

BRIEFING PAPER

CUTS Centre for International
Trade, Economics & Environment
CUTS-CITEE



IBSA 3/2005

SACU and India: Towards a PTA

Regional economic and trade cooperation, including bilateral and regional trade agreements (RTAs), is a central mechanism employed by an increasing number of developing countries to expand mutual trade and investment. Regional arrangements offer momentous possibilities to enlarge economic space, attract foreign direct investment (FDI) to the region on better terms, and pool economic, human, institutional, technological and infrastructural resources and networks of participating countries.

The Southern African Customs Union (SACU) and India have proclaimed an interest in concluding a preferential trade agreement (PTA) by 2006. Apart from offering mutual benefits, the PTA is expected to be an important link in the trilateral India-Brazil-South Africa (IBSA) initiative. Of interest is the rationale behind this proposed PTA, the negotiation modalities and interests of the two trading partners which are exploring mutual complementarities of trade, and the impacts such a trading arrangement would have on the plan of a trilateral free trade agreement (FTA) that would include the IBSA (and associated) countries.

According to Willem van der Spuy, Director, Bilateral Trade Programmes: Asia, Department of Trade and Industry (DTI), Pretoria, South Africa, the governments of the SACU – comprising South Africa, Botswana, Lesotho, Swaziland and Namibia – and India have proclaimed a mutual interest to conclude a PTA before the end of 2006. The mooted agreement is aimed at cementing and expanding the burgeoning trade relations between SACU (predominantly South Africa) and India. In the event of the signing of an India-Mercosur PTA and a Mercosur-SACU PTA in early and late 2004, respectively, the trade deal promises to inject further momentum into the IBSA process.

What is the rationale for the proposed SACU-India PTA? How will negotiation modalities be determined? What are likely to be the respective SACU and Indian negotiating interests? What are the potential challenges and constraints, and how might these impinge on the negotiation process? How will the outcome of the negotiations dovetail with the touted plan to create a trilateral FTA including the other IBSA partner, Brazil? These are some of the key questions addressed in this briefing paper.

Background to PTA Negotiations

The impetus for negotiating a bilateral PTA between SACU and India grew out of a meeting between India's Commerce and Industry Minister and his counterpart in South Africa's Trade and Industry Ministry at New Delhi, in January 2000. The two countries enjoy a strong political rapport, and have been bound by very close historical and cultural ties. In 2002, they agreed to initiate negotiations to conclude a PTA, designed to strengthen bilateral trade and investment (Ministry of Commerce and Industry, 'India's current engagement in RTAs', http://commerce.nic.in/india_rta.htm#b8).

An understanding was subsequently reached that such a trade deal would include South Africa's four SACU partners. A Framework Agreement was eventually worked out providing for

the implementation of limited tariff liberalisation in the initial stage with a view to broadening the scope and coverage of the agreement into a full-blown FTA later (Ministry of Commerce and Industry, 'India's current engagement in RTAs'). Although it was originally envisioned that the negotiations would terminate in 2005, they are now expected to wind up only by the end of 2006, according to Willem van der Spuy.

Rationale for Negotiations

Several factors explain the two trade partners' desire to conclude a PTA. From the SACU perspective, it can benefit from India's rapidly expanding economy and consumer market (Alves P, 'Understanding Indian trade policy – Implications for the Indo-SACU agreement,' SAIIA Trade Policy Report No.5, November 2005). In particular, South Africa is eager to exploit a trade deal with India to reduce protectionist barriers that have hampered its potential exports to the Indian market (Stern M and Stevens C, 'FTAs with India and Brazil: An initial analysis,' TIPS Working Paper No.10, 2000). Research conducted by the Indian Institute of Foreign Trade (IIFT), New Delhi, found that more than 50 percent of India's exports faced a tariff of less than 10 percent in South Africa, while only 33 percent were subjected to a tariff rate of over 20 percent. Conversely, 55

Tariff Comparisons between South Africa and India

Tariffs	Exports to	
	South Africa	India
Less than 10 percent	50 percent products	34 percent products
More than 20 percent	33 percent products	55 percent products
Weighted average	16.36 percent	22.89 percent

Source: IIFT, New Delhi

percent of imports from South Africa faced tariffs of over 20 percent in India, with merely 34 percent of imports from South Africa attracting a tariff rate of 10 percent and less.

