of the Southern Africa Development Community (SADC) commissioned two studies. One was on the compatibility of trade policies in the context of the current regional economic integration processes in the SADC, and the other was an assessment of the impact of EPAs on the SADC[1] and preliminary adjustment scenarios[2]. The studies were conducted by Moses Tekere and Dan Ndlela of the Trade and Development Studies Centre (TRADES CENTRE), in accordance with the framework of priority actions prepared by the ACP Secretariat and in consultation with ACP states and regional organisations.

The studies:

(i) review the compatibility and coherence of SADC members' trade policies and liberalisation programmes with the SADC regional economic integration framework;
(ii) offer a preliminary assessment of the impact on SADC economies of an EPA with the EU;
(iii) suggest possible scenarios for economic and trade adjustments; and
(iv) make recommendations for the SADC's regional integration process and the content of EPAs.

Context

The SADC is a regional organisation consisting of 14 African countries that, following the signing of the Cotonou Partnership Agreement in June 2000, are entitled to enter into EPAs with the EU by 2008. South Africa, which is only a qualified member of the ACP, already concluded a free trade agreement with the EU in 2000 (i.e. the Trade, Development and Cooperation Agreement - TDCA), and will not therefore be part of the EPA negotiations. As illustrated by Figure 1, SADC membership often overlaps with other regional arrangements, which have different (and sometimes conflicting) integration and trade programmes, and whose members are also expected to negotiate EPAs with the EU. In development terms, the SADC is a very diverse region consisting of eight least developed countries (LDCs), five non-LDCs and one developed country (i.e. South Africa). This diversity poses a major challenge to the EPA negotiations because LDCs can benefit from the Everything-But-Arms (EBA) initiative, which provides non-reciprocal tariff-free and quota-free access to EU markets for all products from LDCs (except arms and, for certain transitional periods, bananas, rice and sugar). The non-LDCs, however, stand to lose their current Lomé preferences by 2008.

Regional challenges facing the SADC

The authors of the studies assume that all SADC countries (South Africa excluded) will negotiate EPAs and recommend that this be done within the framework of the SADC (including its SACU sub-region), together with COMESA. Based on these premises, they have assessed the current state of economic integration within the region and have identified the main challenges ahead.

Intra-regional trade policies

In order to negotiate EPAs as a region, the SADC should at least constitute a free trade area, thus substantially eliminating all internal barriers to trade among its members. The SADC is currently in the process of establishing a free trade area, which, according to the SADC Trade Protocol adopted in 1996 and implemented since September 2000, should lead to the liberalisation of 85% of all intra-regional SADC trade by 2008. The Protocol provides for the phasing out of tariffs on an asymmetric basis: SACU countries have been given eight years to do so (i.e. by 2008), whereas other SADC member states have 12 years in which to phase out tariffs (i.e. until 2012).

Despite the ambitious agenda of the Trade Protocol, progress so far has been very limited. First, little to no liberalisation is about to happen in the immediate future. SADC countries have significantly back-loaded their tariff reduction schedules, so that nearly all tariffs for competing products will not be liberalised until the latter part of the implementation period. Second, tariff revenue generation has been applied as a proxy for product sensitivity, excluding some of the most important product lines from any liberalisation. Third, contrary to the 85% criterion agreed in the Protocol, the trade volume of goods that SADC states wish to exclude a priori from any regional liberalisation is worth more than 15% of all trade. Reviewing this lack of progress, the authors note that missed opportunities for effective

---

[1] *TRADES CENTRE (2002), Study of the Compatibility of Trade Policies in the Context of Current Regional Economic Integration Processes: The Case of SADC, Report prepared by Trade and Development Studies Centre - TRADES CENTRE (Moses Tekere and Daniel Ndlela with assistance of Hurungo James) for the African, Caribbean and Pacific Group of States (ACP Group) and Southern African Development Community (SADC). Available on line at www.acp-eu-trade.org*

[2] *TRADES CENTRE (2002), Impact Assessment of Economic Partnership Agreements on the Southern African Development Community (SADC) and Preliminary Adjustment Scenarios, Report prepared by Trade and Development Studies Centre - TRADES CENTRE (Moses Tekere and Daniel Ndlela with assistance of Medicine Masiiwa, Rusare Masiiwa and Stella Mushiri) for the African, Caribbean and Pacific Group of States (ACP Group) and Southern African Development Community (SADC). Available on line at www.acp-eu-trade.org*

European Centre for Development Policy Management
Centre européen de gestion des politiques de développement
ecdpm

regional integration, as well as non-compliance with WTO rules for liberalising substantially-all-trade within an FTA, endanger the future of the economic integration process as envisaged by the Trade Protocol.

