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TRADE POLICY REVIEW

REPUBLIC OF SOUTH AFRICA

Report by the Secretariat

This report, prepared for the second Trade Policy Review of South Africa, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement Establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from the Government of South Africa on its trade policies and practices.

Document WT/TPR/G/34 contains the policy statement submitted by the Government of South Africa.

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SUMMARY OBSERVATIONS

(1) Economic Environment

1. The transfer of power, the end of apartheid and the holding of multi-party elections in 1994 politically transformed the Republic of South Africa. Following the elections and coincident with the conclusion of the Uruguay Round, the Government embarked on new trade reforms and is rapidly re-integrating the economy into the multilateral system. Adopted in September 1994, the Reconstruction and Development Programme (RDP) aims at the socio-economic development of the majority and provides the framework for South Africa's economic policies. In line with the RDP, the Government has introduced a five-year trade liberalization programme comprising, inter alia, a Tariff Rationalization Process (TRP) and a restructuring of incentives. These measures aim at an improvement in the investment climate and a re--orientation of resources away from the highly capital-intensive industrial structure that was a heritage of the apartheid era.

2. Since South Africa's last Trade Policy Review in 1993, economic growth has averaged over 3% a year. This followed growth of less than 1% a year over the previous decade, a period of import-substitution and international sanctions. Since then there has been a decided move toward outward orientation, albeit with a bias toward export promotion. Quantitative import restrictions are now largely absent and the tariff has been somewhat simplified, rates have been lowered and almost all lines are bound; nevertheless, the tariff remains complex and is frequently changed for selective protection. Concurrently, the Government has pursued fiscal and labour reform, has liberalized the exchange system and macro-economic policy has been prudent. In 1996, the Government released its Growth, Employment and Redistribution (GEAR) strategy, which includes a tight monetary policy, fiscal consolidation, and further trade and structural reform: the strategy aims at export-led growth of some 6% a year from 2000. Unemployment remains very high and job creation is an important element of the GEAR strategy.

3. Mining and related activities remain at the centre of the South African economy. The mining and quarrying sector accounts for between 8 and 10% of GDP and for some 40% of earnings from merchandise exports. Gold alone accounts for about 50% of mineral exports, and more than 20% of total merchandise exports. In consequence, developments on world mineral markets are critical to South Africa's economic performance. The manufacturing sector, largely centred around mineral processing, contributes nearly 25% of GDP. The recent decline in the production of gold, together with an increase in exports of manufactured goods, has contributed to a rise in the share of exports of non-mineral products; these accounted for almost 56% of foreign exchange earnings from merchandise exports in 1995 as against 49% in 1993. South Africa is usually a net exporter of agricultural products, depending on domestic harvests; agriculture accounts for some 5% of GDP and for 8 to 10% of goods exports. Services are the largest employer, with over half of total employment, and account for some 53% of GDP.

4. The reintegration of South Africa into the world economy has contributed to an increase in its foreign trade. Merchandise imports have grown faster than exports, leading to a contraction of South Africa's traditional trade surpluses and to external current account deficits since 1994. The rise of merchandise imports also reflects the increase in investment; capital and intermediate goods, particularly machinery and mechanical appliances, represent some 30% of South Africa's total merchandise imports. South Africa is also a net importer of a broad category of services. International reserves (including gold) represented 1.3 months of imports in 1996, compared to 1.9 in 1992.

5. South Africa's exports include machinery, motor vehicles and fertilizers to African countries, and minerals, mineral and agricultural products to developed markets, mainly Germany, Italy, Japan, the United Kingdom and the United States. South Africa's main suppliers of imports are Germany, Japan, the United Kingdom and the United States.

(2) Institutional Framework

6. The Republic of South Africa enacted a new Constitution on 3 February 1997. Under the Constitution, South Africa is a parliamentary democracy with a bicameral Parliament, comprising the National Assembly and the National Council of Provinces. National legislative power is vested in Parliament and the President. The President, Head of State, is elected by the National Assembly from among its members; tenure is limited to two five-year terms. Members of the Assembly are elected for five years by universal adult suffrage under a system of proportional representation. The Cabinet, consisting of the President, the Deputy President and Ministers appointed by the President, formulates government policy. The National Economic Development and Labour Council (NEDLAC) is the major vehicle by which the Government, labour, business and community organizations cooperate in formulating economic and social policies.

