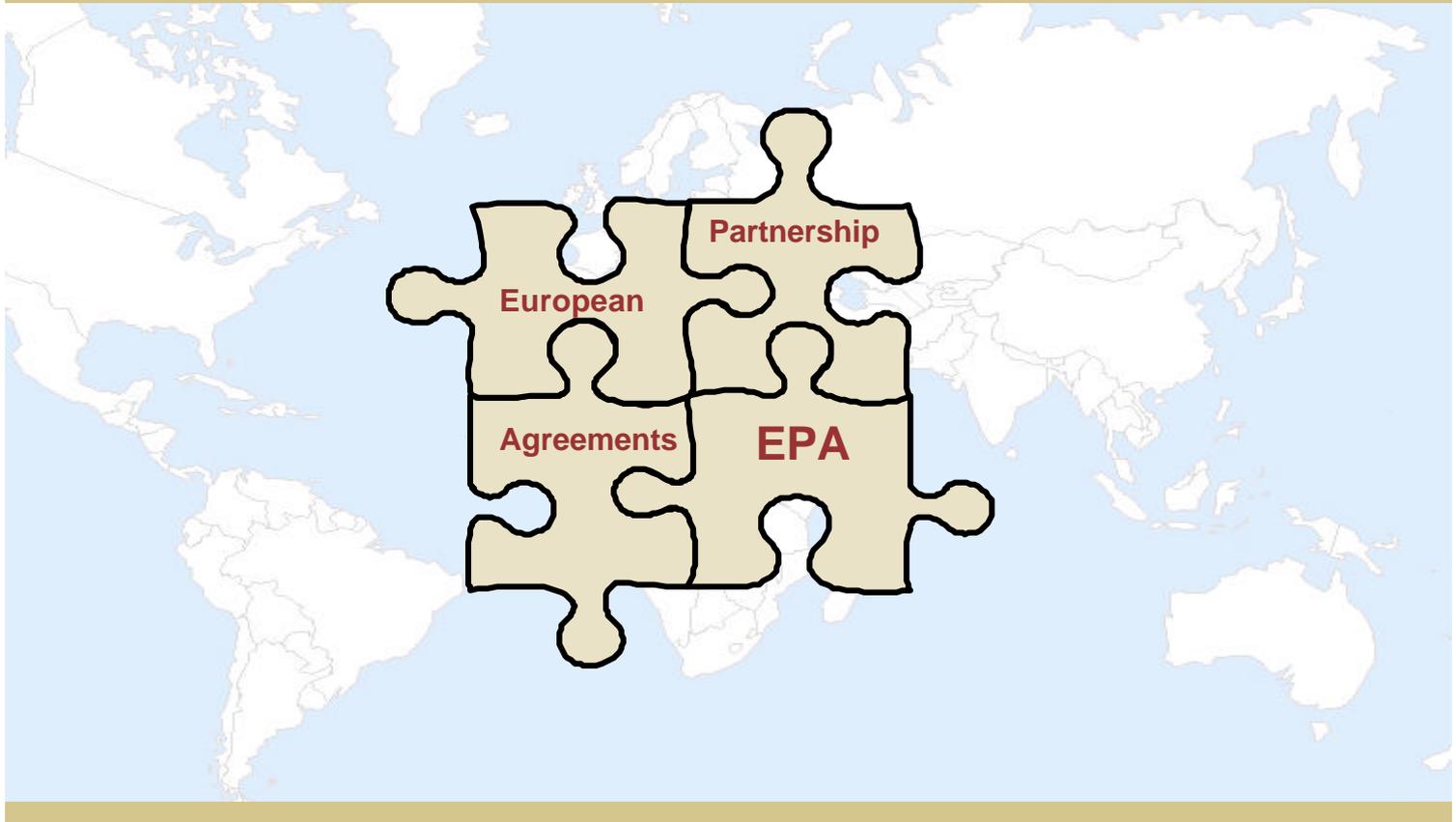


TRADE MATTERS



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Overlapping Membership in COMESA, EAC, SACU and SADC Trade Policy Options for the Region and for EPA Negotiations



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Executive Summary

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Abbreviations

ACP	African Caribbean and Pacific Group
AEC	African Economic Community
ANC	African National Congress
AU	African Union
BLNS	Botswana, Lesotho, Namibia, Swaziland
CEMAC	Central African Economic and Monetary Community
CET	Common External Tariff
COMESA	Common Market for Eastern and Southern Africa
CU	Customs Union
DRC	Democratic Republic of Congo
EAC	East African Community
EBA	Everything-but-Arms
EC	European Commission
ECCAS/CEEAC	Economic Community of Central African States
ECOWAS	Economic Community of West African States
EEA	European Economic Area
EEC	European Economic Community
EFTA	European Free Trade Area
EPA	Economic Partnership Agreement
ESA	Eastern and Southern Africa (EPA configuration)
EU	European Union
FDI	Foreign Direct Investments
FTA	Free Trade Area
IGAD	Inter-Governmental Agency for Development
IOC	Indian Ocean Commission
LDC	Least Developed Country
MERCOSUR	Mercado Común del Sur
MFN	Most Favoured Nation
NAFTA	North American Free Trade Area
OAU	Organization of African Unity
OPDS	Organ on Politics, Defence and Security (SADC)
REC	Regional Economic Community
RII	Regional Integration Initiative
RoO	Rules of Origin
RPED	Regional Programme for Enterprise Development
SACU	Southern African Customs Union
SADC	Southern African Development Community
SADCC	Southern African Development Co-ordinating Conference
SME	Small and Medium Enterprise
TDCA	Trade and Development Co-operation Agreement
UNECA	United Nations Economic Commission for Africa
UNIDO	United Nations Industrial Development Organisation
WTO	World Trade Organisation

Abstract

There is overlap of membership among Regional Economic Communities (RECs) in the Eastern and Southern African region to an extent unparalleled anywhere else in the world. This has a bearing on the costs and benefits particularly of deeper integration. Moreover, membership in more than one Customs Union (CU) is technically impossible. As most RECs in the Eastern and Southern African region wish to move to a CU, member states with multiple membership at present will have to strike the balance of the costs and benefits of belonging to one or another CU grouping. Solely concentrating on tariffs and revenue foregone would mean missing out on some of the more fundamental aspects of regional integration.

The present paper identifies three options which are essentially between deeper and faster economic integration on the basis of the existing CUs acting as fast-track RECs on the one hand, and a larger but shallower integration project for the region as a whole on the other. While each of the options identified has its trade-offs it is shown that only fully functional CUs can act as relevant facilitators of trade expansion and can therefore be expected to impact most positively on investment and growth.

- **Option 1 – “Status Quo plus larger integration project”:** SACU and EAC with their current members serve as fast-tracking groupings, while SADC and COMESA remain FTAs with a view to forming one larger, integrated Eastern and Southern African trade zone at a later stage.
- **Option 2 – “Variable Geometry Option” or “SACU+ and EAC+ Option”:** Enlarged SACU and EAC become fully fledged CUs by 2010, and countries not participating in the CUs remain members of the SADC or COMESA FTAs for the time being but with a view to forming two separate CUs as SADC and COMESA in the medium term.
- **Option 3 – “Leap Forward Option” where COMESA and SADC move to CUs in the near future:** COMESA and SADC become CUs by 2010/12 and merge with the current SACU and EAC respectively. All countries take a decision regarding their membership in either the SADC or the COMESA CU.

In the view of the authors, Option 2 (“Variable Geometry Option”) is the most realistic and economically most feasible option for the region. The main risk of this option is that the envisaged deeper integration in SADC and COMESA will slow down substantially and be limited to integration efforts within the fast-tracking groups. To avoid this, all countries should decide as soon as possible on moving forward with the CU agenda of either EAC+/COMESA or SACU+/SADC – and withdraw from the other.

The ongoing negotiations to conclude Economic Partnership Agreements (EPAs) with the EC should provide an important stimulus and support the process of deeper integration by promoting intra-regional trade and capacity building initiatives. The negotiations are, however, severely constrained by the fact that none of the groupings currently negotiating is a CU yet.

Executive Summary

1 Introduction

There is overlap of membership among Regional Economic Communities (RECs) in the Eastern and Southern African region to an extent unparalleled anywhere else in the world. This has a bearing on the costs and benefits of integration, and more fundamentally, it has implications for the processes of deeper integration that large parts of the region have embarked on. In addition, membership in more than one CU is technically impossible.

The present paper discusses the implications of overlapping membership and identifies options to solve the problem of multiple memberships. RECs with overlapping membership considered here are the Common Market of Eastern and Southern Africa (COMESA), the East African Community (EAC), the Southern African Customs Union (SACU) and the Southern African Development Community (SADC). All four are either already a CU (SACU), in the transition phase to a CU (EAC), or intend to become one in the near future (COMESA, SADC).

The paper also looks into the implications of the overlap for the ongoing negotiations with the European Union (EU) on EPA which shall be concluded by end of 2007. The EPAs are provided for in the Cotonou Agreement which has replaced the former Lomé Conventions. It is argued here that while the EPAs can serve as an important catalyst in this critical phase of decision-making and can strengthen regional integration processes, EPAs should not 'straight-jacket' the future regional integration process in Eastern and Southern Africa.

2 Objective and methodological approach

The objective of this paper is to address the question, how to deal with multiple and overlapping membership from the point of view of the RECs and their members. The paper does not aim at providing recommendations for individual countries. Rather, it seeks to stimulate the discussion in the region and contribute to finding a viable solution

for the problems arising from overlapping membership, particularly in view of the envisaged move to CU in the region. It looks into the history of the RECs and the current scope of overlap, discusses the political, legal, and economic consequences of multiple membership, and identifies three options and their implications for the ongoing processes of economic and political integration in the region.

3 The history of overlapping membership

The creation of different Regional Integration Initiatives (RIIs) in Eastern and Southern Africa dates back to colonial times but was also influenced by the first wave of regional integration based on the model of the European Economic Communities. In Southern Africa, it reflected a political and security motive in the struggle against the apartheid regime in South Africa. The political agenda tended to overrule the trade aspects. The economic impact was not always fully internalised when countries signed new agreements and protocols. The political rationale to join or withdraw underwent significant changes as the RIIs themselves changed over time, adopting new structures and agendas, meanwhile developing their own internal dynamic.

However, in many instances the RIIs became known more for solemn declarations and lengthy protocols than for firm implementation of agreed policies and proven economic impact on the ground. The situation of multiple and overlapping membership became more complex. In the early 1990s, most of the RIIs in the region were still fragile co-ordinating bodies rather than supra-national institutions. Membership as well as the associated integration processes appeared to be reversible.

The end of the apartheid regime in South Africa coincided with the second, more trade-oriented wave of regional integration in Eastern and Southern Africa. An overview of current membership is presented in table I (see Introduction). The various RIIs have moved on to become Free Trade Areas (FTAs). They all embrace trade integration as the necessary intermediate step towards the ultimate objective to become an African political and economic union. However, it has also become clear in the process that other areas besides trade are critical for deeper integration and economic development in the region.

Meanwhile, most RIIs have turned into Regional Economic Communities (RECs), while non-trade matters stayed prominently on the agendas of some as well. As from the year 2000, declarations and later political commitments were made to turn COMESA, EAC and SADC into CUs before long. This, however, marked a new era of regional integration in Sub-Saharan Africa as no country can be a member of two or more CUs at a time.

4 Multiple membership from a legal point of view

From a legal as well as from a technical point of view a country cannot apply two different common external tariffs (CET) and therefore cannot be a member of more than one CU. Hence, the current pattern of overlapping membership becomes impossible to maintain once COMESA and SADC also become CUs in addition to SACU and EAC. The principal possibilities which arise are that the current and future CUs merge into one (for instance SACU with SADC and COMESA with EAC) thereby adopting a CET – and that all members withdraw from other overlapping grouping(s) and decide for membership in only one CU. From the point of view of individual countries it is also possible to join one CU and maintain membership in a FTA of another REC.

With regard to taking the next step towards establishing the CUs, decisions need to be taken urgently. Member states will have to decide which REC will serve their interests best in the process of deeper integration. Once COMESA and SADC become CUs, countries with multiple memberships will ultimately have to opt for membership in one CU only. A FTA relation between the various CUs can be established under certain conditions spelled out in more detail below. The negotiations of EPAs with the EU can serve as a catalyst for decision-making. The ongoing EPA negotiations are moving into a critical phase where market access issues are being discussed. Compatibility between the regional integration agenda and the EPA configurations needs to be ensured as a matter of urgency.

The legal analysis reveals that the treaties and respective protocols of SADC, EAC and COMESA do not preclude members from maintaining prior trade arrangements or from

entering into new ones. They do state, however, that any preferences granted by a member state to a third party or by two or more member states have to be extended to all other member states according to the common customs territory principle. This suggests that countries with multiple membership should not seek individual exemptions but rather cooperate in efforts to negotiate new arrangements between the RECs concerned. Free trade agreements between two regional blocs are a viable option to substitute for foregone trade preferences when a country leaves one arrangement in order to concentrate on another. But when it comes to the adoption of a CET and common trade policies for a CU, countries with multiple membership must make a decision. Besides, membership in different trade blocs tends to absorb much-needed human resources, institutional capacity and limited financial resources.

The existing RECs with the exception of SACU have not yet adopted common policies and trade regimes. This creates some tensions and stretches the coordination and negotiation capacities of the RECs that are not yet equipped with the respective mandates nor the appropriate institutional capacities of a fully-fledged CU. This problem has been noted particularly with respect to WTO and the ongoing EPA negotiations.

Whenever any one member of a CU or FTA negotiates individual trade agreements, the whole group has to bear the costs of administering several trade regimes within the same REC. Generally this implies maintaining border controls and enforcing rules of origin (RoO) to prevent preferential trade from entering the countries that are not party to the agreement. Other important questions relate to the legal bodies and mechanisms that will need to be set up in each grouping and for each trade agreement, such as a dispute settlement mechanism or a court. The legal basis and mandate of each such institution has to be clearly defined if the overlap amongst the RECs persists.

5 The Private Sector's perspective

The economic part of the paper identifies costs and benefits of multiple memberships from the point of view of the economic operators in the region, looking at product market integration and investment. The analysis moreover provides insights from the perspective of the private sector. For it is companies, not countries, that react to altering trade incentives and pick up the new opportunities for growth and development – or ignore them.

Between 1999 and 2003, the share of regional trade has grown faster for all RECs than has extra-regional trade. Intra-regional investment comes mainly from South Africa but is also growing for Kenya and Mauritius. The analysis based on the different proposed tariff structures of the envisaged CUs does not offer a definitive indication of the “best” integration strategy for any one country. Rather, the balance of the costs and benefits is likely to hinge on which REC is able to actually fully implement the commitments made and then move beyond trade integration to address some of the other pressing issues related to creating a conducive environment for doing business in the region.

While tariff preferences are important to companies in the region (less so for South African companies) business people view the current trade agreements as existing on paper only. This applies in particular when it comes to enforcing liberalisation of sensitive products or implementing measures to facilitate trade in the context of poorly administered customs procedures and lack of capacity. Private sector priorities are elimination of non-tariff barriers to trade, in particular overcoming red tape, policy uncertainty, corruption, discriminatory taxes, temporary bans, divergence in standards and requirements, non- or late payments, and lack of financial services. It should be noted that most of these constraints and impediments could be addressed by measures that do not technically require the establishment of a CU.

RECs’ capacity constraints to properly administer the existing agreements and their agendas are a serious problem in the region. Moreover, their focus risks to be diluted by overlapping membership. A clear political will to implement the agreements can best be demonstrated by member states taking the decision to deepen regional integration in only one of the various RECs.

6 Options for Countries Wishing to End Multiple Membership - Experience from Outside the Region

The decision for only one REC is difficult given that all countries had reasons to join several RECs in the first place. The scope and pace of the integration agendas differs, and some countries see some of their interests served better in one REC, some in another. In this situation, the decision for one CU may best be combined with the decision to become an “associate” member of the other REC in order to remain part of that other REC’s non-trade integration agenda. With regard to trade it has already been mentioned above that it is possible that either individual countries or blocs maintain a FTA relation with a CU they are no longer part of.

Experience from other countries and regions in the world can be drawn upon to assess the choices available to countries wishing to withdraw from a REC in order to be a member of only one CU. Norway and Chile may serve as examples for “managed” or associate membership with RECs that are CUs. The EU itself is applying the “variable geometry” option in terms of various members not part of the monetary union but of the common market and the political union. Moreover, the relationships between the EU and EFTA and wider Europe, respectively, provide further examples for associate membership, FTAs between blocs etc.

Associate members will be free of tariff reduction/liberalisation obligations, could attend meetings, but would not have voting rights on trade issues. And cooperation in a number of areas not related to trade – e.g. security matters, migration, management of shared resources etc. – could be maintained or even intensified. Economic criteria alone do not set the regional integration agenda although they are invariably an important element. Members willing to push for deeper integration in some areas should be free to do so, while others are free to abstain.

7 Three Options and their Implications

With respect to trade policies, the difficult decision ahead for countries with multiple memberships will ultimately be a political one. In any case, these decisions should be informed ones where all feasible options are clearly spelled out with their respective costs and benefits. The choice is basically between deeper integration in smaller or fast-track groups which already are or move to CUs in the foreseeable future, and the less ambitious option of a more shallow but potentially broader integration arrangement as an FTA.

- **Option 1 – “Status Quo of CUs plus larger integration project between COMESA and SADC”:** SACU and EAC remain fast-tracking groups of SADC and COMESA respectively, while SADC and COMESA remain FTAs with a view to forming a larger, integrated Eastern and Southern African trade zone at a later stage.

Implications: This option would imply a new integration agenda for COMESA and SADC which deals with a larger number of countries and consequently with a less ambitious but potentially still quite effective trade liberalisation and facilitation policy, thus embracing the vision of Pan African integration. Instead of further pursuing their trade agendas with the objective of becoming separate CUs and to move on to a common market, COMESA and SADC would remain FTAs. At the same time they would undertake to adopt common trade policies for the whole Eastern and Southern African region. The current CUs (SACU and EAC) would serve as fast-tracking groups that set standards in various areas of economic integration but would not necessarily later define common policies. More effective integration mechanisms would need to be developed, probably at the level of the African Union (AU). These mechanisms could embrace the larger groupings and coordinate policy harmonisation between the existing RECs.

In terms of EPA negotiations, following the logic of this option, it would be most straightforward to negotiate as two groups; one consisting of the current SACU which would basically concentrate on the revision of the Trade and Development Cooperation Agreement (TDCA) in favour of Botswana, Lesotho, Namibia and Swaziland (BLNS); and the other one comprising all other countries irrespective of their current membership in COMESA, EAC and/or SADC, i.e. as had been suggested by the Eastern and Southern

Africa (ESA) EPA group earlier in the process. The general framework of the agreements on RoO and other trade policy measures would be the same for all countries, but tariff phase-down schedules would be negotiated individually with the EU. For ESA, this option may preclude the grouping from offering a single trade regime to the EU.

Trade-offs: This option would come at the cost of deeper economic integration in SADC and COMESA. The economic and political signals given to potential investors will at best be ambiguous if their earlier trade agenda is not pursued firmly by these two RECs any longer. For COMESA, it would substantially slow down the progress in trade integration that has been achieved with the implementation of the FTA among the majority of COMESA members. By pursuing this option and keeping the FTA open for further countries, COMESA would postpone its CU plans to an unknown date. For SADC, even the move towards full implementation of the FTA may lose momentum if the objective to achieve the SADC CU by 2010 was to be removed. As tariffs will continue to differ from country to country, RoO will have to be enforced within the region. For EPAs, each country not part of SACU or the EAC CU will need to come up with its own tariff phase-down schedule and negotiate it individually with the EC. This, however, may not even be feasible within the timeframe left for the negotiations. The experience of the TDCA also suggests that it will be difficult to harmonise, at a later stage, tariff phase-down schedules that have been agreed upon individually by the countries with the EC. Moreover, the EC may be reluctant to accept such an approach, as it will seriously stretch its own negotiating capacities.

What the RECs and their members need to be clear about: While this option seems to be the easiest and potentially most realistic one, it is certainly neither consistent with SADC's envisaged integration process spelled out by the Regional Indicative Strategic Development Programme (RISDP) nor with COMESA's stated more ambitious objective to establish a CU by 2008. The economic and political consequences have to be clearly anticipated by both RECs and their member states. Trade liberalisation would still be part but no longer the centrepiece of SADC integration, while COMESA would basically postpone the coordinated and ambitious move towards the CU in favour of the larger

regional integration project. The main appeal of this option lies in the fact that it reflects current realities with the caveat that the respective clear political decisions have not been taken as yet. If pursued deliberately, this could be the option that is most realistic in terms of how ready the larger region currently is for deeper trade integration. All countries should moreover consider the potential loss of bargaining power in EPA negotiations, the cost of administering various trade regimes in the region - and the abandonment of the concept of five regional pillars of the envisaged African Economic Community.

- **Option 2 – “Variable Geometry Option” or “SACU+ and EAC+ Option”:** Potentially enlarged SACU and EAC become fully fledged CUs by 2010, and countries not participating in the CUs remain members of the SADC and/ or COMESA FTAs for the time being but with a view to form two separate CUs as SADC and COMESA in the medium term.

Implications: For Eastern Africa, this option would imply a consolidation and/ or increase of membership (e.g. Rwanda) with the current EAC setting the standards. Tanzania would have to commit herself to concentrate on the EAC, and the CET of the EAC would set the standard for other COMESA members to follow this faster and more comprehensive integration track. For Southern Africa, this would mean that additional countries (Mozambique being a likely first candidate) decide to become a member of SACU. For the countries joining SACU it would effectively imply taking over the SACU CET and other common policies, including existing trade agreements between SACU and third parties. The other SADC member states would remain members of the SADC FTA, hence postponing to 2010 or later the decision to move to a CU. Both COMESA and SADC, would, however, pursue their stated objective to become CUs in the foreseeable future.

In the meantime, EAC and SACU would have a FTA agreement with the non-CU members of COMESA and SADC, respectively. Here the possibility of establishing an associate membership comes in, either individually as countries or between groups. The “variable geometry” option thus caters for the fact that some countries may not consider

themselves ready to join a CU yet or before the suggested dates but still plan to do so at a later stage.

In view of the EPA negotiations, the enlarged SACU+ group could negotiate and implement an EPA provided common policies are quickly developed alongside the respective negotiation machinery that FTAs commonly lack. Members of the SADC EPA not part of SACU by 2008 will need to negotiate individually how to reciprocate market access vis-à-vis the EU, or leave the SADC EPA group. The regrouped ESA would negotiate an EPA with the EU, independent of the partner states' membership in EAC, COMESA or SADC. The tariff phase-down will be identical for all members of the enlarged EAC+ group that adopt the EAC CET whereas all other countries have to come up with their own proposals.

Trade-offs: The main trade-off is that deeper integration is likely to take place in the fast-tracking groups SACU+ and EAC+ only, while among the remaining members of SADC and COMESA the process of deeper integration risks being postponed. In particular, the next stages of economic integration such as a common market are likely to be delayed in the larger groupings. Moreover, political decision-making will be further postponed, and the overlap problem is likely to persist. All countries outside the fast-tracking groups - but with the perspective to join later - need to be clear about one thing: The later they join the respective CU, the more internal regulations and external agreements (the *acquis communautaire*) will already be in place without the latecomers having had a part or say in the negotiations. Therefore, the decision not to join the CU should not postpone a later accession but rather be informed by a clear estimate of the benefits of maintaining a purely national trade policy agenda. The costly administration of RoO will still be necessary in both SADC and COMESA, thereby diminishing the benefits of trade and economic integration. The economic gains of a FTA alone are limited, as it may not trigger additional investment and growth.

For EPA negotiations, decisions on how to reciprocate market access vis-à-vis the EU will be rather complex. Obviously, the existence of the TDCA would have a bearing on the negotiations, and the question for the SACU+ group is whether it is more costly to

fully accept the terms of the TDCA, or to pursue a negotiation position where, for instance, lists of sensitive products will be exempted from the overall liberalisation schedule and transition periods will be extended. In East Africa the current ESA, including the EAC+ group, would negotiate jointly but apply different tariff phase-downs, a single one by the EAC+ group based on their CET, and individual ones for all remaining FTA members on a country-by-country basis. This would draw on scarce resources and the date of 2008 for the EPA implementation will be difficult to achieve.

What the RECs and their members need to be clear about: For the Southern African region, the costs and benefits to join SACU under the current tariff regime will need to be assessed by each country very thoroughly. Moreover, the possibility to extend the SACU revenue sharing mechanism in its current or revised form to additional members needs to be looked into by the current SACU members and the potential accession countries. Those countries which decide to join both SACU and converge to the TDCA should negotiate for additional technical and financial support from the EU as they will open up much faster than what is currently required in the context of the WTO or is intended for the EPAs. In East Africa, Tanzania needs to assess the costs and benefits of committing herself fully to one or the other integration process, i.e. within the EAC or SADC including the SADC EPA. Potential candidates for joining EAC need to make the same assessment, and consider in parallel the possibility of remaining an associate member of another REC. Again, the EPA negotiations could be used to achieve additional technical and financial support for those willing to pursue a faster and deeper trade integration process.

- **Option 3 – “Leap Forward Option”:** SADC and COMESA both become fully fledged CUs by 2010 and will merge with the current SACU and EAC respectively. All countries take a decision regarding their membership in either the SADC or COMESA CU.

Implications: Rather than concentrating on the currently existing CUs, all SADC and COMESA states would aim at forming operational CUs as soon as possible. Internally in both RECs the pace to eliminate all trade barriers and coordinate trade policies would

need to be increased to ensure that the eventual CUs are fully fledged CUs, i.e. they effectively implement a CET and no longer require RoO. Most importantly, both RECs would have to agree on a realistic and credible date for achieving the CU, and on a detailed implementation plan. In Southern Africa, for the members of the future SADC CU, this would include agreeing on a CET to be negotiated between SACU and non-SACU member states. In Eastern Africa, similarly COMESA and the EAC will need to agree on a single CET. In each case, the whole group will adopt common trade policies vis-à-vis third parties, and a mechanism to pool and distribute revenue from tariffs will need to be established.

Deeper integration will obviously imply both costs and benefits in terms of revenue effects and increased competition. The CUs will need to develop adequate financial mechanisms to support the necessary adjustment measures. In cases where pre-existing preferential trade agreements by one or more members of the CU appear unacceptable to the rest of the union – with the TDCA being a likely one – the group will either need to administer different tariffs with that particular trading partner for a transitional period, or adopt the same tariff schedule as part of the CET. The bargaining power of the two enlarged and consolidated RECs and their role as regional pillars of the AU will be enhanced. Their credibility as RECs will be strengthened, including in the eyes of potential investors.

EPA negotiations will be straightforward as the configurations will be clear and a CET established in time for a collective tariff phase-down scenario vis-à-vis the EU. For SADC this will essentially be the TDCA schedule. If SADC were to decide quickly, the interests of SADC members could still be taken on board during the ongoing review of the TDCA, and a mechanism to compensate SADC CU members for opening up faster than required could be negotiated with the EC. The expected transition phase before the tariff phase-down begins on the side of the ACP (back-loading of liberalisation) would cater for the time gap between the application of a CET and the implementation of the EPAs.

Trade-offs: It will not be an easy task for SACU and non-SACU member states of SADC as well as for EAC and COMESA members to agree on a CET given the divergence of current tariff regimes and partner states' divergent industrial development. Although apparently easier in Eastern Africa, the task is still enormous, bearing in mind the different trade policies and levels of development. In view of the EPA negotiations, under this option all countries would need to link their decision for a CU with their choice of an EPA configuration. This can put several countries in a dilemma, and will most immediately affect Tanzania as the country could not be part of EAC and the SADC EPA any longer.

In Southern Africa, the TDCA will still prevail, *de facto* requiring the rest of the SADC CU to accept the same terms (as the BLNS) and converge to South Africa's tariff phase-out agreed on with the EU. Otherwise the region would have to administer a differential tariff offer with respect to the EU. That would undermine the future SADC CU. The TDCA is expected to reach full implementation of the FTA in 2012, while the transition period for the EPAs could expand to up to 20 years from the date of implementation, i.e. until 2028.

What the RECs and their members need to be clear about: All countries with double membership in COMESA and SADC need to decide which CU they wish to join, and all countries have to define their positions vis-à-vis a proposed CET. Costs and benefits of establishing a CU should, however, always be seen in the light of medium-term gains of deeper integration and not only against short-term considerations of potential revenue implications. The possibility of establishing an FTA between the two future CUs should be part of the overall assessment, that is, SADC members would not necessarily lose the preferential market access they currently enjoy as COMESA members, and *vice versa*. In Southern Africa, in the interest of regional integration, an early convergence date for the CET and common policies including vis-à-vis the EU should be considered for the SADC CU. If this were decided on in principle, a mechanism to compensate or specifically support those countries ready to reciprocate the EU much faster than required in other EPAs (and by WTO standards) would need to be put in place. For the BLNS, this was

planned but never operationalised. Moreover, a mechanism to compensate SADC for the need to enforce RoO in order to administer different tariffs in its territory due to the TDCA could be discussed and negotiated. Both COMESA and SADC have to assess the capacity needs to ensure that revenue collection and the enforcement of common trade policies are administered properly.

8 Further Considerations Regarding the SADC EPA Group

In Southern Africa, the EPA configuration is one of a SADC-8 group where South Africa has an observer status, see Annex I. This configuration is not discussed as a separate option above as it has resulted from EPA considerations rather than the regional integration process itself. The three options discussed above are considered to be the most viable in terms of the ongoing *regional* integration processes. None of the three lends itself to being fully compatible with the current EPA configurations. Options 1 and 2 would speak in favour of negotiating an EPA as the current or enlarged SACU+ group. Under both options, it only makes sense for Tanzania to stay in the SADC EPA configuration if it withdraws from the EAC CU.

Option 3 would suggest that all future SADC CU countries negotiate the EPA as a bloc to ensure that the tariff phase down is the same for everyone and compatible with a future SADC CET. All SADC members that wish to be part of the future SADC CU should therefore negotiate the EPA accordingly. Otherwise, they will have to adopt the tariff phase down and other policies agreed on between the SADC EPA group and the EC later without having been part of the negotiations.

9 Conclusions and Way Forward

The successful move towards a fully fledged CU by several RECs in the region is in and of itself a challenging task and requires negotiation and management of coordinated tariff phase-outs, establishment of a CET as well as the creation and implementation of joint revenue collection mechanisms. All this depends on the necessary institutional and technical capacities as well as upon mutual trust in order for the eventual CUs to work effectively and not exist on paper only. Important decisions at the highest political levels

to this effect have been taken in the recent past in all four RECs considered here. However, the move towards deeper integration is contradicted by the persistence of multiple and overlapping membership in the region. Many of the very practical impediments to economic integration have not even been tackled yet, chief among them the proliferation of new non-tariff barriers to trade. Choosing the “right” REC should not obscure where some of the more important constraints really are.

Discussions among stakeholders and policy makers in the region should now urgently lead to some clear decision-making. The principal options have been spelled out above. Even if some countries choose to remain a member of more than one REC, they need to take a decision regarding their participation in only one CU. Moreover, it will be far easier to deepen integration including going beyond product market integration in each of the RECs once the overlap is overcome – and to build the necessary institutions and capacity.

Without wanting to prescribe a decision to any one country in the region it can be concluded from the above that Option 2 (“Variable Geometry Option”) is the most realistic and economically the most feasible option for the region. But this option should not be mistaken for one where the decisions can easily be postponed. All countries need to decide for one CU and withdraw from all other future CUs as soon as possible. The earlier such a decision is taken the better, as countries will be able to focus their resources on negotiations in those groupings that will really matter for them. Note that when a country withdraws from a REC it can still establish a FTA relation with it. In the interest of the whole region, COMESA and SADC in particular should urgently improve the coordination of trade matters between them, and take an initiative to establish a FTA between the two RECs.

The EU has gained valuable experience in how to raise and administer funds that are spent to address the structural and regional weaknesses in its member states - notably in those at the periphery – in order to overcome the supply-side constraints and infrastructural bottlenecks in the process of integration. As indicated in the discussion of

the options, this experience should be brought to bear especially in the framework of the non-trade aspects of the EPAs.

Introduction

The region of Eastern and Southern Africa provides a complex picture of overlapping Regional Economic Communities (RECs) and Regional Integration Initiatives (RIIs) (see Table I).¹ The region even has the highest incidence of overlapping memberships in the world. Most states are at the same time members of two or more regional organisations with an economic agenda. These organisations are:

- The Common Market for Eastern and Southern Africa (COMESA), comprising of a large group of 20 economically and politically extremely heterogeneous countries, eleven of which are part of a COMESA Free Trade Area (FTA).
- The Southern African Development Community (SADC), which has 14 member states, with South Africa being the largest economy by far. SADC is in the process of establishing a FTA among its members but also covers a broad range of other areas of co-operation, including of politics and security issues.
- The Southern African Customs Union (SACU), one of the oldest Customs Unions (CU), is made up of five countries, South Africa being its economic centre. All SACU countries are simultaneously SADC members. Four SACU member states (less Botswana) are also members of the Common Monetary Area with the smaller members pegging their national currencies on par to the South African rand.
- The East African Community (EAC) is composed of only three countries that are in the process of establishing a CU and implementing a FTA.
- The Intergovernmental Agency on Development is an East African organisation that was created to combat drought and desertification. As of yet, it has largely served as a negotiating forum with regard to the civil wars in Sudan and Somalia.

¹ We would like to thank Rainer Engels, Regine Qualmann, Michael Stahl and Alexis Valqui for helpful comments and suggestions on earlier drafts of this study. Cord Jakobeit owes a special note of gratitude to Felix Gerdes for valuable research assistance. All remaining errors remain solely our own and should not be attributed to GTZ or any of their staff or officials.

- The Indian Ocean Commission (IOC) is an organisation that was established in the 1980s, with the aim of linking the economies of five island states. However, it has transferred the responsibility for trade policy to COMESA.

As long as regional economic integration made little progress, multiple memberships in RECs posed few problems. As the above-mentioned suggests, the Inter-Governmental Agency for Development (IGAD), IOC and the Regional Integration Facilitation Forum are of little relevance to the problem of overlapping membership with regards to trade and economic integration. Yet, as COMESA, SADC, SACU and EAC now embark on similar integration paths and deeper integration, the dilemma of conflicting objectives and commitments to the various regional organisations is arising. Technically, no country can belong to more than one CU. This means that where a country is a member of more than one REC aiming to establish a CU, it will have to make a decision as to which REC's trade agenda it wants to follow, unless their different agendas can be harmonized and merged.

This problem has been accentuated by the recent restructuring of EU-ACP relations following the Cotonou Agreement. One of the underlying objectives of the agreement is to make ACP-EU trade relations WTO compatible, i.e. trade preferences must be granted on a reciprocal basis, except for countries belonging to the Least Developed Countries (LDCs) category. Largely due to the initiative on behalf of the EU, the intention is that future agreements be negotiated with existing regional organisations of ACP countries and take the form of (Regional) Economic Partnership Agreements (EPAs). This entails introducing reciprocity to the existing trade relations even for LDCs, albeit after a long transition period.

Clearly, one country cannot negotiate two different trade agreements with the EU as a member of two different RECs. In this sense, EPAs were expected to serve as a catalyst in the process of regional integration and of the rationalisation process among the RECs. Two subgroups that are willing to negotiate an EPA with the EU have been formed in the region. These configurations are the Eastern and Southern African grouping (ESA)

comprising of 16 of the 20 COMESA member states, and the SADC EPA configuration (subsequently SADC EPA) comprising of four SACU countries as well as Angola, Mozambique and Tanzania. South Africa already has a free trade agreement with the EU, the Trade Development and Cooperation Agreement (TDCA) which was concluded in 1999. Therefore, South Africa only has an observer status in the EPA negotiations. At first sight the necessary decisions regarding the EPA negotiations have been taken. But problematic implications connected to EPA negotiations concerning multiple memberships persist, as will be discussed in more detail below.

The present study aims at analysing the problems arising from multiple and overlapping membership from a political, legal and economic and trade policy perspective. It also suggests three viable solutions. The study is divided in three parts: Part one analyzes the historical, political and legal aspects and implications of multiple membership in the region; and part two looks into the economic consequences. The concluding third part discusses three options to address the overlap problem and identifies the trade-offs entailed by each option. Recommendations are made for the way ahead.

Table I: Membership in RIIs/ RECs in Eastern and Southern Africa, in the WTO, and LDC Status as of July, 2005

	COMESA	COMESA FTA	ESA EPA	SADC SACU	SADC EPA	EAC	ECCAS ²	IGAD ³	IOC ⁴	WTO	LDC
Angola				*	*		*			*	*
Botswana				*	*	*				*	
Burundi	*	*	*				*			*	*
DR Congo	*		*	*			*			*	*
Comoros	*		*						*		*
Djibouti	*	*	*					*		*	
Egypt	*	*								*	
Eritrea	*		*					*			*
Ethiopia	*		*					*			*
Kenya	*	*	*			*		*		*	
Libya	*										
Lesotho				*	*	*				*	*
Madagascar ⁵	*	*	*						*	*	*
Malawi	*	*	*	*						*	*
Mauritius	*	*	*	*					*	*	
Mozambique				*	*	*				*	*
Namibia				*	*	*				*	
Rwanda	*	*	*				*			*	*
Seychelles	*		*						*		
South Africa				*	*	Observer Status				*	
Sudan	*	*	*					*			*
Swaziland	*			*	*	*				*	
Tanzania				*	*	*				*	*
Uganda	*		*			*		*		*	*
Zambia	*	*	*	*						*	*
Zimbabwe ⁶	*	*	*	*						*	*

² ECCAS is the Economic Community of the Central African Communities and includes in addition to the countries listed Cameroon, Central African Republic, Chad, Congo (Brazzaville), Equatorial Guinea, Gabon, and São Tomé and Príncipe.

