Institute for Public Policy Research

70-72 Frans Indongo Street PO Box 6566 Windhoek Namibia Tel: +264 61 240514 Fax: +264 61 240516 economist@ippr.org.na www.ippr.org.na

Economy Watch Namibia – July 2015

Tripartite FTA launched

On 10 June 2015 24 Heads of State and or Government signed the Declaration for the establishment of the Tripartite Free Trade Area (T-FTA) and 16 signed the T-FTA Agreement. The T-FTA combines three regional groupings, namely the Common Market for Eastern and Southern Africa (COMESA), the East African Community (EAC) and the Southern African Development Community (SADC). The creation of the T-FTA is an attempt to break the impasse caused by overlapping membership between the three groups. For instance, Tanzania is a member of the EAC and of SADC, Swaziland a member of SACU, SADC and COMESA, and most of the non-SACU SADC countries are also members of COMESA. This has hampered efforts to achieve deeper regional integration within SADC. Once fully implemented the T-FTA establishes a Free Trade Area from Cape to Cairo consisting of 26 African countries with a population of some 560 million people and a combined GDP of over USD 1 trillion.

Not all SACU Member States have signed

This is a commendable undertaking that could link small and fragmented markets in the region and eventually increase cross-border trade, production and hence employment and the standard of living. However, substantial work remains for this to materialise. So far, South Africa as the largest economy within the T-FTA as well as Botswana and Lesotho and thus the majority of SACU Member States have not signed. Since SACU Member States are bound by a Common External Tariff, it is not possible for just some of them to join the T-FTA. Furthermore, South Africa has reportedly offered to zero rate 60 per cent of tariff lines. However, 56 per cent of tariff lines are already zero rated. It remains to be seen, whether the zero rating of the additional 4 per cent will have a visible impact on trade flows.

The challenge with the acquis

The ongoing negotiations build on the acquis, meaning on what exists. Existing trade agreements are not renegotiated and countries – or SACU for that matter – negotiate agreements with countries they do not yet have an agreement with. Whether this will solve the challenge of overlapping memberships and result in more efficient trade arrangements is doubtful. It is likely that this approach will increase the so-called 'spaghetti bowl' and add to the complexity of different trade arrangements and consequently of border procedures within the region. One of the challenges is that the Regional Economic Communities (RECs) have established Secretariats that facilitate the arrangements, but do not have a mandate to negotiate on behalf of Member States with other RECs. Moreover, the signed Agreement covers Trade in Goods, but not yet Trade in Services, the free movement of business persons or the free movement of people at large. These components will be negotiated in Phase II and following. Ser-

Trade in Services not yet part

Tripartite Free Trade Area

Source: http://www.bbc.com/news/world-africa-33076917.

Overlapping memberships, T-FTA members

	COMESA	EAC	ECCAS	IOC	SACU	SADC
Angola			X			X
Botswana					X	X
Burundi	X	X	X			
Comoros	X			X		
Djibouti	X					
DRC	X		X			X
Egypt	X					
Eritrea	X					
Ethiopia	X					
Kenya	X	X				
Lesotho					X	X
Libya	X					
Madagascar	X			X		X
Malawi	X					X
Mauritius	X			X		X
Mozambique						X
Namibia					X	X
Rwanda	X	X	X			
Seychelles	X			X		X
South Africa					X	X
Sudan	X					
Swaziland	X				X	X
Tanzania		X				X
Uganda	X	X				
Zambia	X					X
Zimbabwe	X					X

Source: Authors' compilation based on the web sites of the Regional Economic Communities.

COMESA – Common Market of Eastern and Southern Africa

EAC – East African Community

ECCAS – Economic Community of Central African States (Only T-FTA members are listed)

IOC – Indian Ocean Commission

SACU – Southern African Customs Union

SADC – Southern African Development Community

No T-FTA Secretariat and Tribunal established

vices, however, play an important role in the production and distribution of goods and hence the efficiency and competitiveness of an economy relies also on the efficient provision of services. Last but not least, the implementation of the T-FTA is not supported by a T-FTA Secretariat, but by a Task Force consisting of the three secretariats. The agreement does not foresee the establishment of a Tribunal or Court that governments and business persons could approach in case Member States fail to meet their obligations under the T-FTA Agreement.

