trade & industry MONITOR

A Joint Trade & Industrial Policy Strategies & Development Policy Research Unit Newsletter • December 2002 • VOLUME 24

Special Edition

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Doha and Developing Countries: Proceedings of the 2002 TIPS Forum

Trade and Industrial Policy Strategies (TIPS) held its Annual Forum – from 9 to 11 September 2002. The topic this year was: "Global Integration, Sustainable Development and the Southern African Economy."

Trade and Industrial Policy Strategies (TIPS) held its Annual Forum – from 9 to 11 September 2002. The topic this year was: "Global Integration, Sustainable Development and the Southern African Economy." Over 350 economists, policy makers and academics from South Africa and abroad attended the Forum, which focused on a number of timely issues, especially given that trade and finance figured prominently at the World Summit on Sustainable Development, concluded the previous week in Johannesburg.

Some of the issues covered by the Forum include: agriculture, standards and the environment; industrial tariffs and market access; financial architecture and the exchange rate; liberalisation and poverty; trade and the environment; agricultural trade; services and GATS negotiations; and regional issues. Of particular note, and the focus of this article, were contributions from Kym Anderson (University of Adelaide, Australia), John Whalley (University of Western Ontario, Canada), Bernard Hoekman (World Bank) and Bijit Bora (World Trade Organisation). For more information about the TIPS Annual Forum and other events, please check the TIPS website: http://www.tips.org.za.

John Whalley, the keynote speaker gave an overview of some key issues relevant to the developing countries in the context of the WTO. He began with an overview of developments at Doha and subsequently looked at some of the critical economic issues facing developing countries.

What Happened at Doha?

The Doha Round was supposed to have been concluded by 2005. It appeared to indicate the way forward despite considerable scepticism about its eventual success because of the tensions between the United States and the European Union in areas such as steel and agricultural subsidies, and continued bilateral negotiations between some countries.

The Doha Round[1] had now been launched and was supposed to have been concluded by 2005. It appeared to indicate the way forward despite considerable scepticism about its eventual success because of the tensions between the United States and the European Union in areas such as steel and agricultural subsidies, and continued bilateral negotiations between some countries.

The Doha agenda already consisted of a long list of negotiating positions ranging from agriculture to services, market access, intellectual property, transparency in government procurement, environmental issues, e-commerce, small economies, trade and debt financing, trade and technological transfers, technical co-operation, special arrangements for least developed states and special and differentiated treatment.

Many observers were optimistic that Doha was shaping up as a seemingly significant successor to the Uruguay Round[2] , but it was clear that many developed countries had built-in agendas in areas such as agriculture and services while aiming to broaden multilateral trade negotiations to cover issues such as competition policy, the environment and intellectual property.

A significant new development was the effort to tier developing countries with special arrangements for the least developed and smaller states, and an emphasis that trade should go hand in hand with development and poverty alleviation.

The key issues for developing countries arising from the negotiations so far included:

- Security of access vs access alone, with dispute resolution mechanisms that gave stronger retaliatory powers
- Textiles- the phasing out of the Multi Fibre Agreement (MFA) had been

largely cosmetic so far

- The bargaining power granted to developing countries
- The sensible handling of the broadening of the scope of the negotiations
- The push and pull effects of regionalism through a myriad of free trade agreements, the enlarged EU and the planned African Union
- The possible negative effects of continued unilateralism in defiance of multilateral liberalisation
- The increased use of anti-dumping measures by developing countries such as Brazil and India
- Did it make sense to pursue rule-based trade objectives alone or could more leverage be obtained elsewhere?
- Could there be a common negotiating strategy with so many diverse interests?

The Economics Gains from Trade

One of the overarching questions at the Forum was: What do changes in the global trade architecture specifically those pertaining to multilateral liberalisation mean for developing countries? Discussions revealed that if one reviews economic models used to evaluate the likely impact of a new round on the global economy, the size of gains is debatable. There is growing recognition that the size of these gains is small and generally not more than 1 percent of world GDP. Moreover, gains for developing countries were shown to be even more modest.

One of the overarching questions at the Forum was: What do changes in the global trade architecture specifically those pertaining to multilateral liberalisation mean for developing countries?

A corollary question was: Where would most of the gains come from – domestic reform or improved access to foreign markets? It was observed that empirically, if countries were fairly open, most gains from trade would come from improved access to foreign markets. However, if domestic tariffs are high, access to foreign markets is unlikely to generate these gains. An important point that was highlighted was that in order to maximize the gains specifically for poor regions such as Sub-Saharan Africa from a new potential round, improved market access and domestic reform in these regions have to be equally significant.

Another critical point that was highlighted was that static gains are also considered institutional gains, i.e. gains from participating in a rules-based system where there is a framework and consensus regarding multilateral reductions in tariffs, with transparency preventing the likelihood of back-sliding. Moreover, small countries that rely heavily on export markets are better off than large countries, and this is particularly true for developing countries.

Some Challenges

According to Whalley trade was driven by comparative rather than absolute advantage. He argued, based on basic economic theory, that free trade was generally the best policy in small, open, price-taking economies. The real policy debate, however, started when it came to the terms of trade and weighing up what countries hoped to achieve through trade. Did they want to protect infant industries? What would be the unintended consequences? What interventions might be needed? What market structure was desired? What profit shifting would take place and what effect would trade have on unemployment?

John Whalley argued that trade was driven by comparative rather than absolute advantage. He argued, based on basic economic theory, that free trade was generally the best policy in small, open, price-taking economies.

Trade policies, in developing counties specifically, often conflicted with policies aimed at increasing employment, and also raised many questions about the future direction of industrial policy. A key challenge is how do we introduce efficiency -

Kym Anderson, Professor of Economics, University of Adelaide, Australia pointed out that a large portion of the gains from global liberalisation will come from a reduction of agricultural distortions.

enhancing policies, such as further trade reform, in the context of high levels of unemployment and incidence in poverty.

Implications of Changing Distortions in Agriculture for Developing Economies

The importance of the current global agricultural regime to developed countries is well known. As Kym Anderson, Professor of Economics, University of Adelaide, Australia pointed out, a large portion of the gains from global liberalisation will come from a reduction of agricultural distortions. The problem of agricultural protection in developed countries has been well documented. The experience of agricultural reform is, however, mixed for different developing countries, and depends on the following:

- how much supply-side capacity a country can take advantage of in terms of market openings abroad;
- the presence of tariff preferences, specifically for countries that enjoy relatively privileged access to restricted markets; and
- whether the country is a net food importer or exporter.

Anderson said that developing countries were not very enthusiastic about agricultural trade liberalisation because they believed that they did not have the supply capacity to take advantage of markets opening up abroad and could even lose out through tariff preference erosion, which could see them paying more for food imports and receiving less food aid. They were also concerned that it would require agricultural reform at home that might undermine their food security.

The biggest gains from removing all remaining trade barriers would come from: OECD agriculture (almost half) even though it was only 4 percent of the global economy, indicating the huge distortions created by these agricultural markets while 7 percent would come from textiles and clothing, depending on the assumption that the Uruguay Round was fully implemented by 2005, and a quarter would come from other manufactures (not counting trade barriers for services). Moreover, three-quarters would come from the rich-country farm policies, with the rest coming from developing countries.

Developing countries could get the most from agricultural reform under Doha by freeing up their own domestic product and factor markets so that farmers were better able to take advantage of new opportunities abroad. Secondly, by ensuring that their own reforms gave them more bargaining power while also reciprocally opening other markets.