³ IGAD is the Intergovernmental Authority on Development and includes in addition to the countries listed Somalia.

⁴ IOC is the Indian Ocean Commission and includes in addition to the countries listed La Réunion.

⁵ Madagascar joined SADC in August 2005.

⁶ Zimbabwe was not classified an LDC in the Cotonou Agreement (Annex VI, Art. 1), but has been reclassified into that category by the World Bank in 2001.

Part I: Historical, Political and Legal Aspects

1 The SACU, SADC, COMESA, EAC and the AEC

1.1 Historical Background, Integration Agendas and Evolving Institutional Arrangements

1.1.1 African Union Vision and Previous Rationalisation Efforts

African Economic Community

African leaders have long recognized the importance of cooperation and integration among African countries for Africa's sustained development. They decided to integrate their economies into sub-regional markets that will eventually lead to the formation of an Africa-wide economic union. Representatives of 32 Africa countries for that reason signed a Charter establishing the Organization of African Unity (OAU) on 25 May 1963 in Addis Ababa.⁷ A further 21 states have joined gradually over the years, with South Africa becoming the 53rd member on 23 May 1994. In 1980 African Heads of State adopted the Lagos Plan of Action at an Extraordinary Summit of the OAU as the first step towards increased integration on the African continent. These objectives were put into action with the adoption of the Treaty establishing the African Economic Community (AEC) in 1991. In a further step to expedite the process of economic and political integration on the continent, members of the OAU decided in 2000 to transform the OAU into the African Union (AU). The AU was officially launched at the Durban Summit of the OAU in 2002.⁸

The AEC Treaty or Abuja Treaty as it is more commonly referred to, came into force in May 1994.⁹ Since the entry into force of the Abuja Treaty the OAU has been operating on the basis of two legal instruments. The AU however now aims to evolve the OAU and the AEC into one unified institution. The objectives of the AEC are to promote economic,

⁷ Transition from the OAU to the African Union
http://www.au2002.gov.za/docs/background/oau_to_au.htm

⁸ African Union in a Nutshell <http://www.africa-union.org>

⁹ African Economic Community, South African Department of Foreign Affairs
<http://www.dfa.gov.za/foreign/Multilateral/africa/aec.htm>

social and cultural development in Africa to ensure higher standards of living, economic stability and peaceful relations between member states. It sees the various existing and future RECs in Africa as the building blocs for the AEC. The Treaty provides for the gradual formation of the AEC through the integration, harmonisation and coordination of the various RECs' activities.

Due to the special role of RECs in the establishment of the AEC, a Protocol was concluded in 1998 on the relations between the AEC and RECs. This Protocol serves as a framework for the harmonization of integration between the RECs on one hand and between the RECs and the AEC on the other hand. A number of RECs have been designated pillars of the AEC. These are SADC, COMESA, the Economic Community of West African States (ECOWAS), the Economic Community of Central African States (ECCAS/CEEAC) and the Arab Maghreb Union. Other active RIIs include the IGAD, the Central African Economic and Monetary Community (CEMAC), the EAC, SACU and the West African Economic and Monetary Union.¹⁰

It is envisaged that the process of establishing the AEC will take place in six stages to be completed by 2028 and that it will mainly consist of activities of the RECs. The Abuja Treaty requires these RECs to have the establishment of the AEC as one of their final objectives.¹¹ The six stages of the process consist of specific activities to be implemented alongside one another. It requires RECs to establish free trade areas followed by CUs, to eventually form a continental CU followed by the establishment of an African Common Market and eventually an African Economic Union.

The first stage consists of the strengthening of existing RECs and the creation of new ones where needed. This stage was foreseen to not exceed five years. The second stage focuses on the stabilization of the economies and the strengthening of sectoral integration, particularly in the field of trade, agriculture, finance, transport and communication, industry and energy, as well as coordination and harmonization of the

¹⁰ African Economic Community, South African Department of Foreign Affairs
<http://www.dfa.gov.za/foreign/Multilateral/africa/aec.htm>

¹¹ Article 88 of the Treaty establishing the African Economic Community, 2001

activities of the RECs and should be undertaken in eight years. In the third stage RECs have to move to establish FTAs followed by a CU over a period of ten years. Stage four envisages the formation of a Continental CU through the coordination and harmonization of tariff and non-tariff systems among RECs within two years. Stage five allows a further four years for the establishment of an African Common Market and the adoption of common policies. The final stage envisages the integration of all sectors, the establishment of an African Central Bank and a single African currency, the establishment of an African Economic and Monetary Union and the creation of the first Pan-African Parliament within five years.¹²

It is clear that the AU depends on the progress of integration within the various RECs for its ultimate success. The aim of the AU is to reach the deepest level of integration possible on the African continent by 2028. The timely implementation for this will however depend on the timely implementation of the integration agendas of the different RECs on the continent. Most of the RECs in Southern and Eastern Africa are, however, behind on implementation and there is a widely perceived lack of commitment to deeper integration. To attain the level of deep integration as foreseen by the AU, countries in the region will have to rationalize and consolidate the various RECs. The UN Economic Commission for Africa (UNECA) has recently carried out their second report on rationalisation among the RECs and RIIs in the Africa Region which was commissioned by the AU and is being discussed at a series of regional workshops. While several scenarios for the rationalisation process of the RECs are suggested the fundamental message is that a substantial reduction of overlap and duplication of programmes and agendas is necessary to ensure that the benefits of integration can eventually be reaped (cf. AU, 2005; ECA, 2005a; ECA, 2005b; UNECA, 2005).

1.1.2 Southern African Customs Union

SACU was first established by the Customs Union Agreement of 1910 between the Union of South Africa and the three so-called High Commission Territories of

¹² African Economic Community, South African Department of Foreign Affairs
<http://www.dfa.gov.za/foreign/Multilateral/africa/aec.htm>

Bechuanaland (now Botswana), Basutoland (now Lesotho) and Swaziland. The 1969 Customs Union Agreement between South Africa, Botswana, Lesotho and Swaziland subsequently replaced the 1910 Agreement. Namibia became a contracting party to the 1969 Agreement in 1990 upon its independence from South Africa. SACU currently consists of the BLNS-countries and South Africa, who still is by far its economically most important and politically most influential member.

SACU is the most advanced regional integration arrangement on the African continent and the oldest CU in the world. Members have a CET and four of the five member states form a common monetary area (CMA).¹³ The main objectives behind the establishment of SACU were to promote regional integration and the facilitation of trade between the members of the Agreement in order to improve the economic development of the region, in particular the less advanced members.

South Africa enjoyed a highly dominant position under the 1969 Agreement. It had the sole authority to determine customs, excise and sales duties as well as trade policies for the whole customs area, limiting other member states' sovereignty in the areas of monetary, fiscal and foreign exchange policy. All customs and excise duties collected in the common customs area were paid into South Africa's National Revenue Fund. The revenue was shared by all members according to a revenue-sharing formula provided for in the Agreement. SACU revenue constitutes a substantial share of the state revenue of the BLNS countries.

The BLNS countries were becoming increasingly unhappy with the revenue-sharing formula and the lack of a democratic structure providing for joint decision-making in SACU. Efforts were made by the BLNS states to renegotiate the 1969 Agreement in the early nineties but it was only after 1994 when South Africa got its first democratic government that the negotiations got off the ground. SACU member states signed a new SACU Agreement in 2002, which entered into force in July 2004. This new agreement

¹³ Botswana is the only member state falling outside of the CMA. Its currency, the Pula, is linked indirectly to the Rand via a currency basket of which rands make up more than 50%.

established a new institutional framework providing for democratic decision-making processes as well as a new revenue-sharing formula.

SACU is now an international organization with a Secretariat based in Windhoek, Namibia. The Secretariat is responsible for providing administrative support to the member states and the other SACU institutions. The Council of Ministers is its primary decision-making institution. A Customs Union Commission serves an advisory role to the Council and oversees the implementation of the Agreement. A Tariff Board will make recommendations on the CET and other duties to the Council. The agreement furthermore provides for a number of Technical Liaison Committees, National Bodies and a Tribunal.

The SACU Secretariat and the various new institutions are in the process of being set up. In the interim South Africa is still administering the common revenue pool and undertaking trade remedy investigations on behalf of the BLNS. The new revenue-sharing formula has a built-in bias in favour of the BLNS countries to compensate them for the fact that they are involved in a CU with the economically better developed South Africa. The new formula also for the first time includes a development component of which the distribution is weighted in favour of the less developed states.

The 2002 SACU Agreement contains an important provision prohibiting any member state from entering into trade negotiations with third parties without the consent of the other Member States. Member States have agreed to in future negotiate all trade agreements jointly and to establish a common negotiating mechanism. This will prevent a single Member State from negotiating trade agreements with third parties that could have negative effects on other members, such as the case with the TDCA between South Africa and the European Union. We will look at the implications of this new provision for overlaps in regional integration arrangements in more detail below.

SACU is currently involved in a number of trade negotiations with third parties. It concluded a Preferential Trade Agreement (PTA) with MERCOSUR in December 2004 and expects to finalize a free trade agreement with EFTA by end 2005. It has expressed interest in negotiating similar agreements with India, China and Nigeria. It is also

involved in negotiations with the USA to conclude a free trade area, but talks have come to a virtual standstill due to lack of agreement on substantive issues such as investment and the protection of intellectual property. One of the reasons for this is that SACU still needs to develop common policies on a number of issues.

The new SACU agreement requires member states to develop common policies on industrial development, agriculture, competition and unfair trade practices. Furthermore, these negotiations include issues such as services and investment that are not currently covered by the jurisdiction of SACU. Member states will therefore have to take a look at developing these policies and to expand the agreement to cover these new issues if they are really serious about further integrating SACU.

1.1.3 Southern African Development Community

SADC differs from other regional integration organizations in Southern Africa in that it did not start off as a typical regional trade arrangement.¹⁴ The predecessor to SADC, the Southern African Development Coordination Conference (SADCC) was established as a development organization with its main objective to form a group of *frontline* states to counter the dominance of the then apartheid South Africa in the region.

SADCC was established in April 1980 with nine members.¹⁵ It was to be responsible for the mobilisation of funding and the coordination of the implementation of development projects of common interest among its member states. The priority areas to be focused on included food security, agricultural research and the development of transport and communications infrastructure. SADCC's agenda did not include regional integration or market integration as focus areas. The responsibility of coordinating the different sectors was allocated to specific member states. This decentralised approach meant that SADCC

¹⁴ A typical regional trade arrangement is considered here to be based on opening up trade between its members and follows the normal economic integration route from free trade area to a customs union, common market, economic union and ultimately developing into an economic and political union.

¹⁵ The founding members of the SADCC were Angola, Botswana, Lesotho, Malawi, Mozambique, Swaziland, Tanzania, Zambia and Zimbabwe. Namibia joined the organisation after its independence in 1990.

only had a small secretariat in Gaborone, responsible for overseeing the various regional projects and for organizing meetings of its constitutive organs.

SADCC was transformed into SADC on the 17th of April 1992 with the signing of the SADC Treaty in Windhoek, Namibia.¹⁶ The founding members were Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Swaziland, Tanzania, Zambia and Zimbabwe. South Africa became a member in 1994 and the Democratic Republic of Congo (DRC) and Seychelles acceded in November 1997, bringing SADC's total membership to 14 countries. The current membership of SADC stands at 13 countries, as Seychelles's withdrawal of membership became effective at the beginning of July 2004. It will however be back to 14 countries soon as Madagascar was awarded "candidate membership status" at the 2004 Summit in Mauritius. Its membership is expected to become effective in August 2005.¹⁷

Personal relations formed during the anti-apartheid struggle and the sense of unity continue to impact on regional integration in both positive and negative ways. Certainly, there is some sense of a common identity. For some states the reluctance to concentrate on one REC and leave the other is at least in part informed by grown personal loyalties. For others, they may have facilitated the decision to concentrate on one REC.¹⁸ Clearly, dynamics of regional integration go far beyond personal politics. In fact, regional integration in its second, more export-oriented and trade-focused wave has become a global trend since the 1990s (Jakobeit 1997: 27-30), and Southern Africa is not more integrated than other regions in the developing world although it has a rather rich and long history of integration attempts of various kinds.

¹⁶ SADC Corporate Profile, <http://www.sadcreview.com/sadc/frsadc.htm>

¹⁷ SADC Today, SARDC, <http://www.sardc.net/Editorial/sadctoday/v7-3-8-04/sadcs Summit.htm>

¹⁸ Mozambique was very active in FLS politics, and as all FLS are in the SADC, Mozambique's decision to concentrate on that RII is in conformity with the "personal politics" thesis. Similarly, the Namibian South West African People's Organisation (SWAPO) fighting South African occupation had much closer contacts to the Frontline States and the ANC (African National Congress) than to other COMESA states. It was a SWAPO government that took the decision to leave COMESA.

The transformation into SADC was led by a number of regional and international developments. Namibia achieved independence in 1990 and the imminent demise of apartheid in South Africa removed the main political rationale behind SADCC. The OAU was established with the aim of creating an African Common Market using the various RECs as building blocks.¹⁹ To participate in this process, SADC had to extend its agenda to include regional integration and trade liberalization.

The SADC Treaty basically re-enacted the institutional structure of the SADCC. Its principal organs are the Summit of Heads of State and Government, the Council of Ministers, Sectoral Commissions, the Standing Committee of Officials, and the Secretariat. The SADC Tribunal was the only new institution provided for under the Windhoek Treaty. The overall responsibility for implementing the new trade integration agenda remains with the Sectoral Coordinating Units in the governments of member states. These national units were however not always best placed to coordinate regional activities.

This and other institutional deficiencies led to a review of SADC by the Council of Ministers. At an Extra-Ordinary Summit on 9 March 2001, in Windhoek, Namibia, the SADC Heads of State and Government approved the restructuring of SADC's institutions. In contrast to the country-based coordination of sectoral activities and programmes, SADC has now adopted a more centralised approach through which the 21 Coordinating Units have been grouped into four clusters:

- Trade, Industry, Finance and Investment;
- Food, Agriculture and Natural Resources;
- Infrastructure and Services;
- Social and Human Development and Special Programmes.

One of SADC's objectives as stated in the Declaration and Treaty of SADC is to *“develop policies aimed at the progressive elimination of obstacles to the free movement of capital and labour, goods and services, and of the people of the Region generally,*

¹⁹ Website of the African Union available at www.africa-union.org

among Member States".²⁰ In 1996 eleven of the then twelve member states of SADC signed the Protocol on Trade in Maseru, Lesotho. Angola, the only country not to sign it at the time acceded to the Protocol in March 2003. It entered into force on the 1st of January 2000 after being ratified by the required number of member states. Before implementation of the Protocol commenced, member states concluded an Amendment Protocol in August 2000 dealing with issues of implementation and matters such as rules of origin (RoO) and dispute settlement. This Amendment Protocol entered into force on the 1st of September 2000. The DRC is the only member state not yet signatory to the Trade Protocol.

The main objectives of the Trade Protocol are to *"further liberalize intra-regional trade in goods and services on the basis of fair, mutually equitable and beneficial trade arrangements"* and *"to establish a free trade area for the SADC region."*²¹ According to the Protocol the FTA will be established between all signatories to the agreement by 2008. In terms of SADC's Regional Indicative Strategic Development Plan the FTA is seen as the first step towards creating a CU by 2010 and a common market by 2015.²² Currently these targets seem to be on the optimistic side as many of the member states have back-loaded the bulk of their liberalisation commitments under the Trade Protocol. Angola still needs to make a tariff offer to its SADC FTA partners and has therefore not even started to implement the Trade Protocol.

The Trade Protocol provides for a period of eight years for the completion of tariff liberalization between member states. The actual tariff phase-downs are asymmetrical with SACU liberalizing faster than non-SACU member states. SACU's tariff offers were front-loaded while the other member states' offers were back-loaded, meaning that for them the bulk of tariff cuts will only take place towards the end of the phase-down period. The timetables for liberalization of tariffs differ according to different categories of products. Certain products were to be liberalized immediately upon implementation of the Protocol, while other products would be liberalized over a period of 8 years. Certain

²⁰ Article 5(2)(d) Declaration and Treaty of SADC

²¹ Article 2 SADC Trade Protocol

²² SADC RISDP (2003), para. 3.2.2.2. and Table 10.

products deemed to be “sensitive products” received an additional 4 years for liberalisation while others were completely excluded. The Trade Protocol contains highly rigid product-specific RoO for trade conducted under the protocol.

1.1.4 Common Market for Eastern and Southern Africa

COMESA is currently the largest regional grouping in Africa. It consists of nineteen member states, almost half the total number of African countries.²³ The predecessor to COMESA, the Preferential Trade Area for Eastern and Southern African States was established in 1982. The Treaty establishing the Preferential Trade Area was signed in 1981 and came into effect on September 30, 1982 after the required number of member states had ratified it.

The Preferential Trade Area was established to take advantage of a larger market and to allow for greater social and economic co-operation between countries in the region. It was the first step towards the ultimate goal of forming an Economic Community. The treaty called for the gradual reduction and eventual elimination of customs duties and non-tariff barriers. It provided for the transformation of the Preferential Trade Area into a common market within ten years after the entry into force of the Treaty. This objective was fulfilled with the establishment of COMESA. The Treaty establishing COMESA was signed in Kampala, Uganda in 1993. It entered into force on 8 December 1994 upon ratification of the Treaty by 11 signatory states.

The COMESA Treaty contains two important principles that set it apart from its predecessor. Firstly, it allows for variable geometry or multiple speeds making it possible for a group of countries to move faster in the regional economic integration process than other countries. It furthermore provides for the imposition of sanctions on countries that

²³ The member states of COMESA are Angola, Burundi, Comoros, DRC, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe.

default in the implementation of agreed COMESA programmes and for the settlement of disputes arising from the interpretation or implementation of the Treaty.

The systematic development of COMESA from a Preferential Trade Area to a common market to an economic community is in conformity with the objectives of the Abuja Treaty that envisages the formation of an African Economic Community using the various regional economic groupings on the continent as building blocks. It is one of COMESA's stated objectives to contribute towards the establishment, progress, and the realisation of the objectives of the AEC.²⁴

COMESA's main objective is the promotion of regional economic integration through trade and investment. It aims to facilitate the removal of structural and institutional weaknesses of member states so that they can achieve sustainable economic growth. The focus areas for cooperation are trade in goods and services, payment and settlement arrangements, investment promotion and facilitation, infrastructure development and peace and security

The Authority consisting of the Heads of State or Government of member states is the supreme policy organ of COMESA. It is responsible for the general policy direction and control of the performance of the executive functions of the common market and the achievements of its aims and objectives.²⁵ COMESA's Secretariat is based in Lusaka, Zambia, and is the main administrative organ. A Council of Ministers supervises the Secretariat and monitors the activities of COMESA. They also make recommendations on policy direction and development. Other institutions include the Committee of Governors of the Central Banks, an Intergovernmental Committee responsible for the development of programmes of cooperation and various technical committees. The COMESA Court of Justice interprets COMESA law and settles regional disputes between member states.

²⁴ Article 3(f) Treaty of the Common Market of Eastern and Southern Africa

²⁵ Article 8 Treaty of the Common Market of Eastern and Southern Africa

The COMESA Treaty contains the agenda for regional integration under COMESA. It provides for the formation of a free trade area, to be followed by a CU and eventually an economic union. The first step has been achieved with the formation of a FTA in October 2001. Trade within the FTA has to conform to relatively simple RoO in comparison to SADC's detailed product-specific rules. Only eleven out of the twenty member states at the time joined the FTA, while the others were free to join at a later stage. Egypt, Djibouti, Malawi, Kenya, Mauritius, Madagascar, Sudan, Zambia and Zimbabwe were original signatories, while Rwanda and Burundi joined the FTA in January 2004. Lesotho and Mozambique withdrew from COMESA in 1997, followed by Tanzania in 2000 and Namibia in 2004.

COMESA is currently in the process of moving towards a CU between the existing members of the FTA. Member countries are working on the structure and the implementation of a CET. The original target set by the COMESA Treaty was to reach a CU by 2004, but this did not realise.²⁶ It is expected that this will be achieved by 2008 with an Economic Union to follow by 2025.²⁷

1.1.5 East African Community

The treaty establishing the EAC, comprising Kenya, Tanzania and Uganda, was signed on 30 November 1999 and entered into force on 7 July 2000. Rwanda is expected to join EAC in the near future. Burundi has also applied for membership.

EAC regional cooperation dates back to the early 20th century. From 1967 to 1977, the former EAC existed but collapsed mainly due to Kenya's economic dominance and the related perceived unequal distribution of integration benefits among the EAC Partner States and to political, ideological and personal differences between the respective leaders.

²⁶ Article 47 Treaty of the Common Market of Eastern and Southern Africa

²⁷ COMESA, 2003b

In the context of changing global, political and economic circumstances – particularly Uganda’s reorientation toward economic liberalism and the replacement of *Ujamaa* socialism by more pragmatic and liberal politics in Tanzania – the integration of the three countries was revived during the 1990s. A Permanent Tripartite Commission was established in 1993.

EAC’s stated objective is to engage in “fast track” integration among the Partner States by establishing a CU within 5 years, thereafter creating a common market, a monetary union and, eventually, a political federation. The objectives of the new EAC are to develop policies and programmes aimed at widening and deepening cooperation among the member states in political, economic, social and cultural fields, research and technology, defence, security and legal and judicial affairs. The vision that EAC could represent a fast-track integration group within COMESA was undermined in 2000, when Tanzania left COMESA.

On 2 March 2004, the EAC Partner States signed a CU protocol, which was ratified by all three parties by end 2004 and came into effect on 1 January 2005. The EAC Customs Union Protocol stipulates the immediate duty-free import of all goods from Tanzania and Uganda to Kenya, and free trade between Tanzania and Uganda. Uganda will phase out tariffs on 400, and Tanzania on 800 goods imported from Kenya within five years. The EAC CU will be fully operational in January 2010. In accordance with the CU Protocol, an EAC CET of zero percent on raw materials, medical equipment, essential drugs, machinery and agricultural inputs, of 10 percent on semi-finished goods and of 25 percent on finished goods was established in January 2005. The EAC CET agreed upon implies a very significant liberalisation of tariffs on third-country imports for Kenya, a marked decline in Tanzania’s tariffs on such imports and a substantial increase in third-country import tariffs for Uganda. The impact of the EAC CET implementation clearly dominates the effect of the CU on EAC member states, while intra-EAC tariff liberalisation seems to have only a relatively moderate impact. Since the start of the implementation of the EAC CU Protocol in January 2005, trade disputes among the EAC

partner states have been intense reflecting the less industrialised partners' fear of marginalisation.

The EAC CU Protocol provides for the elimination of non-tariff barriers. Other provisions cover RoO, dumping, subsidies and countervailing duties, settlement of disputes, securities and other restrictions to trade, competition, duty drawbacks and remission of duties and taxes, customs co-operation, re-exportation of goods and harmonization of trade documentation and procedures.

The CU Protocol does not directly address the issue of Kenya's membership in the COMESA FTA and Tanzania's in the SADC FTA, but stipulates that "*the Partner States shall honour their commitments in respect of other multilateral organisations and organisations to which they belong*" (Art. 37 (1)). However, a "*common policy in the field of external trade*" is envisaged (Art.37 (2)). For that purpose, "*the partner states shall formulate a mechanism to guide the relationships between the Customs Union and other integration blocs, multilateral and international organisations upon the signing of this Protocol*" (Art. 37 (3a)).²⁸ Art. 14 and Annex III provide for RoO for intra-EAC trade of goods not originating in the community, i.e. in COMESA and SADC in particular. Art 47. (4a) further stipulates that "*Partner States may separately conclude or amend a trade agreement with a foreign country provided that the terms of such an agreement or amendment are not in conflict with the provisions of this Protocol.*" The other parties have to agree to such agreements or amendments (Art. 47 (4e)). The EAC members agreed to negotiate, as a bloc, FTA agreements with SADC and COMESA. These are planned to be concluded when the EAC will become a fully functioning CU in 2010. The member states' individual trade preferences with SADC and COMESA are, therefore, considered to represent temporary exceptions from the CET. As of yet, there is no mechanism in place to deal with the problem of Kenya and Uganda having signed up to the ESA and Tanzania to the SADC grouping for EPA negotiations with the EU.

²⁸ It could not be established in full to what extent this had actually materialised. Presumably little progress has been made.

EAC Heads of State have launched an initiative to fast-track the creation of the EAC political federation. However, the political will of the highest political level is not complemented by the Partner States' administrations, where free movement of labour and persons and free establishment of private enterprises within the Community to fast-track the EAC common market encounter strong opposition. Thus, the fast-tracking of an EAC political federation remains doubtful.

EAC has the following organs: The Summit of Heads of States formulates the overall policy direction concerning the development and achievement of the objectives of the Community. The Council of Ministers is the major policy organ and *“has powers to make legally binding regulations, issue directives, take decisions and make recommendations”* (EAC 2003: 21). Its decisions are binding for all EAC institutions except for the Summit. The Legislative Assembly receives and approves bills, including the EAC budget, and has monitoring and reviewing functions. Sectoral Committees are responsible for negotiating and approving and monitoring sectoral policies on cross-border issues. The Secretariat is charged with a broad range of tasks, including co-ordination, initiation of policy proposals and studies, record keeping, financial management, strategic planning, organisation of meetings, relations with bilateral and multilateral development partners and public relations. The Co-ordination Committee is primarily responsible for ensuring consistency and complementarity of projects and programmes.

The East African Court of Justice's function is to interpret the EAC Treaty and adjudicate, discuss and rule on disputes and make EAC a law-based institution. Judges are appointed and can be removed by decisions of the Summit. A regional parliament, the East African Legislative Assembly, comprises 27 members elected by the Partner States' parliaments. These provisions ensure a strong influence of the national governments on the parliament (Mair 2001: 17). The Assembly's most important competence is budget authority, but it essentially serves as a debating forum on matters pertaining to the Community. It provides reports to the national assemblies and liaises with them, as their opinion has to be considered in the Assembly's debates. The small size of the Assembly

relative to the workload casts doubts on its ability to adequately monitor Community processes (ibid.).

1.2 Compatibilities and Incompatibilities of Multiple Memberships

1.2.1 EPA Negotiations and Future Customs Unions

EPA negotiations might impact on future regional integration in several ways. It has to be recalled that EPAs are to be finalised by the end of 2007. This implies a very tight schedule, given that so far little progress has been made and that in the region as well as globally comprehensive free trade agreements tend to take much more time than two to three years to negotiate. EPA negotiations face more obstacles than is conventionally the case because (African) states which do not have a common trade policy have to negotiate together. Yet, countries must have a common trade policy when they establish a CU, terms of which are unclear as of yet. The level of harmonisation needed is even greater when the REC evolves to a monetary union and a common market. This translates into countries not having a common trade policy but negotiating now for a time period when they must have one.

Countries in Eastern and Southern Africa formed regional groupings for the purpose of negotiating EPAs with the EU. Due to the overlaps in membership of the existing regional organizations they could not be used for this purpose, resulting in a split into two negotiating configurations. The first is the Eastern and Southern Africa (ESA) configuration consisting of Burundi, Comoros, DRC, Djibouti, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Uganda, Zambia and Zimbabwe. The SADC configuration consists of Botswana, Lesotho, Namibia, Swaziland, Angola, Mozambique, and Tanzania. The BLNS-countries as members of the SACU are already *de facto* part of the Trade, Development and Cooperation Agreement concluded between South Africa and the EU in 2000. Discussions are ongoing whether or not a formal accession of the BLNS to the TDCA should be finalized – and what the implications would be. In practice, the tariff phase-down as envisaged under the TDCA appear to be applied to the BLNS as well.

As these configurations are not in line with the memberships of the existing regional organizations, the question is how these configurations can be reconciled to facilitate regional integration. The EPAs in fact mean bilateral FTAs between the individual African states and the EU. This poses few problems when all SADC EPA or ESA countries sign the same agreement, but in the end, all countries could end up signing different agreements.²⁹ Not least due to the inadequate relation between the time frame and negotiating capacities, this is a realistic possibility. It would seriously complicate, if not prevent, any harmonisation of trade policies necessary for future deeper regional integration.

In order for CUs to function fully, it is advisable that all its members have the same trade commitments to the rest of the world. Therefore, countries that negotiate an EPA together should sign essentially the same agreement. Exceptions can be made in that some countries, particularly LDCs, should be allowed to back-load implementation of parts of the agreement, e.g. tariff reductions. The EAC countries should negotiate an EPA together, countries aiming at joining a COMESA CU should negotiate an EPA with ESA and countries aiming at joining a SADC CU should negotiate an EPA within the SADC EPA framework. ESA and SADC members DRC, Malawi, Mauritius, Zambia and Zimbabwe will face difficulties should they want to join a possible SADC CU. For Tanzania, it seems acceptable that the country negotiates an EPA with ESA without being a COMESA member.

1.2.2 Multiple Memberships in SADC/COMESA/SACU

There is overlap of membership between regional integration arrangements in the Southern and Eastern African region to an extent unparalleled anywhere else in the world. These arrangements include SACU, SADC, COMESA, EAC, IGAD, IOC and the CBI. This section deals with the lack of consistency in the membership of these regional trade blocks in Southern and Eastern Africa and the implications of this state of affairs for

²⁹ In fact, this is an almost inevitable outcome of a COMESA proposal on the structure of EPAs (COMESA 2003:§33), which however currently seems unlikely to be realised. Cf. as well Tandon 2004.

areas such as the EPA negotiations with the EU. As IGAD, the IOC and the CBI do not currently pose any problems in this regard the discussion below will focus on the other arrangements mentioned.

These overlaps are cause for concern as they create many problems and uncertainties. Conflicts in jurisdiction arise where two different integration organizations have similar mandates, or where a country belongs to two or more integration organizations with conflicting policies. This increases the burden placed on these organizations and their member states already lacking the necessary capacity and resources. It also leads to legal uncertainty in cases where more than one trade arrangement applies to trade between two countries. Uncertainties of this kind not only undermine the implementation of the agreements that aim to establish rules-based dispensations, but it also adds considerably to transaction costs and duplication in both regional trade and trade with outside partners. The general uncertainty and unpredictability caused by this also impacts negatively on the investment climate in these countries and their organizations. The need for reducing this overlap in membership is very clear.

SACU and SADC

All five SACU countries are members of SADC and in the process of implementing the SADC Trade Protocol. The different integration agendas of SACU and SADC do not pose any problems at this point in time, as all members of SACU are in the process of implementing the SADC FTA. Once SADC establishes a CU, SACU countries will not be able to still be part of SADC unless the two organizations' customs rules and CETs can be harmonized.

SACU and COMESA

Swaziland is the only SACU member that is also a member state of COMESA. It wants to become part of the COMESA FTA, but as it has to implement the CET of SACU, COMESA FTA members had to give Swaziland derogations from its obligations under the COMESA FTA. This means that Swaziland enjoys preferential access to the markets

of COMESA FTA states, but Swaziland does not have to reciprocate these preferences. This is necessary as Swaziland cannot break SACU's CET without the consensus of the other SACU member states. Namibia enjoyed the same derogations as Swaziland until it withdrew from COMESA in 2004.

This problem is complicated further by the fact that COMESA is moving towards becoming a CU. The position of Swaziland would then become untenable and it will require a serious discussion and decisions in SACU on how to deal with this matters. Swaziland maintains that she is highly dependent on the trade with COMESA and that these markets have been developed over a long period of time. The position she is in at present, namely to rely on derogations is creating uncertainty and unpredictability and in any case expires in 2005. Swaziland therefore wants to negotiate a more permanent arrangement, but in terms of the new SACU agreement it needs consensus of the other SACU member states for concluding or amending any new trade arrangements with third parties.³⁰

SADC and COMESA

Of the fourteen SADC member states, eight are also members of COMESA. Tanzania, Namibia and Lesotho have recently withdrawn from COMESA while the Seychelles opted to pull out of SADC. Madagascar is in the process of completing its accession to SADC, but remains at the same time a member of COMESA. At the current level of integration the overlaps between SADC and COMESA do not pose serious problems. It does however create uncertainty as to which tariff rates and RoO should be applied to trade between two countries belonging to both organizations. COMESA is in the process of implementing a CU, but SADC is still working towards forming a FTA by 2008. The planned formation of a SADC CU by 2010 will make it impossible for its members to also remain part of the planned COMESA CU.

While it has been often suggested that these two organizations will be better off if they were to merge, the matter has proved to be very politically sensitive. Efforts have been

³⁰ Article 31 SACU Agreement of 2002

made to coordinate the work of the two organizations in order to prevent duplication and conflict of their programs, projects and activities. Since 2001 the two organizations have been cooperating on a number of areas such as trade analytical work, capacity building and negotiations, transport issues and international relations such as preparations for and negotiations with the EU and in the WTO.

SADC and EAC

The position of Tanzania within the EAC further complicates matters. Tanzania announced its withdrawal from COMESA in July 1999, citing the proposals by COMESA to reduce customs duties by 90% as the main reason.³¹ It announced that it wanted to focus on its membership of the EAC and on implementing the SADC Trade Protocol. This state of affairs will however have to change once SADC moves towards becoming a CU, as Tanzania cannot implement more than one organization's CET. The EAC will also have to maintain customs and RoO to ensure that products entering into Tanzania under the SADC Trade Protocol do not find their way into Kenya and Uganda, effectively avoiding having to pay the normal import duty into those countries. The EAC is therefore only a partial CU at the moment.

COMESA and EAC

Kenya and Uganda are both members of the EAC and of COMESA. Up to very recently this did not pose problems, as the EAC is basically a fast track of the COMESA integration agenda. The EAC has however recently started to implement a CU. This means that Kenya and Uganda's membership of COMESA will become incompatible with their EAC membership as soon as COMESA moves to become a CU. In order to prevent this, harmonization of the two different RECs CET will be a prerequisite.

³¹ Profile: Common Market For Eastern And Southern Africa (COMESA)
<http://www.africa-union.org/Recs/recs.htm>

The SADC EPA Configuration

The biggest complicating factor for this configuration is the FTA between the EU and South Africa, the TDCA. Although the agreement is only between the EU and South Africa, it applies *de facto* to the BLNS countries due to their membership of SACU. Because of this existing agreement South Africa only has observer status in the EPA negotiations, as the EU and South Africa have indicated that they do not wish to renegotiate the terms of the TDCA. This creates many uncertainties as to the options available for the SADC EPA configuration. BLNS countries are in effect already providing the EU with reciprocal market access. The question is whether these countries should join the TDCA. This will mean that they will not enjoy the same market access than what they are currently enjoying under the Cotonou Agreement and the Everything-but-Arms Initiative (EBA). One of the main objectives of the EU is to increase existing market access for ACP countries through the EPA negotiations. The Cotonou Agreement contains a commitment that for ACP countries EPAs, or the alternative to EPAs would, at a minimum, be “*equivalent to their existing situation*”³². This means that the ACP countries should be no worse off than their position under Cotonou in terms of market access.

The TDCA could therefore be extended to include the BLNS countries, but then a number of annexes will have to be negotiated to ensure the preservation of their preferences. It will also have to provide for specific development provisions for the BLNS. It is unclear what position the LDCs, namely Lesotho, Mozambique and Angola will take in the end. If they decide to join the SADC EPA they will have to face reciprocal EU market access. As LDCs they will however be able to have longer phase-out periods than the non-LDCs in an EPA. They could decide to opt out of the EPA, but then they will have to rely on the Generalized System of Preferences and EBA for future access into the EU markets.

³² Cotonou Agreement, Article 37(6)

The ESA Configuration

The Eastern and Southern Africa (ESA) EPA configuration consists of Burundi, the Comoros, DRC, Djibouti, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Uganda, Zambia and Zimbabwe. As pointed out above Kenya and Uganda's membership of the EAC will become incompatible with their membership of COMESA and therefore also incompatible with their membership of the ESA configuration once COMESA also establishes a CU.

Malawi, Mauritius, Zambia, the DRC and Zimbabwe are members of both SADC and COMESA. If they want to remain part of the ESA configuration in the future, they will have to adopt the COMESA CU. If these countries choose to pursue the CU of SADC they cannot also remain a member of an EPA configuration that will eventually form a separate CU. Therefore, unless these various CUs are harmonized these countries will have to make a decision to withdraw from a certain EPA grouping or RTA.

1.3 Dynamics of Regional Integration: Interests and Activities of States in the Region

1.3.1 General Considerations on Regional Integration and its Motives

In the past as nowadays, regional integration efforts have strongly been driven by pan-African ideologies prominent among large parts of African elites. As is widely known, the frontiers of African states have for the most part been drawn by the colonising powers, and have rarely if ever been fully endorsed by the African intelligentsia. The colonial era witnessed the birth of pan-African ideologies, which have had a strong impact on political thought ever since. In the African actors' perspective, regional integration is an opportunity for Africans themselves to decide on their political boundaries. In the eyes of many and as expressed in the Lagos Plan of Action of 1980, regional integration is a step towards achieving a continental union.