7. The Constitution, Acts of Parliament and Government Notices are the main components of South Africa's laws. Bills, including those dealing with trade, are initiated by the competent Ministries and submitted for comment and approval to Cabinet before submission to Parliament. The 1964 Customs and Excise Act and the 1986 Board on Tariffs and Trade Act (as amended) are South Africa's main legislation for foreign trade. The 1979 Maintenance and Promotion of Competition Act (as amended) includes provisions for the control of restrictive business practices, mergers and acquisitions, and monopoly situations. Several acts, including the 1978 Patents Act, the 1993 Trade Marks Act, the 1993 Designs Act and the 1978 Copyrights Act protect intellectual property rights in South Africa; the Intellectual Property Laws Amendment Bill was drafted in 1996 to bring South African law into conformity with its obligations under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

8. National treatment applies to foreign direct investment in South Africa; apart from limitations in pursuance of exchange control and immigration, foreigners are free to invest in all industries open to local investors and to repatriate the earnings. Sector-specific acts regulate investment in South Africa; various incentive schemes, including tax holidays, accelerated depreciation, export marketing, investment assistance, and a small/medium manufacturing development programme, are provided to foreign investors and local companies. Investment South Africa, a non-profit organization, was established by the Government in January 1997 to promote foreign direct investment into South Africa.

9. Through the early 1990s, South Africa privatized or commercialized a number of public enterprises, including for iron and steel and telecommunications. Since then the process has slowed: several State-owned enterprises hold monopolies or exercise such rights in various areas, including electricity, water, transport and communication, and mining and quarrying; 14 marketing boards for agricultural products still operate. In 1996, NEDLAC defined the National Framework Agreement (NFA) under which Government-labour relations will be addressed in the process of restructuring state assets and public enterprises. The NFA will terminate in April 1999 at the earliest.

10. South Africa is a founding member of the World Trade Organization (WTO) and grants at least MFN treatment to all WTO members. Previously, South Africa was a founding member of the GATT and participated in, or observed, several Tokyo Round Agreements and Arrangements. Under its Uruguay Round commitments, South

Africa bound some 98% of its tariffs at the HS eight-digit level (excluding petroleum products); tariff bindings are at ad valorem rates, with a simple average of 19.8% but with maximum ceiling rates of almost 400% (on agricultural products). In addition to petroleum products, unbound tariffs are mostly on fishing products and preparations thereof, and arms and ammunition. Subject to limitations on the presence of foreign natural persons, South Africa bound market access and national treatment under the General Agreement on Trade in Services (GATS) for several categories of services, including in the areas of business, communications, distribution, tourism and environment.

11. South Africa is a member of the Southern African Customs Union (SACU). Under SACU, members apply to imports into the Union the customs, excise, sales, anti-dumping, countervailing and safeguard duties, as well as related laws, set by South Africa; however, each member has its own legislation on quantitative import restrictions. Customs, excise, sales and additional duties collected by the members are pooled in the Consolidated Revenue Fund and subsequently distributed to members by South Africa, according to a formula. The Agreement is under renegotiation, particularly with respect to the revenue-sharing formula, time lags in revenue distribution, and joint management of the SACU system; some members have also expressed the need for a dispute settlement mechanism.

12. South Africa joined the Southern African Development Community (SADC) in August 1994. The Trade Protocol under the SADC Treaty provides for the establishment of a SADC free trade area. South Africa has bilateral trade agreements with Malawi and Zimbabwe, and grants preferential tariff treatment to a list of products from Mozambique. South Africa is negotiating a bilateral trade agreement with the European Union; a protocol on South Africa's partial accession to the Lomé Convention was finalized in April 1997. Since its 1993 Trade Policy Review, South Africa has not been directly involved in any WTO dispute settlement proceedings.

(3) <u>Features of Trade Policies</u>

(i) <u>Policy instruments and their effects</u>

13. Tariffs and "supply-side measures" are South Africa's main trade policy instruments. Since 1993, South Africa has reduced both the total number of its tariff lines and the number of non-ad valorem tariffs; it has also increased the percentage of lines carrying zero rates, and lowered certain rates. However, South Africa's tariff remains complex: the wide variety of duties, ranging from ad valorem, specific, compound, mixed and "formula" duties to their combinations, has not changed since the last Review. Based on minimum import prices, formula duties, originally designed to combat "disruptive competition", are still used, although South Africa also applies anti-dumping actions. Protective tariffs can also be introduced relatively easily. South Africa has not requested delayed application of the WTO Agreement on Implementation of GATT Article VII (on customs valuation).