However, it preyed on the minds of many developing countries that trade reform could be harmful to them through the erosion of preferences enjoyed under the ACP or Everything But Arms programmes. This was because preference schemes typically excluded some developing countries and could therefore harm them. One example was the EU banana regime, now being reformed. Those benefiting from the schemes could switch from seeking reform abroad to defending them. Developing countries were better off with MFN tariff cuts abroad plus extra direct aid to compensate for any preference erosion.

Anderson did not necessarily agree with the argument that food-importing developing countries could, in fact, suffer the double blow of a higher food import bill and maybe less food aid from further agricultural reform.

Agriculture Reform and Food Security

Anderson did not necessarily agree with the argument that food-importing developing countries could, in fact, suffer the double blow of a higher food import bill and maybe less food aid from further agricultural reform. This was because many developing countries were very close to being self-sufficient in food, and higher international food prices might encourage them to be more productive and become net food exporters.

Other developing countries could be net exporters if it were not for their own policy distortions that harmed farmers, in which case higher farm prices would attract resources back to the sector with strong comparative advantage. Within food-importing developing countries, farm households were the poorest, making up four-fifths of all households. An increase in their product prices would therefore reduce poverty and improve income distribution.

Anderson rejected the commonly held belief that food security would diminish because of the reform-induced hike in food prices. Food security meant having access to a minimum supply of basic food for survival. This provided peace of mind, efficiently functioning food markets and strengthened the purchasing power of the poor. Most of all, it alleviated poverty as it was not about expanding food production per se, but rather about the capacity to consume and hence to generate income.

In addition, if Doha did indeed deliver on agricultural reform in developed countries, agricultural production in Africa would rise, benefiting farm households and landless labourers, who were the region's poorest people. Rural infrastructure would also improve and only the poorest urban households would need targeted compensation for higher food prices. Humanitarian food aid was almost completely independent of agricultural policy while reforms in agricultural policies in developed countries would result in huge savings for those governments, which could be channeled into food aid.

Two implications of changing global prices that were identified are as follows: The reduction of agricultural subsidies and the likely increase in agricultural prices may have negative effects for food-importing counties in the short run. In addition, the increase in international food prices as a result of a reduction in world distortions in agriculture may induce agricultural-led export growth.

Implications of Changing Global Prices in Agriculture

Two implications that were identified are as follows: first, reduction of agricultural subsidies and the likely increase in agricultural prices may have negative effects for food-importing counties in the short run, although there will likely be some benefits in the long run, as well as positive effects for food-exporting countries. In addition, the increase in international food prices as a result of a reduction in world distortions in agriculture may induce agricultural-led export growth.

When it came to the tricky question of what would happen to developing countries whose comparative advantage was now in labour-intensive manufactures, such as clothing and textiles, Anderson said that: industrialisation reduced their direct interest in agricultural reform, but heightened their interest in lower barriers for their products. Such lower barriers would boost their manufactured exports as well as their agricultural imports, thereby helping nearby food exporting developing countries. However, lower agricultural barriers abroad would mean fewer developing countries would compete in the textiles and clothing markets and would go into agriculture instead. This would give textiles and clothing exporters an indirect interest in agricultural reform.

Part of the Doha game therefore would be that demands for greater access to OECD agricultural and textiles and clothing markets would require developing countries to reciprocate with their own reforms. Trade liberalisation by both sides would boost agricultural output and exports, but more so should developing countries undertake reforms themselves.

An important factor to bear in mind is that changing or reduced global distortions may induce some structural changes in respective countries. Developing countries could inhibit their industrial development by expanding agricultural production at the expense of manufactures, but much would depend on simultaneous liberalisation in textiles and clothing.

It was pointed out during Forum deliberations that reasons for low export performance in the Southern African region relate to either the demand or the domestic side.

Market Access as a Constraint to Export Growth

It was also pointed out during Forum deliberations that reasons for low export performance in the Southern African region relate to either the demand or the domestic side. In the former case, major problems include: increasing volatility in export markets; declining terms of trade in commodities; increasing market access problems that relate specifically to protection in developed country markets in products that matter; and increasing threats of non-tariff barriers to trade. Regarding the supply side or the domestic level, there is low investment and productivity, high anti-export bias, and exchange rate mismanagement.

Key questions in this regard were: To what extent has the current market access regime in the world impacted on the export potential of developing countries? Has tariff escalation in developed countries realistically biased the exports of developing countries, or more specifically, their ability to diversify exports? In other words, how significantly would exports from Africa, for example, be influenced by unrestricted market access?

An important conclusion that was drawn is that better market access will increase exports. However, more dramatic growth in exports will depend less on market access and more on the domestic incentive system, coupled with improvements in human capital, infrastructure, and overall supply-side measures. Market access matters, but less so in countries and regions where supply side and trade facilitation problems are overwhelming.

Another important factor identified was the security of access: a large part of market access is not only establishing low or no duties, but ensuring that access is secure and predictable. This implies that, with more serious market access problems, there is the potential threat of non-tariff barriers, which are sometimes used as a smokescreen for protection.

Bijit Bora, counsellor in the Development and Economic Research Division of World Trade Organisation, focused on Industrial Tariff Liberalisation and the Doha Development Agenda.

The Market Access Landscape

Specific attention has been given to the question of industrial tariffs and market access. Bijit Bora counsellor in the Development and Economic Research Division of World Trade Organisation, focused on Industrial Tariff Liberalisation and the Doha Development Agenda. He identified a range of important issues in the Doha negotiations on industrial tariffs:

- The issue of coverage of tariffs bindings between developed and developing countries.
- Applied MFN tariffs, or the actual rates charged at borders
- Preferential tariffs, which could be reciprocal or non-reciprocal
- Tariffs aimed at providing market access for least developed countries.

For developed countries, the key issue was how to tackle the residual protection arising from low overall levels of protection, mainly involving issues of peaks and escalation. For developing countries, on the other hand, the key issues included the high levels of tariffs and the limited coverage of bindings for some members, although there were also problems of peaks and escalation. For the least developed countries, the issues involved the degree of effective non-reciprocal market access granted by developed countries, the very high levels of protection they faced in developing country markets, and the role that high levels of protection were playing as industrial policy instruments in their own economies.

Tariff Bindings are important as they are the level at which tariff levels are locked in.

Tariff Bindings

It is important to bear in mind that the WTO operates on what member countries

bind their tariffs at, as opposed to their applied tariffs. Bindings are important as they are the level at which tariff levels are locked in.

Developed countries had bound all or most of their non-agricultural tariffs. In general their bindings are low but certain products, such as textiles and clothing, leather and footwear or fish, and fish products, have higher tariffs than others, with a higher tariff dispersion, tariff escalation and tariff peaks. These peaks and high tariffs particularly affected developing and least developed countries as they protected products, which were of particular export interest to developing countries.

Most developing countries, on the other hand, had either bound their tariffs at relatively high levels or they had bound only a limited number of tariff lines. Developing countries applied rates were, however, often far below their bound levels. The basic message that came out of Bora's presentation was that poor WTO members had not bound many of their lines.

Looking at bindings from different perspectives, the Quad countries (the US, the European Union, Japan and Canada) had bound tariffs on about 30 to 40 percent of their imports while developing countries had generally bound less than five percent of their imports at zero. Most Latin American countries had bound almost all of their industrial tariff lines while most African and Asian countries had bound only a limited number of tariff lines.

Tariff Peaks in the World Economy: Where do they Prevail?

If one looked at the global economy, four categories of products had higher tariff averages. These include both developed and developing countries.

