Trade liberalisation and financial compensation

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The BLNS states in the wake of the EU-South African trade and development agreement

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To the people who helped make my time in South Africa such a successful adventure

My family and my friends in South Africa

Contents

Maps and photographs

Maps

Photos

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List of abbreviations

ACP	African, Caribbean and Pacific countries
BLNS	Botswana, Lesotho, Namibia and Swaziland
CAP	Common Agricultural Policy
DTI	Department of Trade and Industry
EBA	Everything But Arms
EC	European Commission
EDF	European Development Fund
EEC	European Economic Community
EFTA	European Free Trade Association
EISP	Economic Integration Support Programme to the BLNS
EPA	Economic Partnership Agreement
EPRD	European Programme for Reconstruction and Development
EU	European Union
FTA	Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
GEAR	Growth, Employment and Redistribution Strategy
IMF	International Monetary Fund
LDC	Least Developed Countries
Mercosur	Mercado Común del Sur
NEPAD	New Partnership for Africa's Development
REPA	Regional Economic Partnership Agreement
SACU	Southern African Customs Union
SADC	Southern African Development Community
TCB	Trade Capacity Building
TDCA	Trade, Development and Cooperation Agreement
US	United States
WTO	World Trade Organisation

Abstract

With the ascendance of liberal approaches to economic development since the 1980s, developing countries have faced strong international pressure to reduce trade barriers with advanced, industrialised economies. A striking example is the fate of Botswana, Lesotho, Namibia and Swaziland (BLNS) following the 1999 trade and development agreement between the European Union (EU) and South Africa. As members (with South Africa) of the Southern African Customs Union, the BLNS countries are now effectively locked into reciprocal trade liberalisation with the EU. The BLNS governments' acceptance of the agreement was accompanied by offers of various forms of financial assistance. This report aims to clarify links between trade liberalisation and financial compensation, and their longer-term implications for BLNS countries' economic relations with the EU. How well do compensation programmes conform with the liberal rationale of easing transitional economic adjustment costs in the move to freer trade? To what extent do they appear motivated more by the need to secure BLNS governments' political acceptance of the EU-South Africa trade agreement? Analysing several programmes and drawing on personal interviews with public officials, the report concludes that compensation has provided political 'side payments' that deviate in important ways from liberal economic principles. The broader implications for understanding the political economy of trade liberalisation and financial compensation in developing countries are also briefly discussed.

1

Introduction

Since the mid-1980s, global North-South trade relations have increasingly emphasised greater and more reciprocal reductions in trade barriers. An important recent example is the 1999 free-trade agreement concluded between the European Union (EU) and South Africa. Because South Africa is a member to the Southern African Customs Union (SACU) with Botswana, Lesotho, Namibia and Swaziland (BLNS), its so-called Trade, Development and Cooperation Agreement (TDCA) with the EU meant that the BLNS states have effectively been incorporated into that agreement. Currently, the BLNS states and many other African countries are also renegotiating their Lomé Convention trade relations with the EU. The EU has been trying to direct this agreement towards enhanced reciprocal free trade. The BLNS countries are moving toward trade liberalisation largely because of EU and South African shifts in trade policy.[1]

[1] Henry Bienen (1991: 74-96) defines trade liberalisation as 'the relaxation or elimination of tariffs and removal of duties and/or quotas on exports; alteration in non-tariff barriers such as import quotas and quantitative restrictions;

Meanwhile, aid to the developing world has become linked more closely to the acceptance of trade liberalisation. Since the TDCA's inception, the EU has offered various forms of financial assistance to the BLNS countries. These payments aim to compensate for the detrimental effects of enhanced free trade, such as greater competition from EU products to the SACU market; greater competition from South African products for BLNS exports to the EU; a partial loss in revenue; and indirect effects from changes to the South African economy and from changes in investment in the BLNS states. When in 2002 the five SACU countries concluded the renewal of their customs treaty, South Africa compensated the BLNS states for their move toward trade liberalisation through the TDCA.[2]

