South African Trade with developing and developed Partners: Do the same principles apply?

Introduction

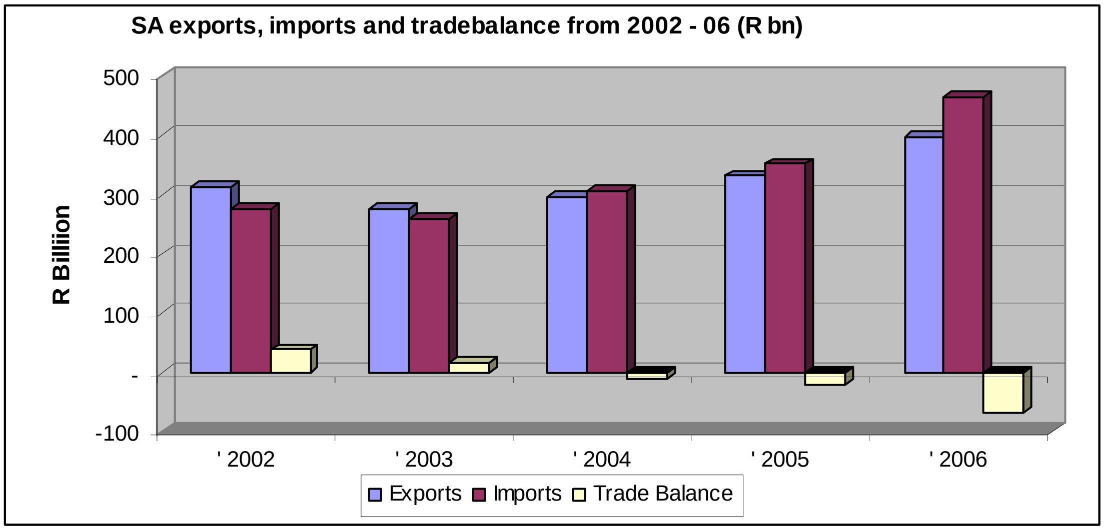
Post-apartheid South Africa embarked on a trade policy framework to make the economy competitive by engaging the international community. That framework took the economy through a gradual process of reforms that resulted in a shift – from being one of the most protected and distorted markets in the world to the one that reflects openness. The momentum was carried forward by the signing of the General Agreement on Tariffs and Trade (GATT) in 1994 and implementation of the free trade agreements (FTAs) with the European Union (EU) and the Southern African Development Community (SADC) in 2000.

Furthermore, South Africa has given consideration to FTAs with China, India, Brazil and Unites States as it tries to broaden trade relations across the globe. The most observable feature of these commitments is the reduction of import protection. This is based on the principle that resources will flow from uncompetitive sectors to sectors with a comparative advantage as competition increases, known as allocative efficiency. The same argument can be used to refer to the trade partners that dominate relations with South Africa: that trade should be biased in favour of the competitive ones at the expense of uncompetitive ones.

Trade statistics can clearly show which partners dominate trade relations; however, the details of their competitiveness are not contained in those statistics. In this article we look at South African trade with both developed and developing countries in the last five years. The developing partners are divided into two groups, middle-income developing countries and Africa, to take out the influence of major partners such China and India. Developed countries include two major trade blocs, the EU, the North American Free Trade Agreement (Nafta) and Japan. Middle-income developing countries consist of China, India and Brazil, while the rest of developing countries are made up of Africa, broken down in to SADC and rest of Africa.