Products where protection is high:
- textiles and clothing
- leather, rubber, footwear and travel goods
- transport equipment
- fish and fish products .

Preferences

It is important to bear in mind that when we look at the global tariff landscape, MFN tariffs could be misleading in the sense that a myriad of overlapping preferential agreements exist. Least developed countries benefit from preferences granted by developed countries, which also granted preferences to certain developing countries and to other developed countries as part of regional trade agreements.

The Economic Effects of a Next Round

Joseph Francois, Professor of Economics at the University of Erasmus, Rotterdam, the Netherlands,said: A major question to be asked about the Uruguay Round was whether negotiators had delivered on their promises, or whether – as seemed more likely – they had cheated and that liberalisation had not taken place as expected. This was particularly evident in agriculture in the case of developed countries, while developing countries still applied the highest duties against each other.

Joseph Francois, Professor of Economics at the University of Erasmus, Rotterdam, the Netherlands,said: A major question to be asked about the Uruguay Round was whether negotiators had delivered on their promises, or whether – as seemed more likely – they had cheated and that liberalisation had not taken place as expected.

Agriculture had not been liberalised to the extent envisaged. Tariffication still provided a critical mass of protection and there were now tariffs inside and outside of quota rates apart from the quotas themselves, resulting in a very complex system. Moreover, quotas on textiles and clothing had not been removed.

A major issue that had emerged was that of binding overhangs. This involved a comparison between average applied rates and average bound rates, with the gap between the two illustrating how much room there was to cut the tariff bindings without changing the applied rates.

The gains realised depended on the extent to which a country liberalised trade

The possible options to dealing with tariffs under the Doha Round ranged from the flexible, country specific formula approach such as that adopted by Switzerland, or the request-and-offer approach favoured by the US.

How should we Negotiate Tariff Reductions?

A large share of tariffs remained completely unbound, which made it difficult to judge how countries would negotiate their reduction. Would they get credits if they offered to bind them for the first time? How could there be liberalisation if there were no bindings?

The possible options to dealing with tariffs under the Doha Round ranged from the flexible, country specific formula approach such as that adopted by Switzerland, or the request-and-offer approach favoured by the US even though it involved a lot more individual negotiations and took longer to finalise. The choice made in Geneva would determine how long it took to negotiate the new round, whether tariff peaks and escalations would be dealt with and whether the products that mattered to developing countries would be dealt with.

Francois recommended that the WTO agreed on a cut in average tariffs and then used the structure of the Swiss formula to determine what individual cuts were necessary given the tariff schedule. This would bring down average tariffs and deal with peaks and escalations.

Bernard Hoekman, of the World Bank, highlighted the challenges facing countries approaching the next round of WTO negotiations.

Developing Countries and the Political Economy of the Trading System

Bernard Hoekman, of the World Bank, said the challenges facing countries approaching the next round of WTO negotiations were:

- improving market access abroad
- disciplining trade distorting policies such as subsidies in agriculture
- improving domestic efficiencies through incentives and trade policy reform, especially for the services sector, investment and institutions
- improving supply-side capacity to benefit from increased market access.

The Economic Benefits of the WTO

Economists often asked why these challenges had to be tackled through international negotiations when improving domestic policies was something that should be done unilaterally. Equally, improved supply-side capacity required domestic investment and regulatory reforms.

The reasons were many-fold:

- reciprocity to get something in an export market, a country had to give something to induce interest groups in countries that it wanted to export to, to engage in a political process.

- the terms of trade argument - large countries that could affect the terms of trade had an interest in applying trade barriers, so they had to be given something to induce them to lower those barriers.

- a whole set of externalities in the form of policies imposed by countries that could have negative external effects on other countries.

- transaction costs and redundant policies If it could be agreed in principle to eliminate these collectively, this could result in trade gains.

- there was scope for linkage across different issues for example, linkages could be made between trade negotiations and foreign aid and these linkages could be made explicit in future.

Furthermore, Hoekman said, one of the main reasons why the WTO process and related negotiations had become so much more complex and difficult was what he called the "Uruguay Hangover".

The Political Economy of Trade Negotiations

Hoekman further argued that the political economy dimension of these negotiations was a key issue because trade policy was a tool for distributing income domestically. Some sectors that had protection gained from this, consumers tended to loose, the gains were more concentrated than the losses were, and therefore this

was a political economy problem in terms of trying to move the policy regime towards one which was less distorted in terms of resource allocation.

Changing the status quo through domestic reform called for domestic support for the reforms, which affected the way WTO negotiations were approached by individual countries. Some groups in those countries benefited from the status quo, which, for example, made it difficult for the minister in a developing country to support liberalisation in agricultural trade when farmers could point out that US or EU farmers were heavily subsidised and were dumping products. It was important to identify all these issues clearly and distribute all the information available on who would be the winners and losers.

Hoekman said that one of the main reasons why the WTO process and related negotiations had become so much more complex and difficult was what he called the "Uruguay Hangover". Until the Uruguay Round, many developing countries had not been active participants in world trade negotiations. With the creation of the WTO, all existing GATT members became subject to many agreements that in the past had been voluntary. That imposed a heavy implementation burden on them, which was not widely recognised.

A number of agreements in the Uruguay Round had required investment in order to implement them rather than just a change in regulations or laws.

Implementation

Implementation problems in the Uruguay Round had largely been due to the fact that many constituents in developing countries did not know about, or understand, what had been negotiated, how that could be implemented and how it could help achieve development goals.

A number of agreements in the Uruguay Round had required investment in order to implement them rather than just a change in regulations or laws. Examples included the TRIPS agreement on intellectual property which required investment in enforcement capacity, training people and customs valuation.

One could argue about whether the rules applied made economic sense. Most did, but when they were negotiated not enough attention had been given to the fact that they would be costly to implement. One of the lessons from the Uruguay Round, therefore, was that countries had to think about what it would take to implement the rules being negotiated, and whether these were a priority at their stage of development. These issues had not, however, been the focus of debates in the Doha context yet.

Ensuring a change in the outcome in the Doha negotiations, that promoted Development, would require a much more participatory process at the national level.

Ensuring Development in Doha

Ensuring a change in the outcome in the Doha negotiations, that promoted Development, would require a much more participatory process at the national level. This meant that stakeholders had to be identified and mobilised. The priorities had to be identified and it had to be clearly understood what the gains and losses would be. This called for analysis and research.

Policy makers had to ensure that governments did not conduct the negotiations unilaterally and took place as part of a larger development agenda and debate. Without this, it would be difficult to sell the process domestically as being in the interests of the economy, and also much more difficult to sell to donors in terms of getting the additional resources needed to implement what could be beneficial agreements.

Reciprocity posed the challenge of identifying what could be put on the table in terms of quid pro quos that made sense domestically. What developing countries did not want or need was requests from trading partners when it was not clear whether acceding to these would benefit them.

One of the major problems were developing country capacity to negotiate effectively. Many of these countries were not represented at the WTO

headquarters in Geneva, which made it very difficult for them to engage in the negotiations. South Africa was one of the best represented countries in Africa. Moreover, the WTO was dominated by major players such as the US and EU while small developing countries were not seen as being interesting potential export markets, giving them little leverage. This indicated the need to concentrate on building coalitions and partnerships in a bid to try to change the status quo. These could not only push a certain agenda, as was increasingly being done by African countries but also create relationships with groups that cared about outcomes.