Negotiations towards Continental FTA launched

A few days later, on 15 June 2015, an even more ambitious plan was signed at the AU Summit in South Africa, namely the beginning of negotiations for a Continental Free Trade Area (C-FTA) covering the whole of Africa. A decision was taken to follow the same approach the T-FTA is taking, namely the acquis. This implies that not the T-FTA as a bloc negotiates with the remaining regional blocks on the continent such as ECOWAS, but again individual Member States with each other.

Political declaration, but implementation lacking

While these ambitious plans receive support at the highest level, what is happening on the ground often points in the opposite direction – namely towards more inward-looking policies. The unilateral decision of South Africa last year to close the border for livestock imports – an issue that should have been addressed at least at SACU level – and the decision by Zimbabwe to introduce a surtax of up to 40 per cent on imports without prior consultations are just two examples of the realities. In addition, currently negotiated draft SADC Guidelines on Tax Incentives and Indirect Taxes reflect the unwillingness of some Member States to cede policy space. Although phrased broadly and setting minimum tax rates that are below any existing tax rates no deadline for the implementation of the guideline is mentioned. On top of it, the draft Preambles of both Guidelines state that they are not binding for Member States. The Committee of Ministers has to approve these guidelines and could still make changes, since deeper regional integration without binding agreements and realistic deadlines is not possible.

SACU at a crossroads…

Moreover, SACU is at a crossroads. The Council of Ministers, the highest decision making power, has not met for a long time. South Africa has indicated for some time that it would like to change the Revenue Sharing Formula in order to substantially cut transfers to other SACU Member States, although the region as a whole including South Africa has benefitted socially, economically and politically from the current arrangement. After more than a decade institutions such as the SACU Board of Tariffs and the SACU Tribunal envisaged in the 2002 Agreement have not yet been established. Furthermore, South Africa is reportedly considering dissolving the Common External Tariff, which would actually imply the end of the oldest existing customs union in the world. The stalemate does not bode well for deeper regional integration within the T- and C-FTA. Neither does it support the creation of regional and global value chains as envisaged in the recently agreed SADC Industrialisation Strategy. What is currently missing in the region and on the continent is a champion

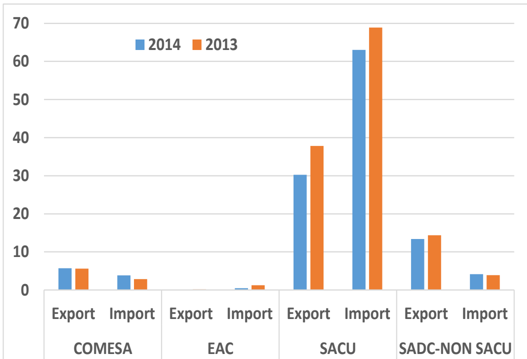
…Champion for regional integration missing

Population and GDP per capita, T-FTA member countries, 2011

	Population	GDP per capita in USD
Angola	18 314 441	5 540
Botswana	1 933 719	7 255
Burundi	8 624 208	251
Comoros	649 291	767
Djibouti	810 100	1 575
DRC	58 819 038	446
Egypt	75 491 922	3 256
Eritrea	5 382 163	504
Ethiopia	82 621 190	472
Kenya	38 773 277	1 166
Lesotho	1 972 199	1 135
Libya	5 876 805	13 303
Madagascar	19 926 785	445
Malawi	14 138 207	266
Mauritius	1 244 121	9 111
Mozambique	22 762 525	593
Namibia	2 110 791	5 770
Rwanda	10 222 961	630
Seychelles	86 956	11 689
South Africa	49 344 228	7 592
Sudan	34 040 065	1 698
Swaziland	1 153 929	3 290
Tanzania	42 353 790	835
Uganda	31 778 799	653
Zambia	12 456 527	1 772
Zimbabwe	12 784 041	909

Source: World Bank, World Bank data at http://databank.worldbank.org/data/views/reports/tableview.aspx?isshared=true

Namibia's trade with other T-FTA RECs in percent of total trade, 2013 and 2014



Source: Namibia Statistics Agency, Trade Statistics of regional integration that can push the agenda forward. Namibia could take on this role, especially since becoming a regional logistic hub requires smooth border procedures.