South African trade flows

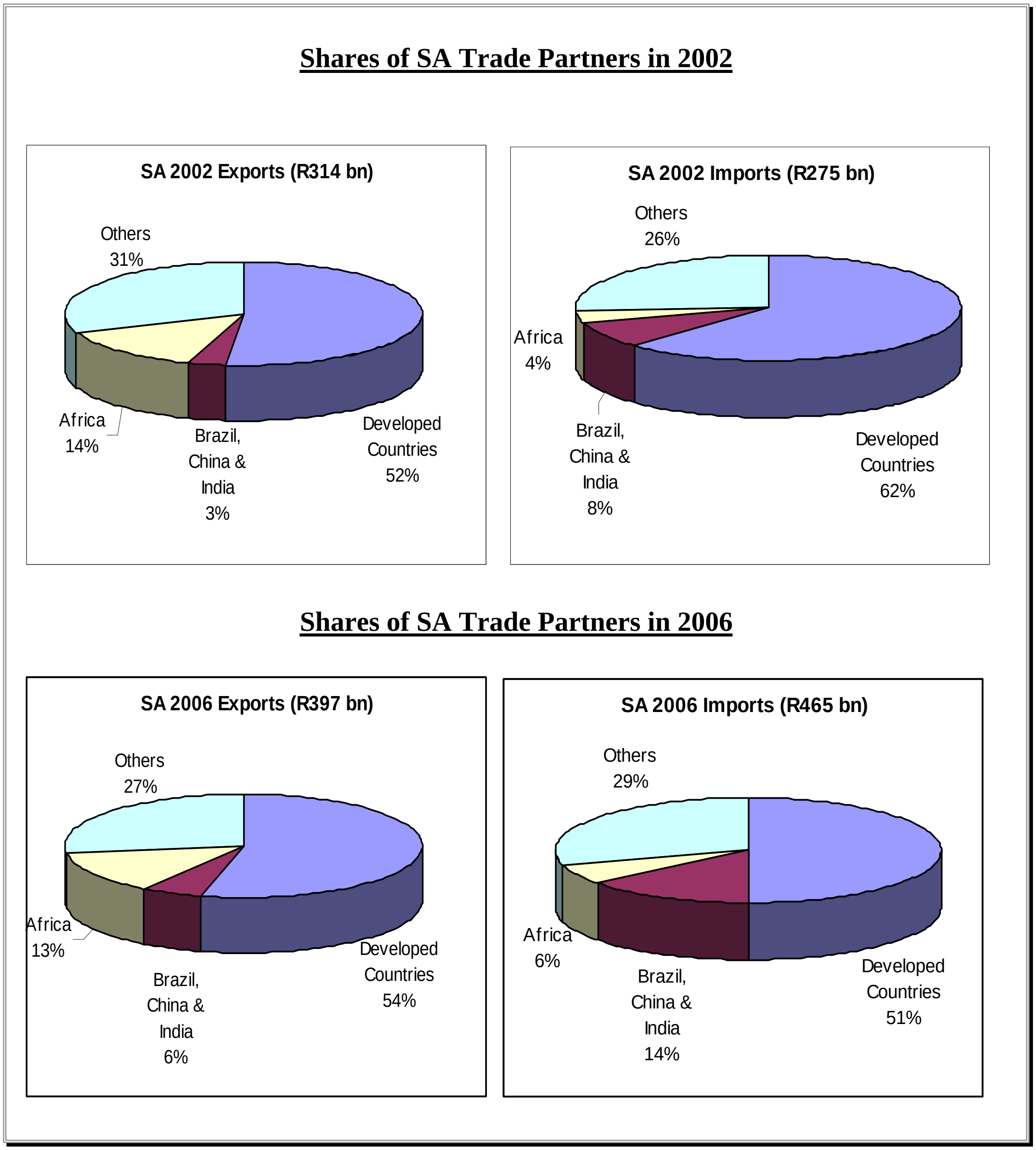
South Africa's total trade, both imports and exports has surged in past five years from about *R295 billion to R430-billion. This is equivalent to growth of about 40% per annum*. The interesting pattern is depicted by the growth of imports (R275-billion), which was below the value of exports (R314-billion) in 2002. By end of 2006, the import value was about 15% more that exports at R465-billion. Figure 1 shows that the trade deficit started in 2004 and has been steadily growing since then. This development has sparked a number of concerns regarding the nature of consumption, the capacity to produce manufactured goods and the very same competitiveness of our exports in international markets, which was supposed to be enhanced by the trade reforms. However, the fast-growing imports also reflect the expansion of the South African economy, which has grown at an average of over 5% since 2004. The resulting economic growth led to higher demand, including higher demand for imported goods.