Negotiating a PTA with India also forms part of South Africa's broader global economic strategy to intensify economic relations with other developing countries. This is a calculated move to reconfigure South Africa's position in the global economy by decreasing its reliance on developed country markets – especially the European Union (EU) – and forging trade relationships with new and growing markets in Africa, Asia and Latin America. The ultimate goal is to promote the progress of South Africa as a vibrant, export-oriented manufacturing economy.

Three pillars underpin South Africa's trade policy: multilateralism; regionalism; and bilateralism. Multilateral engagement is aimed at facilitating South Africa's re-integration into the global economy and pushing for a greater role for developing countries in moulding international economic governance. Regionally, South Africa's foreign economic policy has striven to consolidate RTAs as stepping-stones towards the incorporation of the Southern African region into the world economy. At a bilateral level, South Africa has sought to forge strategic collaboration with designated developing nations (principally India and Brazil but also China and Nigeria) in order to maximise trade and investment among them as part of South-South Cooperation (DTI, 'South Africa's global economic strategy: A policy framework and key elements', Pretoria, May 2001).

India's intention to forge a PTA with South Africa is an element of the country's policy to continue the reforms initiated in 1991 to liberalise the Indian economy (Narayan S, 'Trade policymaking in India,' paper presented at a workshop on trade policymaking in developing countries, London School of Economics, 25 May 2005). These liberalisation efforts subsequently found expression in the 'India Shining' *mantra* propagated by the National Democratic Alliance (NDA) Government, which exhorted Indians to embrace capitalism and encouraged modernity and entrepreneurship – partly with the intention to appeal to Indian patriotism (Dasgupta S, 'India dimming?' The Wall Street Journal, 17 May 2004).

India's trade policy, like South Africa's, is predicated on multilateral, regional and bilateral fronts (Narayan S). At a multilateral level, India has collaborated with like-minded developing nations to challenge the structural inequities of the multilateral trading regime and to push for a successful completion of the multilateral Doha Round trade negotiations. Bilateral and regional FTAs are pivotal to India's strategy to bolster its exports and increase its share of global trade, which currently stands at one percent (Press statement, Ministry of Commerce and Industry, New Delhi, 20 January 2005, <http://pib.nic.in/release/release.asp?relid=6674>).

Furthermore, FTAs have provided an avenue for Indian firms to transform themselves into global players and full-fledged transnational corporations (TNCs) (Mukherjee A, 'The Indo-Thai FTA is great news but who will it benefit?' Outlook India, 12 October 2004). In the context of SACU, these TNCs perceive South Africa as a springboard into other African markets.

Bilateral Trade Relations

Over the past decade there has been a considerable rise in trade between India and South Africa, the most economically advanced and dominant SACU partner – the average annual

growth in total trade exceeding 31 percent (Alves P). This can be ascribed preponderantly to the expansion of Indian gold imports from South Africa. In 2002, total bilateral trade amounted to US\$2.3bn, up from US\$271mn in 1994 (Alves P). During 1998-1999 to 2002-2003, India's imports from South Africa increased by more than 54 percent, while exports increased by more than 22 percent (Ministry of Commerce and Industry, 'India's current engagement in RTAs'; Roy J, 'Priorities for Indian trade policy,' Financial Express, May 05, 2005).

Even so, trade remains very low on both sides – just more than one percent of total trade. This is partly due to the fact that their external trade is still dominated by the Organisation of Economic Cooperation and Development (OECD) and East Asian states (Stern M and Stevens C). Moreover, a key problem is the persistence of obstacles for the promotion of trade and investment between the two countries, including tariff and non-tariff barriers (NTBs). The proposed PTA is expected to ease these hurdles.

SACU's imports from India include textiles and clothing (T&C), food products and live animals, beverages and tobacco, machinery and transport equipment, cotton products, pharmaceuticals, rice, vegetable products, vehicle parts, and spices. SACU exports to India encompass raw materials such as gold and silver, coal, iron, steel and non-ferrous metals, mineral fuels and lubricants, chemical wood pulp, sugar, vegetable products, as well as arms and war materials.