External trade policies

Apart from the problem of harmonising intra-regional trade policies, the member states' external trade policies also remain highly divergent. The authors claim that the SADC has not made any 'attempt to harmonise the actual plans and activities of the member states and there is no centrally coordinated, internally consistent set of principles and policies'. Despite the presence of the Trade Protocol, no progress has been made towards formulating a common external trade policy or a coherent SADC trade policy framework. Current import tariff rates range from 0-20% in some countries (e.g. Zambia) to 0-80% in others (e.g. Mauritius and Zimbabwe). Moreover, the studies list the various national proposals for reducing external tariffs in the years to come and conclude that the divergence is so great that the SADC is unlikely to achieve even some external tariff convergence in the near future.

Macro-economic policies and political relations

On the basis of an analysis of basic macro-economic indicators such as debt, inflation and economic growth, the authors claim that the SADC currently has extremely divergent policies in this area as well. This further undermines the trade liberalisation process. The picture is similar as regards political relations. Internal relations are fragile, as several member countries are involved in political, civil or military conflicts.

Impact assessment of a SADC-EU EPA

The impact assessment study covers the effects a future EPA could have on the SADC economies. Only static effects are estimated quantitatively, leaving the dynamic effects - probably the most significant ones - to be discussed only in general terms.

Table 1 **Trade creation and trade diversion in USD millions**

SADC	*Trade creation*	*Trade diversion*	*Net trade effect*
Botswana	*25.7*	*0.6*	*25.1*
Malawi	*18.4*	*14.1*	*4.3*
Mozambique	*21.0*	*6.5*	*14.5*
Tanzania	*103.0*	*78.8*	*25.5*
Zimbabwe	*82.9*	*21.5*	*61.4*
Mauritius	*136.5*	*87.5*	*49.0*
SACU	*835.0*	*472.0*	*363.0*

Positive effects

Adopting a static, partial equilibrium analysis and assuming that all tariffs are completely phased out during three periods of four years (i.e. 50% in 2012, another 30% in 2016 and the remaining 20% in 2020, leading to a cumulative reduction of 100%), the authors estimate that, for all SADC countries, free trade with the EU will bring net (trade) welfare gains to the region as a whole. In other words, trade creation outweighs trade diversion, as shown in Table 1. In particular, countries that currently have higher tariffs vis-à-vis the EU (i.e. Mauritius, Zimbabwe and the SACU countries) will experience more trade creation than countries with lower tariffs.

The dynamic effects of EPAs are only discussed in general terms, with no attempt to quantify them. Basically, an EPA should enhance the overall competitiveness of the SADC economies, unlock inefficient production structures and improve the performance of regional exporters. Tariff liberalisation will allow domestic companies to buy better and cheaper inputs, thus leading to both lower prices and better-quality consumer products. The removal of the remaining tariffs and tariff escalation in the EU will improve export opportunities and set off diversification in the region. Furthermore, an EPA will create larger regional markets that extend beyond national borders, allowing for economies of scale to emerge. Technology transfers could foster the development of new branches of manufacturing and engineering. Finally, an EPA with the EU could also serve as a lock-in mechanism for trade liberalisation, fostering sustainable policy-making and increasing the attractiveness of the SADC region for domestic and foreign investors.

Trade creation and trade diversion

The economic concepts of trade creation and trade diversion refer to the static welfare effects that are caused when trade between two partner countries or regions is liberalised. Trade creation is the effect caused when products that used to be produced domestically at a relatively high cost are replaced by relatively low-cost imports from more efficient producers in a partner country. Trade creation constitutes a net gain in national welfare, because consumers and firms profit from lower prices. Trade diversion, on the other hand, implies a net loss of national welfare. Here, low-cost imports from a third country that is not a member of the trade agreement are replaced by high-cost imports from less efficient producers in the partner country. Though, here too, consumers and firms profit from lower prices compared with the situation before the agreement, the net welfare effect is negative because previous government revenues from tariffs are lost.

Negative effects

Although an EPA should have a positive impact on SADC economies, it will also cause some potentially severe negative effects on some sectors of the economy and on fiscal revenues.
The authors claim that increased competition from EU companies, which can exploit economies of scale and may be able to dump exports on SADC markets, will adversely affect local import-competing producers. They argue that small and medium-sized firms in the SADC will be particularly vulnerable because of their inability to exploit economies of scale and their lack of access to advanced technologies. This could lead to significant job losses and possible de-industrialisation in the SADC, at least in the short run.

