Three Painful Lessons the African Union Should Learn from the Southern African Customs Union

By:

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Most African states adopted the text of the Agreement establishing the African Continental Free Trade Area (AfCFTA) in May 2018, but they might as well have written that text 50 years ago. While the paper on which the text of the Agreement lies has not yet fully oxidized, the challenges that it covers have been around for decades. Count among them customs unions.

In establishing the African Continental Free Trade Area, the African Union (AU) wished to pave the way for the Continental Customs Union (CCU). However, unlike the negotiators of some earlier trade agreements, the drafters of the AfCFTA Agreement do not appear to have thought deeply about this continent-wide customs union.

For that reason, states will likely take some leaves from the pages of the

Southern African Customs Union (SACU) Agreement, which set up the world's oldest functioning customs union in 1910. But, as experience from SACU could teach them, customs unions can badly hurt some of its members, in at least three ways: by delaying industrialization; curtailing a country's ability to protect domestic industries; and diverting trade.

This does not imply that AU member states should not join the CCU. On the contrary, receipts from SACU represent the largest source of income for three of the five SACU members (i.e., eSwatini, Lesotho, and Namibia). Indeed, customs unions can serve as a force for prosperity and therefore political stability. Rather, the dilemma is that, while SACU certainly boosts the gross domestic product (GDP) and the revenue of members, a customs union is not necessarily worth the candle.

Customs unions may hold back the industrialization of their smaller members

To a large extent, the question as to whether the CCU and the AfCFTA generally will benefit its members hinges on how the trade area manages the economic disparities among its members. One aspect of that question that the majority of experts overlook relates to the wide economic differences among AU countries. Nigeria, South Africa, and Egypt alone account for more than half of the continent's GDP. In stark contrast, Africa's six island nations only represent about 1% of that GDP.

These data suggest that, while behemoths such as Nigeria, Egypt, South Africa, and Ethiopia stand to gain a lot from the CCU, smaller trading nations such as Benin, Namibia, and Seychelles, may not automatically reap the same fruits from the AfCTA tree. Some of the differences in manufacturing performance originate in history. The superiority of one country over others in one branch of production does not inhere in that country's make-up but often only arises from having begun it sooner.

In the *Clover Dairy Namibia (Pty) Ltd & Anor. v. Minister of Trade & Industry and Others, (Clover Case)* dairy producers in Namibia complained to the Namibian trade ministry that imports of cheaper dairy products from South Africa were

threatening their business. Unless the government intervened, those imports would make them lose business or drive them out of the market altogether. In fact, one of the domestic producers, Namibia Dairies, claimed that it accounted for 50% of the domestic dairy industry in respect of UHT[1] milk – a market share that underlines the injury that industry suffered.

In response, the Namibian trade ministry published in July 2013 a notice prohibiting the importation of dairy products into Namibia. South African dairy producers protested and took the Namibian Trade Minister to court. They argued that the Minister violated the provisions of the SACU Agreement. The High Court of Namibia set aside the Minister's notice, but not directly because the notice violated the SACU Agreement, but mainly because the minister did not comply with the rules of administrative law. (See pp.380-383 of the book *International Law in Namibia*) Thus, *Clover* shows how customs union rules have prevented a member state from developing its dairy industry and, thereby, held back the industrialization of that state.

Customs unions limit the ability of their members to protect their domestic industries

In *Clover,* the Namibian Trade Minister granted infant-industry protection to domestic dairy producers. However, the plaintiffs submitted that the Minister violated Article 26 of the SACU Agreement, which circumscribes infant-industry protection (IIP). Regrettably, though industrialization and economic development rely on IIP, the AfCFTA Agreement pays scant attention to IIP:[2] "For the purposes of protecting an infant industry having strategic importance at the national level, a State Party may, provided that it has taken reasonable steps to overcome the difficulties related to such infant industry, impose measures to protect such an industry."

As formulated, this clause of the Agreement (the 'IIP clause') will most likely fail to achieve its intended purposes. For one thing, unlike Article 26(2) of the SACU Agreement, the IIP clause does not define 'infant industry'. (In terms of Article 26(2) of the SACU Agreement, "[i]nfant industry means an industry which has been established in the area of a Member State for not more than eight (8) years.") As a consequence, states will not know in which situations the clause

applies. The clause does specify that the industries protected by the AfCFTA must “have strategic importance at the national level”, but that point does not clearly indicate which industries and which situations call for IIP. For another thing, the clause does not provide for the widely accepted ‘Bastable condition’, which lays down that the net benefits of protecting an industry must exceed its net costs.

Nonetheless, the IIP clause mandates the AU to adopt guidelines on how to implement the IIP clause “as an integral part of this Protocol”. Hopefully, the framers of the AfCFTA Agreement will seek to remedy the shortcomings of the IIP clause by proposing key guidelines, drawing on the rich IIP literature, and a method to interpret them to overcome the non-binding nature of ‘guidelines’.

Customs unions can ‘divert’ trade and decrease welfare

Aside from exporting inflation from one member to others, customs unions can also divert trade. Understanding this risk requires a fuller concept of ‘customs union’. Except when members deploy IIP through tariffs, customs unions encompass states that have undertaken as a group to eliminate or reduce trade barriers, particularly customs duties, among themselves and to establish a common external tariff. Customs unions primarily aim at shifting sources of supply, and they can shift supply to either lower-cost or higher-cost sources.

Viner, who pioneered the theory of customs unions in 1950, said that customs unions benefit its members depending on whether the customs union creates or diverts trade. Trade creation shifts supply sources from a high-cost domestic producer to a low-cost producer in a member country; trade diversion shifts supply sources from the lowest-cost producer in a non-member country to a higher-cost producer in a member country. Though no evidence definitively shows that SACU diverts trade, the CCU would divert trade if, for example, Côte d’Ivoire stopped importing cheaper textile from China because the CCU induced it to buy relatively more expensive textile from Lesotho, instead. For Viner, creating trade raises the home country’s welfare whereas diverting trade lowers it.

Let’s customize customs unions

While the AfCFTA is most probably the next best thing in terms of economic benefits (for instance, huge trade volumes and larger financial flows) since states on the continent created the AU itself, it poses certain dangers. In particular, like SACU, the CCU envisaged in the AfCFTA Agreement will likely injure the economies of some of its member states. And, unless the AU delegates custom-design it carefully, bearing in mind the policy choices brought up in this piece and in older regional trade agreements, the CCU can prove prohibitively costly.

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[1] UHT stands for ‘ultra high temperature’. [2] Article 24(1) of the Protocol on Trade in Goods, AfCFTA.

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