A detailed trade/tariff analysis carried out by the Trade and Industrial Policy Secretariat (TIPS), South Africa, revealed principal areas in which trade could be stimulated between SACU and India through liberalisation. It identified a list of under-traded products for which market access barriers were 'sufficiently high' in order to hamper imports from SACU and India respectively (see Tables 1 and 2). The findings of the TIPS analysis may be somewhat outdated (the study was published in 2000), as high tariff barriers to some or all the under-traded SACU and Indian exports may have fallen over time.

From the SACU viewpoint, it has also been contended that trade liberalisation could benefit SACU by providing access to affordable medicines, competitive prices for motor vehicles, and equipment for heavy industry. Moreover, it could create fresh export markets for iron and steel, chemicals, aluminium and furniture (Singh S, 'SA looks east in bid to reduce dependence on West,' Financial Mail, March 25, 2005). Considerable potential has also been recognised for increased trade in intra-industry trade in basic fabricated metals, precious stones and jewellery, and non-metallic minerals (Alves P).

Modalities

Preliminary negotiations between SACU and India were scheduled to commence in August 2005, but were postponed at the request of India following a change of government in that country. The first round of

Table 1. Under-traded Indian exports facing tariff barriers in SACU

Product Description
Fish, frozen exports fillets
Crustaceans, frozen
Edible nuts fresh, dried
Oil-cake, oilseed residue
Tobacco, not stripped
Cotton, not carded, combed
Tyres, pneumatic, new, bus
Cotton yarn, excl. thread
Cotton fabric, woven, unbleached
Curtains, other furnishings
Passenger transport vehicles
Source: Stern and Stevens (2000)

Table 2. Under-traded SACU exports facing tariff barriers in India	
Product Description	
Other ferrous waste, scrap	negotiations will now begin 'soon' and are planned to conclude by the end of 2005 or early 2006, according to Willem van der Spuy. This round of negotiations is expected to finalise broad negotiating modalities with a view to agreeing on product lines
Other inorganic bases, oxides	
Nitrogenous chemical fertilisers	
Fertilisers	
Silver	
Machines, appliances, special industrial	
Parts, data processing etc. machines	
Parts, telecommunication equipment	
Gold, non-monetary excl. ores	
<i>Source: Stern and Stevens (2000)</i>	

that will be covered under the PTA. The general PTA talks are poised to terminate before the end of 2006.

Like the India-Mercosur and the SACU-Mercosur negotiations, these discussions are expected to adopt a 'positive list' approach: only those sectors listed in the agreement will be liberalised. It is not clear at this stage what the total number of products covered by the PTA will be. Nonetheless, the India-Mercosur agreement contained more than 600 products in the agricultural, chemical, automobile and pharmaceutical sectors (AFP, 'India signs free trade deal with South American bloc,' March 19, 2005), while the SACU-Mercosur trade deal designated 2,000 products for tariff liberalisation.

Within SACU, the process of compiling product lists will take place at two levels: among the SACU member states and in the National Economic Development and Labour Council (Nedlac), a statutory tripartite body set up to promote social and economic dialogue among the government, business and labour (AFP, 'India signs free trade deal with South American bloc,' March 19, 2005). Some commentators have voiced a concern that formulating negotiating modalities in Nedlac could allow protectionist interests to hold the negotiations to ransom. (Draper P, 'The SACU-US free trade agreement: In search of a contract zone,' The Exporter, June 2004) Willem van der Spuy dispelled this anxiety on two grounds in an interview with the author. First, erstwhile experience had demonstrated that drawing up product lists for a PTA was relatively easier than doing it for a comprehensive FTA. And second, there had been no 'significant' resistance within Nedlac and SACU, to the planned SACU-India PTA.

Negotiating Interests

Previous FTA negotiations involving SACU and India provide general pointers to the possible offensive and defensive negotiating interests of both parties.

In the field of services, India has a clear offensive interest in the expansion of cross-border work opportunities and flexible movement for its technical personnel, especially software and Information Technology (IT) experts (Narayan S). But, as a trade analyst averred, considering that the South African IT sector is almost open to external competition 'SACU cannot offer anything that is not already available to Indian IT firms' (Alves P). Notwithstanding the difficulties SACU governments have had in rallying their services sectors, which explains their defensive postures, they have advocated liberalisation in specific sectors (Draper P). South Africa, in particular, has a dynamic and very competitive financial services industry that has begun to make inroads into the protected Indian market. It is

conceivable that South African negotiators will push for more liberalisation of laws governing foreign ownership in this sector.