Source: SADC Trade Database, 2007

Figure 1: South African trade balance from 2002 to 2006

More than half of South Africa's trade in 2002 was with developed countries, i.e. the EU, Nafta and Japan, and it was still so in 2006 as Figure 2 shows. These countries accounted for more than 50% of South African exports and imports, respectively, in 2006. However, developed countries' import shares were reduced by more than 10% from 2002 to 2006. Africa contributed only 14% of as export destination, while imports from the continent improved slightly from 4% to 6% from 2002 to 2006. This is considered low, taking into accounts efforts of an FTA with SADC as well as the continent-wide, New Partnership for Africa's Development (Nepad) and others. The most impressive improvements are from the combined shares of Brazil, India and China which doubled in exports and also increased from 8% to 14% in imports, picking up shares dropped by developed countries. This development is hardly surprising considering that India and China are the fastest growing economies in world, and have population of more than a billion each.



Source: SADC Trade Database and author's calculations

Figure 2: Changing Shares of South Africa's Trade Partners between 2002 and 2006

The two figures show that South Africa's trade still relies on developed world for markets but is slowly shifting towards developing countries for sources of supply. The domination of developed world as a supplier is being challenged by middle-income developing countries. The concerning factor is that Africa is being left behind; this calls for considerable action to review African programmes.

Driving factors

The recent visits to South Africa and discussions with senior political leaders from Germany and India indicate that there are possibilities for future cooperation with these countries, even in areas outside trade. This provides indications that it is not only trade and economic forces that are at play in determining the trade developments. Some of the factors include the following:

- **Political and colonial history**: South African trade and economy has for many decades been linked to the European partners, mainly the United Kingdom, the Netherlands and Germany. Such bonds are important in trade and not easy to break.
- **Exchange rates**: The period under review has mainly been under the strong South African rand, and thus imports are relatively boosted compared to exports, hence a growing trade deficit.
- **Nature of the commodities**: A breakdown of the types of commodities being traded shows that South Africa exports more finished consumer goods and advanced manufactured goods to Africa, and imports raw materials from the continent. That order is almost reversed when it comes to trade with developed partners, where machinery, electronic equipments and highly specialised and high-tech products are imported from, and raw- to semi-manufactured goods are exported, to the developed world.
- **Infrastructure development**: The preparations for the 2010 Soccer World Cup, construction of the Gautrain Rail Link, housing projects and other infrastructural developments in the country imply that some of the most sophisticated equipment be brought into the country, and usually it will be the developed country that is capable of consistently supplying such materials. Furthermore, such factors contribute to the trade deficit.
- **Income in the importing partner**: The higher income per capita of the partner is a reflection of potential demand and affordability, and thus exports tend to gravitate towards those countries with high income per capita.

Considerations to enhance trade with developing partners

Trade agreements are signed with the aim of strengthening the relations between countries, and thus require that either new trade be created or previous trade be diverted from other partners. Again, this may be an indication of resources being shifted from a less efficient partner to a competitive one. In the case of Africa, there was not much trade that was created; hence the share of trade with Africa has actually declined. That usually reflects existence of other constraints in supply capacity, which consequently affects its competitiveness globally. Furthermore in SADC and Africa in general, these constraints are pointed at poor infrastructure, lack of diversification beyond mining and agricultural products, lack of institutional measures to enforce and co-ordinate and lack human capacity. It is therefore imperative that initiatives such as Nepad succeed and that continental institutions like the African Union (AU) are effective as they carry hopes for intra-African relations.

South Africa's consideration for preferential trade agreements with the middle-income developing countries of India, China and Brazil may require additional strategies that are different from those with developed countries to strengthen them. To a larger extent, the economic structures of these partners are similar to those of South Africa, and so are their areas of comparative advantage. For example, the strengths of India and China are in labour-intensive goods, which is an area South Africa should focus on to reduce the high unemployment rate. Brazil is strong in the agricultural and automotive sectors – again that is where South Africa needs to consolidate its competencies.

Nevertheless, there are also lessons that can be exchanged with the new partners and these may not necessarily have to be in merchandise goods. For example, Brazil is the world leader in biofuels production; China's other strengths are in the electronic equipment; while the Indian information technology and pharmaceuticals sectors can also provide important complements to South African industries.

On the other hand South African service sectors on the continent such telecommunications, financial, retail and even processed minerals can also be expanded to the new partners. These may even include transfer of knowledge and production technologies rather than exchange of services with currency. Both these and others can provide alternative policy options and priority areas of cooperation while engaging in trade partnerships with partners of more or less similar economic structures.