Yet, conflicting rationalities, interests and preferences prevented a straightforward approach to the pan-African project. On the one hand, being seen as engaging in

integration offered prestige to leaders and increased their political status, a factor which furthered integration. On the other hand, pan-African ideology was at conflict with economic and political interests (cf. Lee 2003: 30). Political integration threatened the space of manoeuvre and elite power, as it is inevitably associated with a loss of sovereignty. Economically, countries relied on protectionism to strengthen their economy and economic elites depended on close political connections for their activities. The taxation of trade is among the most prominent sources of revenue for the state which is why a reduction of this revenue in the process of the lowering of barriers to trade via regional integration is not wholeheartedly welcome by everyone. This is the prime reason why economic integration threatened economic and financial interests in neo-patrimonial and protectionist settings, but as will be detailed below, it is problematic in more liberal environments too. The problem of multiple membership in several but barely advancing RECs arose partly because of this conflict between ideology and the search for prestige on the one hand and economic, financial and political interests on the other.³³

Since the end of the Cold War, efforts at regional integration in Eastern and Southern Africa have been revived along with the second wave of regional integration elsewhere. This is partly explained by pressures jeopardising the viability of the neo-patrimonial, authoritarian and protectionist model of government, the ongoing marginalisation of the continent in global trade, and the fall in international development assistance. The global rise of both neo-liberal principles and regional integration are additional factors. The change in attitude of the US toward regional integration, “*from active hostility to a broadly enthusiastic stance*” (Schiff/Winters 2003: 10) is in itself a major cause for the rise of the latter. Several countries in the region witnessed a change in political

³³ So far, the debate on motives for regional integration and multiple memberships in RECs is far from being conclusive. Lee largely considers a desire for domestic prestige and lack of political commitment to integration the prime reason. Multiple memberships create the impression of actively pursuing integration, while at the same time giving an opportunity to avoid a decision on deepening integration in one REC to the detriment of another (Lee 2003: 2-3). She may be right in that there is more rhetoric about integration than political will to make hard choices. Yet, political will still appears to be substantial, while African leaders tend to underestimate the economic and political obstacles as detailed below (Hansohm et al. 2003b: 255). Similarly, Goldstein and Ndung'u (2001: 18) conclude that “until these issues [i.e. problems arising from the integration of competitive rather than complementary economies and industry relocation to the more prosperous states, C.J.] are resolved, political will alone is not sufficient to restart the regional trading bloc”, in this case the EAC.

leadership, and the new generation of leaders as well as those who sought to maintain their grip on power had to re-orient towards alternative models of political and economic development. Regionalism was one of the perceived answers to the most pressing problems.

African rhetoric about the motives for regional integration highlights economic development. Regional free trade allows for benefiting from neighbouring markets and is estimated to stimulate growth by creating economies of scale for both domestic producers and foreign investors. Competition is perceived to increase, preparing regional business for competitiveness in world markets. Political integration, i.e. common commitments to the promotion of democracy and human rights as well as regional security initiatives, is considered to improve the international image of the region, thereby attracting foreign investors and working against the economically disastrous consequences of political instability.

Whether these assumptions are valid and African states can have an interest in regional integration is much in doubt. According to the mainstream of economic analysis, free trade among countries with weak economic structures is unlikely to have welfare-increasing effects for all.³⁴ It is likely to lead to a relocation of industries to the more prosperous states in the FTA and a concentration of FDI in these states, thereby increasing regional disparities (Schiff/Winters 2002: 69-71). Furthermore, political integration in regions where authoritarian structures are still strong and the democratic states are too weak to provide effective leadership should not be expected to significantly impact on democratisation (ibid.: 198-201).³⁵ Last but not least, so far regional security

³⁴ For an analysis of economic integration in Southern Africa, cf. Schweickert 1996; Dieter 1997; Gibb 1998, 2001; Lee 2003. For general considerations, cf. Schiff/Winters 2003: 63-93. If FTAs between poor countries are to have any positive effect on growth, this is due to dynamic effects difficult to predict of enlarged markets. This means that positive effects should not be expected in the short run, which in itself is an impediment to regional integration. For a rather positive view of regional integration in developing countries, cf. Shams 2003.

³⁵ However, several African leaders as well as donors base their perspective of democracy promotion on “dynamic effects” of regional integration. The effective action of the Economic Community of West African States (ECOWAS) in the case of Togo in February 2005 illustrates that this is not an altogether unrealistic perspective. Yet, the same should currently not be expected in eastern and southern Africa, as the region lacks an undisputed and widely accepted hegemon, as is the case with Nigeria in West Africa.

initiatives in Africa have been rather disappointing, and future developments are uncertain due to relatively weak institutional capacities of the relevant states and a lack of unanimity. In addition, losses in customs revenue cause governments to be reluctant with respect to further integration, although the international donor community has recently provided relatively large sums to finance a restructuring of the states' revenue basis.

However, the above motives should not be discarded as irrelevant. There are uncertainties in the analysis of economic effects, and, more importantly, several African leaders indeed believe in their vision of a better future in a unified Africa and are willing to overcome obstacles to integration. However, the importance of trade integration to African leaders should not be overestimated. Rather than being an end in itself or a measure from which significant economic benefits are expected, it essentially is politically motivated and regarded a step towards further integration (cf. Streatfield 2003).³⁶ It is important to note that the problems mentioned above are nonetheless likely to put a strain on integration processes. On balance, these are therefore still fragile, reversible and usually long on solemn declarations and lengthy protocols but short on real implementation and proven impact on the ground. Yet, additional external interests in an accelerating integration process might well work as counterbalancing factors to these obstacles.

The objective of forming alliances and increasing bargaining power to counter Africa's increasing international marginalisation is certainly important. These considerations might have gained relevance in recent years particularly due to the ongoing Doha round in the WTO and the EPA negotiations. These alliances are political rather than economic, and are based on common interests vis-à-vis the rest of the world. Yet a common trade policy as is necessary in a CU can increase common interests, thereby strengthening unanimity and negotiating power (Schiff/ Winters 2003: 225). Another prime consideration is to increase capacities in and efficiency of the management of trans-border issues, particularly infrastructure development, law enforcement/crime prevention, transboundary resources (water) and environmental protection.

³⁶ Similarly, Bischoff (2002: 292) states that in SADC(C) in particular, integration is largely driven by political concerns, although he is quite ambiguous about the motives for regional integration.

An equally important consideration is to attract more donor assistance. Overall development assistance to Africa has decreased in the last decade and has only recently begun to recover. But donors were and are willing to endorse regional integration efforts. Regional integration is largely, in the case of SADC probably up to 90 percent, funded by donor contributions (Bischoff 2002: 288). In the case of SADC, it is argued that several countries chose not to withdraw from the organisation because of the regional development programmes implemented by the four Directorates. In recent years, donor contributions financed about 80 percent of their costs, and important revenue flows are therefore attached to SADC membership (Lee 2003: 58). Generally, governments profit from internationally funded formal sector employment in the organisations for their citizens and development projects implemented by the RECs. Yet in the case of COMESA and probably the EAC as well, participating governments seem to consider the membership contributions they have to pay a worthwhile sacrifice. Membership in RECs does not seem to be considered a self-financing or immediately rewarding activity. Although this in fact was a minor consideration, Mozambique, Tanzania and Namibia explained their withdrawal from COMESA primarily with the burden provided by membership fees.³⁷

The complex mixture of motives for regional integration, and the comparatively subordinate role trade integration is playing as such, might well mean that trade issues are often pursued only half-heartedly, decisions are not fully implemented, and that hard choices in case of conflicting commitments tend to be avoided.

In light of the above, it may seem surprising that Western governments are so willing to support regional integration. In particular, these governments are likely to give greater credence to the neo-classical analysis that casts doubts on the supposed economic benefits of free trade among poor countries. Yet, assumptions on dynamic, welfare-increasing effects of enlarged markets indeed impact on donors' considerations. These

³⁷ It is currently hard to analyse in a more thorough way the impact of donor assistance, as it is not transparent to what exact extent integration schemes are donor funded nor which activities are financially prioritised by both African leaders and donors (Meissner/Ross 2004: 7).

hopes are in part a reaction to the failure of traditional development assistance. Generally, two other sets of objectives, one economic and one political, largely account for donor support of integration initiatives. Firstly, regional free trade reduces costs for both Western exporters and investors.³⁸ It furthermore is expected to strengthen interdependencies, thereby reducing risks of erratic decisions of national leaders.³⁹ Secondly, political integration is expected to increase stability by promoting democracy and establishing capacities for regional security initiatives. The latter ones are estimated to be less costly and more effective in the long-term than interventions by former colonial powers or multilateral agencies (particularly the UN) respectively, as neighbouring states are expected to have a greater interest in stability and greater legitimacy to interfere in “domestic affairs” or matters of regional interests. In addition to the obvious human development benefits of stability, it is expected to reduce the “nuisance value” of African states and further interests of Western exporters and investors.

The above considerations are valid in principle for both the USA and the EU. The free trade element and promotion of interests of domestic exporters and investors is relatively more important to the USA, whose foreign policy toward Africa is to a greater extent determined by national interests as traditionally defined (cf. Schraeder 2002). In addition, US security co-operation, whether under a regional banner or not, is at least as much determined by a desire to establish links with influential elites in Africa as by interests in stability.⁴⁰ The EU’s Africa policy, at least on the level of rhetoric, is to a greater extent based on values or ideal interests in democracy, stability and human development (Grimm 2003: 245-258). But this is not to say that the EU is not very well aware of its interests which it will try to defend in EPA negotiations.

³⁸ Surely, this is only true if the fall of internal tariff barriers is not complemented by a rise in tariff barriers against the rest of the world. Tariff barriers have however generally fallen sharply in the last decade, and are likely to be further reduced due to ongoing WTO trade talks and EPA negotiations.

³⁹ This assumption is particularly pronounced in the EU and being informed by its own historic experience, rather than being based on World Bank analysis such as Schiff/Winters (2002) who are very sceptic about RECs among poor countries.

⁴⁰ As a senior US diplomat in Botswana asserted, in view of the “ongoing influential role of militaries in transitions to democracy in the post-Cold War era”, it was only logical that the US “seek to ensure close ties with military leaders of tomorrow” (Schraeder 2002:343).

1.3.2 South Africa

South Africa is by far the strongest and most developed economy in the region and therefore needs to be examined more closely.

In order to understand South Africa's role in regional relations, we need to take a look at its history. Under apartheid rule, South Africa's regional policy was characterised by aggressive attempts to extend its sphere of economic and political influence and active destabilisation of neighbouring states supporting the anti-apartheid struggle. This legacy still impacts on regional relations, but in many ways the transformation to majority rule marked the beginning of a new era.

Broadly speaking, two phases in post-apartheid South Africa's foreign policy can be distinguished, which coincide with the terms of office of its Presidents. Nelson Mandela's foreign policy was characterised by a desire to reconcile South Africa with its regional neighbours, strong idealist leanings, and a still relatively strong influence of apartheid officials in the Department of Foreign Affairs. Although it largely had Mandela's fingerprints (or probably rather those of his successor, Thabo Mbeki, considered to be the prime architect of South Africa's post-apartheid foreign policy), South Africa's neighbours continued to view the country with some suspicion. Reasons for this were the legacy of regional relations and South Africa's economic dominance, the influence of apartheid officials pushing for a more assertive foreign policy, and Mandela's willingness to interfere in what frequently is regarded as internal affairs, as was exemplified by the Zimbabwe issue. The new government clearly started with a new foreign policy for the region without necessarily being always coherent.

South Africa's idealist foreign policy suffered from several setbacks, notably by being left alone in its sanctions policy against Nigeria ruled by General Sani Abacha at the time, and the near-breakdown of relations with Zimbabwe, without any noticeable impact on that country's politics. Consequently, it was decided to put foreign policy on a more realist basis without jeopardising relations with the neighbours. In 1999, wealth creation and security were defined as prime national interests. Democracy promotion and human

rights have since received less attention, probably decreasing wariness of some of its neighbours.⁴¹ On the other hand, slow economic growth and rising unemployment meant that South Africa pushed its interests in regional free trade negotiations, strengthening perceptions of South Africa as the “bully” in the South. By some, it is considered an arrogant hegemonic power and a latent or manifest threat to other economies.

South Africa’s economic strategy after the end of apartheid has essentially been to reintegrate into global markets. The end of its international isolation entailed that SACU, which it used to dominate, has lost in importance to South Africa. As has been mentioned, towards the end of their regime, apartheid officials increasingly considered SACU dispensable. South Africa’s efforts to integrate into global markets have had a direct impact on SACU and indirect ones on SADC. Until the new SACU agreement concluded in 2002 entered into force in July 2004, South Africa took trade policy decisions affecting the SACU CET largely on its own. In 2000, South Africa concluded a TDCA with the EU without consulting the other stakeholders (Baumhögger 2004: 337), although the agreements will result in decreased revenue for BLNS.⁴² The TDCA is likely to strongly impact or even predetermine the results of the SADC-EU EPA negotiations.

South Africa has significant interests in the region and in regional integration. Firstly, SADC is a promising export market for South Africa’s internationally uncompetitive products, as was and is the SACU. It is currently hard to say how important the SADC market is to South Africa. Official statistics seem to indicate a minor importance, as SADC only absorbs a single-digit percentage of total South African exports, the EU appearing as the main trading partner. Yet, according to Alden/Pere (2003: 57) (partly quoting Davies), South Africa’s *“biggest export market is SADC. This is often overlooked when surveying South Africa’s trade figures, the reason being that a great*

⁴¹ In recent years, South Africa, Namibia, Mauritius and Botswana were the only SADC countries considered “free” according to the Freedom House index (www.freedomhouse.org).

⁴² However, shrinking external tariff revenues are a secular tendency connected to global liberalisation. Recently, SACU’s successive tariff reductions under WTO commitments have reduced the overall revenue pool. As well, the implementation of the TDCA and the EFTA agreements was strongly back-loaded in favour of South Africa and in extension of SACU.

*portion of South Africa's exports to other countries are 'hidden' within SACU. Once SACU figures are disaggregated, South Africa's 'exports to SADC in 1994 and 1995 were larger than those to the EU and its exports to non-SACU SADC countries almost doubled between 1993 and 1996. Consequently, the importance of the SADC market to South Africa should not be underestimated.'*⁴³

Interests in access to economically strategic resources may be of even greater importance than free trade. These interests relate to mining, water and energy. South Africa has got a relatively developed mining industry (although two important companies have recently relocated their headquarters to other countries), and seeks to secure destinations of investment for it. The admission of the DRC to SADC is frequently explained by South African interests in that country's mining potential and, to a lesser extent, in its water (Miti 2002: 150; Erasmus 2003: 91).⁴⁴ Both South Africa's agricultural and industrial sectors are dependent on regional water resources, particularly for their future development (Erasmus 2003: 81). Future water imports are expected to come from countries further north. It is also argued that the military intervention of South Africa (and Botswana) in Lesotho in 1998 was motivated by the objective of avoiding a disruption in the Lesotho Highland Water Project deliveries to the industrial hub of Johannesburg (cf. Ajulu 2002; Alden/Pere 2003: 24). Another major interest of South Africa in the region is that of limiting immigration (Miti 2002: 148-149), although Miti's assertion that this was the prime perceived security threat (ibid.:157) is probably exaggerated. The Zimbabwe crisis and its implications on regional economic stability is a

⁴³ Recently, South African business seems to have discovered the advantages for international competitiveness of relocating labour-intensive processes to neighbouring countries. This, however, seems to have had little impact on integration negotiations so far (cf. Brenton et al. 2004).

⁴⁴ Of course, the issue is much more complex than that. Notably Zimbabwe and Angola along with Namibia intervened militarily in that country's war in 1998 to support the Kabila-government and had mining and arms trade interests in the DRC. South Africa estimated that a democratisation process and negotiations between the warring parties, which would take into account Rwanda's security interests, were a better approach to restoring stability. It opposed the military intervention and thereby attracted the hostility of the DRC's government. It should be added that despite the DRC's admission to the SADC, integration of that country should not be expected to make much progress in the near future. The governments of the region's war-torn states, i.e. Angola and DRC, are much more preoccupied with short-term interests in (regime) stability and access to their countries natural and mineral wealth than with long-term political visions (cf. Peters-Berries/Naidu 2003: 124).

major concern too. The free movement of labour in the SADC region is, if at all, only a long-term perspective given South Africa's reluctance in this issue.

Law enforcement, i.e. control of arms trade, trans-border trafficking in stolen goods, and poaching, also ranks among prime security concerns. Crime has rocketed in South Africa in the last decade due to a breakdown of the excessive mechanisms of social and police control caused by apartheid rule. Organised crime is taking on a regional dimension. Crime is nowadays perceived a prime threat to foreign investment and the tourism industry. Interests in reliable water supply, curtailing immigration, controlling arms trade and securing export markets imply that South Africa has a significant interest in a regional security structure. The fact that South Africa has not been able to effectively address the crisis in Zimbabwe has therefore led to significant irritations among donors.

Concerning regional integration, Pretoria has on the whole adopted an approach aiming at regional unity and strengthening regional security capacities. *“The guiding principles of South African policy towards the crises within SADC have focused on three basic concerns: to keep SADC united; to work to resolve institutional problems within SADC's framework (i.e. the OPDS-SADC relation); and, where necessary, to use other multilateral instruments and avenues to pursue conflict resolution [e.g. UN backing for an intervention in the DRC]”* (Alden/Pere 2003: 37-38).

At the same time, it has pushed its regional economic interests. In the negotiations on the SADC FTA, South Africa negotiated on behalf of SACU, largely without any discussion with the other SACU members (Lee 2003: 130). There are clear capacity reasons for this, but there can be little doubt that South Africa primarily pursued its own interests and the SADC FTA agreement was in large parts tailored to suit the perceived interests of its business community. Furthermore, in the negotiations on the SADC FTA, South Africa's strategy has essentially aimed at opening up regional markets for its products, while protecting its domestic agricultural and manufacturing sectors as much as possible. Despite the reservations against South Africa, the countries in the region hope to benefit from improved access to South Africa's market and to attract foreign direct investment

(FDI) from its business community. Yet, there are occasionally mixed feelings about FDI, as some fear a South African “take-over” of the domestic economies.

According to Lee (2003: 85), “*regional integration via SACU is clearly the priority for South Africa*”. Reasons for this orientation are the historically extremely influential position South Africa had in the REC and the greater importance of the SACU market as compared to others in the region. South Africa has shown an interest in increasing its regional market access. When the idea of dissolving the SACU was expressed, it was envisaged that it be replaced by a larger CU including Malawi, Mauritius, Zambia and Zimbabwe. The infeasibility of such a CU in the short run was one of the considerations informing the decision to renegotiate the SACU agreement. There are reservations among business associations and labour unions alike about further trade integration, as competition from countries with cheaper labour is feared. But recently business circles seem to have discovered the advantages for international competitiveness of relocating labour-intensive processes to neighbouring countries as has been stated above (Brenton et al. 2004). South Africa hit by rising unemployment urgently needs additional export markets and actually suffers from the slow pace of SADC trade integration.⁴⁵ On the whole, South Africa clearly has important interests in SADC integration and enlarging the CU, particularly as the course of negotiations of the FTA suggests that it will be capable of imposing its interests.

South Africa has demonstrated the will to concentrate on regional integration in its vicinity. South Africa was invited to join COMESA in 1994, but rejected the offer after a meticulous evaluation of its interests and joined SADC instead. Concerning SADC – COMESA relations, South Africa has worked for a clearer separation of the organisations and against dual memberships. For most countries with dual memberships, COMESA provides an occasion to evade or counter South African influence. This consideration also

⁴⁵ This concerns export markets in SADC and, more importantly, in the rest of the world. Despite initially lobbying for RoO that effectively constitute non-tariff-barrier-protection for South Africa’s industries, South African business circles now seem to consider the restrictive RoO as detrimental to their long-term interests. For instance, they inhibit the relocation of labour intensive processes with little value added to SADC states with lower labour costs, thus increasing prices and preventing competitiveness of the South African industries on world markets (cf. Brenton et al. 2004).

informed Zimbabwe's decision to eventually ratify the COMESA treaty of 1993 in 1998 (Lee 2003: 89).⁴⁶

1.3.3 Botswana, Lesotho, Namibia, Swaziland

Although the TDCA is a FTA only between the EU and South Africa, it applies *de facto* to the BLNS countries due to their membership of SACU. Because of this existing agreement South Africa has only observer status in the EPA negotiations, as the EU and South Africa have indicated that they do not wish to negotiate in terms of the TDCA.

This creates many uncertainties as to the options available for the SADC EPA configuration. BLNS countries are in effect already providing the EU with reciprocal market access. The question is whether these countries should join the TDCA. This will mean that they will not enjoy the same market access than what they are currently enjoying under the Cotonou Agreement and the EBA Initiative. One of the main objectives of the EU is to increase existing market access for ACP countries through the EPA negotiations. The Cotonou Agreement contains a commitment that for ACP countries EPAs, or the alternative to EPAs would, at a minimum, be "*equivalent to their existing situation*"⁴⁷. This means that the ACP countries should be no worse off than their position under Cotonou in terms of market access.

The TDCA could therefore be extended to include the BLNS countries, but then a number of annexes will have to be negotiated to ensure the preservation of their preferences. It will also have to provide for specific development provisions for the BLNS. It is unclear what position the LDCs, namely Angola, Lesotho, Mozambique and Tanzania will take in the end. If they decide to sign and implement the SADC EPA they will have to face reciprocal EU market access. But as LDCs they will be able to have longer phase-out periods than the non-LDCs in an EPA. They could decide to opt out of

⁴⁶ Zimbabwe had been a member of the Preferential Trade Area but was extremely slow to develop a position on its transformation. Although Zimbabwe's delegation had fully endorsed the COMESA treaty, the country subsequently hesitated to sign, officially citing a need to examine its impact more carefully. This led to significant irritations among its partners. Zimbabwe signed the treaty with a month delay, but did not ratify it, thereby keeping a back door open.

⁴⁷ Cotonou Agreement, Article 37(6).

the EPA, but then they will have to rely on the Generalized System of Preferences and EBA for future access into the EU markets.

Swaziland is the only SACU member that is also a member state of COMESA. It wants to become part of the COMESA FTA, but as it has to implement the CET of SACU, COMESA FTA members had to give Swaziland derogations from its obligations under the COMESA FTA. This means that Swaziland enjoys preferential access to the markets of the COMESA FTA states, but Swaziland does not have to reciprocate these preferences. This is necessary as Swaziland cannot break SACU's CET without the consensus of the other SACU member states. Namibia enjoyed the same derogations as Swaziland until it withdrew from COMESA in 2004.

This problem is complicated further by the fact that COMESA is moving towards becoming a CU. The position of Swaziland would then become untenable and it will require a serious discussion and decisions in SACU on how to deal with this matter. Swaziland maintains that she is highly dependent on the trade with COMESA and that these markets have been developed over a long period of time. The position she is in at present, namely to rely on derogations, is creating uncertainty and unpredictability and in any case expires in 2005. Swaziland therefore wants to negotiate a more permanent arrangement, but in terms of the new SACU agreement it needs consensus of the other SACU member states for concluding or amending any new trade arrangements with third parties.⁴⁸ All BLNS deserve further attention.

1.3.4 Kenya

Kenya is the most important economy in Eastern Africa, the hub of the EAC and an important COMESA member. In 2003, Kenya's exports to its two EAC neighbours reached more than 16 percent, while another combined eight percent went to its most important COMESA partners, Egypt and Rwanda.⁴⁹ The Kenyan case is now considered

⁴⁸ Article 31 SACU Agreement of 2002.

⁴⁹ Cf. IMF, Direction of Trade Statistics, December 2004.

more closely because its membership in the EAC CU and the COMESA FTA (and probably a COMESA CU) involves incompatibilities.

Kenya's main interest in the EAC is the further opening of markets for its manufactured products and, to a lesser extent, secure investment opportunities for its business community, particularly in tourism and mining in Tanzania. A few years ago, observers estimated that Kenya was quite sure of its regional economic dominance and did not consider it necessary to make significant concessions to Tanzania and Uganda in order to further EAC integration (Mair 2001: 34-35). The EAC CU Protocol signed in 2004 indicated a marked shift in Kenya's evaluation of its interests, as it has made large concessions to its partners. Kenyan exports to its neighbours had increasingly been rivalled by South Africa, and South African FDI in Tanzania's mining and tourism potential exceeded those from Kenya by far, threatening its share of the market.

Mair (2001) speculated that Kenya and Uganda might join SADC and the EAC "fast track" integration could therefore take place within the SADC FTA. The discussion on SADC membership of Kenya seems to have produced a different result. South Africa was in favour of Kenya joining the SADC. Yet, Kenya's exports are oriented toward COMESA and Tanzania,⁵⁰ and there were concerns about South Africa's capacity to rival Kenya's manufactures. East African markets are of great importance to Kenya's manufacturers, while its exports to the EU are overwhelmingly made up of primary products. As has been stated, it is envisaged that the EAC negotiate a free trade agreement with the SADC. Kenya has joined the Eastern and Southern Africa group (ESA). As long as Tanzania is not a member of ESA but the SADC EPA, this is incompatible with an EAC CET. The EAC itself would have been an EPA candidate, but the member countries decided that they had greater bargaining power by joining larger formations.

1.3.5 Interests in Dual Membership in COMESA and SADC

⁵⁰ Only 0.41 percent of Kenyan exports went to South Africa in 2003.

Countries with dual membership in COMESA and SADC that are now considered more closely are Malawi, Mauritius, Zambia and Zimbabwe. The DRC is a special case because although being a member of both COMESA and SADC, the DRC has not yet signed up to the relevant FTA commitments. All five countries have decided to negotiate an EPA with ESA, which is incompatible with joining a future SADC CU.

Generally, being a member of two different FTAs is a quite comfortable position, as it entails having preferential access to markets which mutually discriminate against each other. Such a hub position maximises market access and attractiveness for investments (Schiff/Winters 2003: 78). It can be inferred that in principle, these countries have an interest in preventing the evolution to a CU, as this would force a decision between two RECs, and an interest in preventing more extensive integration, as their advantage is conditional on mutual discrimination of the two RECs.⁵¹ In case these countries block further integration, it should be recalled that the present situation confers them a privilege to the disadvantage of the other REC member states. The same applies to Egypt, as it is a member of the Arab FTA.⁵²

Mauritius is the only one of these five states whose economic relations are quite clearly oriented toward the COMESA. Exports and imports to the COMESA outweigh those to the SADC by far, but South Africa is of interest particularly to the textile industry (Meyn 2004). Mauritius has already concluded a bilateral preferential trade agreement with South Africa. It will thus try to defend these trade relations, which might not be helpful for establishing a COMESA CU. Moreover, Mauritius has recently taken a decision to radically reduce its Most Favoured Nation (MFN) tariffs on a unilateral basis, a step which will be difficult to reconcile with any future CU.

As has been mentioned, for most countries integrated into SADC simultaneous COMESA membership is not only motivated by an interest in improved market access but is also a

⁵¹ In the case of Zambia, this ambivalence is nicely summed up in the following quote: "... when and if it comes to choosing between COMESA and SADC membership, Zambia is certain to choose both." CUTS-ARC Policy Briefs, No. 3/2005, p. 6.

⁵² The case of Egypt's and South Africa's FTAs with the EU is different because it can be expected that in the near future all countries in the region will be in a FTA with the EU.

means to counter South Africa's influence. This is particularly the case for Zimbabwe, its problems with South Africa having been mentioned above. Its choice is politically motivated, rather than economically. The main advantage of simultaneous membership in two FTAs, attractiveness for investment, currently ranks low among the regime's priorities. It is occupied with its survival in the short-run, and has deliberately employed tactics that might increase popularity at least with parts of the population, but scare foreign and domestic investors. In response to the economic crisis, it has resorted to protection rejecting SADC FTA tariff reduction obligations and raising non-tariff barriers.

In contrast, Zambia's and Malawi's choice was essentially economically motivated. As has been mentioned, the South Africa-EU TDCA is likely to have predetermined results of the SADC EPA negotiations. Zambia and Malawi consequently feared that they would be forced to accept the TDCA, and decided to negotiate the EPA with more similarly structured, i.e. less industrialised, and in their interests towards Europe more like-minded countries. As for Zambia, another consideration is likely to have strongly influenced its choice. Lusaka, Zambia's capital, is the site of the COMESA Secretariat. Therefore, the government can hardly afford to be seen as distancing itself from COMESA.

When either SADC or COMESA establishes a CU, these countries will have to choose whether and which one they want to join. If they join a CU, they can no longer be part of another FTA unless the two CUs negotiate a new FTA between them. Their choice of EPA configuration impacts on future choices.

- The first and technically least problematic option is for the countries to join the COMESA CU and leave the SADC FTA. This may be acceptable for Mauritius, but is extremely problematic for Malawi, Zambia and Zimbabwe, as their economic relations are oriented towards South Africa. A COMESA-SADC FTA still to be negotiated would limit their losses, but means as well less deep economic relations with South Africa than would be possible in a CU. However,

- if further regional and continental integration is accepted as a political goal, this seems the most realistic option.
- The countries could renounce on the COMESA CU/FTA and the ESA-EU EPA at a later stage and decide to join a SADC CU/FTA and the SADC-EU EPA. This would imply that they accept an EPA without having had a voice in negotiating it. This seems rather unlikely.
 - The countries decide not to join any CU. Given their rather comfortable current position and the regional history of “decisions not to decide” on regional integration, especially when this implies hard choices, this option is probably the most likely one. It is the option most detrimental to further African integration as well.

These options will be discussed in more detail later in this study.

1.3.6 The Situation of LDCs

17 of the countries which have joined an EPA configuration in Eastern and Southern Africa are LDCs, and currently enjoy largely unrestricted, non-reciprocal EU market access under the EBA provisions. Three out of the four RECs considered here apply the asymmetry principle within their groupings to cater for the special needs and interests of their economically weaker members. The most advanced mechanism in this regard is applied in SACU where the revenue sharing mechanism that was negotiated as part of the new SACU agreement of 2002 introduced a development component. The BLNS receive more than proportional shares of the common revenue pool while South Africa's share is relatively smaller given its high share in the total revenue collected from tariffs. SADC and EAC only have provisions for longer transition periods for the full implementation of their FTAs for the LDCs. In COMESA, some LDCs (e.g. Uganda) opted to join the FTA at a later stage only but there are no phase-in periods. Financial mechanisms to compensate the smaller countries or LDCs for revenue losses or other adjustment costs are generally lacking.

The situation becomes more complex with the negotiation of Third-Party agreements such as the EPAs. Decisions need to be taken as to how the groupings shall be treated given that the degree of economic development within each group varies greatly. A COMESA report proposes to start negotiations with the aim of extending the EBA provisions to the EPA configurations (COMESA no date: §xxxvii). Most observers, however, estimate it unlikely that the LDCs will face more favourable or equal terms under an EPA than under EBA (Lee 2003; Gibb 2004). It could therefore be expected that several of them might leave the EPA negotiations, eliminating the impact of EPAs on their choice to join a future CU.

The following reasons account for LDCs decision to nevertheless join an EPA group:

- 1) The EPAs are considered to be more than trade agreements, which means they are expected to include a “development” component. This could mean that LDCs expect development rents to compensate for decreased preferential rents in a post-ACP setting and for the breakdown of manufacturing and agricultural branches due to increased imports from the EU. As well, LDCs may consider EU development assistance a means to increase market access, as European quality standards and poor physical and marketing infrastructures constitute a more important obstacle to market access than tariffs. Generally, the EU is interested in concluding the EPAs and might apply pressure, and LDCs may consequently fear that not entering EPA agreements might reduce the overall availability of development assistance.
- 2) The Cotonou Agreement provides for “*special treatment for ACP LDCs*” (Art. 35 (3)), meaning that LDCs will be granted delays in introducing reciprocity.⁵³
- 3) LDCs expect benefits from RECs and fear that staying aside from EPAs could result in them being sidelined in RECs.

⁵³ LDCs might interpret the clause in a way which has been ruled out by the EU. “It has sometimes been understood that the principle of differentiation implies that reciprocity would not be required from least developed countries (LDCs), participating in an EPA. [...] This is, of course, not the case. Reciprocity is one of the basic elements of EPAs from which no partner wishing to participate can be excepted without depriving EPAs of their essence” (EC 2001: 13).

- 4) LDCs expect to evolve to the category of developing countries in the near future and want to be prepared for that eventuality.
- 5) LDCs expect benefits from parts of the future EPA agreements other than tariffs, e.g. more favourable RoO and quality standards. Sanitary and phytosanitary regulations are expected to be key components of the EPAs.
- 6) LDCs consider it necessary to reduce their external tariffs in order to increase competitiveness and consider EPAs an opportunity to do so with minimal effects on state revenue. The EU held out the prospect of transitional adjustment aid to compensate for losses in customs revenue and readjustment costs of state finance. This is a rather unlikely consideration, as most LDCs have already lowered their tariffs considerably under structural adjustment programmes, more than the “developed” countries in the region.

The Cotonou Agreement as well as additional explanatory documents on EPAs by the EC are, however, silent on practical ways to accommodate the LDCs within one EPA grouping that also comprises non-LDCs. Even if the EU would accept a variation in the reciprocal tariff-phase downs and accord longer phase-in periods to the less developed countries this would leave the cost of administering such different tariff regimes to each EPA configuration. For instance this would imply that RoO would be necessary within the region to avoid transshipment of EU imports via the country with the lowest preferential tariff, i.e. via the most developed member state in each region. The alternative would be for the other countries to accept the lower tariff, to the potential detriment of their revenue and their industries – which is precisely the choice between two bads the BLNS are currently facing with the *de facto* application of the TDCA tariff to their imports from the EU.

The discussions within COMESA and SADC on a CET have not yet started or have been postponed. The interests of the LDCs in the two RECs with regards to trade policies and tariffs in particular differ from those of the more developed countries in two fundamental aspects: (1) the LDCs depend to a much greater extent on revenue from tariffs and face much greater difficulty in replacing tariff revenue by other indirect taxes; and (2) LDCs on

the other hand have less interest to protect certain industries with peak tariffs than their more industrialised partners (especially Kenya, South Africa, Egypt) do. One of the most difficult decisions for LDCs to make is therefore who they negotiate with – and how much flexibility and understanding for their needs they will find. The more developed countries in the region have so far proven to be very difficult partners to bargain with, and the negotiations ahead on CUs and EPAs will not be any easier.

2 International Legislation and Rules on Regional Integration

2.1 WTO Rules and Multiple Memberships

Regional trade arrangements (RTAs) are an exception to WTO rules. Article XXIV of the General Agreement on Tariffs and Trade (GATT) 1947 allows RTAs covering trade in goods as one of the few legal exceptions to the basic GATT MFN principle of non-discrimination.⁵⁴ Article V of the General Agreement on Trade in Services (GATS) allows a similar exception for RTAs covering trade in services. In addition to this the so-called Enabling Clause (The 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries) allows preferential trade arrangements in trade in goods between developing country WTO members.⁵⁵ For the sake of this discussion we will only be taking a look at RTAs covered by Article XXIV of GATT.

In order to have a better understanding of the rules on regional integration, it is necessary for us to take a brief look at the various levels of regional integration and how the rules relate to the various types of regional integration arrangements. RTA is a very general term that could refer to a whole range of different levels of economic integration. At the first or lowest level we find preferential trade agreements, normally concluded at a bilateral level. Countries use these to liberalize trade in specific products or sectors and these agreements are therefore very limited. As stated above, developing countries are

⁵⁴ Article I GATT 1947. Each member treats all the other members equally as “most-favoured” trading partners. If a country improves the benefits that it gives to one trading partner, it has to give the same treatment to all the other WTO members.

⁵⁵ Paragraph 2(c) Decision of 28 November 1979 (L/4903) (Enabling clause).

allowed under the Enabling Clause to enter into regional or global preferential trade arrangements for trade in goods. The Enabling Clause therefore covers not only preferential trade agreements, but also other agreements such as FTAs. It however only applies to agreements between developing countries.

Other RTAs covering trade in goods have to comply with the various requirements set out in Article XXIV. Article XXIV (4) contains a general requirement that FTAs and CUs must facilitate trade between the constituent territories and not raise barriers to trade between other parties and these territories. Article XXIV (5)(b) allows the formation of FTAs or interim agreements leading to the formation of a FTA, provided that the duties and other regulations of commerce imposed by the constituent territories on trade with WTO members not party to the FTA or interim agreement at the time of establishing the FTA are no higher than before the formation of the free trade area or interim agreement. In this type of RTA members remove all barriers to internal trade within the FTA, but they retain their individual external tariffs. Examples of FTAs include the bilateral TDCA between the EU and SA, the SADC FTA under the SADC Trade Protocol and the COMESA FTA.

As the external tariff differs from one member of a FTA to another, detailed RoO need to be included in these agreements in order to prevent transshipment and to ensure that only countries that are party to the agreement benefit from the preferences provided by it. If it were not for these rules, third countries would simply transship their products duty free through the FTA member with the lowest external tariff to those with higher tariffs.⁵⁶ As RoO can prescribe a certain percentage of local content or local value added, it can be effectively used as non-tariff barriers to trade and often leads to trade diversion. This means that RoO are often used for protectionism, but unfortunately there are no WTO rules regulating the use of RoO in FTAs.

The next step in deepening integration is the establishment of a CU. In a CU we also have free movement of goods between members as in a FTA, but it goes further as it requires

⁵⁶ This practice is also known as trade deflection.

members to adopt a CET. Members therefore need to have the same external trade policy. Similarly to the case with FTAs, Article XXIV (5) (a) allows the formation of CUs, as long as the duties and other regulations of commerce imposed at the establishment of any such union or interim agreement in respect of trade with WTO members not party to such union or agreement are not higher or more restrictive than prior to the establishment of such union or the adoption of such interim agreement. Examples of CUs are SACU and MERCOSUR.

Article XXIV (5)(c) furthermore requires interim agreements, FTAs and CUs to be established within a “*reasonable length of time*”. Another requirement is that in both an FTA and a CU the elimination of tariffs and other regulations of commerce must be on “*substantially all trade*”.⁵⁷ These terms are clarified to a certain extent by the Understanding on the Interpretation of Article XXIV of the GATT 1994.

When countries move to form a common market, they start moving beyond shallow integration. In a common market the free movement of labour and capital is allowed between members. An example of this is the European Economic Community (EEC) which had achieved a common market. The EU is currently moving towards becoming an economic union with its members adopting common fiscal and monetary policies and a common currency. This form of deep integration is also the long term objective of the AU.⁵⁸

As mentioned earlier, most countries in Southern and Eastern Africa belong to more than one RTA. Some of these RTAs are already FTAs, while others are moving towards establishing CUs. Countries derive legal obligations from their membership of these arrangements. As the integration agendas and obligations differ from one RTA to the next, multiple memberships often lead to a country having to implement conflicting obligations.