The authors do not discuss in detail any particular product or industry that is most likely to suffer from these developments. Because agriculture and manufacturing are the major contributors to economic growth and employment in the region, these two sectors may be assumed to contain the most sensitive products. An impact study commissioned by the EU in 1998 pointed to the agricultural sector, cereals, food processing, dairy products and beef as being the most sensitive industries. The most sensitive areas within the manufacturing sector are textiles, clothing, beverages, leather and footwear.

Fiscal revenue losses as a consequence of EU tariff liberalisation are thought to constitute the most serious adverse effect of EPAs. The authors believe that the majority of SADC countries will suffer substantial declines in government revenues. Mauritius, Tanzania and Zimbabwe are cited among the most badly affected countries, where the losses are likely to represent over 30% of total import revenues, as indicated by Table 2. In addition, government resources could be drained as EPAs will require heavy expenditure on so-called flanking measures. Besides the resources required to put regulatory frameworks in place, massive investments will be needed in infrastructure and adjustment programmes in order to prepare essential sectors for EU competition.

In order to mitigate the adverse affects of government revenue losses, SADC countries

Table 2 **Tariff revenue losses as a percentage of total import revenues**

Country	t<50% in 2012	t<30% in 2016	t<20% in 2020	Total loss
Botswana	1.93	2.69	3.08	7.7
Malawi	4.23	5.93	6.77	16.9
Mauritius	9.87	13.82	15.79	39.5
Mozambique	7.00	9.81	11.21	28.0
Namibia	6.02	8.43	9.63	24.1
South Africa	2.58	3.62	4.13	10.3
Swaziland	2.47	3.45	3.95	9.9
Tanzania	9.42	13.18	15.07	37.7
Zimbabwe	8.30	11.62	13.28	33.0

will have to find new sources of government revenue by means of new or improved tax systems that do not create significant economic distortions and are collected fairly and effectively. Account must be taken of the extent to which governments depend on tariff revenues and have the administrative capacities that are needed to change tax systems.

Recommendations for EPA negotiations

The authors assume that the SADC countries no longer have the option of rejecting an EPA because of the risk of losing aid from the EU and preferential market access to the EU. For this reason, the studies focus on the scope, content and geographical configuration of a future EPA, and not on its desirability or possible alternative trade arrangements.

Geographical configuration

In spite of the challenge of overlapping membership and the lack of trade policy convergence, or simply coherence among SADC countries, the authors contend that 'all SADC countries (non-LDCs and LDCs) need to negotiate an EPA with the EU'. The authors cite 'maintenance of market preferences' and the possibility of 'influencing or demanding concessions from the EU in return for reciprocity' as being the most important advantages of such a strategy.

Though the integration process within the SADC itself has made insufficient progress, the authors regard a SADC-wide EPA as being feasible provided that it builds on the ongoing integration processes in Eastern and Southern Africa. This would mean joining COMESA and EAC to negotiate an EPA with the EU. These two regions are currently implementing their own free trade areas with the aim of forming a joint customs union by 2004. Assuming that this timetable is respected, five SADC members that are also members of COMESA or EAC (i.e. Mauritius, Malawi, Tanzania, Zambia and Zimbabwe) will already have a common external tariff from 2004 onwards.

Currently, the SACU, the one sub-region that is already a customs union, is the only grouping that lends itself to EPA negotiations in terms of capacity and institutional development. Since Botswana, Lesotho, Namibia and Swaziland (BLNS) are already de facto part of the TDCA between the EU and South Africa through their common external tariff, they could opt either to combine a SACU-EU EPA with the TDCA or to negotiate an EPA with the rest of SADC.

The authors argue that, in its current state, the SADC is not capable of collectively negotiating an EPA, as it has neither the mandate, nor the capacity, nor the prerequisite policy coordination and coherence, as is illustrated by the overlapping membership problem. The authors therefore recommend that the SADC:

(i) forms alliances among (all Eastern and Southern African) regional partners for the negotiation of the EPAs;
(ii) effectively pursues trade policy convergence among its members;
(iii) establishes a coherent FTA by 2008 in accordance with the SADC Trade Protocol;
(iv) quickly moves towards the formation of a customs union; and
(v) effectively seeks the harmonisation of the common external tariffs of the subregions in Eastern and Southern Africa (i.e. SADC/SACU, COMESA/EAC, IOC), to address the incoherence resulting from overlapping membership.

The authors conclude that, irrespective of the technicalities, such an approach will enhance, rather than undermine, the regional integration process, while increasing the region's bargaining power.