14. In accord with its Uruguay Round commitments, South Africa has tariffied all quantitative restrictions in agriculture, except on black tea. South Africa maintains import controls on certain agricultural and manufactured products, and on minerals; it prohibits the importation of certain waste and hazardous materials and goods banned under international conventions. The importation of used goods is either subject to controls or prohibited and products such as live animals and animal products, plants and plant products, honey, beeswax, genetically manipulated organisms and fresh water fish are subject to import permits under health, sanitary and phytosanitary regulations.

15. South Africa's simple average MFN import tariff at end-June 1997 was some 15%, with substantial dispersion; because of formula and specific rates the maximum ad valorem rate cannot easily be defined. Duty-

free treatment applies to some 44% of all the tariffs, particularly on inputs of capital goods and products that are not manufactured in, and do not have substitutes in, South Africa. About 23% of all lines carry rates above 30%. Sectorally, the highest average tariff was in manufacturing where it was 15.6%, compared with 5.6% in agriculture and 1.4% in mining and quarrying. There is negative escalation in the tariff overall, but this may be misleading in that it mostly reflects the application of zero, or low duties on industrial products that are neither manufactured nor have substitutes in South Africa. The Tariff Rationalization Process should substantially simplify South Africa's tariff structure but it could increase escalation and therefore the effective rate of protection.

16. In addition to tariffs, imports - like domestic goods - are subject to ad valorem excise duties, ranging to 20%, and to specific excise duties; a value-added tax of 14% applies to goods and services. "Fuel levies" are collected on imported oils and specific levies are charged on agricultural products. An import surcharge introduced in 1985 for balance-of-payment purposes was eliminated in October 1995. The South African Revenue Service (SARS), an administratively autonomous body, was established in April 1996 to improve revenue collection and administration. At end-1996, South Africa had 35 definitive anti-dumping duties in force, mostly on imports of chemical and mineral products, paper and clothing from 16 countries; it had no countervailing or safeguard duties. South Africa is amending its legislation on anti-dumping, countervailing and safeguard measures with a view to bringing it into line with the relevant WTO Agreements. Import controls, under the WTO Agreement on Safeguards, were still in force at end June 1997 on certain products, including new tyres.

17. Under the National Industrial Participation Programme, all State and parastatal purchases and leases with an import content of at least US$10 million are subject to Industrial Participation Obligations; under these the seller must invest in South Africa the equivalent of at least 30% of the value of the imported content of the purchase. South African content is also required for several incentives, including the rebate of import duties under the Revised Phase VI Motor Industry Development Programme, for credit facilities to exporters of capital goods and services, for obtaining type approval for certain telecommunications equipment, and for preferences in government procurement; there are also local-content requirements for coffee and tea packing, blending and roasting.

18. South African trade policy favours export promotion, with a wide variety of incentives, including tariff concessions, credit facilities, financial assistance and guarantee facilities. Export subsidies under the General Export Incentive Scheme were terminated on 11 July 1997. Export controls are maintained on a number of agricultural products, certain minerals and industrial products. Exports of crude or unprocessed tiger's-eye, ostriches and fertile hatching ostrich eggs are prohibited. There is a 15% export tax on unpolished diamonds.

19. The retail prices of petroleum products and producer prices of a number of agricultural products, including meat, oilseeds, wheat, canned fruit, mohair, sorghum, wine and sugar, are controlled. The pricing of certain services, mainly those supplied by parastatals, is also regulated.

(ii) Sectoral policy patterns

20. The South African economy is relatively capital intensive. The major objective of economic policy is thus to enhance value-added in labour-intensive activities.

21. As the backbone of the economy, the mining and quarrying sector receives the largest share of financial assistance to enhance value-added. In addition to the general tax deductions provided to South African companies, prospecting expenditure is deductible from mining income, and mining *companies may also deduct capital expenditure from their current taxable income, whereas other companies may do so over a five-year period.*

22. Large and diverse endowments of minerals, and relatively low tariffs on their imports have contributed to the development of mineral processing; for example, locally produced coal, supplied at low prices, provides 70% of South Africa's primary energy. Tariffs on mineral imports average 1.4%, with a maximum of 18%; higher rates apply to processed minerals. Products subject to import controls include mineral fuels, oils and distillates, radioactive chemical elements and radioactive isotopes, gold, coins, and a variety of other minerals. Export controls, exercised by permits, apply to a number of minerals and mineral products; exports of unprocessed tiger's-eye are prohibited.