⁵⁷ Article XXIV (8)(a) and (b)

⁵⁸ Cf. Evans et al. (2004).

WTO rules do not prohibit member states from belonging to more than one FTA. Article XXIV does not even mention the issue of multiple memberships. It is possible for countries to belong to more than one FTA as the RoO contained in the different agreements make it possible to distinguish similar products originating in different countries from one another. CUs, however, require member states to apply the same external tariff to third countries. This makes it impossible for a country to belong to more than one CU, as it can only have one CET.

As highlighted earlier, countries that are simultaneously members of two RECs moving towards establishing CUs will therefore have to give up their membership of one of the RECs. Examples are countries belonging to both, COMESA and the EAC, SADC and COMESA, SADC and EAC or SACU and SADC. It is practically and legally impossible for a country to implement more than one CET.

The question now remains whether a country that is a member of a CU can also at the same time individually be a member of one or more FTAs. Article XXIV (8)(a)(ii) adds a further requirement in the case of CUs for it to be able to benefit from the exception from normal WTO rules. It states the following:

8. For the purposes of this Agreement:

- (a) A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that***
- (ii) subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union;***

This makes sense as the CET is the factor that distinguishes a CU from an FTA. The implementation of the SADC FTA might therefore violate WTO rules if some members become part of the proposed COMESA CU and seek to maintain the preferential tariffs for imports from SADC countries. This explains why COMESA members offer special treatment to Swaziland, a SACU member that is also part of the COMESA FTA. The CET under SACU cannot be broken by some members granting preferences to COMESA

member states without the consent of the other SACU member states. Their refusal to permit Swaziland to reciprocate arises from the argument that once the CET is broken, it will be difficult to prevent goods illegally crossing to the other SACU members without paying duty. This will necessitate the re-imposition of RoO and customs authorities between the SACU member states. This is also the reason why the EAC could only move to establish a partial CU and had to retain RoO, as Tanzania has to grant preferences to SADC members under the SADC Trade Protocol.

Multi-bloc membership may therefore be a violation of WTO rules where a country is already a member of an existing CU. If individual members of a CU enter into a number of different FTAs with third parties, the impact on the CET and the resulting array of different RoO might render the original CU unrecognizable as such and it might no longer be able to qualify as a CU under Article XXIV.

An example of this is the proposed EPA involving the BLNS countries (and perhaps even new members) but apparently excluding South Africa, which already has its own TDCA. A separate EPA which excludes South Africa will further impact on the CET of SACU and its common policies. Article 31 may then become largely redundant. If this happens the very existence of the CU as technically conceived under Article XXIV GATT may be in jeopardy.

Further legal issues could arise from the implementation of the various protocols that might be inconsistently executed or even conflicting in application among the various blocs to which a state may belong. These could include differences in the RoO applied under the various agreements or differences in the sanitary and phytosanitary measures and standards included in the various agreements.

Furthermore, issues such as the cost of administering these rules, and the cost to the private sector or business community in fully understanding and taking full advantage of the various agreements also merit attention.

2.2 Regional Trade Agreements and Overlapping Membership

2.2.1 The SACU Agreement

The new SACU Agreement entered into force on 13 July 2004 and envisages the establishment of a completely new organization with “*common policies and common institutions*”. It wants to be a rule based organization dedicated to the integration of the economies of the member states into the global economy and the furthering of the objectives and regional integration of SACU itself. It has also, and this is an important new development, established a Tribunal which is responsible for all disputes with respect to the implementation and interpretation of the new Agreement. The new Agreement further provides for common policies to be developed in a number of areas.⁵⁹

SACU seems to be committed, at least on paper, to a proper and effective regional trade organization that wants to give effective application to its own rules and procedures and to enhance its integration. However, it faces a number of historical and contemporary issues and problems that relate directly to the complications with respect to overlapping membership. The SACU Agreement provides a procedure to potentially deal with this problem but not clear and final rules. Article 31 of the SACU agreement deals in general with trade relations with third parties. Article 31 reads as follows:

- 1. Member States may maintain preferential trade and other related arrangements existing at the time of entry into force of this Agreement.*
- 2. Member States shall establish a common negotiating mechanism in accordance with the terms of reference to be determined by the Council in accordance with paragraphs 2 and 7 of Article 8 for the purpose of undertaking negotiations with third parties.*
- 3. No Member State shall negotiate and enter into new preferential trade agreements with third parties or amend existing agreements without the consent of other Member States.*
- 4. When goods imported by a Member State from outside the Common Customs Area under a preferential agreement are exported to another Member State, the normal import duty applicable to such goods when imported into the rest of*

⁵⁹ Part 8, SACU Agreement of 2002.

the Common Customs Area will be charged. Any difference between the normal duty and the duty originally charged on these goods shall be paid into the Common Revenue Pool.

A number of principles can be distilled from this provision. Paragraph 1 legitimates the existence of preferential trade agreements predating the present SACU Agreement. Member states are allowed to maintain such preferential trade arrangements. It should also be noted that article 31(1) is unqualified. Provisions of this kind are regularly found in the agreements of regional trade organisations, but are often qualified to ensure compatibility between the new arrangement and the trade agreements of the original member states predating the new agreement. For instance, in the case of article 27(3) of the SADC Trade Protocol that permission is qualified. We take a more detailed look at similar provisions in other RTAs below.

In the case of the SACU Agreement no such qualification has been added. The intention of the parties to this Agreement apparently was quite clear; to allow member states to maintain their existing preferential trade arrangements in a manner as they were originally negotiated.

The Trade Policy Review of the WTO for SACU conducted in 2003 has listed a number of individual trade agreements between certain member states of SACU and third parties. The most important one is the TDCA between South Africa and the EU. This agreement covers trade between South Africa and its most important trading partner; a consideration also applicable to the whole SACU CU. That agreement is under review at present and it offers an opportunity to address this problem and to involve the BLNS states in the process and to create clarity and an answer to the problem of *sui generis* membership.

The SACU Agreement requires member states to establish a common negotiating mechanism and policy mandates for future negotiations between SACU as a whole and third parties. Examples of this are the FTA negotiations currently being conducted between the United States and SACU and between SACU and EFTA.

The consent of the other member states will most likely have to be obtained from the Council of Ministers. The Council takes decisions on the basis of consensus and this may result in complicated discussions within this body. Paragraph 3 is furthermore incomplete in the sense that it does not say anything with respect to the conclusion of the negotiations and the conditions that will apply when consent of this kind is granted. In cases where such consent is granted, it should be made conditional and should depend on clear policies and guidelines on what should be reported on to the Council before any agreement is concluded.

The legal consequences for SACU if the original member states continue to maintain existing trade agreements with third parties or conclude new ones will be that the CET of SACU will come under strain. SACU is a CU and as such trade restrictions among members are removed and the organization has a CET. Article 22 of the Agreement stipulates that *“Except as otherwise provided in this Agreement Member States shall apply similar legislation with regard to customs and excise duties”*. Article 19 states that *“Except as otherwise provided in this Agreement, a Member State shall not impose any duties on goods which were imported from outside the Common Customs Area on importation of such goods from the area of any other Member State”*. The latter makes sense because the normal duty has already been levied on that product to the CET.

All preferential trade agreements between individual SACU states and third parties will have an impact on the CET of SACU. If trade is conducted in terms of a FTA between a single member state of SACU and a third party, that trade will be free (or the tariffs on the goods will be removed over time in terms of the provisions of that agreement). The products so imported will however remain dutiable when imported into any other SACU member state. The source of revenue for the Common Revenue Pool normally available through the duties payable on all imports into SACU will now fall away for SACU in respect to those imports channeled through the bilateral preferential trade agreement between a particular member and a third party.

This problem can to some extent be addressed by paragraph 4 of article 31. But in order to give effect to that article the necessary customs capacity will have to be in place in all

the SACU states. This type of arrangement may also have serious rule of origin implications when transformation into other products takes place within that particular SACU member state with respect to goods imported into it from the third party and when those goods are re-exported into other SACU states.

The question is whether Article 31 provides an answer to this problem. The substantive obligation in Article 31 forbids SACU member states to unilaterally negotiate and conclude preferential trade agreements with third parties. For this they need the consent of the other member states, but as already pointed out, that consent is not described in any detail with respect to substantive issues such as the impact on the CET and the common revenue fund. As a matter of fact the existence of such *ad hoc* agreements with third parties undermines the existence and implementation of the CET for SACU.

Article 31 deals with a complicated matter and it needs to be clarified and expanded. One possible solution would be to compile a complete list of all existing trade agreements between the individual member states and third parties predating the new SACU Agreement. An analysis should be made of their impact on the CET, revenue pool and the RoO implications if any. Then a policy should be developed as to how to reconcile them with the new SACU Agreement. If required they should be renegotiated with the third parties in order to ensure compatibility with the new SACU Agreement. Another technical solution may lie in the conclusion of agreements with groups of states outside SACU or concluding free trade agreements with respect to third parties which will bind SACU as a whole. Instead of allowing one particular SACU member to enter into an *ad hoc* agreement with third parties, SACU as a whole should enter into such an agreement. This agreement can take the form of an FTA between SACU on one side and the third party on the other. In this manner the respect for working of the CET will be restored. Interpretation of such a policy will then invoke Article 31(2) where the common negotiating mechanism for SACU as a whole is provided for and a common negotiating policy for the whole organization can be developed.

Another requirement will be to enforce a consistent pattern of obligations and membership and behavior for all the SACU member states. They should fully respect the

fact of the legal personality of SACU and requirements of the CET. The integrity of SACU as a whole should be recognized and protected in trade relations with all third parties; including updating those that predate the coming into force of the present agreement.

2.2.2 The SADC Trade Protocol

Article 27 of the Trade Protocol deals with trade relations between SADC member states and between SADC as a bloc, and with other regional and international entities in general.

- 1. “Member States may maintain preferential trade and other trade related arrangements existing at the time of entry into force of this Protocol;*
- 2. Member States may enter into new preferential trade arrangements between themselves, provided that such arrangements are not inconsistent with the provisions of this Protocol.*
- 3. Member States party to any existing preferential trade arrangements and of other trade related arrangements undertake to review the further application of such preferential trade arrangements, with a view to attaining the objectives of this Protocol.”*

The SADC Trade Protocol, similar to the SACU Agreement, does not prevent member states from maintaining any preferential trade arrangements predating the Trade Protocol, but it adds an important qualification. It requires any new arrangements to be consistent and compatible with the Trade Protocol Member states can therefore maintain such trade arrangements, as long as it does not frustrate the main objectives of the Protocol.

Where a member state wishes to maintain any such arrangement or enters into any new arrangement, Article 28 puts a further obligation on them. It requires them to accord MFN treatment to the other members of the Trade Protocol. Article 28(2) states the following:

- 2. “Nothing in this Protocol shall prevent a Member State from granting or maintaining preferential trade arrangements with third countries, provided such trade arrangements do not impede or frustrate the objectives of this*

Protocol and that any advantage, concession, privilege or power granted to a third country under such arrangements is extended to other Member States.”

Therefore any SADC member state that gives trade preferences to another country, whether that country is a SADC member or not, that are better than the preferences negotiated in the liberalisation schedules of the Trade Protocol will have to extend such preferences to all other SADC member states due to the MFN requirement.

2.2.3 The COMESA Treaty

Article 56 of the COMESA Treaty contains almost exactly the same provisions regarding trade with third parties as the SADC Trade Protocol. Member states are also allowed to maintain trade arrangements predating the Treaty and to enter into new trade arrangements, as long as these arrangements do not impede or frustrate the objectives of the Treaty. Any preferences extended between a member state and a third party or between two or more member states also have to be extended to all other member states according to the MFN principle. Article 56 provides the following:

Most Favoured Nation Treatment

- 1. “The Member States shall accord to one another the most favoured nation treatment.***
- 2. Nothing in this Treaty shall prevent a Member State from maintaining or entering into new preferential agreements with third countries provided such agreements do not impede or frustrate the objectives of this Treaty and that any advantage, concession, privilege and favour granted to a third country under such agreements are extended to the Member States on a reciprocal basis.***
- 3. Nothing in this Treaty shall prevent two or more Member States from entering into new preferential agreements among themselves which aim at achieving the objectives of the Common Market, provided that any preferential treatment accorded under such agreements is extended to the other Member States on a reciprocal and non-discriminatory basis.”***

2.2.4 The EAC

Both the Treaty establishing the EAC and the EAC CU Protocol contain provisions dealing with trade arrangements with third countries and organisations outside of the EAC. In terms of Article 130 of the Treaty the EAC member States reiterate their commitment to their obligations under the multinational and international organisations they belong to. They confirm one of the objectives of the EAC as being a stepping stone towards the creation of the African Economic Community. They also undertake to foster co-operative arrangements with other regional and international organisations whose activities might have an impact on the fulfilment of the objectives of the EAC.⁶⁰

The Protocol on the Establishment of the East African CU provides for the establishment and the implementation of the CU. As the goal is to reach a CU where all members have the same external tariffs and external trade policy it contains various provisions that aim to harmonise the member states' policies and other regulations such as RoO. Article 37 of the EAC CU Protocol regulates trade arrangements with third countries and other regional organisations. It provides the following:

Trade Arrangements with Countries and Organisations Outside the Customs Union

- 1. The Partner States shall honour their commitments in respect of other multilateral and international organisations to which they belong.***
- 2. The Community shall co-ordinate its trade relations with foreign countries so as to facilitate the implementation of a common policy in the field of external trade.***
- 3a Upon the signing of this Protocol and before its coming into force, and taking into account, inter alia, the provisions of paragraphs 1 and 2 of this Article, the Partner States shall identify the issues arising out of their current relationships with other integration blocs and multilateral and international organisations of which they are members in order to establish convergence on those matters for the purposes of the Customs Union.***
- 3b For purposes of this paragraph, the Partner States shall, upon the signing of this Protocol formulate a mechanism to guide the relationships between the Customs Union and other integration blocs, multilateral and international organisations.***

⁶⁰ Article 130 (1), (2) and (3) of the Treaty establishing the EAC.

4a A Partner State may separately conclude or amend a trade agreement with a foreign country provided that the terms of such an agreement or amendments are not in conflict with the provisions of this Protocol.

In terms of Article 37 the EAC members states have to harmonise their trade relations with third countries in order to achieve a common external trade policy. Paragraph 3 requires them to identify the issues arising out of their current overlapping memberships of RTAs and to set up a mechanism to address these issues. This means that the EAC will have to enter into FTA arrangements with both COMESA and SADC in order to achieve convergence of the external trade policies of its members.

3 Drawing on Experience with Multiple Memberships

This section is intended to review past experience with multiple memberships in economic RIIs and establish how these have been made compatible. For that purpose, the arrangements regulating Norway's regional relations, Swaziland's trade relations and Chile-MERCOSUR relations are shortly examined.

3.1 Norway – EFTA, EEA and Nordic Co-operation

Norway exhibits a pattern of regional relations seemingly as complex as in Eastern and Southern Africa. Norway is a member of EFTA, the European Economic Area (EEA) and is active in Nordic co-operation.

Nordic co-operation takes place within the institutional framework of the Nordic Council and the Nordic Council of Ministers. Both institutions provide a forum for largely informal co-operation. Despite its informal nature, the Nordic Council has achieved significant results in regional integration, among them a Nordic passport union, a common labour market, a common social insurance convention and a harmonisation of Nordic national laws. The Council of Ministers is mainly organising co-operation in sectors of regional interest, such as the environment, industry, culture and education.

Nordic co-operation has been successful in furthering Nordic identity and harmonising policies. However, economic co-operation has been limited. Nordic co-operation did not establish an FTA, and early attempts to create a CU have failed.

Furthermore, Norway is a member of EFTA. EFTA was established on the initiative of the UK as a trade bloc rivalling the then EEC. In 1972, Denmark and the UK joined the European Community and left EFTA. The accession states had to leave EFTA not because simultaneous membership in two FTAs would have been incompatible. The conflict between EFTA and EEC was a political one. While the EEC considered trade integration a step towards political integration, EFTA stood for pure trade integration and maintenance of national sovereignty (cf. Jeserich 1963). As further integration was pursued, incompatibilities could have arisen, e.g. between commitments to one CU and an FTA. Leaving EFTA confirmed the primacy of the EEC's integration process, while a rupture of the accession states' trade relations was to be prevented by a successive free trade agreement between the two blocs. In 1973, the remaining EFTA countries concluded a free trade agreement with the European Community, which meant effectively re-establishing free trade among the (former) EFTA countries as well. In 1995, Sweden, Finland and Austria joined the EU and left EFTA. As EFTA had largely followed in the footsteps of the European Community in signing free trade agreements with other countries and regions, this meant very little change to external trade relations of the new EU members.

The history of EU-EFTA relations lends itself to comparison with the integration process in Eastern and Southern Africa. The solution found implies that countries should accord primacy to one REC. Anyway this is inevitable in Eastern and Southern Africa as the EAC, COMESA and SADC all aim at establishing CUs. Free trade agreements between the regional blocs are a viable means to substitute for foregone trade preferences when a country leaves an FTA in order to concentrate on another REC. Yet, countries can remain members of several RECs in case where there are no conflicting commitments involved, and it is useful where duplication of efforts is avoided. This is most likely in co-operation on specific issues, such as, for instance, security, migration, or usage of shared resources.

Norway had applied for EU membership and was invited to join, but the accession was rejected twice by means of referenda. Instead, it is a member of the EEA established in 1994. The EEA covers all EU members and the EFTA members except Switzerland. The EEA agreement is a more comprehensive FTA than the EFTA-EU FTA (of which Switzerland is still a member) and includes the free movement of goods (except for agricultural goods and fishery products), capital, services, and persons. RoO apply to intra-EEA trade of goods not originating in the member states. Dual membership in EFTA and EEA is therefore compatible.

Through the EEA agreement, Norway also participates in a large number of EU programmes covering most EU policy areas. Norway is associated to the European Security and Defence Policy and is a signatory to the Schengen Convention which regulates the formal abolition of border controls for European citizens and the close co-operation of police and customs officials. Norway has voting rights in several other agencies and programmes, but is equally affected by many decisions of core EU institutions, on which it has little or no influence. Norway consequently still considers full EU accession, but needs the public support for a further referendum.

Norway's key to success in its membership in overlapping regional and international organisation is that membership in the differing regional organisations does not involve conflicting commitments. Most importantly, there is no potential conflict between memberships in different RECs as only the EU is a CU and the other regional organisations do not aim to become one. Secondly, adequate technical capacities exist to avoid legal incompatibilities where they could arise. Concerning Nordic co-operation, its effectiveness can largely be explained by sufficient political will and interests in sectoral co-operation and – as compared to Eastern and Southern Africa – a relatively strong regional identity.

3.2 Swaziland – SADC, SACU and COMESA

Swaziland is simultaneously a member of SADC, SACU and COMESA. In 2000, the country deposited a request to become a member of the COMESA FTA. As the other SACU members did not agree to grant the necessary preferences to COMESA, Swaziland currently is in a state of limbo. COMESA effectively granted Swaziland free market access, but Swaziland was unable to reciprocate. The working agreement is meant to be transitional, but has been extended annually ever since, for the last time in July 2004.

Swaziland is a regional producer of Coca Cola concentrate, has important markets in COMESA and has benefited tremendously from free market access. In response to pressure from COMESA, in 2002 Swaziland requested SACU to grant it the ability to reciprocate and import duty-free from COMESA. It proposed that re-exports into other SACU states should face surcharges so that the CET would effectively apply to these goods. Firstly, such a solution would jeopardise the very notion of a CU, and costs inflicted by the necessary border controls strongly diminish the returns of a CU. If it was applied to other cases as well, SACU would effectively be downgraded to an FTA where RoO apply. Secondly, SACU has been a rather well functioning CU for decades, and currently capacities to enforce RoO do hardly exist. Swaziland would therefore be likely to become a transit country for duty free imports into SACU and particularly into South Africa. SACU and South Africa in particular, seem currently very reluctant to consider Swaziland's proposal seriously.

The Swaziland case seems to be a means for COMESA to maintain pressure on SACU to allow its members to enter the COMESA FTA, making possible an extension of the FTA to the south. The current arrangement might therefore be extended again, but has nevertheless to be regarded as being unsustainable. It is not WTO compatible, but COMESA countries are unlikely to sue. Currently, Swaziland is still so dependent on SACU CET revenue that Swaziland leaving COMESA would be the most likely consequence of a WTO lawsuit. Pressure on Swaziland to leave COMESA if it cannot reciprocate is likely to be minimal, as the market of the micro-state is of little interest to COMESA countries, and only one COMESA country would benefit from a possible

relocation of the Coca Cola plant. It should be noted again that Namibia was granted the same exceptional treatment by COMESA, but left the REC in 2004 because of the prevailing incompatibility.

3.3 Chile - Mercado Común del Sur

In a Latin American context, the Chile-MERCOSUR connection is another example of complex trade relations. Since 1996, Chile is an associate member of the Latin American REC MERCOSUR, which is composed of Argentina, Brazil, Paraguay and Uruguay. In 1995, MERCOSUR became a CU and implemented a CET successively. MERCOSUR invited Chile to join the CU, but Chile rejected the offer. It preferred a simple free trade agreement which confers greater flexibility in formulating a trade policy and building international trade relations. The agreement between Chile and MERCOSUR stipulated, among others, the creation of an FTA and the reduction of non-tariff barriers between the concluding parties. For goods not originating in the FTA RoO apply, meaning that the CET or Chile's external tariff are effectively imposed on these goods (BFAI 1997). This implies that both signatories have remained free to sign free trade agreements with third parties.

In 2000, MERCOSUR concluded an FTA with the EFTA,⁶¹ as did Chile in March of 2003, though on slightly different terms. Chile has signed several further bilateral free trade agreements, among others with the EU in 2002 (cf. BFAI 2003), to which RoO apply in trade with MERCOSUR. In essence, Chile's strategy reflects a deliberate decision to value national sovereignty and flexibility higher than regional integration. It should be recalled that the pan-(Latin) American identity has historically been much weaker and less influential than the pan-African one.

⁶¹ EFTA is an initiative on the part of Iceland, Norway, Liechtenstein and Switzerland aiming at preventing that these countries face less favourable conditions on world markets than EU countries. In the past, it has quite successfully tried to sign free trade agreements with countries which previously had established FTAs with the EU.

Part II: Costs and Benefits – A Private Sector Perspective

1 Trade in Goods

1.1 Introduction and Overview

As each of the many overlapping RECs in Eastern and Southern Africa moves along the path towards deeper integration, their members will have to decide which institution will serve their interests best. The negotiation of EPAs with the EU has catalyzed the decision making process on regional integration. The economic analysis identifies the costs and benefits of overlapping memberships of RECs with a view to making pragmatic proposals on defined economic options, looking at product market integration and investment.

While several studies have addressed the issue of overlapping membership, this question has not been looked at from the perspective of the private sector. Given companies, not countries, trade and invest and that the objective for trade policy is to shape the incentives of companies to engender growth and development, this perspective is central to assessing regional integration. The private sector, in terms of their priorities for, and role in, regional integration and how regional integration will impact on their incentives is the main focus of this study.

We will deal with product market integration first. Second, FDI and regional integration will be looked at. The third chapter attempts to make a preliminary economic assessment of the RECs. The fourth chapter lists the priorities and the impact of overlap.

The main concern of overlapping membership relates to the proper administration of RIIs and the poor articulation of tariff liberalisation under the different agreements and the possible infiltration of duty free third party goods. For companies in landlocked countries transport costs can be the biggest single factor in lack of competitiveness. Therefore, it matters to them what the RECs are doing in terms of infrastructure development and

physical integration of markets. Multiple memberships in that regard are seen to rather help than hinder economic development.

Examining the evidence from surveys of manufacturing suggests that if the barriers to regional integration were addressed, the main efficiency gains in the short to medium term will not result from the exploitation of economies of scale, but from the rationalisation and probably relocation of production. Larger companies and more advanced countries are likely to see the greatest increase in output. Data on the likely impact of regional integration on agriculture is scarce, and much of production is effectively outside of formal trade arrangements. However, the extent of non tariff barriers blocking agricultural trade reflects the fears of domestic agriculturalists in the region.

While this process of reallocation and relocation is necessary if the region is to become internationally competitive and if regional integration is to deliver benefits to consumers, it is likely to create winners and losers. In these circumstances, the process of regional integration can become unstable and the experience of the first EAC risks being repeated. How to mitigate these potential costs? To paraphrase one political leader in the region: Factories in other member states can provide goods for people in my country as long as people from my country can find work in the factories making those goods. Movement of semi and unskilled labour could become a critical issue. Compensation mechanisms are a further, possibly equally politically difficult, route by which benefits of regional integration can be more evenly spread.

The conclusions for products market integration are (i) an urgent need to address the main barriers to realising the benefits of regional integration, and (ii) that only deep integration will ensure that integration will be politically sustainable.

It is widely acknowledged that overlapping membership is serving to undermine regional institutions and steps towards deeper integration. In the words of one Rwandan official *“The problem of belonging to several Regional Organisations is that you are not serious*

enough". Indeed where there is shared jurisdiction between different RIIs, where responsibility for enforcement is not precisely demarcated, where there has been no transfer of sovereignty to regional institutions and where the political commitment to a particular RII is not clear, the leverage of regional institutions and Member States to enforce implementation will be limited.⁶²

1.2 Regional Integration: Perspectives of the Private Sector

During the course of the study, several of the main companies operating at the regional level, leading national companies and private sector representatives were consulted in Tanzania, Kenya and South Africa, also drawing on work carried out in Namibia and Rwanda and for the Mid Term Review of the SADC Trade Protocol. Companies operating at the regional level provided a particularly useful window on operating in the region, enabling a direct comparison of their experiences in different countries.⁶³

The general impression from the private sector was that trade agreements currently are of limited relevance to them. This is partly due to agreements existing "on paper only" when it comes to enforcing the liberalisation of sensitive products and trade facilitation in the context of poor, often corrupt customs procedures. This point would seem to be confirmed by several of the companies interviewed finding it easier to trade with countries with which there are no regional or bilateral trade agreements than countries belonging to the same RII. It also because several key constraints to competitiveness relate primarily to the domestic situation. The importance of domestic factors was highlighted in a survey of business in Tanzania carried out by the Confederation of Tanzanian Industry.⁶⁴ 36% of respondents felt high taxes made them uncompetitive in the

⁶² The issue here is one of achieving free trade within the RECs rather than a bureaucratic exercise. A recent review of the SADC Trade Protocol revealed the importance of the distinction: while most countries had implemented commitments on tariff liberalisation in many instances discriminatory taxes, permit restrictions and even bans nullified the impact of these reductions. See "Mid Term Review of the SADC Trade Protocol" (2004) TSG/USAID.

⁶³ The analysis was only able to capture formal trade. While recognising the importance of this trade, the direct impact of most trade policy measures is largely on formal trade.

⁶⁴ "Tanzania manufacturing sector in the EAC trade arrangement" (2002), Confederation of Tanzanian Industry background paper.

East Africa market, with 29% citing high energy rates as a key problem; no companies included trade policy measures as a major concern.

1.2.1 Problems Resulting From Overlapping Membership

The main concerns relating to overlapping membership cited by the businesses and private sector representatives related to the proper administration of tariffs, enforcement of the RoO at the border (which may also breed corruption). The poor articulation of tariff liberalisation under the different agreements, where e.g. Kenya under the EAC transition arrangements may face higher tariff barriers in Uganda and Tanzania than COMESA and SADC members respectively, was also raised as a concern as was the possible infiltration of duty free EU goods from SACU into SADC and via Tanzania into the EAC.

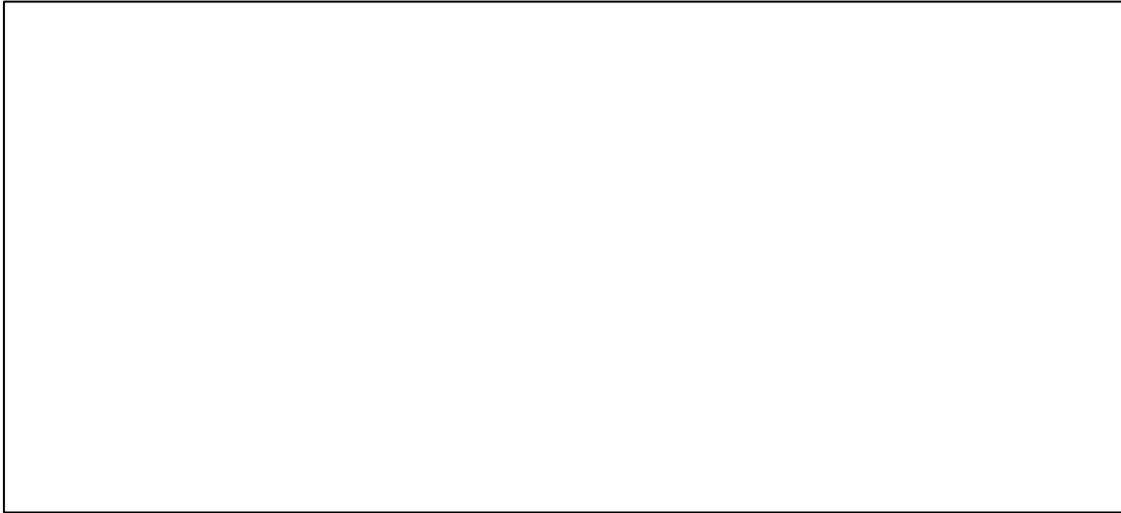
The Perspective of Formal Sector SMEs (South Africa)

SMEs in the region do not tend to export – at least directly. The only SMEs that are significant exporters to the region and operate within the regulation of regional agreements are in South Africa. To get some perspective on the challenges and opportunities facing SMEs, a survey with 79 firms ranging in size was carried out in co-operation with NAFCOC/JCCI in Johannesburg. 46% of firms are engaged in manufacturing (46%), 20% of firms are service providers and 20% included in their activities wholesaling, retailing and agency work. 18% of firms are engaged in more than one activity. 73 firms do business outside South Africa. 57 firms trade with Southern Africa. 45 firms trade with the EU, 33 with the Far East and 32 with Central Africa.

Respondents clearly indicated that the EU is the easiest region to do business with. The picture for southern Africa is less clear, but more firms see it as the easiest region (47%) than see it as the most difficult (39%). Within Southern Africa, 11 firms listed SACU countries as the easiest to do business with. Views on Zimbabwe and Mozambique were mixed, though on balance more firms placed them amongst the most difficult than amongst the easiest countries. Angola, Tanzania, DRC, Ethiopia and Kenya are all unambiguously “difficult” countries.

What makes a region or country easy to do business with?

The most important factors are strong business ethics and culture (27) followed by language and proximity (16). A strong business framework, in terms of financial and legal systems and political stability is important (9), as are good customs procedures and minimal red tape (9), low trade barriers (9) and transport logistics and communications (8).



1.2.2 Barriers to Regional Trade

For firms outside of South Africa, tariffs are a significant issue. Businesses in Namibia have reported being hard hit on regional markets by the withdrawal from COMESA while SADC partner tariff reduction schedules are being phased in. Particularly affected have been low value high volume goods such as salt. In Tanzania discussions with the private sector revealed a strong preference to rejoin COMESA to regain preferential access, a position which is now supported by the East Africa Business Council. This view was also noted by researchers from the Economic and Social Research Foundation in Tanzania: *“Tanzanian business community strongly opposed Tanzania’s withdrawal from COMESA....the feeling we got from the interview with the private sector umbrella organizations is that the private sector benefited much more from COMESA than it is the case with SADC.”*⁶⁵

For many companies throughout the region – excluding South Africa - protection from tariffs on domestic and tariff preferences on regional markets were cited as mitigating domestic constraints to competitiveness. The importance of domestic factors was underscored during consultations. For example, one leading Kenyan business man cited the costs and reliability of electricity supply as the single change in the business and trade

⁶⁵ “Mapping Of Tanzania’s Current Status In International Agreements” (2004) Dr. Josaphat Kweka, Mr. Vincent Leyaro, ESRF Tanzania.

environment that would most improve day to day operations of his company – a view shared by many in East Africa, including Rwanda.

However, the main barriers cited to regional trade related to: customs procedures and red tape, the divergence in standards and requirements on the markets in the region; the closely related issue of high transport costs; and non tariff barriers in the form of import bans, suspended duties and the like. Corruption is another barrier named. Several companies held the harmonisation of requirements or “one set of rules” for entering markets in the region as the single most beneficial change regional integration could deliver: both in terms of documentation and technical requirements/ standards. Other factors related to the business environment, priorities being non or late payments and availability of finance.

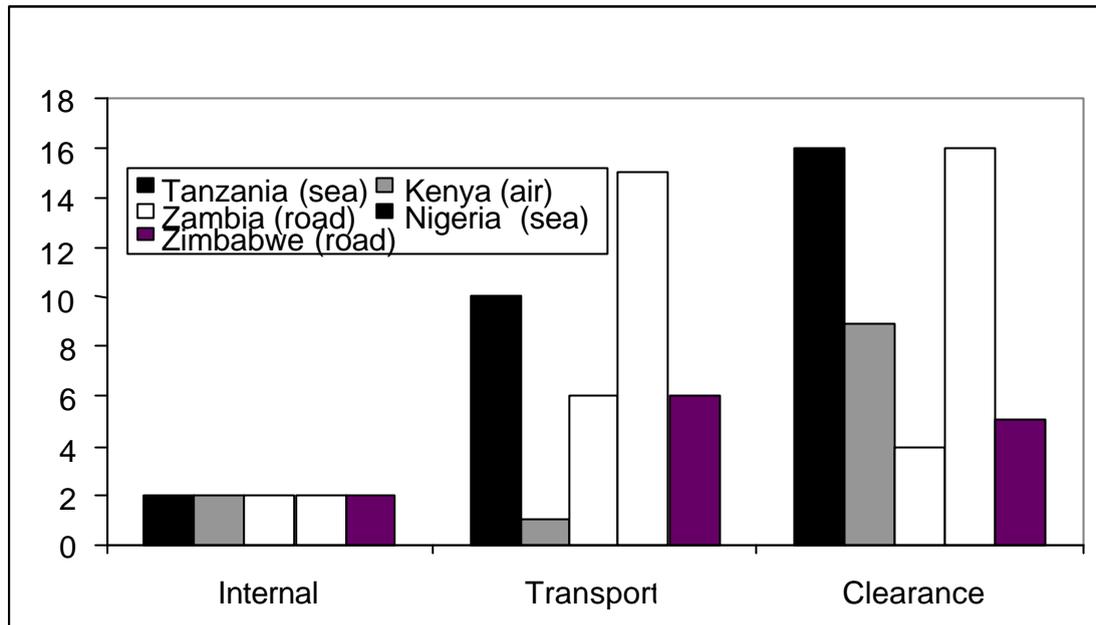
Customs Procedures

The experience of Woolworths in moving goods throughout Sub-Saharan Africa offers a perspective. Figure 1 indicates the shipping process flow. The main points to note are:

- 1) Within SADC experiences differ widely: For example the clearing process normally only takes 2 – 4 days in Zambia while in Tanzania it takes an average of 2 weeks though goods can often be held for over a month. The difference is mainly the result of Tanzania’s requirement for pre- shipment inspection.

- 2) The existence of trade agreements does not seem to have a noticeable impact: clearance times for Tanzania and Nigeria are the same: The fact that the *easiest* countries, logistically speaking, for Woolworths to operate in are Ghana and Uganda, i.e. countries with which there is no regional arrangement in place, serve to underscore this point.

Figure 1: Shipment Process Flow (Woolworths)



Source: Information provided by Woolworths Ltd. See TSG/USD (2004)

The form of transport also matters a great deal. For example, the clearance process of airfreight in Kenya takes between 6 and 8 days, including pre-shipment inspection while the clearing time for sea freight is the same as for Tanzania. The reasons given for this disparity relate largely to differences in “customs infrastructure”, procedures and quality of personnel – this offers some indication of the improvements in performance that are possible through upgrading customs capacity.

Pre-shipment inspection in Tanzania

Tanzania requirement for pre-shipment inspection has been cited as a significant barrier to trade. The experience of a major South African retailer operating in the country revealed the following:

- The sea freight clearing process for PSI takes an average of 2 weeks, a minimum of 4 days and a maximum of up to 30 days
- The airfreight clearing process for PSI shipments 7 - 10 days and non- PSI shipments (under US\$5000) min. 3 days
- PSI adds 1.2% to the Free on Board price

Other problems cited relate more to performance of customs than regulation per se. Many companies highlighted no consistency of application of customs legislation and procedures, including within SACU. Such problems at the border often occurred with

personnel change. Examples include the misapplication of immigration law. In one instance a Namibia Driver was informed that he required a new permit, but after significant delay and on further inspection, the driver had a permit for a further 27 days in Zambia. According to several traders in Namibia, even the tariff rates applied can vary.

Red Tape, Technical Regulation/ Sanitary and Phyto-Sanitary Standards and other Problems at the Borders

Several companies considered the harmonisation of requirements or “one set of rules” for entering markets in the region as the single most beneficial change regional integration could deliver. Table 1 indicates the divergence of requirements, even within SACU.

Table 1: Documentation Requirements

	Namibia	Botswana	Swaziland	Mozambique	Zimbabwe
Tax invoice			X		
SDN		X	X		
CCA1	X	X	X	X	X
Commercial Invoice	X				
BW 500		X			
Health Certificates	X	X	X	X	X
Permits	X	X	X	X	X
BOE				X	X
South African Revenue					
Services export certificate	X	X	X		

All require Bank Clearance F178 if the value of the invoice is over R50,000
 Source: Information provided by Woolworths Ltd. See TSG/ USAID (2004)

During consultations no company indicated standards or technical regulation were being used deliberately as a protectionist tool. But they consistently pointed to divergences in regulation and slow procedures as a barrier to trade. Those companies interviewed which operated across the region often employ specialists in each country to deal with the different requirements. Examples of problems included the same condensed milk being accepted in some countries but not others, differences in the quality of imports permitted with Kenya refusing “Tiger head” batteries and Uganda accepting them and in one example light bulbs accepted in Uganda and Tanzania were not accepted in Kenya due to their standards legislation being out of print and unavailable.