Given that SACU and India have opposed the inclusion of the Singapore issues in the World Trade Organisation (WTO) – bar trade facilitation, which was agreed multilaterally as part of the July Package – they are unlikely to consider substantial liberalisation in these areas in a bilateral setting. Nonetheless, transparency in government procurement as well as investment might emerge as discussion items on account of their contentiousness. One of the concerns raised by South African firms in an IBSA perception survey was the 'discriminatory' awarding of Indian government contracts in favour of local Indian companies (government procurement in India constitutes about 20 percent of gross domestic product) (Alves P).

For their part, Indian investors might take issue with the South African government's black economic empowerment policy, which requires investors to sell equity stakes to black partners as a condition for public tender eligibility.

Regarding investment, SACU and India might exploit their discussions to accelerate the process of negotiating a bilateral investment treaty, which currently does not exist. This is central to promoting and protecting investments, and to dealing with problems such as double taxation. SACU is also likely to argue for a further relaxation of restrictions on FDI into India.

Another issue poised to come up for deliberation is rules of origin (RoO). This has been a major point of contention in both parties' FTA negotiations. It has featured in SACU FTA talks, most conspicuously ended in a deadlock with the US. And it has dominated India's negotiations with trade partners, notably Thailand and the Association of Southeast Asian Nations (ASEAN) (Sharma S and Sengupta N, 'Thai FTA hits rules of origin roadblock,' The Economic Times, October 7, 2005; Sen A, 'Deadlock on FTA with Thailand,' Financial Express, August 13, 2005; and 'New rules of origin for India-Asean FTA by mid-July,' Business Standard, June 22, 2005). Mainly, concerns have revolved around preventing third countries from taking advantage of FTAs negotiated by India with other countries. In the case of the Indo-Thai FTA, India produced a 'sensitive list' of items that would be exempted from tariff reduction under the trade deal.

India's offensive interests are likely to coalesce into textiles and, perhaps, certain categories of motor vehicles. The WTO has identified India, along with China, as a winner from the elimination of quotas in T&C trade in 2005. Naturally, the country will harness this strong competitive advantage to its benefit. SACU countries, losers from the globalisation of trade in T&C, might be inclined to adopt a defensive posture, especially in light of the aggressive competition from Chinese imports that has seriously threatened the viability of the domestic garment sector. However, South Africa has a competitive automotive industry and this remains an essential competitive advantage.

India's defensive interests are likely to centre on agriculture. Although agriculture does not play a central role in the South African economy (as it does in the other SACU economies), there is huge scope for growth of SACU exports of value-added food products to the Indian market (The Economist, 'Prowling tiger, slobbering dog,' February 17, 2005). NTBs to agricultural trade, particularly sanitary and phyto-sanitary issues, might also crop up in the discussions.

Issues about intellectual property rights (IPRs) are likely to form part of the bilateral bargaining. South African businesses are eager to safeguard their intellectual property in foreign

markets. The South African Chamber of Commerce (SACOB) has enunciated this position on numerous occasions, especially with regard to China. The South African government, therefore, might want to use an agreement with India to lock in IPR reforms in the SACU countries and improve the implementation of the domestic IPR regime. The Indian government has an interest in ensuring that IPR concerns do not unduly prevent the country's pharmaceutical firms from providing cheaper drugs to SACU nations, which are beset by public health emergencies including HIV/AIDS, tuberculosis and malaria (Narayan S).

This is underscored by the Indian government's decision to defer the introduction of a patent regime, although it did implement in 2005 – in line with a WTO directive – an amendment to the Patent Act of 1970 providing for the filing of product patent applications in the fields of chemicals, pharmaceuticals, agricultural chemicals and food products (Chakraborty D, 'India's participation in WTO negotiations: the changes in attitude and emphasis,' paper presented at a conference on the "WTO, FTAs and RTAs" organised by the Centre for WTO Studies, College of International Affairs, National Chengchi University, Taiwan, April 22, 2005).

Challenges

Several challenges and possible constraints ought to be tackled if the SACU-India PTA negotiations are to conclude successfully and the resultant trade agreement is to yield optimal economic gains. First, the 'perception gap' between SACU and Indian business sectors must be bridged. This means changing the mindsets of businesses about the importance of South-South trade by creating awareness not only of opportunities in the respective commercial environments, but also of competitive advantages and trade complementarities among exporters.