Scope and content

The studies advocate the effective implementation of the principle of differentiation within an SADC-EPA. Using the TDCA as a benchmark, and recognising that the adjustment costs for SADC firms will be higher than those for South African firms, the authors suggest that SADC countries should be allowed transitional periods of 15-20 years to fully implement an EPA (as compared with 12 years for South Africa in the TDCA) and a product coverage of 80% (as compared with 86% for South Africa). Alternatively, to ensure that an EPA does not undermine regional integration processes and cause 'undue economic hardship', the authors propose phasing in reciprocity depending on 'the achievement of some basic development thresholds'. Indicators such as the Human Development Index, debt servicing, poverty indices and shifts in commodity dependence could serve as a basis for these thresholds. Arguably, the advantage of such an approach would be one of 'early harvest', where full reciprocity could be achieved sooner if more EU aid is provided. Combining both the thresholds and the time-frame approach is an option that would meet the concerns of both parties.

Besides defending differentiation along development lines, the authors recommend that all SADC countries should strive to maintain and improve their access to the EU market, in particular with regard to the future of the commodity protocols. Further, the current rules of origin should be revised in order to improve export opportunities and encourage investment.

The EU should also adapt its own domestic policies that negatively impact on the SADC region, in particular by reforming its Common Agricultural Policy (CAP). The authors suggest that, to allow the ACP economies to compete with EU producers who currently benefit from domestic support measures, 'it will [...] be necessary to dismantle [the] CAP well before EPAs come into force'.

Capacity-building requirements

The authors conclude by identifying areas in which the EU needs to take certain cooperation and support measures. First of all, any EPA should seek to address the various supply-side constraints that prevent the competitive production of goods and services within SADC economies. To ensure effectiveness, the existing institutional arrangements for EU assistance need to be reviewed. Second, in order to cope with the imperative of fiscal reform, SADC countries should push for EU assistance in identifying the most important forms of expenditure for addressing poverty and gender issues, supporting training in alternative revenue systems, and supporting the institutional reform of government revenue collection. Finally, effective preparation for an EPA is a serious challenge, especially for small countries that also need to undertake other trade negotiations at regional, multilateral and inter-regional levels. The human and institutional capacities of the SADC countries and region need to be supported by the provision of secure and predictable financial and technical assistance.

In perspective

The studies have the merit of clearly pointing out some of the key challenges the SADC needs to address in pursuing its own integration process. They also identify the main types of effect (both positive and negative) that an EPA involving SADC is likely to cause. The rough quantitative analysis provides a first estimate of the broad magnitude of the (static) impacts of an EPA on SADC countries. But, as the authors acknowledge, the estimates are purely indicative and should be interpreted with caution, as the analysis is plagued by seriously methodology constraints coupled with data that is poor in quality and only partially complete.

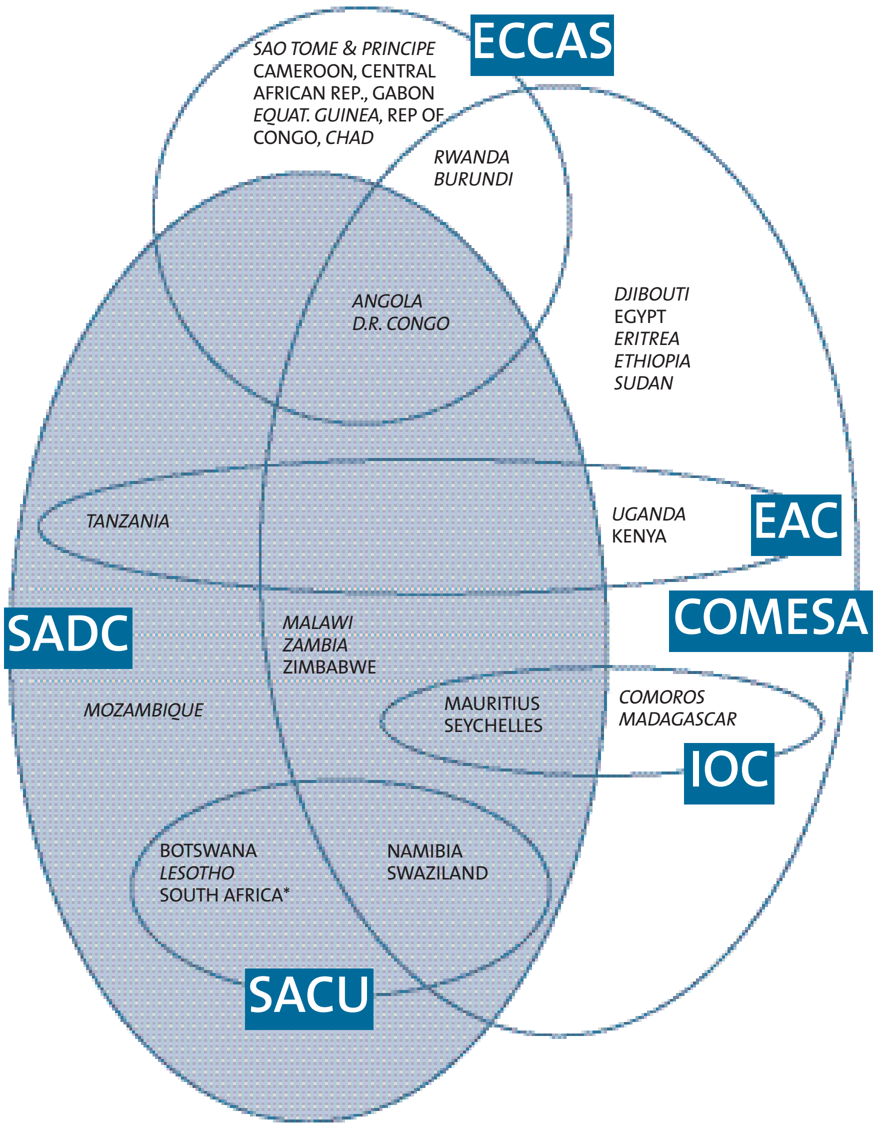
Some of the methodological weaknesses that are in part inherent to such an exercise include:

(i) a focus on the static (as opposed to the dynamic) effects of an EPA;
(ii) an abstraction from parallel trade liberalisation processes resulting from multilateral (WTO), plurilateral, regional and bilateral negotiations;
(iii) the adoption of stylised scenarios assuming full liberalisation of trade with the EU, with no possible exceptions (e.g. for sensitive sectors);
(iv) the absence of any sectoral analysis; and
(v) other technical issues linked to the data and methodology (e.g. calculations based on the elimination of WTO bound tariffs, as opposed to the applied tariffs which are usually lower).

These studies pave the way for further, more systematic impact studies, with stronger qualitative assessments, preferably targeted at individual countries. These could include sector-specific impact studies, trade-policy assessment studies at national and regional levels, alternatives to EPAs, compatibility with future WTO rules, fiscal reform, and all the chapters to be negotiated in an EPA. Future studies would benefit from the input of key stakeholders, including the private sector and civil society.

By assuming, rather than evaluating, the need for the SADC to join an EPA, the studies avoid discussing, let alone assessing, any alternative options to an EPA. The recommendation that the SADC should negotiate an EPA together with COMESA/EAC and should accelerate and deepen its own integration process in becoming a customs union clearly points to the challenges and contradictions still facing the region. A road map has yet to be drawn and alternative scenarios envisaged should the SADC fail to meet its integration objectives.

Figure 1: **The geographical configuration of the SADC and overlapping regions**



Countries whose names are italicised are least-developed countries (LDCs).
*Developed country.

COMESA:	Common Market for Eastern and Southern Africa
EAC:	East African Cooperation
ECCAS:	Economic Community of Central African States
IOC:	Indian Ocean Commission
SACU:	Southern African Customs Union
SADC:	Southern African Development Community

In line with a decision from the ACP Group, the regional ACP groups have conducted studies on impact assessments of the economic partnership agreements (EPAs), and on the compatibility of trade policies in the context of current regional economic integration processes. To promote the dissemination of the results of these studies, ECDPM has started a new series EPA Impact Studies InBrief 2, providing non-technical summaries of the respective regional studies.

'In Brief' provides summarised background information on the main policy debates and activities in ACP-EU cooperation. These complementary summaries are drawn from consultative processes in which the European Centre for Development Policy Management (ECDPM) engages with numerous state and non-state actors in the ACP and EU countries. The Centre is a non-partisan organisation that seeks to facilitate international cooperation between the ACP and the EU. Information may be reproduced as long as the source is quoted.

The ECDPM acknowledges the support it receives for the *'In Brief'* from the Department for International Development in the United Kingdom, the Ministries of Foreign Affairs in Sweden, Finland and the Netherlands, the Directorate-General for Development Cooperation in Belgium, the Swiss Agency for Development and Cooperation and the Instituto Português de Apoio ao Desenvolvimento in Portugal.

European Centre for Development Policy Management
Onze Lieve Vrouweplein 21
NL-6211 HE Maastricht
The Netherlands

Tel +31 (0)43 350 29 00 Fax +31 (0)43 350 29 02
E-mail info@ecdpm.org www.ecdpm.org

ISSN 1571-7542