However the example most clearly illustrating the potential costs of not harmonising and expediting the approach to regulation, in this case the Sanitary and Phytosanitary Agreement, is seed policies and registration⁶⁶. The current situation requires testing by a national authority and its listing on the national variety register for a new seed variety to be marketed commercially in any SADC country. The test can take up to 3 years after which the seed will be considered by a Variety Release Committee. This is irrespective of whether the variety is already released in another country as the rules of variety testing and release differ between countries. This unnecessarily duplicates activities, slowing the release of new varieties to farmers.

Consultations confirmed the importance of corruption. Some companies estimated this added 3% - 7% to operating costs; not paying bribes can delay a shipment for weeks.

Transport Costs

For several landlocked countries in particular, transport costs are the main constraint to competitiveness. Table 2 provides estimates of the cost of importing a key input, indicating the landed price of inputs is between 25% and 43% higher relative to regional competitors. This is in line with several studies in Southern and Eastern Africa suggesting companies in landlocked countries face transport costs which are 50% higher.

Table 2: Import of Raw Materials: Palm Oil (in bulk) Cost Comparisons

	Rwanda (USD)	Uganda (USD)	Kenya (USD)
Free on Board	440	440	440
Sea freight up to Mombasa	45	45	45
Clearing, Storage Charges (Mombasa)	29	29	9
Road/Rail Transport	180	90	35
Insurance	3	3	2
CIF	697	607	531
Import duty	35 (5%)	0 (0%)	0 (0%)
Clearing, Storage Charges (Kigali)	28		
Bank Charges	3.5	3	2.7
Landed cost per ton	764	610	534
<i>Increase vis Uganda</i>	<i>25%</i>		
<i>Increase vis Kenya</i>	<i>43%</i>		

Source: SULFO Rwanda Industries

⁶⁶ This example is taken from "Trade Policies and Agricultural Trade in the SADC Region: Challenges and Implications" (2003), ESRF, Tanzania.

As shown in Table 3, a large part of higher costs result from constraints on physical infrastructure coupled with the need to travel longer distances. However, the breakdown also indicates the direct cost of a “second round” of customs clearance is significant, between 5% – 10% of Free on Board price.

In addition to the direct cost of customs clearance, companies bear the costs of delays at the borders. For one company interviewed in Kenya it is not uncommon to pay up to \$3000 demurrage/waiting fees on a lorry born container worth on average \$35,000; i.e. 5% -10% of the value of the shipment.

Transport costs are also being driven higher by laws restricting the operations of transport companies within the region. These cabotage laws segment and distort the market for transport services by preventing a transporter operating outside the country in which they are registered in the sense that e.g. a Namibian registered truck with a shipment for Gaborone cannot pick up a load in Gaborone to take to Durban. Equally, a South African truck delivering goods to e.g. Oshakati in Namibia cannot accept a consignment for delivery in Windhoek.⁶⁷

The form of transport and value/volume+ weight ratio of cargo also matters. Table 3 sets out the different costing, provided once again by Woolworths, for shipping required stock from Cape Town to Nairobi. The result that airfreight is cheaper than shipping and road is initially hard to believe, but is the consequence of the specific goods moved. With high value goods low in weight and volume, air freight becomes viable. To illustrate, \$700 will buy up to a ton airfreight with a fixed unit space. This allows a lot of e.g. shirts to be transported. \$750 will buy around 27tons on a sea container – beyond the requirements for high value, low weight and volume products. Another example given was the cost of moving a car from Durban to Nairobi: \$800 dollars by air, while Durban to Mombasa alone would cost \$700.

⁶⁷ TSG/USAID (2004) cited above.

Table 3: Freight (high value added products): Cape Town - Nairobi

Options	Rates	Frequency/transit times
Airfreight - Cape Town to Nairobi	R 15,055	Day 1, 3, 5 & 7
Roadfreight - Jhb & Airfreight to Nairobi	R 10,633	Mon & Fri
Rail - Jhb & Airfreight to Nairobi	R 17,143	Daily ex Jhb.
Seafreight Cpt –Mombasa & Road to Nairobi	R 27,279	Weekly 12-13 days
Seafreight Cpt –Mombasa & Rail to Nairobi	R 21,413	Weekly 12-13 days
+ Mombasa – Nairobi		20 days

Source: Woolworth Plc. See text for explanation

This illustrates the extent to which transport costs are higher for low value added, high volume goods, exactly the type of good which is most likely to be produced by agricultural sector and by the poor.

Non-Tariff Barriers

Non-tariff barriers are proliferating⁶⁸ and risk nullifying any increase in regional trade resulting from the phasing out of tariff or quota reductions if unchecked. By way of making a point, one business representative in Kenya remarked that the implementation of the EAC CU will have little impact on export opportunities in Tanzania as exports are “always being hit by suspended duties”.

Intra SACU trade in agricultural products appears as affected by these non-tariff barriers, despite the CU agreement which precludes such measures.⁶⁹ Botswana imposes periodic bread bans. Swaziland imposes levies of between 4% and 25% on selected agricultural products, ranging from maize and wheat to fruit and vegetables to poultry (see table 4). Namibia controls maize imports and effectively bans wheat imports for human consumption through licensing permit, while Lesotho controls imports of bread, fruit and vegetables, pulses, dairy and meat products through use of an import permit system.

⁶⁸ TSG/USAID (2004) cited above.

⁶⁹ SACU has an infant industry clause which legitimately allows members to shelter an industry from competition with other SACU partners for a period of up to eight. The only measures currently covered by this clause relate to three products in Namibia – pasta, broilers and UHT milk.

Non-tariff barriers within Southern and Eastern Africa take different forms. For example, in Zambia, while tariff and quota restrictions have been removed, import licences are required for agricultural imports and these licenses are often not granted. And as tariffs have fallen under COMESA, Zambia has implemented temporary bans on Zimbabwean products (most of them agricultural).⁷⁰ Import licences for meat, poultry, salt and sugar are still required for Malawi. In Tanzania there are several cases where excise duties are highly discriminatory. To illustrate: if the tobacco used in cigarettes is 75% or more Tanzanian, the excise duty is TShs3500 per 1000 sticks; if cigarettes are imported or use less than 75% Tanzanian tobacco, the excise duty is TShs17000 per 1000 sticks. Exporters to Tanzania were also concerned by the increasing use of suspended duties to protect local industry. Suspended duties on batteries are between 25% and 35%.

Table 4 : Swaziland Scheduled Agricultural Products and Levies

Product	Levy (%)
Whole white maize grain	1 - 4.5
Maize meal and other products	7.5
Rice	3.5
Fresh fruits, excluding apples, pears, peaches, grapes and bananas	7
Apples, pears, peaches and grapes	4.5
Bananas	6.5 – 25
Fresh vegetables, excluding cabbages, tomatoes, potatoes and sweet potatoes	1 – 10
Cabbages, tomatoes, potatoes and sweet potatoes and potatoes	
Poultry and poultry products (excluding turkey)	13.5
Turkey and turkey products	20 – 25
Whole wheat	3 – 5
Wheaten products	7 - 18.5
Frozen Vegetables	7.5

Source: Namboard, Namboard Annual Report (2002), National Agricultural Marketing Board Act (1985) and Amendment Notice (2002), WTO Trade Policy Review (2003), A Comprehensive Agricultural Sector Policy for Swaziland (2004), Ministry of Agriculture and Cooperatives. Cited TSG/USAID (2004)

1.3 The Potential for the Private Sector to Enhance Product Market Integration

The last decade has witnessed rapid growth in companies, mainly South African, operating at the regional level, indeed the growth of South African retail chains throughout Southern and Eastern Africa is the most visible sign of regional integration. This expansion of South African industry and commerce is politically sensitive. As one executive put it “*we do not want to become the car park for South Africa*”.

⁷⁰ According to the ESRF (2003) paper cited above, 14 six month bans were imposed in 2002 alone.

However, the ability of these larger companies to absorb risks, their distribution network and their technical capacity offer real opportunities for countries in the region to enhance production for local, regional and international markets.

In a few cases we have seen companies exporting to regional partner countries, building markets that have since been *competitively* supplied locally. In 1995 Unilever South Africa began exporting to Mozambique, building the local market and developing brand awareness. In 2001/2 it invested in local production, with a turnover of 130 – 140 million Rand, creating 65 jobs. In Zambia we have also witnessed regional exporters developing local markets which have then been exploited by local companies investing to produce e.g. pannettes for horticultural exports.

Sourcing locally is the most direct way retail chains can benefit local producers. Balanced against this is the need to ensure the price and quality of goods available to consumers is not adversely affected. While there has been no evaluation of the extent of local sourcing, we have an indication from information made available by Shoprite (PTL) Ltd and set out in table 5. Information was also made available by Metcash, with local sourcing at 95% in Zimbabwe, 75% in Malawi and 10% in Angola. The degree to which local producers are supplying local stores varies widely. Country size, natural resources and climate will be driving differences to a large extent, but are unlikely to explain a range in outcomes of between 5% and 95% and suggest that there are significant opportunities for expansion.

Table 5: Local Sourcing: Shoprite (PTY)

	Number of stores (Incl. Shoprite, Checkers, OK, OK Furniture, Megasave, U-Save, Hungry Lion stores)	Percentage of goods sourced locally
Zimbabwe	1	95%
Namibia	15	90%
Ghana	3 (U-Save's only)	90%
Zambia	25	70%
Mauritius	1	70%
Mozambique	3	60%
Madagascar	6	60%
Average		52%
Uganda	3	50%
Tanzania	7	50%
Swaziland	2	35%
Malawi	8	35%
Botswana	6	10%
Lesotho	4	5%
Angola	3	5%

Source: Shoprite PTY

Several companies pointed to the strong incentive for them to source locally as a result of high transport costs and political sensitivity. The main constraints they face relate to quality and reliability of supply. For one of the premium brand companies, their ability to source outside South Africa is in some instances constrained by the ability of producers to get higher prices on EU markets to which they also have duty free access.

Note the degree of local sourcing is largely unrelated to preferential trade agreements at least as currently implemented. SACU members appear both at the top and the bottom of the table. The same is true for countries with no formal trade arrangements with South Africa – witness Ghana and Uganda’s positions.

There are also opportunities with upgrading standards. In Zambia, Freshmark, the fresh produce buying arm of Shoprite, is working integrally with growers, offering them technical assistance in the application of chemicals and providing chemical spraying equipment. For Nandos, throughout SADC around 60% of the product is sourced locally,

the categories being poultry, bakery products and vegetable ingredients.⁷¹ Nando's assists local producers such as chicken farmers and bakeries to raise their skill level and added value processes to meet their specifications. A Compliance Director provides training and to enable suppliers to meet requirements. There is assistance for suppliers to become HACCAP compliant which is a pre-requisite for supplying poultry to the brand. HACCAP compliance serves to open up opportunities on other export markets, assisting producers in overcoming the Sanitary and Phytosanitary Agreement and technical barriers faced in some key markets.

Opportunities also exist on the South African market for certain niche products. For example, the production of some fresh produce is seasonal in South Africa, whereas the climate in Zambia allows for year round production. In this regard, retail chains can potentially provide what is effectively subsidized transport for exporters to South Africa. Many trucks return empty, implying a low marginal costs for return shipments.

1.4 Realising the Benefits from Regional Integration

Regional trade is being constrained by non tariff barriers, high transactions costs at the border and high transport costs, as well as by tariffs. If these barriers are addressed, how would the benefits from regional integration be realised? And what are the implications for regional integration?

In general, countries within the region do not export what partners in the region import. The majority are competitive exporters of primary commodities and import manufactured products, only South Africa, Egypt, Kenya are significant exporters of manufactured goods. Consequently, most countries are therefore unlikely to benefit from greater regional exports sales of goods regional partners do not produce (note however the discussion of trade diversion in later chapters), rather they will enter into direct competition.

⁷¹ On establishment in a country, initially 80% of product is imported.

How then will regional integration play out and raise economic growth? We consider three mechanisms: exploitation of economies of scale; resources reallocation to more efficient producers; and competition induced increases in individual firms' productivity.⁷² We evaluate each in the light of the surveys of manufacturing in Southern and Eastern Africa carried out under the Regional Programme for Enterprise Development (RPED) and the related work at the International Finance Corporation, UNIDO and the Centre for the Study of African Economies.⁷³

1.4.1 Economies of Scale

Economies of scale are often cited as the main way regional integration will lead to efficiency gains. The focus on the exploitation of economies of scale is in part because of its significance in explaining trade between developed countries and because of its role in EU trade integration. It is also because this process is most likely to lead to a “win – win” situation with all parties to a regional agreement benefiting from an expansion of production at lower costs.

Firm level survey data, necessary to establish whether production can be characterised by constant or increasing returns to scale is relatively scarce. However, since the 1990's the RPED has established the most comprehensive set of surveys for Sub-Saharan Africa. Analysis based on the surveys for Kenya (Lundvall et al 2001), Ghana (Mans and Teal (2001), Zambia (Africa Private Sector Group (2003), Mozambique (Nasir et al (2003) and Tanzania (ESRF (2003) show manufacturing firms operate at constant returns to scale.

Given the relatively low capacity utilisation rates in the region – 48% for Zambia, 51% for Tanzania, 58% for Uganda and 63% for Kenya – the rejection of increasing returns to scale may initially be surprising. However, the reason is the heterogeneity of capital employed. With much of the underutilised capital stock being old – in Zambia 16% of

⁷² In the context of regional integration, product differentiation often plays a role, but generally for more sophisticated and larger markets than herein considered.

⁷³ Survey results and related papers are available at www.worldbank.org/investmentclimate and www.unido.org and the Centre for the Study of African Economies at www.csae.ox.ac.uk

capital is over 20years old - bringing it into production raises unit costs (marginal costs) rather than lowers them. In Tanzania⁷⁴ while on average capacity utilisation runs at 51%, new firms in e.g. the wood products sector operate at a much higher 75% capacity.

Evidence also suggests larger firms in the region are more productive (see next section). However, while the technology embodied in a larger plant may enable a firm to operate at lower units costs for an optimal level of output, increasing production at the individual plant will not necessarily lower unit costs in the short to medium term at least.

In Kenya, however, it is likely that there is some scope for economies of scale for the large producers of fast moving consuming goods. For example, the plant of Eveready batteries was constructed on the basis of serving the East African market and could reduce unit costs by 15% through increased sales to an expanded market. However, even at full production, the company would not be price competitive on world markets.

1.4.2 Resource Reallocation to more Efficient Producers

A more likely route for regional integration to deliver an increase in efficiency for the region as a whole is through resource reallocation to more efficient producers within the region and the likely relocation of production. Currently, protection in domestic markets seems to fragment production and enable less efficient firms to survive (see also section 1.4.3.).

⁷⁴ See Tanzania Manufacturing Enterprise Survey 2002 at www.unido.org

Box 1: Economic Measures of Relative Competitiveness

The most widely available indicator of a sectors' competitiveness is the relative value added by each worker in that sector. Differences generally reflect the amount of capital each worker to use in production and their skill/education levels.

However, in general greater productivity will be compensated by higher wages. Therefore higher productivity may not translate into a competitive edge if wages are proportionately higher. Taking into account wage as well as productivity differences gives us unit labour costs (the wage divided by value added per worker). This offers a better indication of competitiveness. But reliable, comparable figures for unit labour costs are not available for many countries in the region.

Competitiveness is also driven by business costs. While countries may have the same unit labour costs, competitiveness may still be impaired by the costs of doing business, including finance, transport etc., being higher in one country than another. For example, companies in a landlocked country will be at a disadvantage on the markets of a coastal neighbour as they face higher transport costs both for imported inputs and to get goods to the market. Even on the home market, transport costs can have a differential impact, depending on the product concerned. For example, wheat flour used in making biscuits contains 13% water which evaporates during the production; i.e. the final product will be 13% lighter than inputs.

A further measure of competitiveness is Total Factor Productivity. A firm with higher Total Factor Productivity is able to combine the same inputs to produce relatively more output, generally as a result of managerial skill and operational effectiveness.

To evaluate likely impact, the most readily available comparable figure is value added per worker (see Box 1). Using this indicator the increase in competition is likely to see larger companies expand at the expense of smaller ones as a result of their greater productivity: value added per worker increases with firm size as evidenced by the comparison of RPED data for 5 countries in Southern and Eastern Africa presented in Table 6.

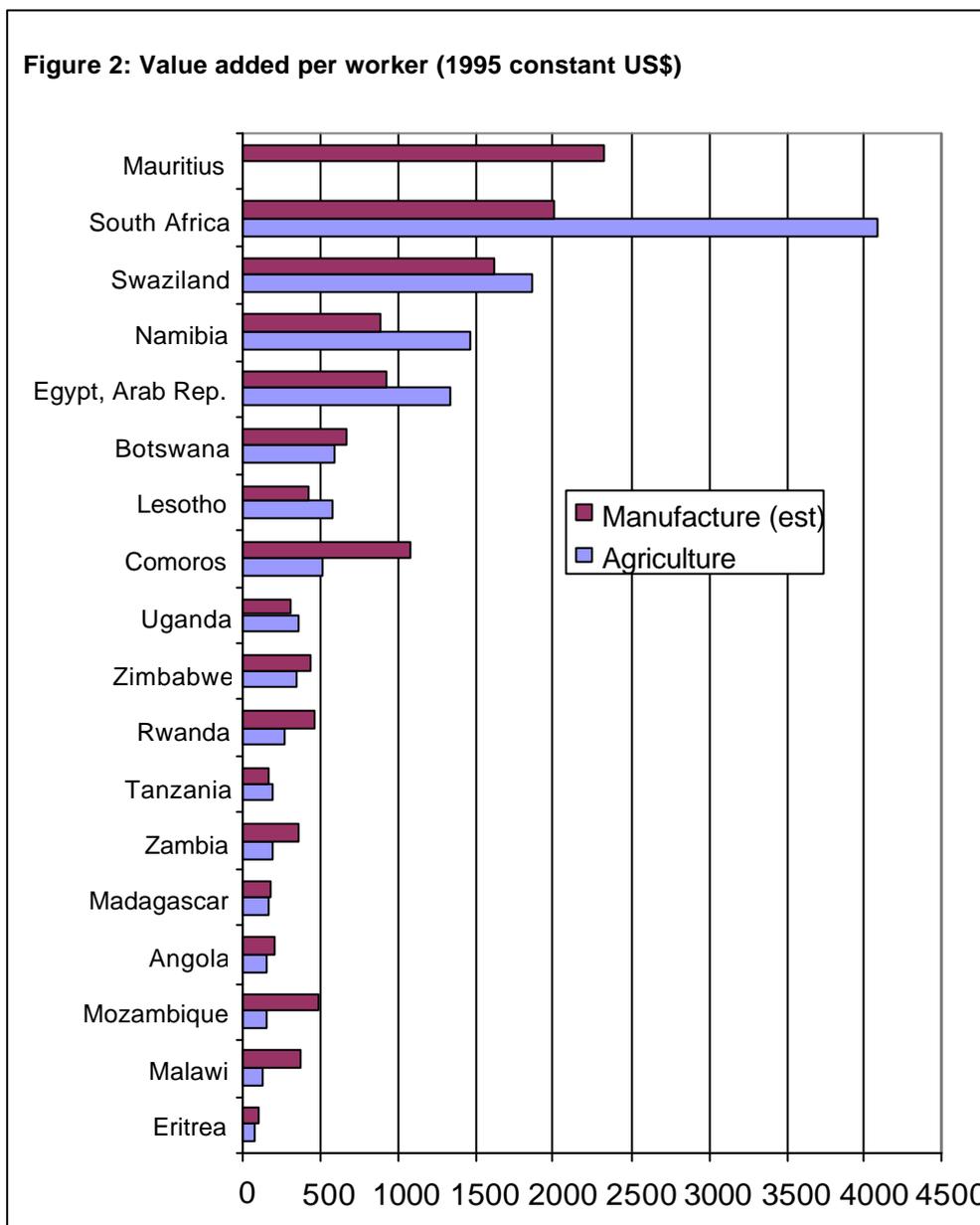
Table 6: Manufacturing Value Added Per Worker by Firm Size (US\$), Food, Metal, Textile, Wood

Firm Size	Kenya	Mozambique	Tanzania	Zambia	Zimbabwe
Median	3337	977	1862	2962	3999
Micro	1568	440	1460	1777	2159
Small	3337	977	1415	3110	3079
Medium	3374	1495	2272	3012	3879
Large	4655	2013	2080	4123	3999
Very large	2830	870	3754	4668	4919

Source: RPED

On the basis of value added per worker across countries at the aggregate level of agricultural and manufacturing production, richer countries in the region are set to have a competitive edge (see figure 2). Large differences in productivity are evident not only in

manufacturing but also agriculture – reflecting the overall differences in infrastructure and the enabling environment.



Source: World Development Indicators (2004)

While a significant increase in exports from the more advanced economies in the region must be expected, the impact needs to take into account large differences across sub sectors, and also the higher wages paid in the more advanced countries which reduce their competitiveness.

The large differences in productivity in sub sectors and between countries are illustrated in Table 7. Tanzania's average productivity per worker in the firms surveyed is 30% lower than Kenya, however the table shows that in chemicals, paints, construction materials, Tanzania's productivity is twice that of Kenya; for plastics, it is five times higher.

Table 7: Manufacturing Value Added Per Worker by Sector and Country

	Tanzania	Uganda	Kenya
<i>Agribusiness</i>	3,074	942	4,270
(observations)	(81)	(122)	(81)
<i>Chemicals and paints</i>	9,220	2,738	4,272
(observations)	(27)	(18)	(25)
<i>Construction materials</i>	8,267	1,082	4,368
(observations)	(11)	(40)	(17)
<i>Metals</i>	1,303	1,383	3,360
(observations)	(29)	(21)	(48)
<i>Furniture and wood</i>	804	554	3,116
(observations)	(65)	(54)	(20)
<i>Paper, printing, and publishing</i>	2,722	3,537	6,045
(observations)	(25)	(23)	(18)
<i>Plastic products</i>	15,409	6,328	3,655
(observations)	(7)	(7)	(19)
<i>Textiles, garments, and leather</i>	950	1,617	2,013
(observations)	(31)	(15)	(47)

Source: Investment Climate Surveys

Higher productivity should also be accompanied by higher wages, reducing the competitiveness gap. Comparative and reliable data is not available to allow a comparison across the region. The RPED survey does, however, offer some information for some countries and sectors, set out in table 8. While these figures must be treated with caution, differences are far less than for value added per worker; also note that the higher wages that large companies pay do not nullify their competitive advantage relative to small and medium companies.

Table 8: Unit Labour Costs (ratio of wages to value added)

Firm Size	Tanzania	Uganda	Kenya	Zambia
Small (10-49 employed)	0.56	0.41	0.38	0.41
Medium (50-99 employed)	0.42	0.41	0.41	0.47
Large (>100 employed)	0.25	0.35	0.34	0.39
Overall	0.39	0.39	0.34	0.41

Source: RPED, ICA Investment Climate Surveys

While the link between wages and productivity implies production displacement resulting from regional integration will be less than suggested by the figures for value added per worker, “creative destruction” is inevitable. Estimates of total factor productivity indicate larger economies in the region are significantly better at combining labour and capital in production; for example all else equal, Kenyan manufacturers output is 5.6% higher than Tanzanians firms with the same input.⁷⁵

Finally, it is important to note that across all countries and in all sectors, exporting firms are more efficient than counterparts providing the domestic market only, even after taking into account the larger size of exporting firms. Exporters in several manufacturing were estimated to be an average of 46% more efficient than non exporters in Kenya, 25% more efficient in Zimbabwe and 16% more efficient in Ghana.⁷⁶ Firms that are currently exporting are set to benefit from regional integration.

1.4.3 Competition Induced Increases in Individual Firm’s Productivity

It is not the intention of the study to try to predict behavioural change at the level of the individual enterprise. What can be shown is the wide dispersion in efficiency at the firm level and therefore the potential for competition – by forcing companies to improve business practice – to raise output.

⁷⁵ ESRF (2003) at www.worldbank.org/businessclimate

⁷⁶ See “What drives manufacturing exports in Africa?” (2001) at www.unido.org. The greater efficiency of exporters is a global phenomenon.

Bigsten et al (1999)⁷⁷ reports that for Kenya, Zimbabwe, Cameroon and Ghana, one fourth of the sampled firms are less than half as productive as the median firm, while another fourth of firms are more than twice as productive as the median firm. For profit rates the variability is even greater.

Table 9: Efficiency Differentials in Mozambique

	Mean Efficiency (0-1)	Variation
Small	0.36	(0.23)
Medium	0.45	(0.26)
Large	0.41	(0.23)
Food	0.34	(0.23)
Wood	0.29	(0.29)
Garments	0.45	(0.36)

Source: CTA/RPED Survey 2002

Table 9 presents efficiency differentials across firm size and by sector in Mozambique, calculated from estimates of production functions.⁷⁸ To interpret the figures, note that “best practice” firms receive a score of 1, while the poorest performing receive a score of zero. The average efficiency of firms in Mozambique is 0.38, showing how far the average firm is away from “best practice”. It also shows the wide dispersion in efficiency both within and across size and sectors.

1.4.4 Convergence or Divergence

The process of regional integration is likely to deliver change through the reallocation and rationalisation of production and introducing greater competition. This process of “creative destruction”, through encouraging production in efficient firms at the expense of inefficient, should lead to income growth and increased competitiveness at the level of the region as a whole.

⁷⁷ “Investment in Africa’s Manufacturing Sector” Oxford Bulletin of Economics and Statistics.

⁷⁸ Nasar et al (2003) at www.worldbank.org/businessclimate

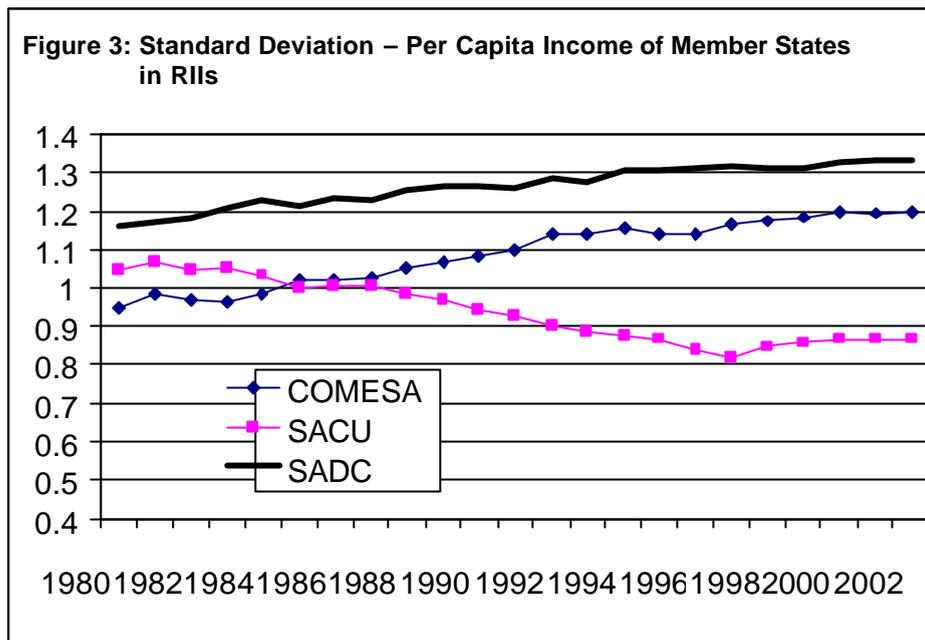
However, the distribution of the gains from this process are unlikely to be evenly spread; at the country level it is likely to disproportionately favour net exporting countries.⁷⁹ Given rigidities in the factor markets of many poorer countries in the region and the low elasticities of exports to the real exchange rate, increased unemployment in the short run also seems inevitable. The danger is therefore that incomes within the region diverge over time.

COMESA and SADC incomes are diverging. The extent to which countries' incomes in the RIIs have converged or diverged is set out in figure 3, which plots the standard deviation of (log) GDP per capita (constant US\$). It is probably too early to judge the impact of the COMESA FTA, and implementation of the SADC FTA is slow, therefore *a priori* there is little reason to expect strong convergence. However the convergence in SACU stands out.

The reasons for convergence in SACU may be because of BNLS access to the South African market (both goods and labour), transfers from South Africa to other SACU members through an enhanced revenue sharing formula;⁸⁰ conservative macroeconomic policies resulting from exchange rate arrangements and also country specific factors which are unrelated to regional integration. The extent to which each of the factors has contributed to convergence is not considered here. However, much mention has been made of the revenue sharing formula compensating the BNLS for possible losses resulting from trade diversion within SACU.

⁷⁹ The process of "creative destruction" is trade creating, though the gains in welfare will be reduced through trade diversion. Taking into account the potential for trade diversion and net exporters may in some instances benefit from increased export revenues without the consumer in the importing country benefiting from lower prices and the region may be worse off. We defer discussion of the potential for trade diversion to a later chapter.

⁸⁰ See Kirk and Stern (2004) "The New SACU Agreement" at www.worldbank.org



Source: World Bank World Development Indicators 2004

Access to the South African market was not restricted to goods, but extended to labour. The ability of unskilled labour from Lesotho to work in South Africa would have been a key benefit. Migrant labour to SA has however been curtailed substantially in more recent years.

Without a full assessment of the drivers of convergence in SACU, conclusions must be tentative. But it is clear that SACU is the only REC which has a history of relatively deep integration in terms of labour migration, compensation and which has the kind of credibility that can induce business to plan on the basis of SACU as a regional market. The movement of labour in particular may be an important factor in allowing the more widespread distribution of the benefits that accrue from integration. To paraphrase a political leader in East Africa: Factories in other member states can provide goods for people in my country as long as people from my country can find work in the factories making those goods.

2 Foreign Direct Investment and Regional Integration

2.1 The Environment for Investment in Sub-Saharan Africa

Reviewing the key obstacles to Foreign Direct Investment (FDI) indicates policy uncertainty and fragmented and narrow markets are amongst the main factors in deterring FDI; areas in which regional integration and developing regional institutions have – in principle – the potential to create change.

Increasing levels of FDI are a pre requisite for enhanced economic growth and more diversified production structures. FDI need not only come from outside the region. Given the increasing importance of South Africa as an investor in Africa we also review its dynamics and determinants. Key determinants of levels of FDI include transparency and liberalisation.

High interest rates and poor financial services are a major constraint to FDI. Regional capital market integration, in so far as it provides a deeper market for the sale of e.g. government treasury bills, may enable governments to finance debt at lower rates, reduce the crowding out of private investment and increase competition for private sector clients. Though it is beyond the terms of reference of the study to examine this in detail, the lower real interest rates and spread between deposit and lending rates in the common monetary area, that is SACU less Botswana, suggest there may be significant benefits.

However, in practice, strong institutions are required if they are to act as “agencies of restraint” and reduce the risk and uncertainty facing investors. A mechanism for policing non tariff barriers is also required to create a genuine single economic space: in interviews to date, businesses (to some extent) plan at the regional (as opposed to the national) level in the EAC and SACU only. The establishment of regional capital markets also requires a strong regional framework for regulation and enforcement of contracts.

Weak regional institutions may therefore be as damaging to attempts to attract FDI through regional integration as they are to efforts in achieving regional free trade.

In line with the global trend, the environment for FDI has radically improved. The sweeping change of policy undertaken by Sub-Saharan Africa during the last decade to liberalise investment regimes and open up their economies is well recognised.

A comparison of the situation facing investors in the different regions has been made possible by the Heritage Foundation's index of economic freedoms. Both Sub-Saharan Africa and the Caribbean score 3 (moderate) on restrictions on Foreign Investment. In general there are restrictions on many investments but official policy conforms to established foreign investment codes though the approval process is bureaucratic.

Table 10: Index of Economic Freedom

	Foreign Investment	Regulation
Africa	3	4
Caribbean	3	3
Fiji	4	3
EU	2	2,5
World Average	3	3,5

Source: Heritage Foundation

The regulatory environment for business in Africa is poor, with major barriers to opening a business, complicated licensing procedures, very high fees and regulations imposing a great burden on business.

2.1.1 Risk and Uncertainty

FDI in Africa has a high rate of return. US FDI in Africa has had a rate of return of 30%, higher than any other region. It has twice the rate of return to FDI in Latin America, and is 10% higher than the return in Asia. Japanese affiliates in Africa were more profitable than in any other region except for Latin America and the Caribbean and West Asia. The rate of return has increased over the period of economic reforms in SS Africa. Net income from British direct investment in the region (excluding Nigeria) was reported to have increased by 60% between 1989 and 1995.

However, these high rates of return have not led to Africa closing the gap between its FDI inflows and the FDI inflows to other developing regions. An important factor in explaining this is the high level of perceived risk. Aside from the volatility that can result from aid dependency, high indebtedness and debt service obligations, surveys of firms highlight the risks of policy reversals. In contrast to other regions, trade reforms and reforms to the investment regime have not been the result of multilateral or regional negotiations but the consequence of structural adjustment programmes.

One of the largest surveys of private investors in developing countries revealed that, in general, firms have little faith in the stability of the regulatory environment in which they operate, both in terms of policy changes and reliability of the judiciary (see Box 2). The problem for Sub-Saharan Africa is considered to have worsened over the last ten years.

Box 2: Policy Uncertainty & Institutional Obstacles to Doing Business

A world wide survey for the World Bank was carried out from 1996 – 97. Of the 69 countries covered, 58 are LDCs. In Sub-Saharan Africa, 1,288 firms from 22 countries responded to the question. The sample included firms from all countries and was reasonably spread across firm size, with a reasonable representation of firms from outside of the major cities. 50% of respondents were exporters, and 50% were, to a greater or lesser extent, foreign owned.

The most important obstacles for African entrepreneurs, arising from government failure, were:

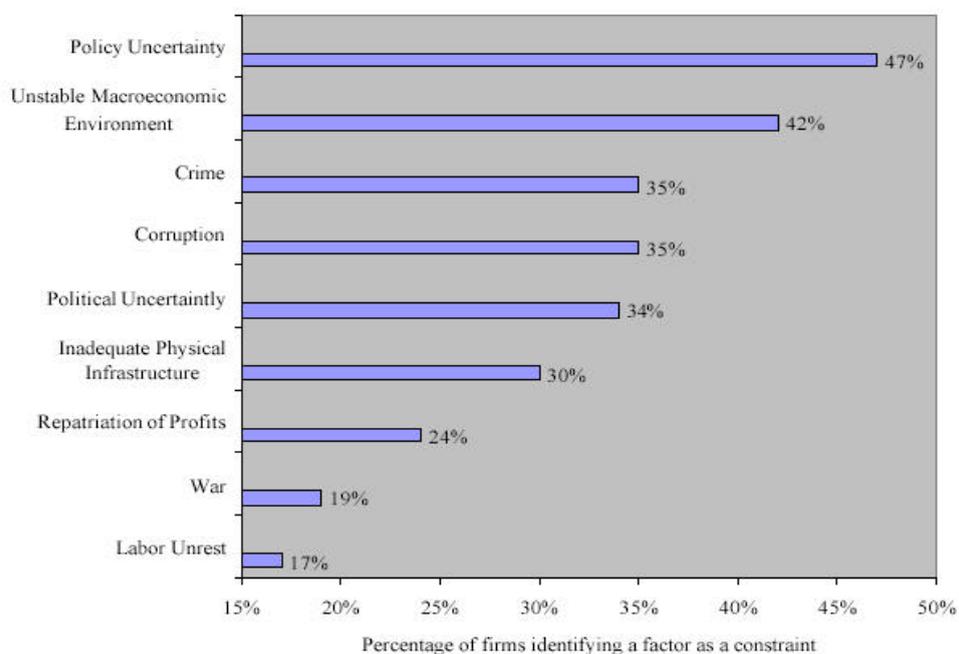
- (1) corruption,
- (2) tax regulation/ high taxes,
- (3) inadequate supply of infrastructure.

The survey also revealed that, in general, firms have little faith in the stability of the regulatory environment in which they operate.

- *Policy Surprises:* Over 50% of firms considered the policy environment to be unpredictable. Nearly half did not expect government to stick to announced policy changes and also feared retroactive changes of regulations that would have a significant impact on their business. The majority of firms felt that the level of policy uncertainty had increased over the last ten years.
- *Political Changes and Changes in Regulation:* Over 60% of firms considered that constitutional changes in government lead to large changes in the rules they operated under, and affect their business.
- *The rule of law:* Over 70% of respondents considered the unpredictability of the judiciary to be a major problem for their business operations.

The importance of policy uncertainty is further underscored by Jankins and Thomas (2002) in their survey of investors in the SADC region. The results, see figure 4, show policy uncertainty is a concern for 47% of firms interviewed.

Figure 4: Constraints to Foreign Investment in SADC



Source: Jenkins and Thomas (2002).

2.1.2 Regional Integration

In surveys of investors of Africa in particular, the importance of market size is mentioned time and again. Insufficient market size was cited as the main factor preventing French companies - already operating in other developing regions - from investing in Africa.⁸¹ In the same survey, 30% of the sample of French firms currently operating in West Africa considered that small or missing markets to be the main constraint to further investment. Small market size pushes up costs – as no economies of scale can be reaped – and prevents expansion. While regional integration was considered one of the most important factors in increasing investment, only one in every three investor felt that RIIs would be able to deliver market integration in the short to medium term.

⁸¹ Enquête Sur Les Principaux Obstacles au Développement des Entreprises en Afrique. This study, carried out by Le Comité ACP de CNPF International in 1998, drew on the responses of 160 French firms, picked by random selection from an survey of around 3000 enterprises, which included both large and small enterprises.