23. Under the Minerals Act, which entered into force on 1 January 1992, the number of authorizations required for operating in the sector has been reduced from some 40 to 3 (prospecting and mining permits and a mining licence). The Act also aims to ensure fair management of mineral prospecting and of mining rights. Distribution, wholesale and retail marketing of liquid fuels are regulated, and trade in crude oil and refined products is controlled.

24. The Government has reoriented its agricultural policy away from self-sufficiency to food security, defined as access by all people at all times to enough food for an active and healthy life. The Marketing of Agricultural Products Act was introduced in 1997 to promote the deregulation of the marketing systems: the number of control boards has been reduced from 22 in 1992 to 14 in June 1997. It is government policy that over the long-term the sector will be "primarily" protected by tariffs.

25. Tariffs on agricultural products range from 0 to 35%, with a simple average of 5.6%. Formula duties apply to preparations of tomato, cornflour, cherries and tobacco, and specific duties to certain animal and fishery products, beverages, products of the milling industry, sugar and sugar confectionery. South Africa bound tariffs on all products covered by the WTO Agreement on Agriculture, except certain albuminoidal substances based on eggs. Ceiling bound rates ranging up to 399.9% leave considerable margins for discretionary increases in applied tariffs. Imports of fish, crustaceans, molluscs, dairy products, oats, maize, wine, vermouth and fermented beverages are subject to controls by permits. Export controls apply to coffee and wattle seeds.

26. The international competitiveness of manufacturing has been hampered by upward pressures on unit labour costs resulting partly from a lack of skilled labour. The sector is protected mainly by tariffs, which average around 16%; textiles, clothing and related items are the most tariff-protected products. Most non-tariff barriers have been phased out except on products such as new tyres and fire arms, which are still subject to import controls, and on chemicals and motor vehicles to which export controls apply.

27. The Tariff Rationalization Process, which is to simplify and rationalize the tariffs, aims to lower cost structures and reduce price distortions. However, by escalating rates from primary to final products - with rates of 10, 20 and 30% generally not to be exceeded on raw materials, intermediate goods and finished items, respectively - the Process may increase effective protection, and thus perhaps raise the capital intensity of manufacturing.

28. South Africa has restructured several State-owned service suppliers; the Government sold a 30% share in Telkom in 1997, and companies such as Sun Air, Autonet, Px (parcel express), Abakor (abattoirs) and Aventura are earmarked for privatization. Except for limitations on the presence of foreign natural persons, services are generally open to foreign investment. However, monopolies or exclusive rights remain in a number of areas, including port, airport, transport and basic switched *telecommunication services. Further liberalization of services should improve the efficiency of other sectors, such as manufacturing and tourism; it would also help the competitiveness of South Africa's exports, especially by reducing costs relating to transport and telecommunication.*

(4) Trade policies and trading partners

29. South Africa is reintegrating itself into the global economy. It is engaged in structural reform that will help its products to compete internationally. South Africa has redrafted almost all its legislation to provide a legal and credible foundation to its reform effort. This reform is encapsulated by the Growth, Employment and Redistribution (GEAR) strategy, a major element of which is trade liberalization.

30. At the same time, South Africa's regional and preferential links are becoming more complex, with renegotiation of the SACU Agreement, the liberalization of regional trade under the SADC Trade Protocol, and the development of new structures that may result from a bilateral trade agreement with the EU. There is a risk that the evolution of this complex set of relations could create a structure of tariffs, preferences and rules of origin that will distort trade patterns.

31. To simplify and coordinate the various aspects of trade policy, plans with respect to trade liberalization should be actively pursued, especially by moving toward lower, more uniform rates. By simplifying the tariff structure through the elimination of non-ad valorem tariffs, the reduction of maximum rates and the number of tariff bands, liberalization will help to prepare South African production for greater foreign competition and enhance its adherence to WTO principles, thus both rendering its reforms more credible and helping to attract foreign investment.