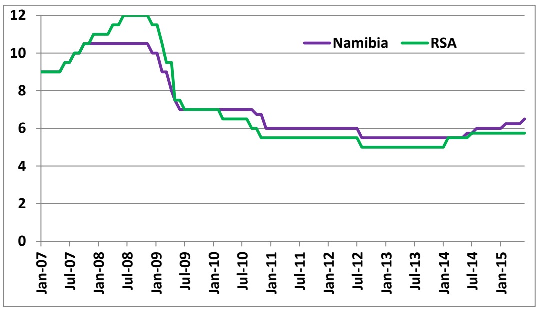
Interest rates…

The period of low interest rates in Namibia has come to an end with the second interest rate increase this year by 25 basis points in June. The repo rate remained at the lowest level for almost two years between August 2012 and May 2014 at 5.50 per cent, before the Bank of Namibia started to gradually increase the leading rate twice in 2014 as well as in 2015 to 6.50 per cent. The Prime Rate was increased accordingly to 10.25 per cent. The increase has not come as a surprise since the central bank has raised concerns about the high level of private borrowing for mainly consumptive spending on imported goods. The increase in imports, not only caused by private consumption but also by large infrastructure projects and private sector investment, resulted in an increasing trade deficit that amounted to NAD21 bln in 2014 compared to NAD13 bln in 2013. Consequently, the foreign exchange reserves, necessary to maintain the NAD's one-to-one peg with the South African rand, have dropped significantly. Although still sufficient to maintain the peg, Namibia no longer meets the international and SADC benchmark of three-month import cover. Based on the foreign currency reserves in June 2015 (NAD12.1 bln) and the latest available import data for 2014 the current foreign exchange reserves would cover less than two months of imports. However, the substantially lower oil prices are providing some relief for the reserves.

…foreign currency reserves, and

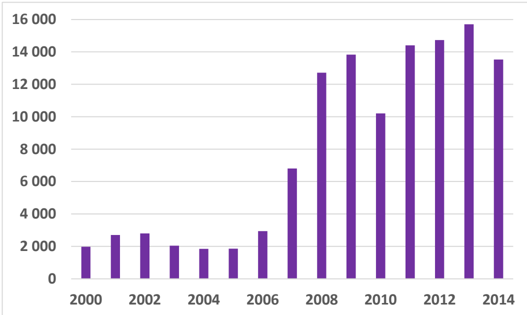
…import cover

Repo rates for Namibia and RSA, Jan 2007 to Jun 2015



Source: Bank of Namibia and South African Reserve Bank

International Foreign Exchange Reserve Stock in NAD mln, Dec. 2000 to 2014



Source: Bank of Namibia, 2015, Annual Report 2014

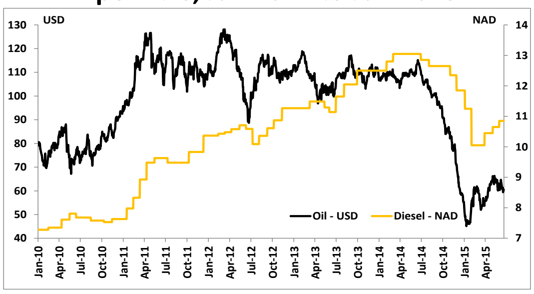
…and impact on National Budget

While the higher interest rate could deter 'unproductive' spending on imported goods, it provides more incentives to save. Last but not least, rising interest rate levels will have a bearing on the national budget since it increases government's costs of borrowing domestically. Therefore, less expensive financing options outside the domestic market, without increasing the exposure to currency risks, could be considered.