A survey of European firms investing in SADC (see box 2) revealed that most FDI in the region is driven by access to local markets. While local markets were particularly relevant for investment in South Africa, some investors tended to view the region as a single market. For this reason many firms are very positive about the potential for regional integration to expand markets. Some also indicated that integration of productive capacity across different countries would be beneficial, though this would require standardisation of e.g. bureaucratic requirements.

Promoting investment in services and the development of supply chain production will require greater harmonisation of business law and regulation - as currently the high fixed cost of learning how to do business in the different countries within the region acts as an impediment for cross border investment. A recent survey of SADC and COMESA found not only different entry requirements within the regions, but also served to highlight the problem of different commercial codes and varying approaches to property rights.

Box 2: FDIs in SADC: a survey of European based multinational firms.

This survey targeted European investors in SADC. Just under half of the investment projects surveyed have been in existence for five years or less. Investments in South Africa accounted for about a third of the survey; the rest located throughout SADC, in particular Zimbabwe, Zambia and Tanzania. The survey covered investment in primary, secondary and tertiary sectors and firms ranging in size from under 50 employees to those with 1000 or more.

Over half of the projects covered are wholly owned by the parent firm. While firms working with local partners frequently argued that this was good for business, however, the use of procurement policies as a way of promoting local ownership was criticised for increasing uncertainty and deterring those firms that wish to retain full ownership for reasons internal to the firm (such as brand management, integration within a supply network).

Motivations for Investment

Most FDI in SADC is driven by access to local markets. More than half of non primary sector interviewees cited size of local market as a key reason for locating in a particular country – this consideration was particularly important for investment in South Africa. Some interviews viewed the region as a single market, too small to support multiple investments. Many firms were positive about the potential for regional integration to overcome the barrier of small market size. Some also indicated that the integration of production across the region would be beneficial, though this would require many changes in the institutional framework, including greater harmonisation of bureaucratic procedures.

Privatisation has also been an important for attracting recent investments, for example in Zambia and Tanzania, though the speed of privatisation was cited as a cause for concern in some countries.

The survey has been carried by the Centre for the Study of African Economies and CREFSA as part of the DFID Research Programme on Globalisation.

2.1.3 Finance and Business Infrastructure

Access to quality financial services is cited as an important constraint. Indeed businesses in Africa pay an estimated extra 20% on loans than businesses operating in OECD countries. Service liberalisation can be a powerful tool in increasing the availability and reducing the cost of basic infrastructure. For example, Ghana in 1997 introduced competition in telecommunications services and established an independent regulator which has led to a rapid increase in coverage of the telephone network relative to countries which have not liberalised, such as Tanzania and Ethiopia.

2.1.4 Other Constraints

Corruption is one of the most widely cited obstacles to investment, particularly in Africa. Though corruption has often been considered independent of investment regime liberalisation, recent research is increasingly pointing to the link between administrative barriers to establishment and corruption.⁸² Unfortunately, research has also shown that poorer countries generally impose a greater number of procedures, that these procedures cost them significantly more, and that they do not lead to e.g. greater levels of health or lower levels of pollution. The number of procedures is also shown to increase the percentage of the economy that operates in the informal economy, thereby constraining the ability of governments to raise fiscal revenue through taxation.⁸³

High and discriminatory taxes and trade taxes are also consistently cited in the various surveys as key constraints. Taxes and tariffs are cited as one of the most important reasons preventing French firms investing in West Africa, and are the fourth most important constraints for those French firms that are operating in the region. The World Bank survey of the private sector (box 2) also found tax regulation/ high taxes weighed very heavily as a concern of foreign and domestic investors in Sub-Saharan Africa. The importance of liberalising trade regimes in attracting investment, for Sub-Saharan Africa

⁸² See, inter alia, Djankov, La Porta, Lopez-de-Silanes, Shleifer (2000) « The Regulation of Entry » National Bureau of Economic Research Working Paper 7892.

⁸³ See Djankov et al (2000) and references therein.

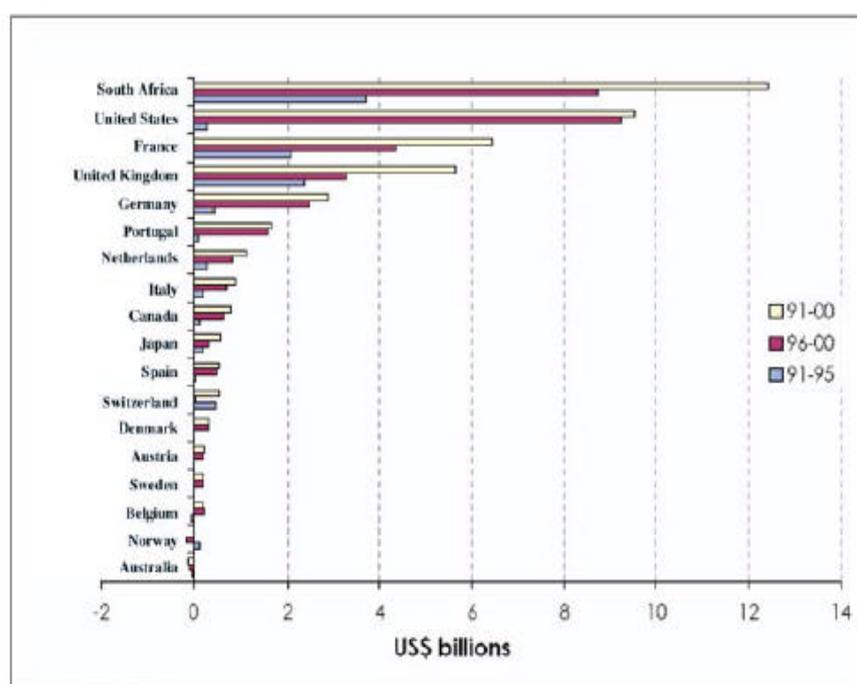
in particular, is also confirmed by recent studies of the determinants of FDI to developing countries.⁸⁴

Poor infrastructure is often sighted as a major constraint to investment. The very high transport costs within Africa are well known and serve to further narrow regional markets. Other basic services are also severely limited in much of the ACP, with few phone lines and power outages imposing major problems on business operations.

2.2 South African Investment in Africa

According to UNCTAD, South Africa has become the most important investor in Sub-Saharan Africa (see figure 5) in the nineties, though United States investment in the region has grown faster in the second half of the decade.⁸⁵

Figure 5: Main Investors to Sub-Saharan Africa



Source: LiquidAfrica, UNCTAD

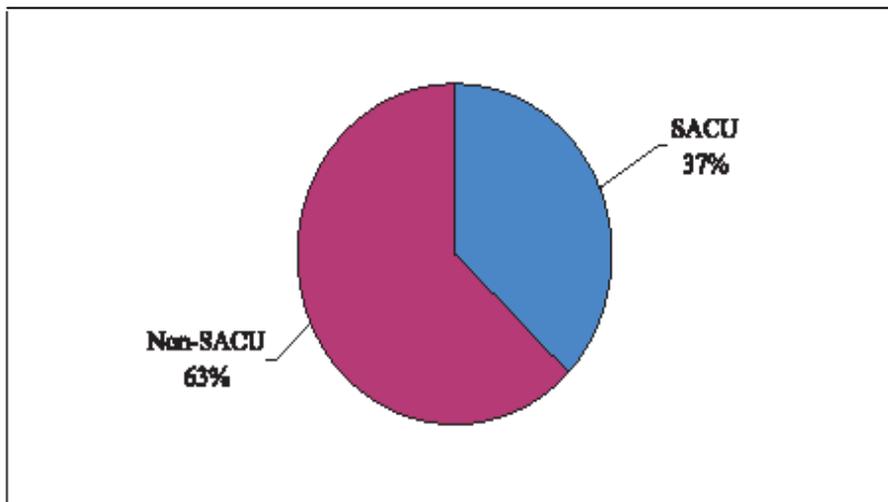
⁸⁴ See, inter alia, Asiedu, E. (2002) « On the Determinants of Foreign Direct Investment to Developing Countries : Is Africa Different ? » World Development, Vol. 30, No. 1 pp.107-119.

⁸⁵ “South Africa’s business presence in Africa” (2004), Occasional Paper No. 3, South Africa Foundation.

There is a very strong “neighbourhood” effect, with an estimated 37% of investment in the region going to SACU, see figure 6. This reflects the results from recent surveys of South African Investment in Africa⁸⁶ which indicate familiarity and the need to use South Africa as the “anchor” economy are important determinants of investment.

Transparency and openness are particularly important for South African investors, though the market size of Nigeria compensates for the high levels of corruption. Investment in ICT and the financial sector have generally followed liberalisation. Investment in Zambia has been in mining and in Tanzania investment has followed regulatory improvements and opportunities resulting from privatisation. In Mozambique, proximity has been an important factor in explaining the increase in investment following the end of apartheid.

Figure 6: SACU Share of South African Investment



Source: Whitehouse & Associates, based on information collected from company records.

Though surveys of South African investors did not explicitly address the importance of trade agreements, no investor cited them (or small markets) as a key concern. Indeed,

⁸⁶ Diana Games (2004), “The Experience of South African Firms Doing Business in Africa: A Preliminary Survey and Analysis” South African Institute of International Affairs, www.saiia.org. Neuma Grobbeloor (2004) “Every Continent Needs and America: The Experience of South African Firms Doing Business in Mozambique”, www.saiia.org.

Kenya, Uganda and Ghana are increasingly important destinations for investment though all trade relations are on a MFN footing.

2.3 Potential Impact of Regional Integration

2.3.1 Credibility and Market Size

The extent to which countries in the region are paying a high and undeserved risk premium⁸⁷ has been widely documented. The potential rewards from enhancing the credibility of the policy framework, in terms of more and more long-term investment is significant.⁸⁸

Greater credibility, and consequent increases in investment, are an often cited benefits of regional integration. NAFTA offers an example of a developing country “locking in” its policy regime and attracting increased investment. Whereas the 1982 debt crisis in Mexico led to the nationalisation, exchange controls and a large increase in protectionism the debt crisis of 1994 did not derail the move towards an open economy. FDI annual inflows to Mexico doubled following 1994.

The increase in FDI to Mexico following NAFTA also reflects the increased market access to the USA and Canada. An upsurge in FDI flows to EU member states was also seen in the run up to the establishment of the single market, with US, Japanese, Korean and Chinese companies establishing operations to take advantage of the larger market. The European Commission found the EU’s share of worldwide FDI inflows rose from 28% to 33% during 1982 – 1993.

Many former Eastern Bloc countries have also benefited from the increased credibility and greater markets offered by accession to the EU, Hungary in particular.

⁸⁷ That is to say there is an upward bias in risk rating for African countries in addition to calculation of risk on the basis of fundamentals.

⁸⁸ See “Credibility of Rules and Economic Growth: Evidence from a Worldwide Survey of the Private Sector” (1998), Brunetti, Kisunko and Weder, *World Bank Economic Review*, Vol. 12, No. 3.

However, to enhance credibility regional agreements need teeth, in the form of strong, supra national regional institutions or in the case of NAFTA a hegemonic partner prepared to enforce agreed investment codes. But as Schiff and Winters conclude “*even if combining small poor economies into a trade bloc has attractions, enhancing credibility is not one of them... only North – South RIAs are of direct interest here, and, of these, only those with the EU are likely to be significant. U.S. trade with Africa is small and dominated by oil; the EU is far more important for Africa in terms of traditional links, location and depth of trading and investment flows.*”

The impact of regional integration on market size and hence investment will also require strong regional institutions or commitment. As noted in chapter 1, there are pervasive non tariff barriers in the form of bans, discriminatory taxation and suspended duties and these will need to be addressed before a genuine increase in market size is achieved. Even if regional market size is increased, there is no guarantee that investment will significantly increase because the regional market will still be very small relative to e.g. Europe, USA or India. Nor is there any guarantee that investment focussing on servicing the regional market alone will enhance welfare; if competition on these markets is low integration may serve to increase monopolistic rent.

2.3.2 Regional Capital Market Integration

Regional capital market integration has a potential role to play in addressing finance constraints that is additional to multilateral liberalisation. Creating regional capital and securities markets will provide a deeper market for the sale of government securities and may enable governments to finance debt at lower rates. Indirect benefits in terms of reducing the crowding out of private investment and increasing competition for private sector clients will probably have an even greater impact. An advantage of the regional approach is that current investors in e.g. Kenyan treasury bills have greater experience of this type of instrument and are better able to evaluate risk when assessing a Ugandan treasury bill than an international investor. The Ugandan government may not therefore have to pay the “irrational” risk premium placed on everything African by international investors.

Though it is beyond the terms of reference to examine this in detail, we see in table 11 countries that are member to the common monetary area – Lesotho, Namibia, Swaziland and South Africa – pay lower real lending rates and have a lower spread than others in the region. Lesotho, a LDC, has a lower real lending rate than Botswana or Mauritius, while it is rated as significantly more risky than either. This would suggest there are potentially significant advantages to capital market and financial sector integration.

Table 11: Deposits and lending rates

Country	Deposit Rate (%)	Lending rate (%)	Spread (%)	Real Lending (%)
Swaziland	8.6	15.3	6.7	1.5
Namibia	7.8	13.8	6.0	4.0
South Africa	10.8	15.8	5.0	6.6
Lesotho	5.2	17.1	11.9	7.4
Kenya	5.5	18.5	13.0	9.0
Botswana	10.3	16.0	5.7	9.9
Tanzania	3.3	16.4	13.1	11.8
Average	11.6	23.5	11.9	12.5
Mozambique	18.0	26.7	8.7	13.9
Mauritius	9.9	21.0	11.1	15.1
Zambia	23.3	45.2	21.9	21.1
Uganda	7.9	25.3	17.4	21.4
Malawi	28.1	50.5	22.4	28.1

Notes: Rates are for 2002

Source: World Bank WDI

Liberalisation of capital flows within the region will also create opportunities for emerging regional investors other than South Africa, such as Kenya and Mauritius, enabling them to exploit their advantages in operations and management. Current levels of outwards FDI are low, but growing. In 2003 Mauritius' outward FDI was 3.2% of her total gross fixed capital formation.

Table 12: Outward FDI, US\$ millions

Country	2000	2001	2002	2003
Mauritius	13	3	9	41
Kenya	-	-	7	2

Source: UNCTAD

2.3.3 Regional Integration

In surveys of investors of Africa in particular, the importance of market size is mentioned time and again. Insufficient market size was cited as the main factor preventing French companies - already operating in other developing regions - from investing in Africa.⁸⁹ In the same survey, 30% of the sample of French firms currently operating in west Africa considered that small or missing markets to be the main constraint to further investment. Small market size pushes up costs – as no economies of scale can be reaped – and prevents expansion. While regional integration was considered one of the most important factors in increasing investment, only one in every three investor felt that RIIs would be able to deliver market integration in the short to medium term.

A survey of European firms investing in SADC (see Box 3) revealed that most FDI in the region is driven by access to local markets. While local markets were particularly relevant for investment in South Africa, some investors tended to view the region as a single market. For this reason many firms are very positive about the potential for regional integration to expand markets. Some also indicated that integration of productive capacity across different countries would be beneficial, though this would require standardisation of e.g. bureaucratic requirements.

Promoting investment in services and the development of supply chain production will require greater harmonisation of business law and regulation - as currently the high fixed cost of learning how to do business in the different countries within the region acts as an impediment for cross border investment. A recent survey of SADC and COMESA found

⁸⁹ Enquête Sur Les Principaux Obstacles au Développement des Entreprises en Afrique. This study, carried out by Le Comité ACP de CNPF International in 1998, drew on the responses of 160 French firms, picked by random selection from an survey of around 3000 enterprises, which included both large and small enterprises.

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Box 3: FDIs in SADC: A survey of European based multinational firms.

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Over half of the projects covered are wholly owned by the parent firm. While firms working with local partners frequently argued that this was good for business, however, the use of procurement policies as a way of promoting local ownership was criticised for increasing uncertainty and deterring those firms that wish to retain full ownership for reasons internal to the firm (such as brand management, integration within a supply network).

Motivations for Investment

Most FDI in SADC is driven by access to local markets. More than half of non primary sector interviewees cited size of local market as a key reason for locating in a particular country – this consideration was particularly important for investment in South Africa. Some interviews viewed the region as a single market, too small to support multiple investments. Many firms were positive about the potential for regional integration to overcome the barrier of small market size. Some also indicated that the integration of production across the region would be beneficial, though this would require many changes in the institutional framework, including greater harmonisation of bureaucratic procedures.

Privatisation has also been an important for attracting recent investments, for example in Zambia and Tanzania, though the speed of privatisation was cited as a cause for concern in some countries.

The survey has been carried by the Centre for the Study of African Economies and CREFSA as part of the DFID Research Programme on Globalisation.

3 Preliminary Economic Assessment of the RECs

3.1 Introduction and Overview

How then to assess the options facing those countries with overlapping memberships? To try and give a perspective on this, we examine the potential impact on economic welfare and international competitiveness of tariffs under different scenarios for the different RECs and on market access. We then examine the potential impact on investment, complementing the work of chapter 2 with an initial look at what the figures for FDI show. For Tanzania, we take the choice as being between COMESA or SADC, rather than the choice between the EAC, with Kenya and Uganda being members to COMESA, and SADC.

On the basis of these criteria there is no clear “winner” between COMESA and SADC for countries with overlapping membership. What we can say is:

- 1) For Tanzania the adoption of the SACU CET (taken as a proxy for an as yet undetermined SADC CET) reduces the likely resource costs and anti export bias of the current tariff structure while the COMESA CET has limited impact. For Zambia, adopting the SACU CET is largely neutral. The COMESA CET slightly increases the bias to produce for domestic as opposed to export markets. For Mauritius the survey data we have to work is limited, but indicates very high levels of effective protection on domestic markets. Both the COMESA and the SADC CET lead to a significant opening up. In the case of the COMESA CET domestic effective protection rates turn negative for several sectors. Given the well functioning duty draw back scheme, the tariff structure does not directly affect the competitiveness of exports to world markets. However, the adoption of either CET would reduce the bias to produce for domestic markets.
- 2) Under the current SADC FTA, SACU exporters stand to benefit significantly from duty free access to the highly protected markets in the region. The adoption of the COMESA or SAC CET will greatly reduce the scope for harmful trade diversion, resulting from the CETs lowering the level of protection in e.g. Mauritius rather than through the creation of a CU per se. On the basis of the pattern of imports, there is little evidence to suggest that either COMESA or SADC is leading to substantial trade diversion, though this may change as the agreements come fully into effect.
- 3) Evaluating the benefits of the different RECs on the basis of “export promotion” is ill advised. Firstly because even though the markets of Egypt and South Africa are large relative to the region, together they account for little over 1% of world GDP. Secondly, countries with overlapping membership export little of what other countries in the region import, and the incentives of the current tariff

structures and those under the two CETs considered, encourage producers to look to domestic not regional markets in all but a few products

- 4) Members of SADC (excluding South Africa) do attract relatively more FDI. While this is largely the result of a “neighbour to South Africa” effect, there is still a residual positive relationship between being party to SADC and FDI. The cause of this is likely to be looser capital restrictions on South African firms investing in SADC. With the move towards a broader relaxation of capital controls it remains to be seen whether the “SADC” effect will diminish
- 5) If overlapping membership has any effect on FDI, it is a negative.

Given the indecisive outcome based on the criteria above, decisions on the future direction of regional integration for countries with overlapping membership are therefore likely to relate to issues that are beyond the scope of the current study, namely: (i) the opportunities emerging from labour market integration and the evaluation of which RECs are likely to achieve the free movement of semi and unskilled labour. (ii) The level of compensation available and the compensation mechanism itself. (iii) The probability of the different RIIs establishing regional financial markets to deliver lower real interest rates. (iv) For landlocked countries the integration of transport policies in the region should be a priority, though much can be achieved through the transport corridors proposed under NEPAD and other Spatial Development Initiatives.

3.2 Tariff Policy under the Different RECs

3.2.1 The Impact of Tariff Policy

Tariffs affect domestic resource allocation by raising the domestic price of tradables above world prices. Quantity restrictions, by reducing supply of imports, also serve to increase the domestic price of the restricted good.

For consumers, the nominal tariff is a tax on their purchases of the protected goods, reducing their real income accordingly. The tax rate they pay is equal to the wedge between domestic and world prices, which in the absence of quantity restrictions is equal to the nominal tariff.

The impact of tariffs on firms is more complex. Firstly, firms both benefit from increased prices and profitability as a result of tariffs on their final product, but also pay higher prices if tariffs are levied on their inputs. Secondly, firms focus on profits and the need to pay wages, and the same nominal tariff on final products will have a different impact on the profitability of different firms depending on how their cost structures differ. To illustrate: firm A has gross sales of \$1000, out of which it pays \$800 for inputs (we do not consider in this example the role of tariffs on inputs). The value added in production, which is used to pay profit and wages, is \$200. A 20% nominal tariff will increase gross sales to \$1200 (by raising domestic prices 20%). With the costs of inputs unchanged, wages and profits increase to \$400; i.e. profitability is doubled. Firm B also has gross sales of \$1000, but has a higher value added of \$600 (with \$400 spent on inputs), then a 20% tariff on final product will also raise profits and wages by \$200, as for firm A, but this represents an increase of profitability of only 30%.

The impact of nominal tariff rates on the protection offered to a producer's profits and to wages therefore depends on the tariff rates on final goods, inputs, and the cost structure of the firm. Taking these factors into consideration gives us the effective rates of protection.

Box 4: Nominal and Effective Rates of Protection:

The nominal tariff rate of protection refers to the total proportional difference between domestic and international prices resulting from import tariffs. The effective tariff rate of protection incorporates the combined effect of price distortions (nominal tariffs) on both outputs and inputs, on the value added of manufacturing activities.

Positive effective rates of protection indicate that domestic industries are able to operate with a higher level of value added than would prevail under free trade, increasing financial profits and/or permitting lower levels of efficiency, and constituting a subsidy to these activities. The higher are the implicit subsidies, the greater will be the incentives for the movement of domestic resources into these activities. Conversely, activities with negative effective rates of protection are being implicitly taxed through the combined effects of price distortions on their inputs and outputs.

High effective rates of protection can be very costly in terms of misallocation of resources and economic inefficiencies. Recent research on the impact of the SADC FTA⁹⁰ has shown that higher rates of effective protection are closely correlated with wider variance in efficiency. This points to the fragmentation of production behind tariff barriers with unproductive firms surviving alongside productive ones. The degree to which this is happening is indicated by the variation in the effective rates of protection amongst firms in the same sector. The analysis of effective rates of protection also shows that unless well targeted and managed nominal tariffs serve to offer greater protection to low value added producers, all else being equal; Note however, that recent work explicitly taking into account structural problems of underemployment in developing countries⁹¹ has suggested “moderate” but highly escalated levels of protection. The analysis puts an upper bound on effective rates of protection “*which is unlikely to exceed 30% and will often be less than 20%*”.

The impact of tariffs on the incentives of the firm varies by market. On the domestic market, firms benefit from the tariff on final goods, but pay tariffs on imported inputs. On world markets, the firms does not benefit from the tariffs on final goods but still pays the tariff on imported inputs⁹² - in this way tariffs can lead to a negative effective rate of protection on world markets, damaging competitiveness. Tariffs also introduce an anti export bias by creating incentives to produce for the smaller local markets. This can be particularly detrimental if the bias to local markets induces producers to invest in smaller scale plants which have a lower initial cost but embody lower technology – leading to higher unit costs than if investment had been in larger scale plants to produce for the more competitive world market.

Within a FTA, MFN rates differ between countries. In this situation producers can face a different rate of effective protection on regional than on domestic markets; where e.g. a partner country’s tariff on final goods is higher than the domestic MFN rate, the firm will have a higher effective rate of protection on the partner countries than the domestic

⁹⁰ “SADC Trade Protocol: Economic Impact Assessment” (2004) TSG/USAID at www.satradehub.org.

⁹¹ Buffie (2003) “Trade Policy in Developing Countries”.

⁹² Unless there is a functioning duty exemption or drawback scheme.

market. With the adoption of a CET, effective rates of protection for producers on domestic and regional markets are equalised across the Custom Union.

For our analysis we will therefore take as the baseline the current level of effective protection on domestic, world and regional markets and the impact of the different RIIs proposed, or likely, CET.

The incentive to export to regional markets relative to the domestic markets offers an indication of the potential for trade diversion under current FTA arrangements, and the extent to which these change with the adoption of a CET provides some guidance as to whether the move to a CU is welfare enhancing.⁹³

Trade diversion arises when, as a result of an FTA or CU, the source of imports changes from an efficient global producer to an inefficient regional producer. To illustrate: Initially, country A imports matches from country C, on which a 15% tariff is levied. Country B is unable to compete on country A's market. As a result of a preferential agreement between A and B, country B exporters are able to displace country C's exports of matches. In the initial situation, the tariff was reducing consumer welfare, but the government and local producers were also benefiting from increased revenue. The net loss from the tariff resulted from the "deadweight" loss of inefficiency. Following the implementation of the preferential agreement, the government is no longer receiving the tariff revenue and the revenue going to local producers may be reduced. This revenue loss is now split between the consumers in country A and the exporters in country B. The share depends on the extent to which consumers in country A benefit from lower prices.

Note however, that even with some trade diversion it is possible that the region as a whole will be better off as a result of underemployed resources being brought into production⁹⁴; the question may be one of how the benefits from integration are

⁹³ Welfare enhancing is meant relative to the current situation of a FTA but not to unilateral liberalisation.

⁹⁴ See Buffie (2003).

distributed. Also, in practice it is often difficult to evaluate the extent of trade diversion (see Box 5).

Box 5: Evaluating trade diversion: The realities “on the ground”

While the theory of trade diversion is clear, evaluating the extent to which it is occurring is often difficult and varies according to the situation “on the ground”. The problem is that business often operates in a “second best” world where factors other than price are important. For example, in the context of Zambian horticultural exports, we came across South African companies providing packaging to the export growers at prices that were significantly above those sold by European producers on world markets. Taken at face value, the conclusion would be South African exporters were surviving as a result of tariff preferences. However, discussion with their clients revealed that key factors were the availability of trade credit, the ability to buy in small units (with the possibility of return), and ready access. In contrast, the large European producers insisted on cash before delivery and would only provide bulk orders. Transactions that appeared to be the result of trade diversion were in actuality driven by the need to overcome the constraints in the financial markets in Zambia and the resulting importance of cash flow.

Customs procedures and practices will also impact on trade diversion. An important example for the region is that of vehicles. While tariff rates are similar throughout the region, in COMESA countries the importation of second cars enables consumers and businesses to reduce the higher transport costs resulting from the tariff. However, in SACU measures are currently being considered that will effectively restrict second hand car imports. In Namibia second hand tyres from outside Customs territory are already restricted on health and safety grounds, in Botswana customs is investigating “under invoicing” of imported second cars, and in South Africa registration of imported second hand cars is problematic for owners. The same tariff leads to a very different impact in terms of trade diversion.

3.2.2 Tariff Scenarios and their impact on countries with overlapping membership

In evaluating the likely impact of forming a CU within COMESA or SADC, we need scenarios for the CETs. For COMESA, we can take the CET as: 0% for Capital Goods, 5% for Raw Materials, 15% for intermediate and 30% for final goods. The EAC tariff structure is suitably close to not require a separate analysis. For SADC, there is as yet no agreement on a CET; we have therefore taken the SACU CET as the basis for evaluation of the impact of a SADC CU. The trade weighted nominal tariffs by sectors under the scenarios are set out below. We also include the SADC average MFN and the EAC tariff rates for comparison.

Average SACU tariff rates by sector are lower than those resulting from the proposed COMESA CET apart from textiles and clothing. However, a word of caution is in order as these averages obscure individual tariff rates in SACU as high as 300%.

Table 13: Scenarios for Analysis: Average Nominal Tariff Protection

2dig	Description	Tariff lines	SACU CET	SADC MFN* (average)	COMESA A CET	EAC CET*
1	Agriculture And Forestry	261	5%	17%	17%	15%
2	Fishing	41	8%	19%	23%	20%
3	Mining	104	1%	9%	7%	6%
4	Food Processing	399	13%	23%	25%	22%
5	Beverages	23	21%	33%	26%	22%
6	Tobacco	6	32%	46%	28%	23%
7	Textile	510	24%	22%	21%	19%
8	Clothing	273	51%	42%	17%	14%
9	Leather and Footwear	67	21%	30%	30%	25%
10	Wood and wood Products	71	9%	20%	20%	18%
11	Furniture	24	19%	35%	29%	24%
12	Paper	120	7%	18%	20%	18%
13	Publishing	36	5%	18%	20%	17%
14	Misc. petroleum and coal products	18	3%	7%	18%	16%
15	Basic chemicals	480	2%	8%	6%	6%
16	Industrial Chemical	262	4%	11%	12%	11%
17	Other chemicals	142	4%	14%	19%	18%
18	Rubber	53	13%	21%	20%	17%
19	Plastics	68	14%	24%	23%	20%
20	Glass and Ceramic	68	7%	20%	28%	24%
21	Ceramic Products	33	8%	21%	29%	24%
22	Other non metallic	87	3%	16%	25%	21%
23	Iron and Steel Products	376	3%	13%	20%	18%
24	Fabricated Metal Products	205	8%	20%	17%	16%
25	Machinery	528	3%	10%	10%	9%
26	Electric machinery and appliances	272	4%	18%	4%	3%
27	Professional and Scientific Equipment	212	0%	14%	9%	8%
28	Vehicles	54	17%	20%	16%	14%
29	Other Vehicles	81	1%	11%	9%	7%
30	Other manufacturing	166	8%	27%	24%	20%
31	All other products	74	2%	11%	12%	11%

* included for purposes of comparison only

Source: COMESA, SADC, Member States

We consider the impact of the two scenarios on those countries with overlapping membership for which we have data – Tanzania, Mauritius and Zambia. In each case we establish the current baseline and evaluate the change in domestic protection, international competitiveness and anti – export bias, and incentives to export to the regional markets.

Tanzania

The table below sets out the baselines effective rates of protection on domestic and world markets and under the SACU and COMESA CET Scenarios. Listed in the table are figures for the number of companies included in the survey and the number of product lines. For textiles, leather and footwear and wood and wood products the results are vulnerable to firm/ product specific factors. However, in general the results of the model are in conformity with other work recently carried out for Tanzania,⁹⁵ the main differences are in wood and wood products, with the other survey indicating a domestic effective rates of protection of 5%, and for industrial chemicals where the estimated effective rates of protection is 215% as opposed to the 30% reported below.

Tanzania				Domestic effective rates of protection			World effective rates of protection		
2dig	Description	Companies	Products	Baseline	COMESA CET	SACU CET	Baseline	COMESA CET	SACU CET
1	Agriculture And Forestry	4	6	30%	8%	0%	-2%	-1%	0%
4	Food Processing	4	8	58%	30%	2%	-45%	-43%	-6%
5	Beverages	6	6	30%	36%	11%	-1%	-1%	-1%
6	Tobacco	2	2	30%	30%	45%	0%	0%	0%
7	Textile	1	1	39%	19%	0%	-3%	-2%	0%
9	Leather and Footwear	1	1	32%	32%	43%	0%	0%	0%
10	Wood and wood Products	1	1	48%	485%	290%	-387%	-210%	0%
11	Furniture	2	4	40%	85%	64%	-53%	-9%	0%
16	Industrial Chemical	2	4	30%	32%	0%	-2%	0%	0%
20	Glass and Ceramic	4	6	49%	56%	10%	-9%	-2%	0%
22	Other non metallic	4	8	43%	44%	0%	-1%	-1%	0%
23	Iron and Steel Products	2	2	36%	36%	0%	0%	0%	0%
24	Fabricated Metal Products	2	4	18%	27%	0%	-1%	-2%	0%
25	Machinery	1	2	10%	2%	0%	-1%	-1%	0%
26	Electric machinery...	2	4	15%	8%	-1%	-7%	-5%	-1%
28	Vehicles	2	2	-7%	-9%	62%	-53%	-9%	0%
30	Other manufacturing	4	4	39%	42%	21%	-3%	0%	0%
31	All other products	2	2	19%	37%	-1%	-9%	-5%	-1%

For the majority of sectors, current tariff policy is leading to effective rates of protection that are 30% or above (shaded grey in the table), creating incentives that distort the

⁹⁵ See "Tariff policy and Effective Rates of Protection: Tanzania" (2003) Maxwell Stamp.

efficient allocation of resources. The extent to which high levels of protection are leading to resources being wasted is indicated by the dispersion of effective rates of protection within a sector. We have calculated the standard deviation of effective rates of protection for firms included in the survey: it is highest for food processing (a 39% expected variation in effective rates of protection) agriculture (20%) other non metallic (15%) and glass and ceramics (9%). The variation is generally low for sectors with low levels of effective protection, such as electronic machinery and appliances and machinery. Confidence in the results of the analysis is obviously affected by the number of firms and product lines in each sector.

Effective protection on domestic markets changes little with the adoption of the COMESA CET. However, the adoption of the SACU CET would reduce the distortions arising from tariffs in most sectors except vehicles, though we should be wary of the result for textiles which may well be firm/ product specific.

Turning to effective rates of protection on world markets, of particular note is the damage being done by the current tariff to food processing activities. This demonstrates how industrial policy, which is currently seeking to support this sector, can inadvertently be undermined by tariff policy. Under the COMESA CET, tariffs continue to discriminate against the export of food processing. The SACU CET is the most export neutral. However, it should be noted that important sectors such as clothing are excluded due to lack of data and that agriculture is underrepresented given its importance to the Tanzanian economy.

On regional markets, Tanzania stands to benefit from the high effective protection on the on wood and wood products in Mauritius, Zambia, Zimbabwe, Ethiopia and Burundi, and food products to Mozambique and Zimbabwe. Under both the COMESA and SACU CET, the incentive to export wood and wood products to the regional markets remains.

Tanzanian exporters have no incentive to export to the SACU market as effective rates of protection on SACU markets are currently lower than domestic effective protection. The different CETs have little impact on this.

Zambia

Effective rates of protection in Zambia are high for agricultural and forestry, clothing, plastics and fabricated metal products. The very high rates of effective protection for vehicles results from the very low value added in the assembly of trailers and the high nominal tariffs on vehicles. The dispersion of effective protection in Zambia is high for vehicles (a 1,347% expected variation) plastics (95%) agriculture (47%) fabricated metal products (27%), industrial chemicals (24%) and food processing (20%). A higher dispersion is, as expected, largely correlated with a higher domestic level of effective protection.

The impact of the COMESA CET is limited, if anything increasing the level of effective protection in the economy, while the SACU CET would push up protection for clothing with the resultant welfare losses to households. Current tariffs are significantly reducing the incentive to export to world markets of vehicles (trailers) and to a lesser extent fabricated metal products and industrial chemicals. Adopting the COMESA CET would, overall, slightly reduce the incentive to produce for world markets while the impact of the SACU CET is neutral to positive.

Zambia				Domestic effective rates of protection			World effective rates of protection		
2dig	Description	Companies	Products	Baseline	COMESA CET	SACU CET	Baseline	COMESA CET	SACU CET
1	Agriculture And Forestry	2	2	36%	-1%	-2%	-6%	-10%	-2%
4	Food Processing	15	33	23%	34%	40%	-6%	-12%	-2%
7	Textile	2	2	6%	15%	-12%	-4%	-15%	-12%
8	Clothing	2	2	46%	46%	109%	-4%	-15%	-12%
9	Leather and Footwear	11	19	17%	34%	18%	-8%	-14%	0%
15	Basic Chemicals	3	4	7%	5%	10%	-1%	-1%	-1%
16	Industrial Chemical	8	18	17%	20%	16%	-13%	-10%	-5%
17	Other Chemicals	2	2	13%	32%	11%	0%	0%	0%
19	Plastics	4	9	49%	39%	30%	-5%	-7%	-4%
20	Glass and Ceramic	2	2	5%	32%	9%	0%	0%	0%
22	Other non metallic	1	1	15%	16%	-3%	-1%	-1%	-3%
23	Iron and Steel Products	3	6	7%	25%	3%	-1%	-2%	0%
24	Fabricated Metal Products	1	2	46%	53%	40%	-21%	-20%	0%
28	Vehicles	2	6	510%	1410%	490%	-492%	-375%	-72%
29	Other Vehicles	2	2	-14%	35%	-7%	-14%	-27%	-7%
30	Other manufacturing	2	6	27%	32%	21%	0%	0%	0%

On the regional markets, Zambia stands to benefit from high effective protection for textiles in Tanzania and Zimbabwe, industrial chemicals in Mauritius and Tanzania, and for clothing in Mauritius, Zimbabwe and SACU. Zambia also has an incentive to export trailers to SACU, benefiting from high tariffs on vehicles. The incentive to export clothes to SACU remains under the SACU CET, but diminishes under the COMESA CET.

Mauritius

The data for Mauritius is limited but indicates the currently very high level of effective protection in all but one of the sectors surveyed. The results of the impact of adopting the COMESA CET should be treated with caution as the actual implementation of the CET will matter – for example will Mauritian biscuit makers be allowed to treat butter as an intermediate product rather than a final good and therefore pay less tariff duty? Without such allowances the COMESA CET would put Mauritian businesses at a disadvantage to regional competitor on their home markets with a negative effective rate of protection.

The SACU CET leads to an overall reduction in the levels of effective protection, resulting in a negative domestic rate of protection for “*other non metallic products*” only.

The well functioning duty draw back mechanism of Mauritius counteracts the negative impact of tariffs on imported inputs on sales to the world markets and therefore the effective rates of protection on the world market is taken to be zero irrespective of the tariffs adopted.