One group that could be harnessed more effectively was the development NGOs on an issue-by-issue basis. Oxfam[3] , for example, had been trying to promote the idea that trade was good as part of a poverty reduction strategy if it was done in the right way. It was a powerful voice in the OECD and could be harnessed to push for a development agenda in trade negotiations and in attempts to reduce trade distorting policies.

All of the above would help push for what Hoekman called a “grand new bargain”, which would have several elements. Most notable would be technical support for a formula-based approach rather than the current request/offer system.

Hoekman said that the request/offer process had, for example, involved a lobby in the US requesting better market access from a country for a series of specific industries or sectors, resulting in a fragmented pattern of protection. This might not necessarily benefit the countries concerned and there was a good case to be made for a relatively uniform pattern by introducing a formula approach. In this way, the whole structure could change in one fell swoop rather than having individual request/offer negotiations.

An additional advantage would be that small countries which did not have strong negotiating skills would get more negotiating leverage, while this would cater for the desire of developing countries to get credits for past unilateral trade liberalisation.

More active links were needed with the development community to link the outcome of negotiations to assistance to deal with the implementation of rules. A key condition would be that there was ownership of agreements while donors should have a better understanding of what had been negotiated and why this was regarded as important.

The need is to involve as many constituents as possible in negotiations to ensure their support, which would be invaluable in implementing agreements.

Conclusion: Behind the Border Issues

More complex had been the “behind the border” moves by industrialised countries to gain concessions for services that had traditionally not been part of trade negotiations. Developed countries established services in other countries by having a local presence, which raised issues such as domestic investment and regulatory policies. Many called for caution in expanding the ambit of the WTO into the services sector, but this was already catered for in GATS and, from a development point of view, it had become increasingly important to increase the efficiency of services.

Services helped determine the cost structure of firms and helped define their competitiveness in the world market. The services issue highlighted the fact that WTO was increasingly being asked to take more issues on board – others included investment and competition policy – and developing countries had to have a clear sense of what was important to them and where they could get the "biggest bang for the buck" in terms of market access and domestic reform.

This again highlighted the need to involve as many of their constituents as possible in negotiations to ensure their support, which would be invaluable in implementing agreements.

References

For the references to this summary of the proceedings, please see the list of papers on the following pages.

End Notes

[1] Doha Round: The November 2001 declaration of the Fourth Ministerial Conference in Doha, Qatar, provides the mandate for negotiations on a range of subjects, and other work including issues concerning the implementation of the present agreements. The negotiations take place in the Trade Negotiations Committee and its subsidiaries. Other work under the work programme takes place in other WTO councils and committees. This is an unofficial explanation of what the declaration mandates.

[2] Uruguay Round: It took seven and a half years, almost twice the original schedule. By the end, 125 countries were taking part. It covered almost all trade, from toothbrushes to pleasure boats, from banking to telecommunications, from the genes of wild rice to AIDS treatments. It was quite simply the largest trade negotiation ever, and most probably the largest negotiation of any kind in history.

[3] Oxfam International is an international group of independent non-governmental organisations dedicated to fighting poverty and related injustice around the world. The Oxfams work together internationally to achieve greater impact by their collective efforts. As well as a global network of partnerships and working experience in more than 100 countries, Oxfam International also has member organisations with head offices in four continents.

Glossary

GATS - General Agreement in Services

TIPS - Trade and Industrial Policy Strategies

MFA - Multi Fibre Agreement

EU - European Union

GDP - Gross Domestic Product

OECD - Organisation for Economic Co-operation and Development

ACP - African, Caribbean and Pacific Group of States

MFN Tariff - Most Favoured Nation Tariff

WTO - World Trade Organisation

GATT - The General Agreement on Tariffs and Trade

TRIPS - Agreement on Trade-Related Aspects of Intellectual Property Rights

NGO - Non Governmental Organisation

Tips Forum 2002: Papers – Global Integration, Sustainable Development & the Southern African Economy

AUTHORS	PAPERS
Achterberg, Rosanna - Independent Consultant Hartzenberg, Trudi – Development Policy Research Unit	Trade in Distribution Services in South Africa
Akinboade, O.A. - University of South Africa Niedermeier, E.W. – Competition Commission	The Impact of Electricity Trade on the Environment in South Africa
Asfaha , Samuel & Huda, SN – University of the Western Cape	Exchange Rate Misalignment And International Trade Competitiveness: A Cointegration Analysis For South Africa
Birdi, Alvin – Sussex University and UCT Dunne, Paul – Middlesex University and UCT	Labour Demand and Trade in South Africa: A Dynamic Panel Analysis
Black , Anthony – University of Cape Town Mitchell , Shannon – Virginia Commonwealth University	Policy In The South African Motor Industry: Goals, Incentives, And Outcomes
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Bora, Bijit – Development and Economic Research Division - World Trade Organisation Bacchetta , Marc	Industrial Tariff Liberalization and the Doha Development Agenda
Cattaneo, Niki – Rhodes University	Intra versus Inter-industry Specialisation, Labour Market Labour Market Adjustment and Poverty: Implications for Regional Integration in Southern Africa
Chabane, Neo – University of the Witwatersrand	An Evaluation of the Influences on Price and Production in the Maize Market following Liberalisation
Chasomeris, Mihalis – University of Natal	South Africa's Seaborne Commerce: Trade Flows, Transport Costs and the Maritime Transport Policy Environment
Chauvin , Sophie & Gaulier, Guillaume –Centre d'Etudes Prospectives et d'Informations Internationales (CEPII)	Prospects for Increasing Trade among SADC Countries
Cleary, Susan & Thomas, Stephen – Health Economics Unit	Mapping Health Services Trade in South Africa
De Beer, Jessie – Vista University	The New Financial Architecture: South African Supervisors, Banks and the New Basel Accord
De Vries, Linda – University of the Western Cape	The Challenge of Transformation within the Regulatory Environment of the Gambling Industry- The Role within the Southern African Environment
Eberhard, Anton – University of Cape Town	Energy Services, WTO GATS Negotiations and Energy market Regulation and Liberalisation in South Africa
Edwards, Lawrence – University of Cape Town	A Firm Level Analysis of Trade, Technology and Employment in South Africa
Flatters, Frank – Queens University, Canada	SADC Rules of Origin: Undermining Regional Free Trade
Francois, Joseph – Tinbergen Institute and CEPR Martin, Will – World Bank	Formulas for Success? Some Options for Market Access Negotiations
Hartzenberg, Trudi – DPRU	Competition in SADC
Hess, Simon – Rhodes University	Economic Geography and the Implications of a Free Trade Area within SADC
Hodge, James – University of Cape Town	Extending Telecoms Ownership in South Africa: Policy, Performance and Future Options
Hoekman, Bernard – World Bank and CEPR	Developing Countries and the Political Economy of the Trading System

Tips Forum 2002: Papers – Global Integration, Sustainable Development & the Southern African Economy

Author	Paper
Kusi, Newman Kwadwo – KwaZulu-Natal Provincial Treasury	Trade Liberalization And South Africa's Export Performance
Laubscher, Pieter – Stellenbosch University	The South African Business Cycle Over the 1990s: What Can We Learn?
Loots, Elsabé – Rand Afrikaans University	Globalisation and Economic Growth in South Africa: Do We Benefit From Trade and Financial Liberalisation?
Mafusire, Albert – University of Zimbabwe	SADC Trade: Challenges and Opportunities to the Regional Countries
Mather, Charles – School of Geography, Archaeology and Environmental Studies - University of the Witwatersrand	Regulating South Africa's Citrus Export Commodity
Matlanyane, Adelaide – University of Pretoria	The Need for Policy Coherence for Financial Liberalisation in Southern Africa: Lessons from a Small Developing Economy
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The New Financial Architecture: South African Supervisors, Banks and the New Basil Accord

The TIPS Forum dealt with both trade and financial integration. In the following article, Jesse de Beer looks at the new global financial architecture and what it means for South Africa.