Oil and fuel prices up compared to Jan 2015, but much lower than a year ago

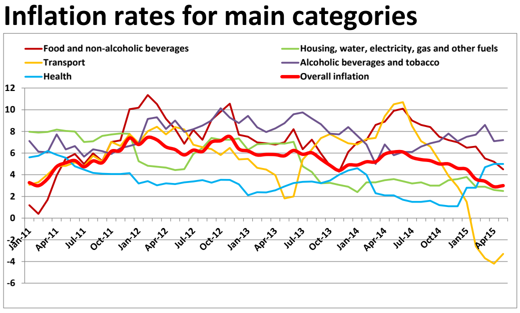
Oil prices have increased by 9.5 per cent since the beginning of the year, but by 15.2 per cent in NAD owing to the depreciation of the NAD against the USD. Prices, however, remain 47 per cent and 40 per cent respectively below prices a year ago, which has brought some relief to motorists, although not to the users of public transport since taxi fares have remained unchanged. Despite three consecutive fuel price increases since April 2015, petrol and diesel prices remain 13 and 17 per cent below prices a year ago. The price increase was not only caused by rising oil prices and a weaker NAD, but also by an increase in the transport levy (10 cents), Road Fund Administration levy (10 cents) and the industry margin (12 cents). Besides declining food prices the lower fuel prices have been the driver of low levels of inflation that dropped to 2.9 per cent in April before rising slightly to 3.0 per cent in May. Fuel accounts for more than 50 per cent of transport inflation. Lower oil prices are also benefiting the country's foreign exchange reserves that are under pressure. The value of fuel imports dropped by 22 per cent between 2013 and 2014 to NAD5.8 bln, saving NAD1.6 bln in foreign exchange or more than 13 per cent of the current reserves of NAD12.1 bln.

Oil prices in USD per barrel and diesel prices in NAD per litre, Jan 2011 to Jun 2015



Source: EIA and Ministry of Mines & Energy, daily data.

Inflation rates for main categories



Source: Namibia Statistics Agency, Namibia CPI

Namibia in international comparison

The World Economic Forum (WEF) has released a number of reports during this quarter that are relevant for Namibia. The reports provide always two measurements, a score and a ranking. While the score is an absolute measurement that indicates how well a country has performed on a scale of one to seven, the ranking is a relative measurement comparing the performance of a country in relation to all participating countries. Both indices are relevant, since the score indicates whether a country's performance has actually improved, while the ranking illustrates the country's performance relative to other countries. Even if the score improves, a country will fall behind if other countries are moving faster.

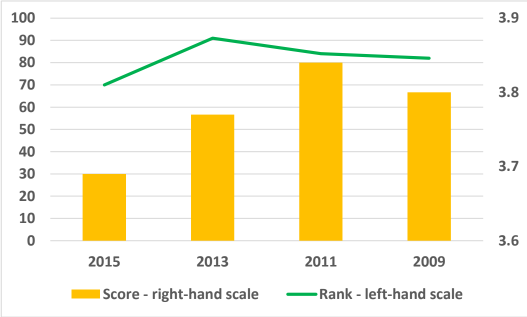
Travel & Tourism Competitiveness improved

The Travel & Tourism Competitiveness Report reveals good news for Namibia since the country moved up the ladder considerably from rank 91 (2013) to rank 70 (2015). Namibia ranks fourth in Sub-Saharan Africa behind South Africa (48), Seychelles (54) and Mauritius (56) and fifth in the whole of Africa (Morocco – 62). The score, however, has dropped from 3.77 to 3.69 out of 7, but this is caused by a new methodology applied in compiling the index. Namibia scored in particular well in the indices 'Price Competitiveness' (5.20), 'Safety and Security' (5.02), 'Business Environment' (4.76) and 'Tourist Service Infrastructure' (4.75), but disappoints in 'Cultural Resources & Business Travel' (1.12), where it ranks 132 out of 141 countries. The poor score is caused by the lack of World Heritage sites and large sport stadiums (only one each), among other factors. Other areas that need attention include 'Human Resources and Labour Market' (3.80) and 'Health and Hygiene' (3.70), despite ranking 22nd in the sub-component of malaria prevalence.