Mauritius				Domestic effective rates of protection			World effective rates of protection		
2dig	Description	Companies	Products	Baseline	COMESA CET	SACU CET	Baseline	COMESA CET	SACU CET
4	Food Processing	2	2	91%	-60%	121%	0	0	0
8	Clothing	5	8	167%	-28%	125%	0	0	0
9	Leather and Footwear	5	5	25%	39%	39%	0	0	0
12	Paper	1	4	231%	49%	51%	0	0	0
13	Publishing	1	2	218%	47%	36%	0	0	0
22	Other non metallic	1	1	410%	-114%	-82%	0	0	0
27	Professional and scientific equipment	1	1	37%	40%%	-1%	0	0	0
30	Other manufacturing	1	1	-9%	-75%	49%	0	0	0
31	All other products	1	2	56%	-105%	25%	0	0	0

Of the sectors covered in the survey, Mauritius stands to gain from high levels of effective protection on processed foods in Malawi, Mozambique, Tanzania, Ethiopia and Burundi, and for leather and footwear in SACU, Malawi, Mozambique, Tanzania, Zimbabwe and Kenya. Incentives for regional exports of leather and footwear remain under the proposed COMESA CET and the SACU CET.

Data is not available to allow us to model Malawi. For Zimbabwe, the data we have relates to the period before the current troubles and will therefore not serve to give a fair indication of firms’ incentives with e.g. high parallel exchange rate premiums and import compression. Swaziland’s future is taken to lie within the South African Customs Union.

3.2.3 The Impact of CETs on Potential Trade Diversion Resulting From SACU Exports

The dominance of SACU, South Africa in particular, in intra regional trade (see table 14 for SADC) merits a closer look at the potential impact of countries in the region adopting the COMESA or SACU CET on the incentives for South Africa to export within the region.

Table 14: Percentage of SADC Imports by Source

Imports into	Source of Imports			
	SACU	Non-SACU SADC	Total SADC	Rest of the world
SACU	17.1	1.8	18.9	81.1
Malawi	40.4	13.6	54.0	46.0
Mauritius	13.5	0.4	13.9	86.1
Mozambique	36.4	4.6	41.0	59.0
Tanzania	8.9	2.3	11.2	88.8
Zambia	39.1	17.7	56.8	43.2
Zimbabwe	36.2	2.6	38.8	61.2
Total	18.1	2.2	20.2	79.8

Under the arrangements for the SADC FTA, South Africa stands to gain from the in some instances very high level of effective protection on regional markets. For example, SACU exporters will benefit from a regional effective rate of protection on industrial chemicals of over 400% in Mauritius, 199% in Mozambique, 196% in Tanzania and 167% in Malawi; on plastics the regional effective rates of protection is 221% in Mauritius, 179% in Mozambique, for beverages it is over 200% in Zimbabwe.⁹⁶ Such levels of protection on regional markets is likely to induce less efficient firms which may be struggling on South Africa's markets to increase sales within the region, which will lead to a reduction in welfare for trade partners.

⁹⁶ See SADC Trade Protocol: Economic Impact Assessment" (2004) TSG/USAID at www.satradehub.org

On SACU markets regional exporters will benefit from high levels of effective rates of protection for textiles and clothing under the FTA.

Adopting either the COMESA CET or the SACU CET will significantly reduce the very high levels of effective protection for regional producers, in particular for Mauritius and Tanzania, largely due to the CETs reducing these countries MFN tariff rates. For example, the effective rate of protection for paper for SACU exporters selling on the Mauritian market is 283%, which falls to 51% with the adoption of the SACU CET, reducing the scope for trade diversion.

3.3 Other Indicators of the Potential for Trade Diversion in COMESA and SADC

In considering the potential for trade diversion, it is important to distinguish between “natural” trading partners and what makes an appropriate preferential trade partner amongst low income countries. “Natural” trade partners export what the other imports, there is complementarity in their trade patterns. While a high degree of complementarity in trade indicates that trade will expand following a preferential agreement, in the context of low income countries it can point to where trade diversion is likely to occur and which countries will benefit from it. If countries have similar trade patterns, there is a greater chance that a preferential agreement will induce efficiency gains through greater competition rather than lead to the displacement of efficient third party suppliers by regional producers.

A recent analysis of trade within COMESA and SADC⁹⁷ shows that Egyptian and Kenyan exports are highly complimentary to the import needs of COMESA members, the same is true for South Africa and to a lesser extent Swaziland in SADC. So although the volume of South Africa’s exports in the region makes any concerns over their contribution to the net benefits from trade arrangements more acute, the potential for

⁹⁷ “COMESA and SADC: Prospects and Challenges for Regional Integration” (2004) Khandelwal, IMF Working Paper WP/04/227

trade diversion is similar in the two blocks; Egypt’s economy is of a similar size to South Africa’s.

Feenstra (2004)⁹⁸ shows that as long as trade with respect to third parties is not affected by the formation of a CU, members will be better off. We approximate this by examining the extent intra regional trade may be growing relative to trade between the trade block and the rest of the world. As shown in the table 15, while intra regional imports have grown at a fast pace, this has been from a low base, in particular for COMESA. For both COMESA and SADC, total imports have continued to grow and the share of intraregional imports has not radically increased. On this indicator therefore there is little evidence of imports for outside the region being displaced, though this may change as the implementation of the agreements progresses.

Table 15: Intra and extra regional trade

	1996-2000	2001-2003
COMESA		
Intraregional imports (% of total imports)	3.6	4.1
Annual growth in intraregional imports	5.9	18.8
Annual growth in total imports	8.0	7.6
SADC		
Intraregional imports (% of total imports)	9.7	10.4
Annual growth in intraregional imports	1.7	8.0
Annual growth in total imports	0.1	11.2

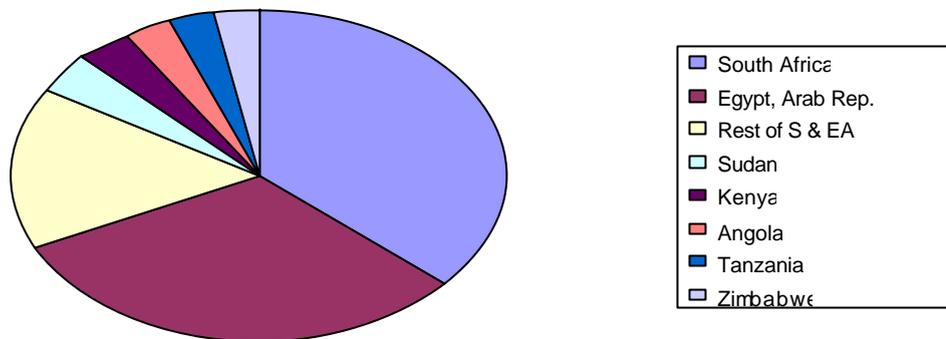
Source: Khandelwal (2004)

3.4 Market Access Considerations for Countries with Overlapping Membership

Consultations in the region suggest a priority for regional integration is to open regional markets for export promotion purposes. Within the region there are effectively two major markets, South Africa and Egypt, as shown in figure 7, though trade with Egypt is still at a low level relative to South Africa’s role in the region.

⁹⁸ “Advanced International Trade: Theory and Evidence” (2004) Feenstra.

Figure 7: Market Size (GDP US\$)



Source: World Development Indicators 2004

The impact of preferential arrangements on competitiveness in regional markets can be significant (see box). However, for Tanzania, Zambia and Mauritius, such a focus risks forfeiting the benefits from deep integration for little by way of return.

SADC Trade Protocol: Competitive advantage on SACU markets

Data made available by the South African Revenue Services, set out in the table below, offers some indication of the competitive advantage for Non SACU SADC as a result of the trade protocol. The value and the number of South African imports under the SADC trade protocol doubled in 2002, while exports registered a slight decline.

For non SACU SADC countries exporting to South Africa, the trade protocol gave them a cost advantage relative to non preferential partners of Rand 64.8 million on exports worth Rand 355.8 million i.e. 18%.

South Africa imports and exports under SADC RoO

	1- 6 months	7 - 12 months	2002
Number of Transactions			
No. Imported	1808	3467	5275
No. Exported	926	878	1804
Customs value of goods traded under SADC (rand million)			
Imported	125.4	230.4	355.8
Exported	71.6	65.6	137.2
Customs Duty and VAT Forgone by the South African Revenue Services (rand million)			
Total	29.7	35.1	64.8
Customs Duty	26.0	31.0	57.0
VAT	3.6	4.1	7.8

Source: South African Revenue Services

Note: Equivalent data is not yet available for COMESA as a whole, though the level of trade within COMESA is roughly 20% intra SADC flows, the latter being dominated by South Africa exports.

This is because, firstly, the scope for increasing exports to the region, in the short to medium term, is limited by several factors; firstly, by the low complementarity in trade between these countries and other regional partners. A trade complementarity index correlates the import of one country with the exports of another. A value of 1 indicates the exports of one country match the import needs of another while a value of 0 indicates the exports of one country are not imported by the other. For Tanzania the strongest correlation between what it exports and what other countries import are with Mozambique (0.2) and Mauritius (0.2). For Zambia, in the context of SADC the highest trade complementarity is with Mozambique (0.23) and Botswana (0.19), in COMESA it is Egypt that imports the most of products Zambia exports (0.18) and with Mauritius the complementarity is 0.19. For Mauritius, the greatest complementarity is with Mozambique (0.21), Botswana (0.17) and Seychelles (15.6). For Swaziland, the highest complementarity is with Mozambique (0.3), Namibia (0.3) and Botswana (0.28). For comparison, the correlation between South African exports and the imports of SADC as a whole is 0.53, for Egypt in COMESA it is 0.43 (and equal to 0.64 for Zimbabwe).

Secondly, for the sectors included in the effective rates of protection analysis, exporters in overlapping countries have generally a greater incentive to produce for the domestic, with lower effective protection on the SACU markets for all but a few products. We are not able to provide a similar analysis for Egypt.

Finally, the entire GDP of Sub-Saharan Africa is less than 2% of World GDP, consumers are very price sensitive and potential for developing niche, high value added products to service these markets is very limited.

3.5 The Impact of the Different RECs on FDI

In Chapter 2 we looked at how regional integration can enhance FDI inflows, and briefly examined the determinants and dynamics of investment from South Africa, the only outward investor of note in Southern and Eastern Africa. In this section we take a first

look at the data to see if there is any evidence of potential benefits – in terms of greater FDI inflows – from being party to one REC relative to another, and whether there is any gain from overlapping membership.

In general, the relationship between the ratio of FDI to GDP and other fundamentals, such as inflation and income growth, is poorly defined. This in part reflects that for low income countries single investments in e.g. infrastructure can have a disproportionately large impact on FDI/GDP. Furthermore, as the macroeconomic climate in many countries in the region has improved investments are increasingly driven by sector specific considerations such as privatisation and how establishment in a particular country fits together with the regional strategy of e.g. banks in particular. In the empirical analysis attempted, parameters are often sensitive to specification. But certain regularities emerged.

3.5.1 A Strong “Neighbour of South Africa” Effect

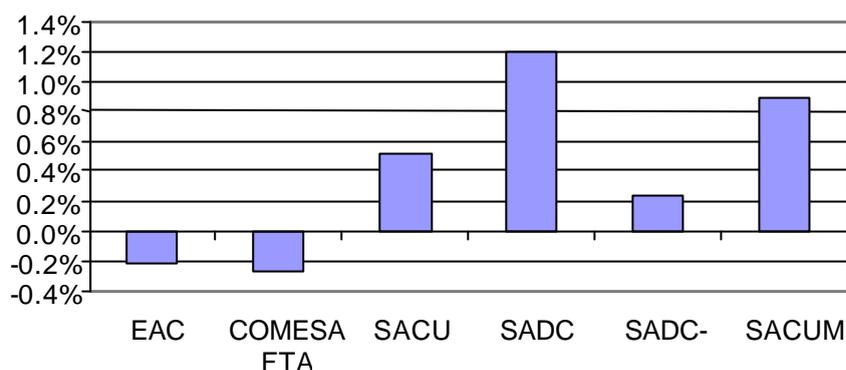
To examine how FDI to GDP during the period 2000 – 2003⁹⁹ varies within the different groups, we first controlled for political instability and for mineral deposits. We excluded FDI inflows to Egypt and South Africa As can be seen in figure 8, countries within SACU and SADC “outperform” the average in terms of FDI inflows.

However, re-dividing countries in SADC between SACU and Mozambique (SACUM) on the one hand and the rest of SADC (SADC-) on the other suggests that being a neighbour of South Africa is more important than belonging to SADC – as noted in chapter 2, South African investors view South Africa as an “anchor economy”. However, there is still a positive “SADC-” effect. The provision by the South African authorities relaxing capital controls on South African investment into SADC has been proposed as one explanation for the residual SADC effect. With moves in South Africa to reduce capital controls across the board, it remains to be seen whether this effect will remain.

⁹⁹ This is the earliest period we might expect the trade agreement to have an impact on the decisions of investors.

Note, the below average rates of FDI to GDP in EAC and COMESA do not indicate these trade blocs are “bad” for investment.

Figure 8: RII FDI/GDP differences from regional average (Controlled for instability and minerals. Excludes SA, Egypt)



3.5.2 No Evidence of Overlapping Membership Encouraging FDI

We undertook an investigation of the data to assess whether overlapping membership encourages FDI by providing greater access to markets in the region for investors locating in countries party to the different trade agreements. As noted, the relationship between FDI/GDP and fundamentals is poorly defined, and the error terms of all regressions reflect the idiosyncratic nature of many of the decisions influencing FDI in the region.

Given this, we should not place much trust in the statistical test of whether a variable is statistically significant in explaining FDI. Results were therefore taken to be indicative only. Results from the preferred model are given below. The indications are that the “neighbourhood” effect is positive and there is still some residual positive impact of SADC. EAC may also have some positive impact. Overlapping membership has a negative impact on FDI.

While parameters are sensitive to the specification of the model,¹⁰⁰ SADC and SACU always have a positive relationship with FDI, overlapping membership a negative impact.

Table 16: FDI and overlapping membership: a preliminary evaluation

	<i>Coefficients</i>	<i>t Stat</i>
EAC	1.1	1.8
Neighbourhood (SACUM)	0.8	1.5
SADC	0.4	0.5
COMESA FTA	-0.2	-0.4
OVERLAP	-0.6	-0.8
Intercept	-4.8	-3.3
lnGDP	1.1	5.8
Instability	-1.6	-3.3
Bus infrastructure	0.003	1.4
Adjusted R Square	0.52	
Observations	60	

With regards to overlapping membership, while access to both EU and US markets has encouraged FDI into several countries in the region by clothes manufacturers in particular, the impact of having access to both SADC and e.g. the EAC does not appear to be currently effecting the decisions of international investors. The negative relationship between FDI and overlapping membership may reflect that countries with overlapping membership are taken to have an equivocal commitment to opening up, or that overlapping membership increases the red tape companies will have to cut through to benefit from the different trade arrangements.

4 Regional Integration Policy: Priorities and Impact of Overlap

4.1 Product Market Integration

Having gained some insight into the perspective and role of the private sector with regards to trade in goods, we are in a position to assess the potential impact of regional integration policy and the extent to which overlapping membership constrains necessary

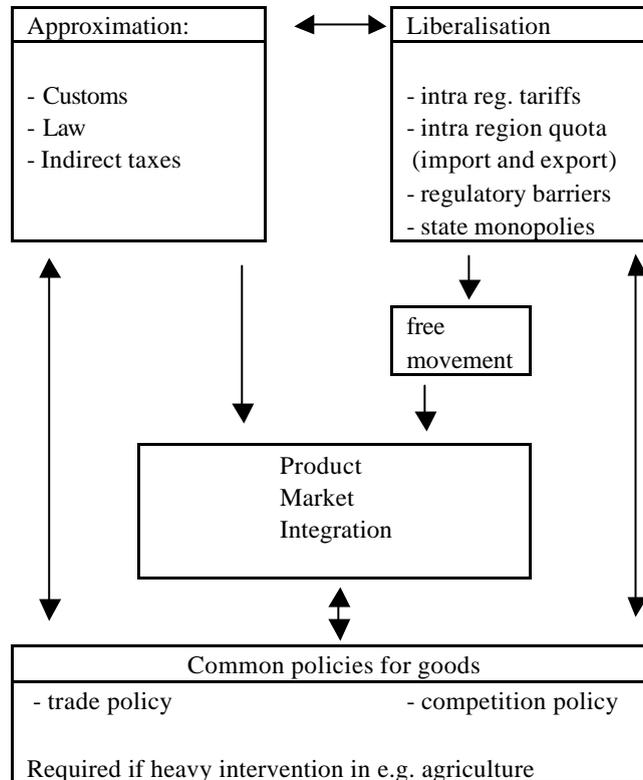
¹⁰⁰ In particular the extent to which the EAC has a positive relationship to FDI.

policy measures. We draw on the experience of the EU to shed light on what is, and what is not, achievable, at different levels of integration.

We characterise the different stages of integration. (1) Free trade agreements: involve reciprocal opening of markets for “substantially” all trade, generally go beyond tariffs and quotas and increasingly cover standards (including mutual recognition agreements) and regulation, trade facilitation, services, investment and competition and in some instances public procurement. Countries maintain sovereignty over their tariff and trade policy with regards to the third parties; fiscal frontiers and RoO remain. (2) Tariff Union: an FTA plus a CET though no common trade policy beyond a CET, and no customs pool. (3) A CU implies CET a customs pool and generally a common trade policy. If all trade arrangements with third parties are harmonised then RoO no longer apply. Fiscal borders still remain and border controls for goods whose e.g. safety standards differ. (4) A Single Market allows for the free circulation of goods. It requires a common trade policy, the harmonisation of standards and common policies in competition as well as trade and in areas where there is substantial intervention in the market (see figure below).

Overlapping membership prevents the establishment of a CET unless the CETs are harmonised. However, it is important to note that the stages are characterisations and advances in e.g. harmonisation of standards can be achieved in an FTA independent of establishing a CET.

Framework for Single Market in Goods



4.1.1 Customs unions and border transaction costs

An important reason for forming a CU is to do away with the transaction costs involved in border formalities, including RoO. And addressing customs procedures and red tape has been identified as a priority.

However, in terms of reducing the red tape at the borders, the impact of a CET may be limited unless a customs pool system is developed, the fiscal frontier is removed, technical regulations are harmonised and individual customs authorities have sufficient confidence in the institutional capacity of other Member States to implement. The experience of the European Union is informative: *“Despite the absence of customs duties in trade between Member States, in fact there was little difference in administrative burden or appearances between intra – Community trade and trade with non – member countries... Customs clearance at the Community’s internal frontiers was elaborate and*

time consuming".¹⁰¹ Before the single market, the free circulation of goods within the Community was not a reality.

The main impact is potentially from doing away with the need for RoO. However, even this requires not only a CET, but a raft of measures harmonising non tariff barriers. Harmonising non tariff barriers is a demanding process, which took the EU 30 years to achieve: in the initial stages Member States were allowed to maintain their own quotas on certain third country imports and use border controls to prevent their circulation.¹⁰² The CU between the EU and Turkey (in industrialised products only) allows both parties to impose antidumping duties on each other, automatically requiring RoO to define partner goods.

Therefore, while establishing a CU can be an important step towards addressing transactions costs, these costs may be addressed in the short run through focussing on trade facilitation under the NEPAD or Spatial Development Initiatives/ Transport Corridors. Furthermore, the experience of the EEA between the EU and EFTA reveals that in principle and given sufficient resources the free movement of goods can be achieved within a free trade area and does not require a CU. According to the EFTA Secretariat, Norway is currently considering applying the same technology that has accommodated the differences in excise and value added taxes within the EEA to take account of different tariffs applied by parties to the EEA.¹⁰³ However, the resources involved are likely to be significant.

4.1.2 The need to address bans, suspended duties, discriminatory taxes....

The main challenges for the private sector included bans, restrictive import permits, discriminatory taxes and suspended duties. These problems do not relate to the absence of a CET. Indeed, many barriers cited were intra SACU. Given the priority given these measures by several companies, it seems likely that addressing these barriers may have a bigger impact on regional trade than, per se, establishing a CET.

¹⁰¹ The European Commission (1999) "The customs policy of the European Union" at <http://europa.eu.int>

¹⁰² "The European Community: a case of successful integration" (1993) Alan Winters.

¹⁰³ For more information visit www.efta.int

4.1.3 Technical regulation, standards and overlapping membership

With regards to Technical Barriers to Trade and Sanitary and Phytosanitary Agreement overlapping membership becomes important when different regions develop divergent regulations and standards. Company interviews revealed some instances of divergences in standards between Kenya and South Africa in particular which may have implications for Tanzania if EAC standards converge to those of Kenya. However, there was little evidence to suggest technical regulations and standards are being used as a trade protection measure.

More importantly, given that the main markets for countries in Southern and Eastern Africa lie outside the region the focus for the development of regulations, standards and compliance should be to access those markets through the adoption of international markets as opposed to the development of regional ones. This however is not always easy given the often different standards applicable in the markets of Europe and the United States. And overlapping membership becomes a potentially significant issue when RIIs are negotiating agreements with trading partners that strongly diverge in their approach e.g. EU – US food safety standards. Interviews with European Commission experts suggest that while in the near term the divergence of US and EU food safety standards may present a dilemma for some countries in the region, over the longer term for each country to maintain access to e.g. the EU market in certain agricultural products, they will have to develop an institutional framework and capacity that will enable them to manage both systems. This is inevitable given the presence of GM crops in the region that countries share the same rivers, and that winds carrying seeds do not respect national boundaries.

4.1.4 Transport Costs

Transport costs are driven largely by poor and fragmented infrastructure in the region - see the map below taken from the SADC Barometer 2003 for an indication of the

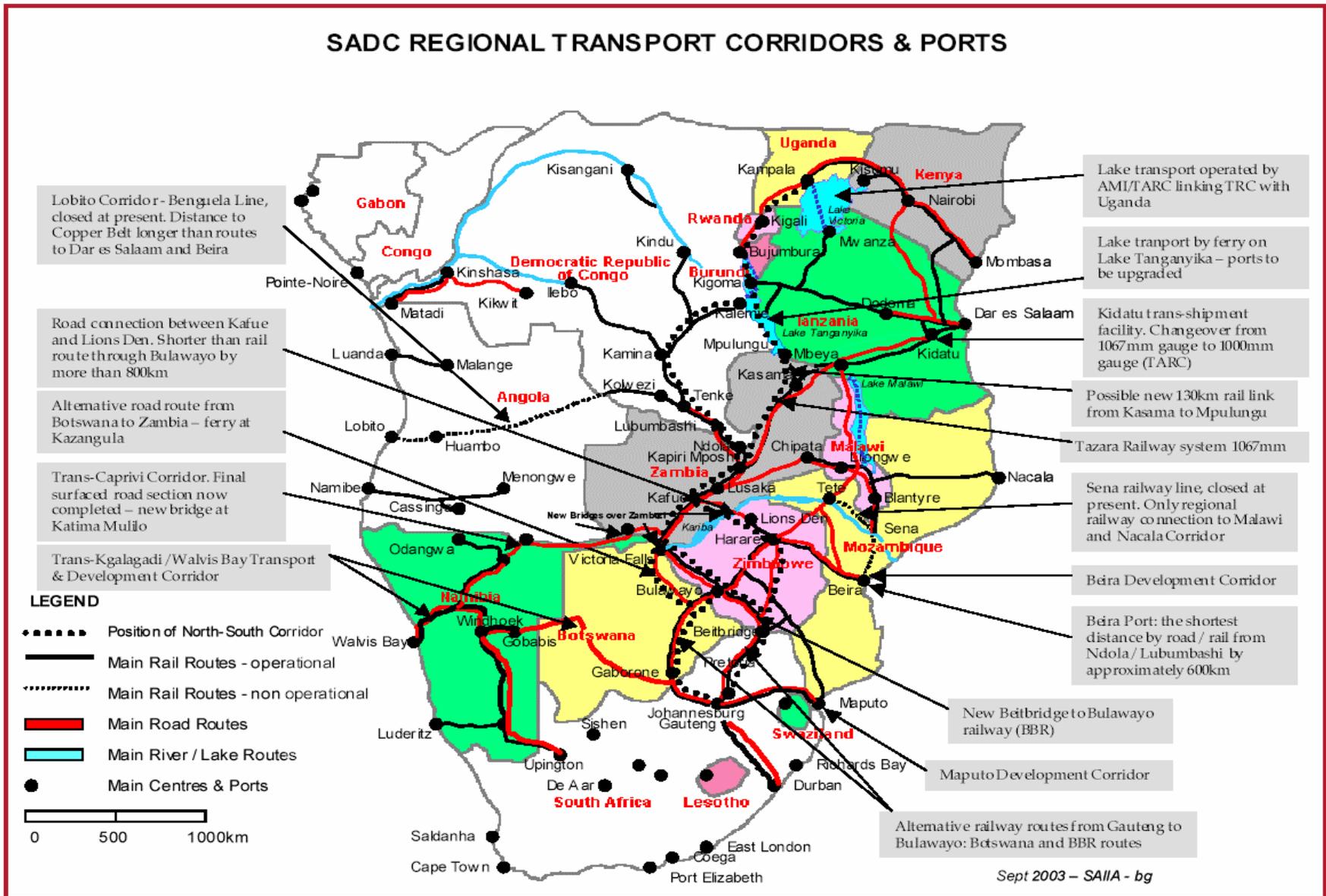
discontinuities of the transport system and also the potential for some of the NEPAD supported infrastructural projects.

Co-operation on transport corridors can be independent of the development of a common trade policy, and some of the factors serving to keep transport costs high –such as cabotage laws – can be addressed by unilateral liberalisation. But the impact will be far greater if the liberalisation of cabotage laws can be negotiated at the regional level.

4.1.5 Other Measures

Given the extent to which late or non payment may be constraining by formal sector small and medium enterprises (SMEs) in particular, establishing credit bureaus and allowing information sharing on credit history through the region could contribute to enhancing intra regional trade.

SADC REGIONAL TRANSPORT CORRIDORS & PORTS



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4.2 FDI and Regional Integration

As already noted, without strong regional institutions to enforce investment codes, regional integration has little extra to offer investors in terms of reducing risk and uncertainty. Furthermore, without strong implementation instruments to ensure national treatment of goods within the region and the expansion of market size through regional trade agreements is illusional. A strong regional framework for regulation and co-operation is also required to create regional securities markets.

Overlapping membership, by undermining the development of strong regional institutions, may be preventing the potential gains from regional integration in terms of greater investment and financial sector development from being realised. However, overlapping membership does not prevent important measures being taken to enhance investment. In particular, the harmonisation of business regulation and developing a monitoring and peer review process for domestic reform and treatment of investors can occur irrespective of the issue of overlap, as evidenced by the OHADA programme in West Africa and the work of the Investment Compact in the Balkans.¹⁰⁴

4.3 The Need for Deep Integration and the Impact of Overlapping Membership

The current process of regional integration, focussing as it does on product market integration, risks unravelling. This is because the benefits from regional free trade in goods are likely to be unevenly distributed between current net exporters and current net importers within the region which will probably lead to the imposition of trade restrictive measures – with the added cost that they will be less efficient than the tariffs they replace.

To make the process sustainable may require deep integration in the form of labour market integration and compensation mechanisms in particular. Countries in the region that see themselves as losing out through free trade in goods may derive benefits through these other measures. In some senses the Nordic process of integration, where labour migration has been achieved even though no agreement has been reached on a CU, may

¹⁰⁴ www.investmentcompact.org

be more sustainable than the process followed in establishing the European Union's Single Market.

The main costs of overlapping membership may therefore be in terms of undermining measures to enable the benefits of regional free trade to be spread more evenly and trapping the region in a low level equilibrium regarding regional integration.

5 Main Findings of the Economic Analysis

5.1 Product Market Integration

Consultations with companies operating at a regional level and with private sector representatives in several countries in Southern and Eastern Africa, and a survey of South African SMEs exporting to the region have provided insights into their perspective of regional integration and their role in driving regional integration. Though tariffs were held to be important for companies outside of South Africa, the main barriers cited related to: customs procedures, red tape and corruption, the divergence in standards and requirements on the markets in the region; the closely related issue of high transport costs; non tariff barriers in the form of import bans, suspended duties and the like. Several companies considered the harmonisation of requirements or “one set of rules” for entering markets in the region to be the single most beneficial change regional integration could deliver. Other constraints to operating in the region related to the business environment, priorities being none or late payments and lack of financial services. For companies in landlocked countries transport costs can be the biggest single factor in their lack of competitive ness.

The main problems to emerge from overlapping membership relate to the proper administration of tariffs and enforcement of the RoO at the border (which may also breed corruption). The poor articulation of tariff liberalisation under the different agreements and the possible infiltration of e.g. duty free EU goods from SACU into SADC and via Tanzania into the EAC were also raised as a concern.

If the barriers to regional integration were addressed, how would the economic benefits be realised and what are the likely costs? We present evidence from surveys of manufacturing which suggests the main efficiency gains in the short to medium term will not result from the exploitation of economies of scale but rather from the rationalisation and probably relocation of production. The larger companies and more advanced countries are likely to see the greatest increase in output. Data on the likely impact of regional integration on agriculture is scarce, and much of production is effectively outside of formal trade arrangements. However, the extent of non tariff barriers facing agricultural trade reflects the fear of regional competition amongst domestic agriculturalists.

This process of rationalisation, reallocation and hopefully competitive clustering of production, is necessary if the region is to become internationally competitive and if regional integration is to deliver benefits to consumers. However, it is likely to create winners and losers. In these circumstances, the process of regional integration can become unstable and politically unsustainable.

We briefly examined how these potential costs can be mitigated and how integration can lead to an upward convergence in incomes. To paraphrase one political leader in the region: *“Factories in other member states can provide goods for people in my country as long as people from my country can find work in the factories making those goods.”* Labour migration becomes a critical, though highly problematic, issue. Compensation mechanisms are a further, possibly equally politically difficult, route by which benefits of regional integration can be more evenly spread.

For product market integration, we conclude strong regional co-operation is required to address several of the main barriers to realising the benefits of regional integration and encouraging a more even distribution of the potential benefits.

5.2 FDI and Regional Integration

Reviewing the key obstacles to FDI indicates policy uncertainty and fragmented and narrow markets are amongst the main factors in deterring FDI; areas in which regional integration and developing regional institutions have – in principle – the potential to create change.

Given the increasing importance of South Africa as an investor in Africa we payed particular attention to its dynamics and determinants. Key determinants include transparency and liberalisation. In general, South African investment in the region is “anchored” in South Africa, building on activities in the home country.

High interest rates and poor financial services are also a constraint to investment and business activity more generally. Regional capital market integration, in so far as it provides a deeper market for the sale of e.g. government treasury bills, may enable governments to finance debt at lower rates, reduce the crowding out of private investment and increase competition for private sector clients. Though it is beyond the terms of reference of the study to examine this in detail, the lower real interest rates and spread between deposit and lending rates in the common monetary area, that is SACU less Botswana, suggest there may be significant benefits.

However, in practice, strong institutions are required if they are to act as “agencies of restraint” to reduce the risk and uncertainty facing investors. A strong mechanism for co-operation is also required to develop a pro – investment framework at a regional level and create a genuine single economic space. In interviews to date, businesses (to some extent) plan at the regional, as opposed to the national, level in the EAC and SACU only. The establishment of regional capital markets also requires a strong regional framework for regulation and enforcement of contracts.

Weak regional institutions may therefore be as damaging to attempts to attract FDI through regional integration as they are to efforts in achieving regional free trade.

5.3 Preliminary Economic Assessment of the RECs

The need for countries in the region to choose amongst their options for regional integration in the short to medium term should not only be driven by the incompatibilities of overlapping membership as the RIIs move to establish CUs. But they should also be driven by the need to establish strong regional institutions, which are undermined by overlapping membership.

How then to assess the options facing those countries with overlapping memberships? To try and give a perspective on this, we examined the potential impact on economic welfare and international competitiveness of tariffs under different scenarios for the different RECs¹⁰⁵ and on market access. We then examined the potential impact on investment, complementing the work of chapter 2 with an initial look at what the figures for FDI show. For Tanzania, we take the choice as being between COMESA or SADC, rather than the choice between the EAC and SADC. This is because given Uganda and Kenya's membership to COMESA, a firm commitment to EAC is likely to imply integration within the COMESA framework. Also the EAC and COMESA CET are very similar so as not to merit a separate analysis.

On the basis of these criteria there is no clear "winner" between COMESA and SADC for countries with overlapping membership.

What we can say is that (i) for Tanzania the adoption of the SACU CET (taken as a proxy for an as yet undetermined SADC CET) reduces the likely resource costs and anti export bias of the current tariff structure, while the COMESA CET has limited impact. For Zambia, adopting the SACU CET is largely neutral, while the COMESA CET slightly increases the bias to produce for domestic as opposed to export markets. For Mauritius the survey data we have to work with is limited, but indicates very high levels of effective protection on domestic markets. Both the COMESA and the SADC CET lead to a

¹⁰⁵ In the context of the analysis of tariff policy a word of caution is in order. Within the SACU CET there are many tariff peaks, individual tariff rates can be as high as 300%, whose impact is not captured if the firms surveyed do not import or produce these specific products.

significant opening up. In the case of the COMESA CET domestic effective protection rates turn negative for several sectors. Given the well functioning duty draw back scheme, the tariff structure does not directly affect the competitiveness of exports to world markets. However, the adoption of either CET would reduce the bias to produce for domestic markets.

- 1) Under the current SADC FTA, SACU exporters stand to benefit significantly from duty free access to the highly protected markets in the region. The adoption of the COMESA or SACU CET will greatly reduce the scope for harmful trade diversion. This is the result of the CETs lowering the level of protection in e.g. Mauritius rather than through the creation of a CU per se.
- 2) On the basis of the pattern of imports, there is little evidence to suggest that either COMESA or SADC is leading to substantial trade diversion, though this may change as the agreements come fully into effect.
- 3) Evaluating the benefits of the different RECs on the basis of “export promotion” is ill advised. Firstly because even though the markets of Egypt and South Africa are large relative to the region, together they account for little over 1% of world GDP. Secondly, countries with overlapping membership export little of what other countries in the region import, and the incentives of the current tariff structures and those under the two CETs considered, encourage producers to look to domestic not regional markets in all but a few products
- 4) Members of SADC (we exclude South Africa) do attract relatively more FDI. While most of this is the result of a “neighbour to South Africa” effect, there is still a residual positive relationship between being party to SADC and FDI. The cause of this is likely to be looser capital restrictions on South African firms investing in SADC. With the move towards a broader relaxation of capital controls it remains to be seen whether the “SADC” effect will remain.

5) If overlapping membership has any affect on FDI, it is a negative.

Given the indecisive outcome based on the criteria above, decisions on the future direction of regional integration for countries with overlapping membership are therefore likely to relate to issues that are beyond the scope of the current study, namely: (i) the opportunities emerging from labour market integration and an assessment of which RECs are likely to achieve the free movement of semi and unskilled labour. (ii) The level of compensation available and the compensation mechanism itself. (iii) The probability of the different RECs establishing regional financial markets to deliver lower real interest rates. (iv) For landlocked countries the integration of transport policies in the region should be a priority, though much can be achieved through the transport corridors proposed under NEPAD and other Spatial Development Initiatives.

5.4 Regional Integration Policy: Priorities and the Impact of Overlap

In chapter 4 we looked at the policy process for regional integration, assessing what matters and where overlapping membership is a key issue. We find that measures to address the priorities of the private sector are not necessarily constrained by overlapping membership or the absence of a common trade policy: many of the barriers were cited for intra SACU trade and several of the companies interviewed found it easier to trade with countries with which there are no regional or bilateral trade agreements than countries belonging to the same REC. Rather regional free trade is held back by a seemingly equivocal commitment to achieving regional integration evidenced by the proliferation of non tariff barriers to take the place of tariffs.

It is widely recognised that overlapping membership serves to undermine regional institutions. In the words of one Rwandan official *“The problem of belonging to several Regional Organisations is that you are not serious enough”*. Indeed where there is shared jurisdiction between different RECs, where responsibility for enforcement is not precisely demarcated, where there has been no transfer of sovereignty to regional institutions and

where the political commitment to a particular REC is not clear, the leverage of regional institutions and Member States to enforce implementation will be limited.¹⁰⁶

Weak regional institutions also prevent regional integration from enhancing FDI flows to the region. However, overlapping membership does not prevent important measures being taken to enhance investment. In particular, the harmonisation of business regulation and developing a monitoring and peer review process for domestic reform and treatment of investors can occur irrespective of the issue of overlap, as evidenced by the OHADA programme in West Africa and the work of the Investment Compact in the Balkans.

But more important is the extent to which overlapping membership undermines deep integration in terms of labour markets and compensation mechanisms. Without deep integration the current process of regional integration is at risk of unravelling.

¹⁰⁶ The issue here is one of achieving free trade within the RECs rather than a bureaucratic exercise. “The Mid Term Review of the SADC Trade Protocol” (2004) TSG/USAID (www.satradehub.org) revealed the importance of the distinction: while most countries had implemented commitments on tariff liberalisation in many instances discriminatory taxes, permit restrictions and even bans nullified the impact of these reductions.

PART III: Conclusions and Way Forward

When discussing options to solve the problem of overlapping memberships, two dimensions have to be distinguished. The first dimension consists of incompatibilities between the Eastern and Southern African RECs. The second consists of problematic implications of the EPA negotiations on these RECs.

1 Options to Solve Incompatibilities between African RECs

With respect to incompatibilities between the Eastern and Southern African RECs, it has already been established that there is no incompatibility as long as COMESA and SADC do not move beyond FTAs. Currently, COMESA seems to be closer to establishing a CU, but the SADC is also likely to do so within the next five years. Options to solve arising problems are further developed into three viable options later on:

Firstly and largely unrelated to the COMESA/EAC/SADC overlap, the relationship between SACU and SADC will have to be clarified. SACU needs to come together as a group in order to solve the problems created by the TDCA between South Africa and the EU for the EPA negotiations. In addition, if SADC is to become a CU, the SACU states will either have to leave the SADC (cf. Hess/Hess 2004),¹⁰⁷ or some form of merger is inevitable. SADC plans to evolve to a CU, albeit given that it took eight years to renegotiate the SACU agreement, five years to establish a SADC CU might seem too ambitious. Hess/Hess (2004) suggests that Tanzania withdraw from SADC (as it is a member of another CU, the EAC), all other states which simultaneously are members of COMESA and SADC would have to leave the former. Yet, the choice of Mauritius, Malawi, Zambia, Zimbabwe and the DRC to enter ESA implies they will not join the SADC CU. As stated, this will be problematic for Malawi, Zambia and Zimbabwe and be detrimental to regional integration as existing economic ties are likely to be disrupted.