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Introduction

The new international financial architecture has its roots in the financial crises that shook emerging market economies in the l990sMexico in 1994-1995 and East Asia in 1997-1998. The problems in Russia in 1998, Brazil in 1998-999, and more recently Turkey and Argentina have only served to underscore the importance of strengthening the international financial architecture.

These crises generated a broad consensus that fundamental reforms were required in the international financial system. Existing institutions and arrangements were widely seen as inadequate for dealing with very large and extremely volatile capital flows, in which an important part of the volatility was caused by large imperfections in the financial markets themselves. Consequently, there is a need for processes and practices to bolster this system.

The New International Financial Architecture

The international community has launched a series of initiatives referred to collectively as the new international financial architecture to strengthen the operation of the global financial system. Work on strengthening the international financial architecture is being undertaken on several fronts simultaneously. The major building blocks encompass transparency and accountability, international standards and codes, the strengthening of financial systems, capital account issues, sustainable exchange rate regimes, the detection and monitoring of external vulnerability, private sector involvement in forestalling and resolving crises, and IMF facilities.

The New Basel Accord

The proposed new Basel Capital Accord is one of the key initiatives for strengthening bank soundness, and thus financial sector stability.

The implementation of the proposed new Basel Accord[1] on capital adequacy is another important initiative of the new financial architecture. The proposed new Basel Capital Accord is one of the key initiatives for strengthening bank soundness, and thus financial sector stability. This is both a wide-ranging and ambitious reform that seeks to better align regulatory capital with economic risk. It represents a real advance on the 1988 Capital Accord, and the proposals mark a decisive step away from a "one size fits all" supervisory approach to capital. Rather than imposing a single method for calculating capital requirements, institutions will be able to select from a range of approaches for capturing, measuring, and controlling credit and operational risks. More sophisticated control structures will be rewarded by lower capital charges. If the Basel proposals are implemented as planned, they will have important effects both on individual banks and on financial markets as a whole.

However, implementation of the proposed Accord creates additional challenges, especially in an emerging market context. It is thus important to identify the challenges posed by the implementation of the proposed capital adequacy framework to South African banks and bank supervisors, and to see how prepared they are for these challenges.

Challenges Posed by the Accord

Several observers warn that the preconditions for implementing important components of the Basel Accord are absent in most emerging-market economies.

However, the new Accord does represent new ground for South African supervisors in several aspects, such as with the evaluation of banks' internal credit risk rating systems.

One important aspect, where current South African bank practices lag behind the Basel requirements, is disclosure regarding credit risk modelling and specifically rating systems.

This seems not to be the case in the South African situation. South African bank supervisors are efficient, as evident in the findings of the FSAP. The factors that seemingly cause minimum capital requirements to be an inefficient tool in enhancing bank system soundness in many emerging market countries do not seem to be present in the South African banking sector. These factors are the lack of a sufficiently deep and liquid capital market that makes the raising of "low quality" capital possible, and the lack of policy measures such as loan-loss provision regulations that complement minimum capital requirements. Indeed, the regulatory framework in South Africa was recently amended so as to be in line with international best practice standards, and to address any limitations pointed out by the FSAP.

New Ground for South African Supervisors

However, the new Accord does represent new ground for South African supervisors in several aspects, such as with the evaluation of banks' internal credit risk rating systems. South African bank supervisors have already started with specific measures to address challenges posed by the implementation of the new Accord. South African banks have also started with preparations for the implementation of the Accord. All the surveyed banks indicated that they want to adopt the advanced IRB approach. The current sophisticated approach to credit risk management and the use of sophisticated models in this regard, constitute a useful platform for this to take place from. However, current practice does not conform to all the requirements set by the Basel Committee[2], and substantial logistical challenges remain.

In general, the credit risk management practices of South African banks seem to be sophisticated and in line with international best practice. The large South African bankshave recognised the challenges posed by the changes in the credit risk environment. The have been working for some time on identifying, modifying, developing and implementing sophisticated credit risk models and the organisational context for a portfolio-orientated credit risk management. The survey also outlined the current state of play regarding credit risk rating among South African banks, and provided some international comparisons. Generally speaking, South African banks' credit risk rating practices appear to be in line with those of their international peers.

A Key Challenge

A key challenge faced worldwide by virtually all developers and users of internal credit risk rating systems is the widespread lack of good long-run data on the performance of banks' loans. This includes prudential supervisors looking to utilise banks' internal ratings for regulatory capital and other purposes. The lack of such data can impact on the ability of an institution to develop effective rating tools. It can also impede efforts to verify the accuracy and robustness of institutions' rating systems, to assign reliable quantitative loss estimates to risk grades, and to make reliable comparisons of ratings from different institutions: all important tasks, not only from the perspective of the banks themselves, but also from the point of view of their prudential supervisors (particularly in the context of proposals to utilise banks' internal ratings for regulatory capital purposes).

One important aspect, where current South African bank practices lag behind the Basel requirements, is disclosure regarding credit risk modelling and specifically rating systems. This would be one of the key areas that need to be addressed before the IRB approach can be implemented. Although many factors might inhibit the successful implementation of the proposed new Basel Accord in an emerging market context, this is not the case in South Africa. The inherent soundness of the South African financial system, the efficiency of bank supervisors and South African banks' sophisticated approaches to credit risk management constitute a useful platform to implement a more sophisticated approach to bank supervision and the determination of regulatory capital requirements, such as the proposed new Basel Accord.

The current risk rating systems of South African banks do not conform to all the requirements set out for the adoption of the proposed new Basel Accord.

Implementation Challenges

However, significant implementation challenges remain, in terms of all three pillars of the Accord. In terms of Pillar one[3], the current risk rating systems of South African banks do not conform to all the requirements set out for the adoption of the proposed new Basel Accord. Data limitations pose the most significant challenge. In terms of Pillar two[4], several aspects regarding the implementation of the IRB approach constitute new ground for South African supervisors. Although they have already started with specific preparations for the implementation of the new Accord, several issues raised by the new Accord have not been addressed by South African supervisors yet. Another problem is the fairly limited nature of discussions between banks and supervisors at the time of the study. In order to address these challenges, supervisors will need to start (and continue) discussions with banks, with a view to establishing a regulatory framework, which is sensible and effective in the South African environment.

In order to address the Pillar one challenges, South African banks will need to continue with data gathering efforts, as well as gap analysis. The latter is intended to identify deviations between their current risk rating systems and the requirements set by the Basel Committee for the adoption of the IRB approach. South African banks will also need to develop strategies to deal with the deviations between their current rating disclosures and the requirements as described under Pillar three[5] of the proposed new Basel Accord.

Apart from implementation challenges in individual countries, there is concern over the impact of the proposed new Basel Accord on global financial system stability.

Concern over the Impact of the Basel Accord

Apart from implementation challenges in individual countries, there is concern over the impact of the proposed new Basel Accord on global financial system stability. This includes questions about its impact on capital flows to emerging market countries and the potential pro-cyclical impact of the new Accord. These concerns highlight the need for greater co-ordination within the international community on the reform agenda in an increasingly integrated international financial system.