A popular liberal belief amongst developed countries states that 'trade not aid' should help developing countries overcome their impoverished position. The BLNS countries were nonetheless given aid in the form of financial compensation for their inclusion within the TDCA. Trade liberalisation and financial compensation in this case are directly connected to each other. Recently the 'trade not aid' paradigm has undergone subtle adjustments. The role of aid in accomplishing trade liberalisation has been awarded a more substantial position. As a result, the popular motto amongst the donor community concerning the relationship between trade and aid has shifted to 'aid for trade'. Although within this view aid is meant to develop economic structures for free trade, an alternative goal could be to create political compliance with these shifts in trade.

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changes in licensing and direct allocation of foreign exchange, and in specific regulations for products; removal or relaxation of export subsidies'.

[2] Compensation in this study is interpreted as financial payments offered by one party to another to offset the detrimental effects that originated from a change in relationship. In the case of the EU and the BLNS countries, these negative effects derive from changes in trade relations caused by the TDCA.

This study was set up to assess the emerging relationship between trade liberalisation and financial compensation in BLNS countries' dealings with the EU and South Africa. It examines different interpretations of the role of compensation. According to one view, compensatory aid mainly intends to serve economic adjustment purposes. Another interpretation explains the aims of compensation as being to overcome political resistance to further economic integration. Finding which view is most helpful to explain the compensation payments to the BLNS states clarifies the current relation between trade and aid in the case of the EU, South Africa and the BLNS countries.[3]

Relevance

In 1996 the EU's executive body, the European Commission, adopted an influential Green Paper on trade relations with African, Caribbean and Pacific (ACP) states. This report proposed a shift towards a more reciprocal form of trade with the region.[4] Since then, the world has followed attentively the way in which this substantial change in world trade relations is progressing. The EU has tried hard to gain acceptance of its policy change by those ACP countries involved. By 2008, the EU expects free trade zones to be formed amongst the ACP countries, the so-called regional Economic Partnership Agreements (EPA). With these groups of countries the EU hopes to forge bilateral free trade agreements. ACP countries, however, have often resisted these plans.[5] South Africa's trade policy towards other African countries shows similar tendencies. After its shift to democracy in 1994, South Africa developed a relationship with other Afri-

3 For stylistic reasons this study uses the term 'BLNS' to avoid the wordiness of repeated references to the BLNS countries.
4 European Commission (1996).
5 Moshoeshoe (2003: 55).

can states in which both development objectives and trade liberalisation were emphasised.

In view of these ambitious liberalisation objectives by the EU and South Africa, and considering the substantial ACP resistance against reciprocal free trade, an assessment of the BLNS states' case can deliver useful information. SACU is virtually the first region within the ACP area to go along with the EU's EPA plans and the regional free trade structures that accompany it.[6] A study of parts of the negotiation process leading up to it clarifies what to expect from future free trade negotiations with other ACP sub-regions. This also brings greater rigour into what to expect from the EU's EPA objective for the year 2008. SACU is currently negotiating free trade with the United States (US) and has recently concluded an FTA with the European Free Trade Association (EFTA). Negotiations for similar agreements with the Mercado Común del Sur (Mercosur), India, China and Nigeria are progressing or are under consideration.[7] Explaining what bearing compensation payments have on the BLNS countries' trade liberalisation process makes it easier to frame expectations about the acceptance and design of these future SACU trade agreements.

Determining whether compensation aims at establishing economic adjustment or political compliance, reveals substantial implications for economic development in the BLNS countries. Installing trade liberalisation without adjusting economic structures hampers the BLNS economies' capability to cope with their new economic vulnerability. Production, employment and income losses as well as lower customs revenues lurk. Focusing on

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6 ECDPM (2001c), ERO (2003d: 3). In similar ways, the SACU-US FTA that is currently under negotiation is considered a model for future agreements between the US and developing countries in Africa and elsewhere. See USTR (2003b).