¹⁰⁷ This currently seems unlikely. Yet it is a real possibility that the southern African CU will consist of the SACU states including Mozambique only, as the other most likely candidates have entered ESA in the EPA negotiations or are an EAC CU member. The remaining SADC EPA member Angola is not even part of the FTA and unlikely to enter a CU in the foreseeable future.

Malawi and Zambia could opt to join the SADC EPA if the EU agreed to renegotiate parts of the TDCA in an SADC-EU EPA.¹⁰⁸ This is rather unlikely.

Generally, it could be decided not to establish further CUs at all, thereby avoiding incompatibilities. Swaziland would have to withdraw from COMESA, the EAC process of establishing a CU would have to be stalled. From an economic point of view, neo-classical analysis suggests that Open Regionalism (Evans 2000) or global free trade may result in greater benefits (Schiff/Winters 2003). From a political point of view, this endows states with greater flexibility, or more space for erratic policy decisions. This option contradicts stated regional policies, and leaves little room for regional trade integration. Regional co-operation on development, cross-border issues and security could still be pursued.

Another possibility to effectively maintain the *status quo* is to establish partial CUs only in which RoO apply. It is implied that the CUs in question will not be fully operative. This would give Malawi, Mauritius, Zambia and Zimbabwe the ability to remain members of both FTAs. It would solve Swaziland's problem as well, but represent a more shallow level of SACU integration. Due to procedural costs involved and the likely evasion of RoO, South Africa is unlikely to agree. Furthermore, direct and indirect ("red tape") costs inflicted by the need to strictly monitor borders within the RECs threaten to render economically useless the exercise of establishing a CU (cf. Bhowon et al. 2003: 22-25). The "partial CU" option is undesirable in several respects, but could be realised, as it represents an opportunity to effectively "do nothing" while maintaining a sense of credibility on the part of regional leaders. Another option would be to maintain the *status quo* of partial CUs and leaving fast-track options for the more willing and able members to deepen economic integration, while also trying to form one single FTA for the Eastern and Southern African region as a whole.

¹⁰⁸ The EU would thereby honour its commitment that EPA negotiations shall not be detrimental to regional integration.

Another option is that COMESA, EAC and SADC/SACU (it is assumed that SADC will form a CU incorporating the SACU) mutually agree on a CET (cf. TRADES Centre 2002: 48). Currently, differences in national interests and economic structures make it unlikely that such a large number of states could agree on a common CET structure in the near future. Yet, in a long-term perspective, there is a clear trend towards convergence in tariff structures, which is strongly occasioned by global pressures such as those emanating from the WTO agreements.

If the RECs are intended to become CUs, it is imperative that they be more clearly separated and that member states clearly prioritise the CU they want to join.¹⁰⁹ Countries would have to leave one FTA and concentrate on the CU they are a member of, or, if they are not in an actual CU, join a future one. As already suggested above, in order to prevent losses resulting from leaving the FTA the three blocs (EAC, COMESA and SADC/SACU) could negotiate an FTA, which should become effective when the EAC becomes a fully functioning CU in 2009 (cf. Bhowon et al. 2003: 24).¹¹⁰ The solution found to the EFTA-EU contradiction parallels this one. Countries that opted for deep integration had to leave the EFTA and concentrate on EU membership. In order not to provoke a rupture in economic relations, an EU-EFTA FTA was established almost simultaneously. This currently seems to be the most realistic way to solve Swaziland's problem and that of the EAC members as well. This would be the most elegant solution, and it would certainly be the one that furthers continental integration the most. Concerning the EAC, technically it would be sufficient if Tanzania withdrew from

¹⁰⁹ Hess/Hess (2004) develop four scenarios on the configuration of RIIs. The first is called (almost) "equal sharing" of members between the SACU (including Mozambique), SADC, COMESA and EAC. This is a rather unlikely possibility, and it is little desirable as it would mean fragmentation rather than integration, and gains already achieved would be lost. The second is based on a merger of the SADC and the SACU, while the COMESA and the EAC continue to exist alongside. As this paper largely deals with incompatibilities arising if existing plans to establish CUs are realised and current plans imply that there will be three Customs Unions in the region for some time to come, this scenario reflects a central assumption of this paper. The third scenario is called "strong COMESA", alongside which exists only an enlarged SACU. This scenario is respected in this paper in as much as it is acknowledged that the EAC might join COMESA in the future, but it is assumed that the "enlarged SACU" will be a SADC CU. This CU might not, however, include all SADC members. Finally, Hess/Hess acknowledge the possibility of a REC encompassing all the Eastern and Southern African states. This scenario is considered a long-term prospect in this paper, which cannot be expected to solve immediate problems.

¹¹⁰ It is desirable that the blocs agree not only on tariffs, but on common RoO as well, as this would remove obstacles to trade and investment, i.e. facilitate establishing regional chains of production.

SADC. Uganda and Kenya could remain members of the COMESA FTA and would have to bear few costs for making possible the EAC CU. Tanzania could rejoin COMESA, which makes sense if the EAC is still considered a “fast track” REC possibly joining a COMESA CU. In both cases, COMESA tariff obligation would impact on the EAC CET, i.e. limit the options available. Simply leaving SADC is politically unattractive and economically problematic to Tanzania. Kenya and Uganda leaving the COMESA and joining the SADC instead is both politically unattractive and economically rather detrimental. In order to offer “equal gain for equal sacrifice”, it was proposed that the EAC members resign from the COMESA and the SADC respectively and seek associate membership status instead. Associate members would be free of tariff obligations, have to pay less membership fees, could attend meetings, but would not have voting rights (Bhowon et al. 2003: 24).

Associate status could make the decision to leave one REC politically more acceptable. Particularly in view of the EAC being a “fast track” initiative probably joining the COMESA CU in the future, it would enable Kenya and Uganda to maintain political contacts and attend negotiations. This solution is not altogether unlikely. The EAC countries have already announced their intention to negotiate free trade agreements with the other regional blocs. Yet, in Kenya, there are strong concerns about the effects of increased imports of South African agricultural and manufactured products on the economy. On the other hand, there are influential voices advocating deeper economic relations with South Africa. South Africa itself seems quite interested in such a deepening. On the other hand, the loss of Tanzania withdrawing from SADC is likely to be resented. It is not sure whether South Africa is inclined to facilitate a withdrawal by consenting to associate memberships. Concerning Egypt, the COMESA market was and is seen as a great opportunity. Egyptian entrepreneurs have had notable success in entering the market, and Egypt might be inclined to extend its access further to the south. Yet it has a large trade deficit with COMESA, and the deficit with the region might increase in an FTA with SADC. Currently, Egypt seems likely to slow down, if not block, negotiations on an Eastern and Southern African FTA.

When countries decide to pursue trade integration within only one REC, they could still pursue political co-operation in another organisational framework, probably with an associate member-status. Roughly comparable with the EU's programmes and the European Security and Defence Policy, SADC's developmental Directorates and the OPDS offer various opportunities for associated membership. The institutional structure of COMESA very much reflects its trade integration agenda, and currently there is little room for meaningful associate membership. This could change in the years to come, as more comprehensive integration is envisaged. In as much as the two SADC institutions mentioned develop their own agenda and decide on their day to day activities, associate members could have decisional rights and should be able to shoulder responsibilities, e.g. participate in peacekeeping mission. Many arrangements are thinkable, but it has to be recalled that SADC and South Africa strived to make the organisation more centralised. If the three areas of activity, i.e. free trade, regional development and regional security functioned largely autonomously, this would fragment SADC and is likely to be resisted.

Concerning regional security in Eastern Africa, the IGAD currently seems to be a more appropriate body than COMESA. In the long run the IGAD could therefore become a larger, Eastern African regional security initiative existing alongside COMESA. This is a scenario which offers possible long-term perspectives on further political regional integration, but is of little relevance to the pressing economic and trade related questions.

2 Options to Solve Problematic Implications of the EPA Negotiations

2.1 Options Developed Before the Establishment of EPA Configurations

The COMESA Secretariat has detailed several options on how to deal with the problem of multiple memberships, one of which is clearly favoured (COMESA 2003):

The EU could negotiate EPAs with individual ACP countries. This option would seriously lead to resource constraints of both the ACP countries and the EU, not promote regional integration and is not favoured by either party. If EPAs were negotiated at the level of existing regional integration organisations, countries with multiple memberships

would have to choose which organisation they want to negotiate an EPA with. According to the Secretariat, “*forcing the issue of which RIO [regional integration organisation] each country should negotiate an EPA with at this stage would not promote regional integration and would have negative political repercussions in the region*” (COMESA 2003: §23). With regard to the first point, it could likewise be argued that countries rhetorically stating that they want to take part in a CU will have to take a political decision on the issue anyway, and that forcing the issue promotes regional integration, as those willing are separated from those unwilling.

Concerning the second point, clearly South Africa would not like to see SADC countries strengthening their links with COMESA, and COMESA would not like its members to become more deeply integrated with SADC. However, political repercussions can be expected to be minimal. Concerning Zimbabwe, EU pressure to rapidly establish EPA groups probably resulted in a decision the country would not have made at a later point in time. As for Malawi and Zambia, the TDCA rather than the EU schedule explains a decision which may be detrimental to regional integration. However, since ESA and a SADC EPA group have been established, everything looks set for this option to materialise.

The option clearly favoured by COMESA was to negotiate a single EPA for all Eastern and Southern African ACP states. A study undertaken for SADC (TRADES Centre 2002: 54) as well as Hess/Hess (2004: 12) proposed a similar solution. Once negotiated, “*the signing of EPAs will be done between the EU and [...] customs territories which are functioning at the time EPAs are to be signed [i.e. December 2007]*” (COMESA 2003: §32, emphasis added). The problem with this option is that it seems to be outdated, as two EPA groups have been formed. This appears to be due to the fact that such an EPA would not build on existing RECs, and political dynamics have not resulted in establishing a separate, all-encompassing REC for EPA negotiations. It is not clear to what extent South African pressure is responsible for this development. The realisation of the option would at least not disrupt sensitive, still reversible integration initiatives negatively affected by the current EPA groupings, i.e. the EAC. Therefore, it might also facilitate further

integration in the region, particularly with respect to creating CUs by establishing largely similar economic regulations for EU trade. Angola, Mozambique and Tanzania are, however, the only non-SACU members of the SADC EPA group, Angola being the sole COMESA member. It can be assumed that their choice reflects a deliberate decision not to join a future COMESA CU although Tanzania might come back on that decision.

EPA negotiations with the SADC face further obstacles. As has already been mentioned, an EU-South African TDCA establishing an FTA came into effect in January 2000. South Africa is not a member of the Cotonou Agreement, and the EU has been unwilling to include the country in the EPA negotiations.¹¹¹ In the SADC EPA, South Africa has only an observer status. If BLNS tariffs on EU imports differed from South African tariffs, SACU would be downgraded to a partial CU. As a result, the level of integration would take damage. As the Imani report (EC 1999) indicates, the South African-EU trade agreement is therefore likely to have predetermined results of the EPA negotiations.

The Imani report, a consultancy study undertaken for the European Commission, suggests three different EU-Southern Africa EPAs (cf. Gibb 2001: 79): The first EPA would cover SACU and intend to formally extend the South Africa-EU FTA (the TDCA) to BLNS. This has de facto already happened (Gibb 2001: 78) at least as far as external tariffs on EU imports are concerned. This EPA would be viable, but as results are largely predetermined it is likely to be regarded as being imposed by the EU.

¹¹¹ An EC document on the issue deserves to be quoted at length: "It is obvious that EPAs cannot be negotiated on the basis of the Cotonou Agreement with third countries that are not signatories to this Agreement. It may, therefore, be questionable whether regional groupings with non-ACP members are eligible for the negotiations of EPAs. [...] This would certainly be difficult to envisage, if the regional grouping concerned formed a customs union, unless the regional grouping allows part of its members (the ACP) to negotiate economic integration agreements with third countries (the EC) [which would mean a step back on integration, C.J.] or **unless the Community and the non-ACP country would be prepared to grant each other similar treatment to that provided for within the EPA**" (EC 2001, emphasis added). It would therefore be possible to include South Africa in EPA negotiations and renegotiate the EU-South Africa FTA, if political will existed. This is not the case. The Cotonou Agreement clearly states that the TDCA takes precedence over EPAs. Similar to the South African problem, integration of the non-ACP country Egypt into a COMESA CU will face difficulties due to the EU's approach to EPAs. EPA negotiations with the Pacific Islands Forum which includes Australia and New Zealand run into the same problem.

An alternative version of this option is to extend SACU to the entire SADC area. This seems impossible in the short run and will involve time-consuming negotiations. Even after long and arduous negotiations, BLNS still receive a relatively higher, compensatory share of the CET pool, and are unlikely to further compromise on the matter. Extending SACU to the whole SADC area would require a comprehensive renegotiation of the revenue sharing formula. The more developed SADC states, i.e. Botswana and Mauritius, are unlikely to agree to lose their benefits or even contribute disproportionately to the pool (Lee 2003: 85).

More realistically, a future SADC CU could include SACU, in a sense that the SACU states continue to apply their revenue sharing formula, while the other states receive their share of CET revenue according to their level of imports. However, this will still involve tough and probably rather long negotiations, as the SACU CET currently reflects South Africa's need for industrial protection. Future CU members are unlikely to accept this CET, and South Africa will not accept paying BLNS a relatively higher share of CET revenue if it is no longer compensated by the protection the CET confers.

If SACU was not extended, the second EPA would include the non-LDCs Zimbabwe, Mauritius, and the Seychelles. Trade preferences between these countries and the EU would have to be reciprocal as is the case with the first EPA, but the agreement would not be predetermined by the EU-South Africa treaty. This EPA is unlikely to be realised. The Seychelles are no longer a member of the SADC, and both the Seychelles and Zimbabwe are ESA members. Additionally, Zimbabwe currently has an ambiguous status between LDC and non-LDC.¹¹²

The third EPA would include the SADC LDCs (except SACU member Lesotho) and be a non-reciprocal agreement. For such an EPA there is no further need. Under the EBA initiative, the LDCs essentially enjoy free, non-reciprocal EU market access. If such an

¹¹² As has been mentioned, Zimbabwe was reclassified an LDC by the World Bank in 2001. The Cotonou Agreement does not define Zimbabwe as an LDC and makes no provisions to include new countries into that category in case of changing World Bank classifications. For political reasons, the EU is unlikely to be forthcoming to Zimbabwe, and will therefore continue to treat the country as a non-LDC.

EPA was negotiated, negotiations would most likely consist of exchanging tariff reductions by the LDCs against EU development programmes.

The implications of the Imani proposal are ambiguous. The “*REPA [Regional Economic Partnership Agreement] model could serve to undermine attempts to promote regional integration*” by fragmenting SADC, or alternatively support a more flexible variable geometry approach (Gibb 2001: 79). But due to recent political and economic changes, the Imani proposal is largely outdated by now and of limited or little relevance. Currently, it seems more promising to negotiate an EPA with the SADC EPA and a further one with ESA, which make special provisions for non-SACU LDCs. The Cotonou Agreement provides for such special provisions (Art. 35 (3)).

2.2 Options Taking Into Account Current EPA Configurations

Currently, there is no mechanism in place to deal with conflicting commitments arising from Tanzania’s membership in the SADC EPA, Kenya’s and Uganda’s membership in the ESA, and EAC membership of all three countries. Options to solve the problem are:

- 1) The EPAs contain a special provision allowing LDCs to unilaterally determine their external tariffs as is the case under the EBA initiative. The EU has ruled out this option.
- 2) Extend the provision of Art. 37 (4a) to cover agreements of the EAC’s individual members with other regional organisations. Given that the EU is one of the most important trading partners of the EAC countries, the application of RoO would mean that the EAC became a CU in anything but by name.
- 3) Negotiate a separate EPA with the EAC. However, the EAC countries (justifiably) assumed that they had greater bargaining power and expected more favourable agreements by joining larger RECs in the negotiations.
- 4) Uganda and Kenya join the SADC FTA and the SADC EPA (cf. Mair 2001). This option seems neither acceptable to Kenya nor to South Africa fearing direct competition of their industries and is therefore unlikely to materialise.

- 5) Tanzania leaves the SADC EPA and will also not be part of a SADC CU but could maintain its SADC FTA relationship. The country joins ESA, negotiates an EPA on the same conditions as Uganda and Kenya, and concentrates on the EAC CU. This option seems realistic and complements the favoured one in 6.1, No. 4. Observers estimated that Tanzania's withdrawal from COMESA was largely motivated by fear of being flooded with Kenyan products (Mair 2001). That problem appears to be solved since the EAC CU protocol has been ratified on the basis of the asymmetry principle. Whether it will be adopted seems to depend on what Tanzania expects from South Africa by joining the SADC EPA and whether it indeed intends to implement the EAC protocol. It would facilitate joining ESA and a future integration of the EAC in a COMESA CU if Tanzania rejoined COMESA together with Kenya and Uganda, but this seems "politically unattractive" to Tanzania (Bhowon 2003: 24).

3 Conclusions from a private sector perspective

For the private sector, main concerns on overlapping membership relate to confusion over which regime and RoO apply at the border, and the potential for the infiltration of duty free goods through partner countries with different trade arrangement with third parties. When it comes to enforcing measures that liberalise trade in sensitive products or facilitate trade in the context of poor, often corrupt, customs procedures, many consider the regional trade agreements to exist on paper only.

The priorities for the private sector relate more to customs procedures and red tape, bans and non tariff duties, transport infrastructure and the business environment, many of which can be addressed by measures that do not require the establishment of e.g. a CU. In the area of investment it is also true that important measures, such as harmonisation of business regulation and the development of a monitoring and peer review mechanism can be taken at the level of the entire Southern and Eastern Africa region and are not directly compromised by overlapping membership. But strong mechanisms of implementation are required to achieve e.g. national treatment of goods within the region. This requires

strong regional institutions, which are undermined by overlapping membership. The slow progress towards genuine free trade in goods may be considered in part a casualty of overlapping membership.

However, one of the main outcomes of the analysis suggests the current process of regional integration – focusing as it does on trade in goods – risks unravelling or at least grinding to a halt before the real benefits may be realised. This is because product market integration is likely to make winners of the current net exporters and losers of the current net importers and favour large firms at the expense of small firms. A situation which is likely to become politically unsustainable and lead to the imposition of unauthorised bans or the use of import permits to restrict trade. The benefits will need to be spread more widely. Ways in which this may occur include a deeper level of integration to enable the movement of semi and unskilled labour in the region and a compensation mechanism. Financial market integration and integrating regional transport policy may also disproportionately benefit the poorer and landlocked countries. In this regard the Nordic process of integration, where e.g. an integrated labour market has been achieved even though no agreement has been reached on a CU, may be more sustainable than the process followed in establishing the European Union's Single Market.

In deciding on which direction to integrate, the economic analysis based on the different proposed tariff structures under COMESA and SADC (taking SACU CET as a proxy for the later) and investment do not offer a definitive indication of the “best” strategy. Rather the decision may hinge on which region is most likely to be able to move beyond trade in goods to achieve deeper integration. How much may Zambia have to gain from the free movement of labour under COMESA or SADC? And how likely is it that either institution will take this step? Is Tanzania likely to benefit from the free movement of labour? And will it be achieved more readily in the EAC than SADC? Can Zambia and Malawi address the extra costs of being landlocked in the context of transport corridors or does it require SADC?

The process of consultation with the private sector has served to confirm transport and trade facilitation as priorities. In the context of EPAs, trade facilitation and co-operation to overcome institutional weakness, in particular in the context of investment, emerge as priorities in negotiations.

Trade facilitation is central to enhancing the competitiveness of the region and is an area where EU assistance may be particularly effective in enhancing co-operation, co-ordination and implementation in the region.

With regards to investment, the EPA framework may offer a way to overcome the institutional weaknesses undermining efforts to enhance investment by establishing “agencies of constraint” to reduce uncertainty and risk for investors. Co-operation on investment should cover all of Southern and Eastern Africa with South Africa’s direct involvement to realise the potential for EPA to increase investment throughout the entire region. Consideration should go beyond fixed investment. Though there are political sensitivities resulting from the Debt Crisis and the Asian financial crisis, the EU should support the development of regional financial markets for government securities in particular, albeit by adopting a prudent approach. EU investors’ participation in these markets may also encourage a reduction in interest rates, in turn reducing the crowding out of the private sector from loan markets.

The provision of a compensation mechanism in the EPAs that also takes into account the impact of trade arrangements between countries in the region, not just the EU, could significantly contribute to making the process of regional integration sustainable. It may also indirectly open the door to the creation of one deeply integrated “happy family”: On the one hand it would reduce the reticence of South Africa, Botswana and Mauritius amongst others to consider a compensation mechanism covering the poorer countries in the entire region if they know they will be sharing the resulting financial burden with the EU; On the other hand, the compensation mechanism would allow net importing countries which will lose out in the initial stages of regional integration to better cushion any adjustments.

In providing support to EPAs the EU may also need to ensure it does not inadvertently provide incentives for countries to continue with overlapping membership by for example enabling them to access additional funds under the Regional Indicative Plans for both SADC and Eastern Africa than if they were party to only one REC.

4 Three Viable Options to Address the Overlap Problem in Eastern and Southern Africa

The following three options are all viable in view of the need to deal with multiple memberships in the region. But they imply certain trade-offs which are discussed in more detail below. And given the inconclusiveness of parts of our economic analysis, we will also give recommendations for further assessments.

- **Option 1 – “Status Quo of CUs plus larger integration project between COMESA and SADC”:** SACU and EAC remain fast-tracking groups of SADC and COMESA respectively, while SADC and COMESA remain FTAs with a view to forming a larger, integrated Eastern and Southern African trade zone at a later stage.
- **Option 2 – “Variable Geometry Option” or “SACU+ and EAC+ Option”:** Potentially enlarged SACU and EAC become fully fledged CUs by 2010, and countries not participating in the CUs remain members of the SADC and/ or COMESA FTAs for the time being but with a view to form two separate CUs as SADC and COMESA in the medium term.
- **Option 3 – “Leap Forward Option”:** SADC and COMESA both become fully fledged CUs by 2010 and will merge with the current SACU and EAC respectively. All countries take a decision regarding their membership in either the SADC or COMESA CU.

We will now address each one of these options in turn:

- **Option 1 – “Status Quo of CUs plus larger integration project between COMESA and SADC”:** SACU and EAC remain fast-tracking groups of SADC and COMESA respectively, while SADC and COMESA remain FTAs with a view to forming a larger, integrated Eastern and Southern African trade zone at a later stage.

Implications: This option would imply a new integration agenda for COMESA and SADC which deals with a larger number of countries and consequently with a less ambitious but potentially still quite effective trade liberalisation and facilitation policy, thus embracing the vision of Pan African integration. Instead of further pursuing their trade agendas with the objective of becoming separate CUs and to move on to a common market, COMESA and SADC would remain FTAs. At the same time they would undertake to adopt common trade policies for the whole Eastern and Southern African region. The current CUs (SACU and EAC) would serve as fast-tracking groups that set standards in various areas of economic integration but would not necessarily define later common policies. More effective integration mechanisms would need to be developed, probably at the level of the AU. These mechanisms could embrace the larger groupings and coordinate policy harmonisation between the existing RECs.

In terms of EPA negotiations, following the logic of this option, it would be most straightforward to negotiate as two groups; one consisting of the current SACU which would basically concentrate on the revision of the TDCA in favour of the BLNS-countries; and the other one comprising all other countries irrespective of their current membership in COMESA, EAC and/or SADC, i.e. as had been suggested by the ESA EPA group earlier in the process. The general framework of the agreements on RoO and other trade policy measures would be the same for all countries, but tariff phase-down schedules would be negotiated individually with the EU. For ESA, this option may preclude the grouping from offering a single trade regime to the EU.

Trade-offs: This option would come at the cost of deeper economic integration in SADC and COMESA. The economic and political signals given to potential investors will at best be ambiguous if their earlier trade agenda is not pursued firmly by these two RECs

any longer. For COMESA, it would substantially slow down the progress in trade integration that has been achieved with the implementation of the FTA among the majority of COMESA members. By pursuing this option and keeping the FTA open for further countries, COMESA would postpone its CU plans to an unknown date. For SADC, even the move towards full implementation of the FTA may lose momentum if the objective to achieve the SADC CU by 2010 was to be removed. As tariffs will continue to differ from country to country, RoO will have to be enforced within the region. For EPAs, each country not part of SACU or the EAC CU will need to come up with its own tariff phase-down schedule and negotiate it individually with the EC. This, however, may not even be feasible within the timeframe left for the negotiations. The experience of the TDCA also suggests that it will be difficult to harmonise, at a later stage, tariff phase-down schedules that have been agreed upon individually by the countries with the EC. Moreover, the EC may be reluctant to accept such an approach, as it will seriously stretch its own negotiating capacities.

What the RECs and their members need to be clear about: While this option seems to be the easiest and potentially most realistic one, it is certainly neither consistent with SADC's envisaged integration process spelled out by the Regional Indicative Strategic Development Programme nor with COMESA's stated more ambitious objective to establish a CU by 2008. The economic and political consequences have to be clearly anticipated by both RECs and their member states. Trade liberalisation would still be part but no longer the centrepiece of SADC integration, while COMESA would basically postpone the coordinated and ambitious move towards the CU in favour of the larger regional integration project. The main appeal of this option lies in the fact that it reflects current realities with the caveat that the respective clear political decisions have not been taken as yet. If pursued deliberately, this could be the option that is most realistic in terms of how ready the larger region currently is for deeper trade integration. All countries should moreover consider the potential loss of bargaining power in EPA negotiations, the cost of administering various trade regimes in the region - and the abandonment of the concept of five regional pillars of the envisaged African Economic Community.

- **Option 2 – “Variable Geometry Option” or “SACU+ and EAC+ Option”:** Potentially enlarged SACU and EAC become fully fledged CUs by 2010, and countries not participating in the CUs remain members of the SADC and/ or COMESA FTAs for the time being but with a view to form two separate CUs as SADC and COMESA in the medium term.

Implications: For Eastern Africa, this option would imply a consolidation and/ or increase of membership (e.g. Rwanda) with the current EAC setting the standards. Tanzania would have to commit herself to concentrate on the EAC, and the CET of the EAC would set the standard for other COMESA members to follow this faster and more comprehensive integration track. For Southern Africa, this would mean that additional countries (Mozambique being a likely first candidate) decide to become a member of SACU. For the countries joining SACU it would effectively imply taking over the SACU CET and other common policies, including existing trade agreements between SACU and third parties. The other SADC member states would remain members of the SADC FTA, hence postponing to 2010 or later the decision to move to a CU. Both COMESA and SADC, would, however, pursue their stated objective to become CUs in the foreseeable future.

In the meantime, EAC and SACU would have a FTA agreement with the non-CU members of COMESA and SADC, respectively. Here the possibility of establishing an associate membership comes in, either individually as countries or between groups. The “variable geometry” option thus caters for the fact that some countries may not consider themselves ready to join a CU yet or before the suggested dates but still plan to do so at a later stage.

In view of the EPA negotiations, the enlarged SACU+ group could negotiate and implement an EPA provided common policies are quickly developed alongside the respective negotiation machinery that FTAs commonly lack. Members of the SADC EPA not part of SACU by 2008 will need to negotiate individually how to reciprocate market access vis-à-vis the EU, or leave the SADC EPA group. The regrouped ESA would negotiate an EPA with the EU, independent of the partner states’ membership in EAC,

COMESA or SADC. The tariff phase-down will be identical for all members of the enlarged EAC+ group that adopt the EAC CET whereas all other countries have to come up with their own proposals.

Trade-offs: The main trade-off is that deeper integration is likely to take place in the fast-tracking groups SACU+ and EAC+ only, while among the remaining members of SADC and COMESA the process of deeper integration risks being postponed. In particular, the next stages of economic integration such as a common market are likely to be delayed in the larger groupings. Moreover, political decision-making will be further postponed, and the overlap problem is likely to persist. All countries outside the fast-tracking groups - but with the perspective to join later - need to be clear about one thing: The later they join the respective CU, the more internal regulations and external agreements (the *acquis communautaire*) will already be in place without the latecomers having had a part or say in the negotiations. Therefore, the decision not to join the CU should not postpone a later accession but rather be informed by a clear estimate of the benefits of maintaining a purely national trade policy agenda. The costly administration of RoO will still be necessary in both SADC and COMESA, thereby diminishing the benefits of trade and economic integration. The economic gains of a FTA alone are limited, as it may not trigger additional investment and growth.

For EPA negotiations, decisions on how to reciprocate market access vis-à-vis the EU will be rather complex. Obviously, the existence of the TDCA would have a bearing on the negotiations, and the question for the SACU+ group is whether it is more costly to fully accept the terms of the TDCA, or to pursue a negotiation position where, for instance, lists of sensitive products will be exempted from the overall liberalisation schedule and transition periods will be extended. In East Africa the current ESA, including the EAC+ group, would negotiate jointly but apply different tariff phase-downs, a single one by the EAC+ group based on their CET, and individual ones for all remaining FTA members on a country-by-country basis. This would draw on scarce resources and the date of 2008 for the EPA implementation will be difficult to achieve.

What the RECs and their members need to be clear about: For the Southern African region, the costs and benefits to join SACU under the current tariff regime will need to be assessed by each country very thoroughly. Moreover, the possibility to extend the SACU revenue sharing mechanism in its current or revised form to additional members needs to be looked into by the current SACU members and the potential accession countries. Those countries which decide to join both SACU and converge to the TDCA should negotiate for additional technical and financial support from the EU as they will open up much faster than what is currently required in the context of the WTO or is intended for the EPAs. In East Africa, Tanzania needs to assess the costs and benefits of committing herself fully to one or the other integration process, i.e. within the EAC or SADC including the SADC EPA. Potential candidates for joining EAC need to make the same assessment, and consider in parallel the possibility of remaining an associate member of another REC. Again, the EPA negotiations could be used to achieve additional technical and financial support for those willing to pursue a faster and deeper trade integration process.

- **Option 3 – “Leap Forward Option”:** SADC and COMESA both become fully fledged CUs by 2010 and will merge with the current SACU and EAC respectively. All countries take a decision regarding their membership in either the SADC or COMESA CU.

Implications: Rather than concentrating on the currently existing CUs, all SADC and COMESA states would aim at forming operational CUs as soon as possible. Internally in both RECs the pace to eliminate all trade barriers and coordinate trade policies would need to be increased to ensure that the eventual CUs are fully fledged CUs, i.e. they effectively implement a CET and no longer require RoO. Most importantly, both RECs would have to agree on a realistic and credible date for achieving the CU, and on a detailed implementation plan. In Southern Africa, for the members of the future SADC CU, this would include agreeing on a CET to be negotiated between SACU and non-SACU member states. In Eastern Africa, similarly COMESA and the EAC will need to agree on a single CET. In each case, the whole group will adopt common trade policies

vis-à-vis third parties, and a mechanism to pool and distribute revenue from tariffs will need to be established.

Deeper integration will obviously imply both costs and benefits in terms of revenue effects and increased competition. The CUs will need to develop adequate financial mechanisms to support the necessary adjustment measures. In cases where pre-existing preferential trade agreements by one or more members of the CU appear unacceptable to the rest of the union – with the TDCA being a likely one – the group will either need to administer different tariffs with that particular trading partner for a transitional period, or adopt the same tariff schedule as part of the CET. The bargaining power of the two enlarged and consolidated RECs and their role as regional pillars of the AU will be enhanced. Their credibility as RECs will be strengthened, including in the eyes of potential investors.

EPA negotiations will be straightforward as the configurations will be clear and a CET established in time for a collective tariff phase-down scenario vis-à-vis the EU. For SADC this will essentially be the TDCA schedule. If SADC were to decide quickly, the interests of SADC members could still be taken on board during the ongoing review of the TDCA, and a mechanism to compensate SADC CU members for opening up faster than required could be negotiated with the EC. The expected transition phase before the tariff phase-down begins on the side of the ACP (back-loading of liberalisation) would cater for the time gap between the application of a CET and the implementation of the EPAs.

Trade-offs: It will not be an easy task for SACU and non-SACU member states of SADC as well as for EAC and COMESA members to agree on a CET given the divergence of current tariff regimes and partner states' divergent industrial development. Although apparently easier in Eastern Africa, the task is still enormous, bearing in mind the different trade policies and levels of development. In view of the EPA negotiations, under this option all countries would need to link their decision for a CU with their choice of an EPA configuration. This can put several countries in a dilemma, and will

most immediately affect Tanzania as the country could not be part of EAC and the SADC EPA any longer.

In Southern Africa, the TDCA will still prevail, *de facto* requiring the rest of the SADC CU to accept the same terms (as the BLNS) and converge to South Africa's tariff phase-out agreed on with the EU. Otherwise the region would have to administer a differential tariff offer with respect to the EU. That would undermine the future SADC CU. The TDCA is expected to reach full implementation of the FTA in 2012, while the transition period for the EPAs could expand to up to 20 years from the date of implementation, i.e. until 2028.

What the RECs and their members need to be clear about: All countries with double membership in COMESA and SADC need to decide which CU they wish to join, and all countries have to define their positions vis-à-vis a proposed CET. Costs and benefits of establishing a CU should, however, always be seen in the light of medium-term gains of deeper integration and not only against short-term considerations of potential revenue implications. The possibility of establishing an FTA between the two future CUs should be part of the overall assessment, that is, SADC members would not necessarily lose the preferential market access they currently enjoy as COMESA members, and *vice versa*. In Southern Africa, in the interest of regional integration, an early convergence date for the CET and common policies including vis-à-vis the EU should be considered for the SADC CU. If this were decided on in principle, a mechanism to compensate or specifically support those countries ready to reciprocate the EU much faster than required in other EPAs (and by WTO standards) would need to be put in place. For the BLNS, this was planned but never operationalised. Moreover, a mechanism to compensate SADC for the need to enforce RoO in order to administer different tariffs in its territory due to the TDCA could be discussed and negotiated. Both COMESA and SADC have to assess the capacity needs to ensure that revenue collection and the enforcement of common trade policies are administered properly.

To conclude after this discussion of the three options, we will finally turn to some more general aspects. The successful move towards a fully functioning CU by as many countries as possible is in and by itself a challenging task for the region and includes negotiation and management of coordinated tariff phase-outs, establishment of a CET as well as the creation and implementation of revenue collection mechanisms. All this depends on the necessary institutional and technical capacities as well as upon mutual trust in order to work effectively and not exist on paper only. Important decisions at the highest political levels to this effect have been taken in the recent past in all four RECs. However, the move towards deeper integration is threatened and contradicted by the persistence of multiple memberships in the region. Many of the very practical impediments to economic integration have not even been tackled yet, chief among them the proliferation of new non-tariff barriers to trade. Choosing the “right” REC should not obscure where some of the more important constraints really are.

Discussions among stakeholders and policy makers in the region should now urgently lead to some clear decision making. The principle options have been spelled out above. Even if some countries choose to remain a member of more than one REC, they need to take a decision regarding their participation in only one CU. Moreover, it will be far easier to move on to deeper integration, including going beyond product market integration and to the creation of viable financial mechanisms to support the potential losers of an integration process.

In consequence, for the integration process to succeed, two more far-reaching aspects should be kept in mind, while focusing on deeper integration: First, the introduction of a development financing mechanism. And second, the free movement of capital and labour which are the next steps for the region in order to reap the full economic and social benefits of the integration processes.

The EU has gained valuable experience in how to raise and administer common funds that are spent to address the structural and regional weaknesses in all member states - notably in those at the periphery - in order to overcome the supply-side constraints and

infrastructural bottlenecks in the process of integration. As indicated in the discussion of the options, this experience should be brought to bear in the framework of the non-trade aspects of the EPAs.

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Annex 1: List of Interview Partners

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Chundu, Ben	Ministry of Finance and National Planning, Zambia
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Dharsey, Heather	Woolworths (Pty) Ltd, South Africa
Draper, Peter	South African Institute of International Affairs
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Glyne, Michelo	Export Board of Zambia
Hess, Simon	Imani Development, South Africa
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Kamote, Hussein S.	Confederation of Tanzania Industries
Khumalo, Nkululeko	SAIIA, South Africa
Kieck, Eric	South Africa Revenue Services
Kilinda, Christina	Confederation of Tanzanian Industries
Lennox, James	South African Chamber of Business
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Long, Derek	Metro Cash & Carry, Kenya
Mackie, Lisa	European Commission, DG Trade, Belgium
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Mans, Herman	Eden International, Namibia
Mero, M.J.	Ministry of Industry and Trade, Tanzania
Michelangelo Margherita	European Commission, Belgium
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Munalula, Themba	COMESA, Zambia
Mushega, Hon N. Amanyanya	EAC, Tanzania
Myburgh, Gert	Metcash Trading Limited
Myburgh, Gert	Metcorp, South Africa
Ngwenya, Sindiso N.	COMESA, Zambia
Nkhoma, Amos	South African International Business Linkages (Saibl)
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Pearson, Mark	COMESA, Zamiba
Reyneke, Nada	Nafcoc, JCCI, South Africa
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September, Angus	DTI, South Africa
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Shaun, Titus	Woolworths, South Africa

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Simuyemba, Shem	RATES, Zamiba
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Tembo, Dorothy	Ministry of Commerce, Trade and Industry, Zambia
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