The complexity of the new Accord, as well as the flexibility allowed to national supervisors, poses the risk of regulatory forbearance. Regulatory capital levels that are not sufficient relevant to risks in a banking system, is another risk in this regard. This all serves to underline the importance of effective and accountable bank supervision. This is not only applicable to the regulatory institutions, and the human resources capacities of supervisory agencies, but it also encompasses aspects such as appropriate accounting standards and reporting systems, and a sufficient legal framework, which is able to enforce supervisory actions when a bank's performance is deemed faulty. These aspects underpin the efficiency of both supervisory review (Pillar two) and bank capital ratios (Pillar one). Efficient markets that send appropriate signals and corporate governance structures that respond to them, are another important aspect in this regard.

Conclusion

It must be kept in mind that the Basel Committee is largely comprised of representatives from the G-10 countries[6]. By developing the original Accord, and now its replacement, this group has performed a great service in promoting a more stable international financial system. However, as with any attempt to develop international consensus on a complex matter, it is inevitable that the new Accord will involve a degree of compromise, and a need to trade-off differing national objectives. Although there are important benefits from conforming to an internationally-agreed standard, the new Accord will not be perfectly suited for South African conditions. At this stage, it seems as if South African supervisors intend to conform with the internationally agreed framework wherever possible. However, it might be advisable to exercise national discretion where this is clearly in South Africa's national interest.

This article is based on a more detailed paper presented at the TIPS Forum 2002.

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For the references to this article, please see the list of papers on the previous pages.

End Notes

1 The new Basel Accord intends to improve the safety and soundness of world financial systems by offering revamped "best practices" guidelines for risk management in international banks. The new Accord has three major components: an increased emphasis on banks' own internal capabilities in determining minimum capital requirements; a process for supervisory review of how banks are assessing their capital adequacy; and greater market discipline through enhanced disclosure by banks of their risk profiles and capital adequacy. The Basel Committee expects the final version of the new Accord to be published at the end of 2001 and to be implemented in 2004.

[2] The Basel Committee, established by the central-bank Governors of the Group of Ten countries at the end of 1974, meets regularly four times a year. It formulates broad supervisory standards and guidelines and recommends statements of best practice

[3] The First Pillar sets out minimum capital requirements. The new framework maintains both the current definition of capital and the minimum requirement of 8% of capital risk-weighted assets.

[4] The Second Pillar: Supervisory Review Process. This requires supervisors to ensure each bank has sound internal processes in place to assess the adequacy of capital based on a thorough evaluation of its risks.

[5] The Third Pillar of the new framework aims to bolster market discipline through enhanced disclosure by banks.

[6] Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Sweden, Switzerland, United Kingdom and United States

Glossary

FSAP – Financial Sector Assessment Programme

IRB – Internal Ratings-Based Approach

IMF – International Monetary Fund

The Institute of Social and Economic Research

The Institute of Social and Economic Research was founded in 1954 by the Rhodes University Council to pool the human and other resources of the social science departments at the university. The ISER was to provide planning and co-ordination for social research in the Eastern Cape and elsewhere in the Republic, and to train research workers of all races. A generous grant from the Carnegie Corporation contributed to the establishment of the new Institute. The ISER has an active publications programme. Its Annual Report (available on request) sets out the organization, achievements and publications of the Institute and its staff and reflects the diversity of activities carried out during a particular year.

Publications from the Institute of Social and Economic Research

ISER Monograph No.1

Migrant Labour and Colonial Rule in Basutoland, 1890-1930 by Judith M. Kimble (1999). 320pp. Price R150,00 (plus postage and packing). ISER Monograph Number One.

This publication brings a significant contribution to southern African historiography and to our understanding of the political economy of the region. The book examines the earlier phase of the incorporation of Basutoland/Lesotho into the broader South African economy and offers sharp insight into the dynamics of labour migration, the penetration of capitalism into the territory, its impact on indigenous production and the operation of the colonial state at this critical juncture.

Occasional Paper No.35

From Reserve to Region. Apartheid and Social Change in the Keiskammahoek District of (former) Ciskei: 1950-1990 edited by Chris de Wet and Michael Whisson (1997). 343pp. Price R68,40 (plus postage and packing). ISER Occasional Paper Number 35.

This book represents an in-depth re-study of the pioneering Keiskammahoek Rural Survey which was conducted between 1947-51 by several Rhodes University departments. The survey investigated the socio-economic structure, land tenure and natural history of the then little-known black communities around Keiskammahoek and four well-acclaimed volumes on the study were published in 1952.. The research on *From Reserve to Region* began in the late 1970s and continued into the 1980s. During this period the area was fully integrated into the Ciskei bantustan. The book draws on original research reports and theses and chronicles and analyses the transformation wrought by apartheid at every level of society. It offers a unique case study of a black rural area over time.

ISER Research Reports Series

Experiencing Space and Place in Grahamstown's Informal Settlements by Jan K. Coetzee (1999). No.1. 50pp. Price R20,00 (plus postage and packing)

West Bank Land Restitution Claim: Social History Report by Landiswa Maqasho and Leslie Bank with Busisiwe Mrawu (1999). No.2. 30pp. Price R18,00 (plus postage and packing)

Youth Development in Grahamstown: A Social Map compiled by Charlotte van Hees (2000) No.3. 44pp. Price R18,00 (plus postage and packing)

"It Takes a Whole Village to Raise a Child": Youth Development in Grahamstown by Charlotte van Hees (2000). No. 4. 130pp. Price R20,00 (plus postage and packing).

Street Trading in Grahamstown by Zanele Silo, Andile Tobi, Mphikeleli Mnguni and Valerie Moller (editor) (2001). No. 5. 34pp. Price R18,00 (plus postage and packing).

Living in Grahamstown East/Rini: A Social Indicators Report by Valerie Moller (editor), with contributions by Cecil W. Manona, Charlotte van Hees, Edmund Pillay and Andile Tobi (2001). No. 6. 88pp. Price R20,00 (plus postage and packing).

East Bank Land Restitution Claim: A Social History Report by Landiswa Maqasho and Leslie Bank (2001). No. 7. 36pp. Price R20,00 (plus postage and packing).

Monitoring Poverty and Inequality in Buffalo City by Robin Richards and Ellen Kamman (2001). No. 8. 33pp. Price R20,00 (plus postage and packing).

Growing Up in Grahamstown East/Rini: A Sample Survey of Youth 15-24 Years by Valerie Moller in collaboration with Charlotte van Hees and Andile Tobi (2001). No. 9. 136pp. Price R20,00 (plus postage and packing).

A Publications Catalogue containing information about available publications and their prices can be obtained from: The Publications Officer, Institute of Social and Economic Research, Rhodes University, Grahamstown 6140, South Africa.

The Automotive Industry in South Africa – Overview and Prospects

Donald Onyango reviews developments in the motor vehicle and components sector based on proceedings of a special Panel on the Automotive Industry in South Africa at the recently held 6th Annual TIPS Forum, together with recently written papers that make some critical footnotes to what otherwise would seem to be the current star performer in South Africa's manufacturing sector.

Overview

The South African automotive industry presently accounts for just over 5.4 per cent of the country's GDP. The origin of this sector can be traced to the early 1920s, and for the most part has developed into a competitive sector with monopolistic behaviour, behind a wall of high tariffs and non-tariff barriers. The local content programme, introduced in the early 1960s, aimed to rationalise both the number of assembly plants and models, so as to boost vehicle sales. However, by the advent of Phase VI of this effort, in 1989, it was clear that this had not happened. As South Africa moved to liberalise its economy at the beginning of the 1990s, the expansion of automotive exports was increasingly seen as the solution to the twin problems of rising trade deficits and attaining efficient scale of production.