...but Global Information Technology Competitiveness rather stagnant

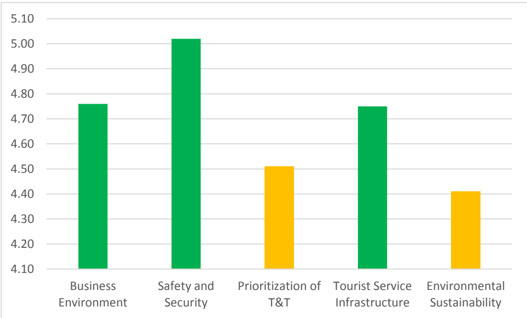
Namibia's results in the Global Information Technology Report 2015 are rather mixed. Namibia improved the score from 3.4 in 2014 to 3.5 in 2015 and moved from rank 105 to 102. The better ranking, however, is due to three countries not being covered in 2015 that were ranked higher than Namibia in the previous year. Namibia performed stronger than her peers in the upper middle-income group in terms of 'Political and regulatory environment', but is lagging behind regarding 'Affordability', 'Skills', 'Individual usage' and 'Infrastructure'. Specific areas that need attention are the costs of fixed broadband internet access and the quality of math and science education. The country is ranked 126 in both components. On the other hand, Namibia excels in terms of mobile network coverage (Rank 1), total tax rates (Rank 15) and the efficiency of the legal system (Rank 29). Interestingly, Namibia dropped 13 places to Rank 104 in the index 'Intensity of Local Competition' between 2013 and 2015 even though the score improved slightly from 4.5 to 4.6. It indicates that competition in Namibia is lagging behind the level of competition in other countries. The separation of Telecom and MTC agreed by Cabinet end of 2015 could support competition in the sector.

Namibia's score and ranking in the T&T Competitiveness Report



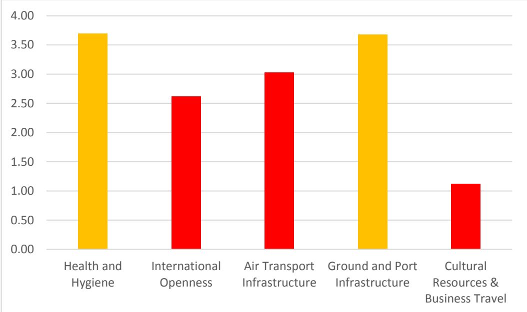
Source: WEF, various years, Travel & Tourism Competitiveness Reports.

Namibia's strength....



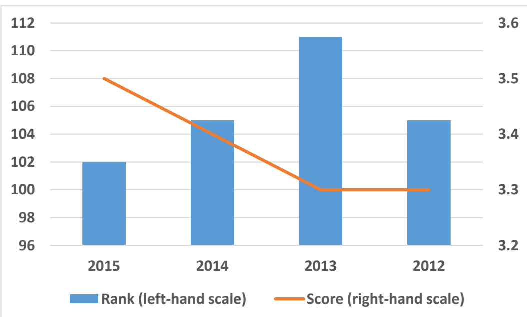
Source: WEF, 2015, Travel & Tourism Competitiveness Report.

...and weaknesses in the T&T index



Source: WEF, 2015, Travel & Tourism Competitiveness Report.

Namibia's score and ranking in Global Information Technology



Source: WEF, various years, Global Information Technology Report.

Economy Watch Namibia is compiled by IPPR Research Associate Klaus Schade (economist@ippr.org.na) and is financially supported by the Hanns Seidel Foundation (HSF). Economy Watch can be downloaded from www.ippr.org.na or www.hsf.org.na and printed copies are available from the IPPR or HSF.