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PROSPECTS FOR INDUSTRIAL TRANSFORMATION IN SADC

Towards a Regional Strategy and Roadmap

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Trade and Industrialisation Nexus

Introduction

Africa has been pursuing trade integration through the African Union as a collective development agenda leading to the eventual creation of an African Common Market. This agenda is premised on the notion that creating a bigger market offers opportunities for enhanced value addition, creating possibilities of higher trade volumes and living standards. Applied to the SADC region, this argument also applies. The SADC Treaty underlines the purpose of regional integration in its first objective, which is to "promote sustainable and equitable economic growth and socio-economic development that will ensure poverty alleviation with the ultimate objective of its eradication, enhance the standard and quality of life of the people of southern Africa and support the socially disadvantaged through regional integration" (SADC Treaty, Article 5).

The SADC Protocol on Trade is the central pillar of the economic integration effort in the region. The main objectives of this protocol are to:

- Liberalise intra-regional trade in goods and services on the basis of fair, mutually equitable and beneficial trade arrangements, complemented by protocols in other areas;
- Ensure efficient production within SADC, reflecting the current and dynamic comparative advantages of its members;
- Create conditions for improvement of domestic, cross-border and foreign investment;
- Enhance the economic development, diversification and industrialisation of the region; and
- Establish a Free Trade Area (FTA) in the SADC region.

Although the objectives of the Protocol on Trade were balanced to include both trade and industrial development considerations, the provisions captured in the document emphasised trade aspects more than the other. The product-specific rules of origin serve as a pointer to the value addition direction that the region chose to take.

The Regional Indicative Strategic Development Plan (RISDP) further elaborates on the value addition objective, noting that the purpose of transforming the Southern African Development Coordination Conference (SADCC) into SADC was to "promote deeper economic cooperation and integration to help to address many of the factors that make it difficult to sustain economic growth and socio-economic development, such as continued dependence on the exports of a few primary commodities" (RISDP, p3).

The implication of this elaboration is that sustained socio-economic growth and development requires much more than just exporting primary commodities and that the region needs to realise better value from its resources by exporting value-added products. It is the trade in these beneficiated and value-added products that offers hope for the improvement of livelihoods, based on experiences elsewhere. The strategy of adding value, especially through the creation of regional value chains, is given more emphasis in the SADC Industrial Development Policy Framework (2012).

Intra-SADC Trade

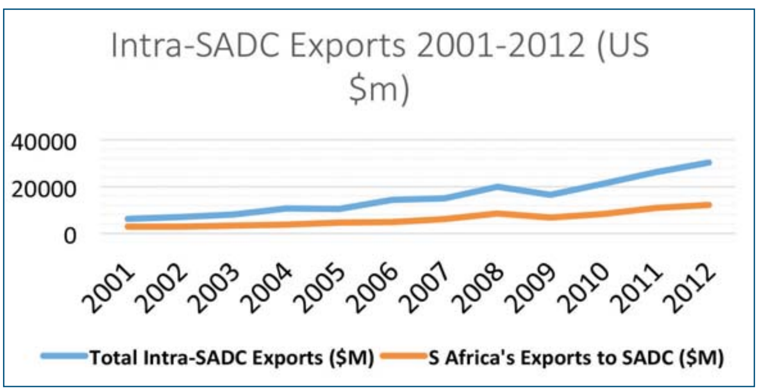
The low level of intra-regional trade in SADC, estimated at an average of 15 percent (SADC, 2012), is generally reflective of the low level of value addition in the region and the similarity of commodities produced, as well as Non-Tariff Barriers (NTBs) to trade. On average, almost 90 percent of total exports from SADC Member States consists of mineral ores and minimally processed metals such as Platinum Group Metals (PGMs), rough diamonds, ferro-chrome, copper, gold, crude oil, and iron and steel; and raw agricultural products such as cotton lint, tobacco and tea. This has resulted in these countries being significant players in the Global Value Chains (GVCs) where they remain anchored at the very bottom, rather than Regional Value Chains (RVCs) that offer better prospects.

The RISDP aims to diversify exports to include non-traditional exports while at the sustaining export growth rates at five percent or more per year. Another objective is to raise the levels of intra-regional trade to at least 35 percent of all trade by 2008 and increase the manufacturing sector share of Gross Domestic Product (GDP) to 25 percent by 2015.