The Motor Industry Development Programme (MIDP) unveiled in 1995, was characterised by inter alia, the reduction of tariffs on light vehicles and components, with the tariffs being phased down faster than required by WTO commitments. Not only were local content requirements abolished, but the duty free importation of components to the value of up to 27 per cent of wholesale vehicle price were permissible. In addition, the MIDP allowed for duty credit rebates to be earned on the export of vehicles and components, to be used in the duty-free importation of vehicles and components.

In the seven years since the MIDP was introduced, there have been far-reaching changes in the automotive sector. For instance, there has been a surge in the importation of motor vehicles, from 7 per cent to 27 per cent, largely due to the use of duty-free credits. Black and Mitchell (2002) however, noted that the many new firms established to export components did not supply domestic assemblers and it seemed that new models would have to rely more heavily on imported components. In the process, a market had developed for export credits. Component firms could sell credits for cash or exchange them on a quid pro quo basis to get favourable international contracts, or be introduced to international clients.

Similarly, there has been some rationalisation of the sector, with the large volume of output now arising from fewer model platforms, together with cost-cutting measures being implemented by domestic firms. Between 1995 and 2001, the total domestic production of vehicles has risen from 242 000 units in 1995 to 320 000 units at the end of 2001, and in addition, exports have risen more than tenfold, from 9 000 to 115 000. The share of exports in total sectoral production has further grown from just 4 per cent to 36 per cent, and significant investments by multinational corporations in the sector have been undertaken, or are in the pipeline. During 2001, for example, South Africa exported R11 billion worth of automobiles with an engine capacity between 1500cc and 3000cc while importing R4 billion worth of these vehicles.

However, despite the rosy picture painted of the “success” sector, there are some pertinent issues that must be considered, specifically in the context of its viability as the incentives under the MIDP are gradually reduced. Black and Mitchell (2002) state that the MIDP is not a costless scheme, and that the cost is ultimately being borne by the South African taxpayer. Without the export credits, government would earn tariff revenues. Government was now considering the phasing out of the scheme by cutting the exports earned per unit, which could herald a move back to protectionism and higher prices for imported vehicles. The other alternative would be to cut import tariffs. On automotive components, the question has to be asked whether export credits force firms to explore potential markets abroad for the first time, resulting in exports that could be economic even without the export credit. Or do they stimulate firms to export goods at an economic loss? Generally, however, policy has moved from being heavily protective of the sector, to one of liberalisation coupled with export support.

Black and Mitchell (2002) further observe that the costs of protection, which directly impact on the consumer, are further amplified by the low-volume, high cost structure of South Africa's automotive industry. The welfare implications arising from the import-export complementation scheme are also less clear, owing to the extent to which exports are economic, or become economic over time. Moreover, other factors to consider include whether costs are lowered over time, through the attainment of scale economies, the extent of learning and agglomeration effects, and also the export expansion of assembled products, which generate increased demand for sub-components that can be produced by domestic suppliers.

Effective Protection

Examining in more detail the economics of the MIDP, Flatters (2002) also points out that the import rebate credit certificate (IRCC) and productive asset allowance programme are both very complex in nature, and are further encumbered by the high costs of compliance, the level of discretion allowed to its administrators, and the burdensome documentation indeed, it has been pointed out that discrepancies in the latter have led to some rebates being overstated, with the possibility of potentially punitive duties being slapped on manufacturers.[1]

Flatters (2002) goes on to note that, with regard to production aimed at the domestic market, it is evident that the increase in effective protection arising from duty reductions on and the abolition of local content requirements on components most probably outweighs any reduction in protection as a result of decreased import duties on fully built-up units (FBUs).

Flatters (2002) goes on to note that, with regard to production aimed at the domestic market, it is evident that the increase in effective protection arising from duty reductions on and the abolition of local content requirements on components most probably outweighs any reduction in protection as a result of decreased import duties on fully built-up units (FBUs).

On the subject of removing the anti-export bias, Flatters (2002) agrees that the MIDP has succeeded in achieving the elimination of a potentially costly policy distortion afflicting the development of the motor industry. However, he sees the export incentives as going beyond just the removal of this bias, to include not only the duty-free importation of FBUs, but also the absence of restriction on the use of imported components to produce exports.

According to Flatters (2002), the effective protection on vehicle exports ranges between 30 and 40 per cent, and on component exports 26 to 30 per cent, with the productive asset allowance arrangement adding a further 20 per cent subsidy of the cost of qualifying new investments aimed at export production. Taking into consideration the structure of current import duties on vehicles and components, together with the Duty Free Allowance (applicable to vehicles sold in the local market), and depending on the import content of such production, the effective rate of protection for this sector thus ranges between 62 and 101 per cent.

Black and Mitchell (2002) identify constraints to the competitiveness of the South African automotive industry as being further exacerbated by inbound and outbound logistics that add major costs, the weak currency and low labour and management costs notwithstanding. In addition, while firms have developed expertise and capacity in low volume and flexible production, this counts for little in the international market, which instead requires cost minimisation and the achievement of optimal performance from world scale plants.

Flatters (2002) argues that the question at hand is not whether or not South Africa should have automotive industry, but rather the justification for the large subsidies that the MIDP provides via its complex protection-based incentive regime estimated to be in the region of R11 billion per annum. Moreover, the export subsidies violates South Africa's WTO and SADC Trade Protocol commitments, and amounted to a waste of economic resources, not to mention the costs imposed on consumers and the harm to overall economic development.

Generally, it is felt that there is need for more detail cost -benefit analyses of the whole issue of the future of the MIDP.

Industry's View

The sentiment from industry takes an opposing view to the above sentiments to the future of the MIDP, opining that although government had foregone considerable import duty revenue through the schemes, it had encouraged exports of vehicles and components worth billions of Rand a year and has ensured the survival of the industry.[2]

Admittedly, the sector remained "small fry" by international standards, but it had also created jobs but it needs continued support. The automotive industry further denies suggestions that the export credit scheme protection means that the taxpayer foots the bill in order to sustain the industry, since the MIDP is funded by tariff reductions and not direct subsidies from the fiscus.[3] It would be better for the MIDP to be replaced by some kind of investment incentive that was "just enough, but not too much" to keep the industry going.

Generally, it is felt that there is need for more detail cost-benefit analyses of the whole issue of the future of the MIDP. There is no doubt, however, that the future of the sector remains bleak in the absence of any form of continued support, but the crux of the matter is the nature and form of this support, taking into consideration matter such as the effect of import parity pricing of steel, the further rationalisation of models and assembly plants, the opportunity costs of training personnel for the industry, and the role of dynamic learning in improving competitiveness.

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End Notes

[1] Business day, 5 September 2002

[2] Ian Plummer, member of the executive of the National Association of Automotive Component and Allied Manufacturers (NAACAM).

[3] Roger Pitot, representative of the National Association of Automobile Manufacturers of South Africa (NAAMSA).

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The Trade & Industry Monitor is a joint publication of the Trade & Industrial Policy Strategies (TIPS) and the Development Policy Research Unit (DPRU).

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Designed and Edited: Bernadette Ontong

Focus on Facts

Increasing South African Exports to Finland: Wherein Lies the Potential

As the table below depicts, trade between South Africa and Finland increased quite dramatically throughout the 1990s, though much of the activity was dominated by Finland as demonstrated by the increasingly negative balance of SA trade with Finland. In light of these events it becomes ever more apparent that it would be in South Africa's interest to try and reverse this trend. As such, it is necessary to investigate, at a commodity level, where South Africa's export opportunities lie vis à vis Finland.