Second, greater coordination and synchronisation between the various PTAs forged by the IBSA countries must be encouraged. International research has shown that multi-level negotiations, if not carried out in an integrated and coherent fashion by developing countries, could jeopardise the economic development (Sanoussi B, 'The coherence of multi-level negotiations: challenges for developing countries,' UNU-Cris Working Paper No. 11, June 2004). Although the PTAs are distinct, there is a need to maximise synergies among them.

Third, it is necessary to accord attention to both the domestic (Nedlac) and SACU dynamics, which could impinge adversely on the negotiations. Striking a balance between domestic/regional pressures and external opportunities is a crucial imperative. Concerning SACU, it is vital to recognise that the member states negotiate as a collective entity. Even though it is an overwhelmingly dominant regional actor, South Africa cannot adopt positions and foist them upon its partners as it did

in the past. Combined with the other parallel FTA (and multilateral) negotiations underway, which have exerted a strain on SACU's stretched negotiating resources, the quest to engender consensus among SACU partners could delay the pace of negotiations.

Fourth, perceptions that the mooted SACU-India PTA is a political rather than an economic project ought to be allayed. Doubts have been expressed at the economic import of the mooted bilateral trade pact. For instance, it has been suggested that India's interest in FTAs is motivated less by a desire for market access than it is by political calculations (Sen J, 'Negotiating trade agreements with India: the reality below the water line,' SAIIA Trade Policy Briefing No.8, November 2004).

Fifth, engagement in bilateral or regional FTAs should not detract SACU-India PTA negotiations from the overriding goal of multilateral liberalisation. Understandably, the penchant for FTAs has been fuelled by disaffection with the pace of liberalisation in the WTO. Moreover, some countries find bilateral liberalisation politically appealing, as it has lesser adjustment costs (Stern M and Stevens C). Still, in the absence of multilateral liberalisation, countries will not be in a position to negotiate significant tariff reductions against the more shielded economic sectors. More importantly, studies have highlighted that in spite of the existence of commercial opportunities in the SACU and India markets, the economic impact of liberalisation will be diminished by the reality that the two parties' trade remains dependent on the OECD and East Asian states, and by the limited complementarities in their economies (Alves P).

The Way Ahead: A Trilateral FTA?

According to South Africa's DTI, there has been 'talk' of forging a trilateral FTA among the IBSA countries in order to intensify economic cooperation as mentioned by Willem van der Spuy. Although attaining such a result is not impossible, it raises a number of questions. For example, how would such an FTA be conceptualised? What would be the scope of its product and sectoral coverage? Would the negotiations follow a negative or a positive list approach? Would the FTA be a by-product of the three IBSA PTAs or would it be constructed as a separate arrangement? How would synchronisation and coherence be fostered between the trilateral FTA, the PTAs and multilateral trade agreements (MTAs)?

These issues require thorough research and analysis, which should also be extended to seeking to understand better how the under-traded sectors highlighted in studies on trade collaboration among the IBSA countries can undergird these trilateral negotiations.

OTHER BRIEFING PAPERS

1. India and Mercosur: Boosting Trade through Regionalism
2. Mercosur-SACU FTA: Strengthening Relations across the South Atlantic

© CUTS-CITEE 2005. This Briefing Paper is produced by CUTS-CITEE with the support of Swiss Agency for Development and Cooperation (SDC) under the project "South-South Economic Cooperation: Exploring The IBSA Initiative" to inform, educate and provoke debate on issues of regional economic cooperation. Readers are encouraged to quote or reproduce material from this paper for their own use, but as the copyright holder, CUTS-CITEE requests due acknowledgement and a copy of the publication.

This Briefing Paper is researched and written by Mills Soko for CUTS Centre for International Trade, Economics & Environment (CUTS-CITEE), D-217, Bhaskar Marg, Bani Park, Jaipur 302 016, India. Ph: 91.141.228 2821, Fx: 91.141.228 2485, E-mail: citee@cuts.org, Web Site: www.cuts-international.org, www.cuts-citee.org. Printed by Jaipur Printers Pvt. Ltd., M. I. Road, Jaipur 302 001, India.