SADC adopted product-specific rules of origin as one of the conditions necessary to encourage the export of value-added products to other Member States. The greater part of trade among SADC countries is in manufactured items although total intra-regional trade constitutes less than 20 percent of their total trade.

Although intra-SADC trade values have risen since the adoption of the SADC Protocol on Trade in 2001, the proportion of intra-regional trade has fluctuated at a low rate of total trade (14 to 17 percent). The SADC data also shows that between 2001 and 2012, the proportion of the manufacturing sector contribution to GDP declined from 16.9 to 11.6 percent. The greater part of intra-SADC trade, which is dominated by South Africa as shown below, consists of manufactured products such that the decline in its contribution to GDP partly explains the lack of growth in intra-SADC trade.

Intra-SADC Exports 2001-2012



SADC Statistical Yearbook 2014

South Africa's trade balance with the rest of SADC rose by 181 percent between 2007 and 2012, for an average annual growth rate of 24 percent. This is clearly unsustainable and requires urgent redress. Calls from some countries for a review of the rules of origin stem from the failure of Member States to increase their exports to other SADC states, especially South Africa, since their producers cannot meet the product-specific rules of origin. This area requires redress even though negotiations have been ongoing for a long time.

While it has been noted that the average intra-regional trade is very low, this is neither surprising nor unexpected. There is no demand for the mineral ores in neighbouring countries. Angola's chief export is crude oil. There is no capacity for large-scale refining of crude oil in the region. Zambia exports copper and there is very limited conversion capacity in the region. South Africa and Zimbabwe export platinum, there is limited regional capacity to manufacture catalytic converters and jewellery for the rest of the world.

Mozambique is in the process of establishing itself as a major Liquid Petroleum Gas (LPG) exporter over the next few years, and the trend is likely to be repeated. Botswana, Angola, Zimbabwe, Namibia and South Africa are all diamond producers. There is "no market" for diamonds in the region, which are exported to the conversion centres of India, Israel, Belgium and United Arab Emirates. All of them have invested heavily in the higher value-adding portions of the global diamonds value chain.

Nevertheless, African countries face numerous trade-related constraints which strongly hinder trade within the continent and with the rest of the world. NTBs and tariff escalation, which target processed, goods, are prime examples. While efforts must be made to address these challenges in the long-run, over the short-term, regional integration offers opportunities for expanding trade in manufactured goods, especially the establishment of the SADC FTA in 2008 and the launch of the Tripartite Free Trade Area (TFTA) by the Common Market for Eastern and Southern Africa (COMESA), East African Community (EAC) and SADC in June 2015.

The apparent lack of response to trade liberalisation is of concern to SADC because the opening of regional markets was viewed as an incentive to accelerate trade among SADC Member States. This concern is sometimes over-dramatized as there can be no hope of an escalation in intra-regional trade in the absence of economic transformation of the region. It is clear that market opening is necessary but not sufficient to ensure sustainable regional industrial sector growth. Member States need to have something to trade in and that can only happen if they increase their capability to add value to either primary products or products in semi-worked forms. There is merit in taking more decisive measures to remove NTBs, which are also acting as a significant constraint to increased intra-regional trade.

Role of Tripartite Free Trade Area

The deepening of trade integration within SADC has been hampered by the issue of multiple memberships of Regional Economic Communities (RECs). Some SADC Member States are members of the Southern African Customs Union (SACU), while others belong to COMESA and/or the EAC. Member States have been reluctant to belong to only one REC because of the potential loss of trade preferences, with the exception of Mozambique which belongs only to SADC. The Tripartite FTA launched in mid-2015 should begin to resolve some of these issues, and is also in line with the longstanding African Union vision to build one African Economic Community.

The RECs were created as building blocks to strengthen intra-regional trade by reducing and eliminating tariffs and non-tariff barriers through trade liberalization schemes. African Heads of State and Government have endorsed an AU Action Plan for "Boosting Intra-African Trade and the Establishment of the Continental Free Trade Area" (AU 2012), with negotiations to begin in June 2015. The objective is to strengthen trade between African economies, with specific focus on seven priority clusters — trade policy, trade facilitation, productive capacity, trade-related infrastructure, trade finance, trade information, and factor market integration. These measures are expected to increase the share of intra-African trade over the next decade, from the current 10-12 percent to more than 20 percent by 2022 (ECA 2013).