Table 1: Imports, Exports and Total Trade Between South Africa and Finland: R million, Current Prices

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	ave92-00
1. South African Imports from Finland : Rm current pr)	158	210	629	608	666	915	1,612	1,695	2,568	2,622	
2. Growth	7	33.20%	199.00%	-3.40%	9.60%	37.30%	76.20%	5.20%	51.50%	2.10%	36.20%
3. South African Imports Total: Rm current pr)	52,569	58,987	71,059	100,241	115,984	129,834	147,454	149,642	190,317	219,916	
4. Growth	0	12.20%	20.50%	41.10%	15.70%	11.90%	13.60%	1.50%	27.20%	15.50%	17.10%
5. Finlands share of South African imports	0.30%	0.40%	0.90%	0.60%	0.60%	0.70%	1.10%	1.10%	1.30%	1.20%	
6. South African Export to Finland: Rm current pr)	69	46	72	75	66	122	87	89	144	198	
7. Growth	5	-33.70%	58.00%	4.60%	-11.80%	83.70%	-28.90%	2.70%	61.40%	37.90%	12.70%
8. South African Exports Total: Rm current pr)	69,253	80,608	59,552	92,861	124,736	137,339	153,374	174,597	226,084	261,863	
9. Growth	0	16.40%	-26.10%	55.90%	34.30%	10.10%	11.70%	13.80%	29.50%	15.80%	17.20%
10. Finland's share of South African exports	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	0.10%	
11. South African Trade Balance with Finland: Rm current pr)	-89	-165	-557	-532	-600	-793	-1,525	-1,606	-2,424	-2,424	
12. South African Trade with Finland: Rm current pr)	227	256	701	683	733	1,037	1,699	1,784	2,712	2,821	
13. Growth	6	12.90%	173.90%	-2.50%	7.30%	41.50%	63.90%	5.00%	52.00%	4.00%	32.90%
14. South African Total Trade: Rm current pr)	121,822	139,595	130,611	193,102	240,720	267,173	300,828	324,239	416,401	481,779	
15. Growth	0	14.60%	-6.40%	47.80%	24.70%	11.00%	12.60%	7.80%	28.40%	15.60%	17.10%
16. Finland's share of South African total trade	0.20%	0.20%	0.50%	0.40%	0.30%	0.40%	0.60%	0.60%	0.70%	0.60%	

Source: Customs & Excise

Reviewing two exports scenarios in the table below, at a disaggregated 22 commodity level, it is possible to begin to distinguish which are the areas of opportunity for growing South Africa's exports to Finland.

Table 2 reveals the most important commodity imports for Finland that, although exported by South Africa to the rest of the world, are not currently exported to Finland. The table simultaneously shows the export scenario of these commodities in the case of South Africa.

It becomes immediately apparent that there may be potential for South Africa to export Hs26: Ores, slag and ash to Finland considering that this commodity cluster reports growth both in terms of Finnish imports thereof, as well as South African exports thereof[2]. Another commodity cluster worth investigating is HS44: Wood and articles of wood, wood charcoal. Finnish imports thereof grew at a healthy average rate of 7 percent over 1996-2000, whilst South African exports thereof also grew, but slightly faster at a an average rate of 12 percent. A similar scenario is evident in the cases of HS76: Aluminium and articles thereof, HS30: Pharmaceutical products and HS29: Organic chemicals. Finnish imports of these clusters grew at an average of 3 percent per annum over the period under consideration, whilst healthy growth rates of South African exports of these commodities were also in evidence. The analysis so far suggests the need for further investigation to determine within these broad commodity clusters which specific commodities hold potential for increasing South African exports thereof to Finland.

Preliminary analysis shows that most of the potential for growth within the HS44: Wood and articles of wood, wood charcoal cluster lies with the HS440399: Logs, non-coniferous nes commodity grouping, which revealed a growth rate of 5 percent in Finnish imports terms and 22 percent in terms of average South African exports thereof over the 1996-2000 period. A similar analysis of HS30: Pharmaceutical products reveals that the potential to increase South African exports thereof to Finland is dominated by HS300490: Medicaments nes, in dosage. More diversified opportunities exist within the HS29: Organic chemicals commodity grouping. Here three commodity groupings show potential: HS290250: Styrene, HS290919: Acyclic ethers nes: derivatives of acyclic ethers and HS290531: Ethylene glycol: ethandiol. Potential to grow exports of another commodity cluster, namely HS76: Aluminium and articles thereof, lies primarily with the HS760612: Plate, sheet or strip, aluminium alloy, rect or sq, exceeding 0.2mmm thick.

Table 2: Important Finland Imports and South African Exports thereof[1]

		Finland's Imports from the World					South Africa's Exports to the World		
HS Code	Product label	Value 2000 in US$ thousand	As a percentage of the value of total RoW imports	Cumulative Percentage	Annual growth in value between 1996-2000, %	Market share in world imports %	Value 2000 in US$ thousand	Annual growth in value between 1996-2000, %	Market share in world exports %
26	Ores, slag and ash	852,938	9%		2	2.6	1,088,114	5	4.1
99	Commodities not elsewhere specified	776,214	8%	18%	11	0.4	3,314,027	-35	1.9
30	Pharmaceutical products	673,643	7%	25%	3	0.7	98,713	13	0.1
29	Organic chemicals	639,883	7%	32%	3	0.4	377,635	8	0.3
44	Wood and articles of wood, wood charcoal	590,090	6%	38%	7	0.8	326,472	12	0.5
88	Aircraft, spacecraft, and parts thereof	460,369	5%	43%	0	0.4	308,988	31	0.3
48	Paper & paperboard and articles	449,905	5%	48%	-3	0.4	413,528	-1	0.4
62	Articles of apparel not knitted	438,086	5%	53%	-1	0.4	100,318	2	0.1
61	Articles of apparel, knitted or crochet	340,598	4%	56%	1	0.4	109,201	15	0.1
76	Aluminium and articles thereof	320,977	3%	60%	3	0.5	910,442	28	1.4
25	Salt, sulphur, earth, stone, plaster, lime	304,972	3%	63%	0	1.5	148,254	-4	0.9
32	Tanning, dyeing extracts, tannins,	247,561	3%	66%	-3	0.7	96,570	6	0.3
74	Copper and articles thereof	200,767	2%	68%	-9	0.5	197,317	-9	0.5
75	Nickel and articles thereof	169,378	2%	70%	11	1.5	98,758	-17	1
64	Footwear, gaiters and the like	156,373	2%	72%	-5	0.3	17,318	-9	0
19	Cereal, flour, starch, milk preparations	147,211	2%	73%	6	0.9	18,446	-1	0.1
33	Essential oils, perfumes, cosmetics	144,104	2%	75%	-8	0.5	73,894	4	0.2
70	Glass and glassware	143,470	2%	76%	0	0.5	61,111	4	0.2
35	Albuminoids, modified starches, glues	135,434	1%	78%	-1	1.3	10,845	-1	0.1
83	Miscellaneous articles of base metal	126,935	1%	79%	0	0.5	26,733	4	0.1
34	Soaps, lubricants, waxes, candles	126,278	1%	80%	-2	0.7	62,372	-1	0.4

Source: ITC calculations based on COMTRADE statistics

[1] Only 21 commodity clusters are shown, as these contributed significantly to overall exports

[2] Growth rates are based on average annual growth in value figures over the period 1996-2000.

TRADE AND INDUSTRIAL POLICY STRATEGIES

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