Policy Considerations

SADC Member States are expected to support the industrialisation agenda through engaging in negotiations to:

- **Modify the Trade Protocol** especially rules of origin through the incorporation of clauses on differential treatment in their application, recognizing the different levels of development, in particular between South Africa and the rest of SADC.
- **Pool Resources** to support technological acquisition and development of indigenous technologies.

The SADC Secretariat is expected to facilitate the following:

- **Operationalisation of the SADC Industrial Development Policy Framework** to drive the domestication of the policy and initiate specific activities. A deliberate programme will be needed to strengthen industrial policy-making and implementation at both national and regional levels and introduce measures to promote regional product value-chains in policy frameworks.
- **Regional pooling of resources and capacities** to support the establishment of regional technology incubation centres (centres of excellence) based on institutions that are already operational in some Member States. These centres can specialise in technologies to produce new products and value addition.
- **Value-chains research** to support decision-making in Member States with regard to their comparative advantages and through the participation of firms in Member States in specific parts of regional value-chains. SADC Member States should ensure that rules of origin promote the development of these regional value-chains. The United Nations Industrial Development Organisation (UNIDO) can assist with this research.
- **SADC Project Preparation and Development Facility (PPDF)** was designed to facilitate the preparation of bankable infrastructure projects and should be further strengthened to deal with industrial project preparation. The proposed Regional Development Fund (RDF) should help to organise financing of projects identified through the PPDF.
- **Infrastructure development**. The development of efficient, integrated and cost-effective infrastructure is key for industrial development, including Public-Private-Partnerships. The region is currently facing a deficit in the electricity sector despite the potential for the development of energy infrastructure. The SADC Regional Infrastructure Development Master Plan adopted in 2012 outlines strategies to address the regional infrastructure gap. Funding proposals for the various infrastructure projects identified in the master plan need to be pursued and the projects developed, including the promotion of development corridors through the African Spatial Development Programme (SDP) which aims to synchronize infrastructure provision with users to enhance investment potential and to provide economic rigour for infrastructure investments.

- **Development of Regional Value-Chain Strategies (RVCs)** to identify where Member States fit into the value chains based on resource endowments, capabilities, capacities and skills, and decide which value chains to fully develop, such as textiles, automotive, or the garment sector among others, which have potential for production of different inputs in various countries. The end products would have a market that encompasses the entire region.

Conclusion

Deepening the SADC Free Trade Area, accompanied by appropriate industrialisation policies and strategies, can facilitate economic growth in the region. SADC should boldly put in abeyance the launch of a Customs Union as that could result in some countries continuing to lag behind. Instead, focus should be on transforming the trade protocol to become an enabler in the industrialisation programme. Some Member States are finding it difficult to fully implement the tariff phase-down in line with the FTA requirements. It is, therefore, necessary that during intra-regional trade negotiations, policy space can be created to enable all Member States to develop industries to produce tradable goods.

The regional integration agenda is already being reformed to give prominence to factors that enhance regional production capacity and address other supply-side constraints such as the high cost of services in the region. This includes the rules of origin referred to above which should be re-negotiated with a view to encouraging the set-up of industries in the less developed parts of SADC.

Some products that are key to individual SADC Member States such as clothing and textiles need a significant amount of time to transform. This is particularly true of the cotton-based textiles sector as the region is currently an exporter of cotton fibres.

What is clear is that southern Africa must build the required capacities and capabilities to add value to both primary and semi-worked products. The integration agenda of the COMESA-EAC-SADC Tripartite Free Trade Area already includes an industrial development pillar which supports the development of agro-industrial and other industrial value-chains.

Trade negotiations with the EU, China and India should necessarily be handled at regional levels and be directed towards enhancing regional production capabilities in addition to market access. The BRICS (Brazil, Russia, India, China, South Africa) arrangement could be transformed to become more inclusive of regional partners, including rapid development of the proposed BRICS development bank, as this has the potential to transform the region.

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