7 Meyn (2003: 1), Kirk & Stern (2003: 16), McCarthy (2003: 621-27).

political compliance indicates widely existing scepticism. Alternatively, adjustment of economic institutions is unlikely to be successful if political acceptance is not properly addressed. Factors such as political leadership, ownership, accountability and a long-term vision are crucial for building institutions that promote economic development.[8]

The role of financial compensation as a subset of trade relations is not always very open to the outside world. Assessing compensation payments unveils some of the tools that trading partners use as part of negotiations on trade liberalisation. In this light, South Africa's role as a regional partner promoting regional cooperation through a combination of development assistance and trade liberalisation is discussed. The role of the BLNS states shows how less wealthy and diplomatically weaker nations act when faced with the negotiating tools of stronger trading partners.

Existing research

Since the economic shocks of the early 1980s, development thinking focusing on the domestic market has increasingly been replaced by theories that promote an opening up to external markets. Freer trade is expected to create a better allocation of resources and to promote export-orientated investment, leading to higher economic growth and development in the South.[9] Over the past three decades, Latin American and especially Asian countries have experienced substantially larger growth and have become more integrated into the global economy. As a result, trade liberalisation has now grown to be an important focus for African countries too. Many blame the continent's relative under-

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[8] Szepesi (2004).

[9] Dollar (1992), Ben-David (1993), Sachs & Warner (1995), Edwards (1998), World Bank (2002).

performance since the 1970s on extreme government interventions in external trade and encourage further trade liberalisation with the North.[10]

The so-called Washington Consensus of the early 1980s constituted a shift in economic policies by developed country governments. The donor community agreed to strive for macroeconomic stabilisation in the South by pressing for the removal of trade barriers and the elimination of government-imposed distortions in the economy.[11] Today, those involved continue to debate whether African governments have accomplished sufficient liberalisation of trade.[12] Most donors seem to support the view that trade in Africa is still insufficiently free. They therefore continue to push for enhanced liberalisation.[13]

One important instrument through which donors have promoted trade liberalisation with their African partners is development assistance. African governments have come under the influence of conditional aid, especially from the International Monetary Fund (IMF) and the World Bank. Other major individual donors, such as the EU, have set up similar structural adjustment programmes.[14]

In spite of ongoing disagreement about the effectiveness of aid as an instrument for creating economic development,[15] most donors have maintained their aid policies and have tried to bring these in line with their trade liberalisation agenda.[16] Substantial parts of development assistance have come to focus on trade-

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[10] Sachs & Warner (1997), Wang & Winters (1998), Collier & Gunning (1999), Block (2001).

[11] Williamson (1990), Haggard (1995), Stiglitz (1998), Leonard & Straus (2003).

[12] Rodrik (1999), Sachs (2000), World Bank (2000).

[13] Lavergne & Daddieh (1997), Hammouda (2004: 3).

[14] Haggard (1995), Mailafia (1997).

[15] Burnside & Dollar (2000), Hansen & Tarp (2000), Easterly, Levine & Roodman (2003), Clemens, Radelet & Bhavnani (2004).

[16] Mailafia (1997), World Bank (1998), IMF Staff (2002), Radelet (2005).

related capacity building in developing countries; the ‘aid for trade’ policy.[17] Since compensation payments can cushion various effects of trade liberalisation these can also be grouped under trade-related aid.

Much of the existing literature on liberalisation-based compensation payments focuses on developed countries and discusses the best ways to compensate groups that are harmed by a move to freer trade.[18] A smaller body of literature discusses the various approaches to Trade Capacity Building (TCB) as part of liberalisation in developing countries.[19] These studies warn of using such TCB programmes as ‘a sweet pill to swallow bitter market liberalising prospects’. They do not, however, attempt to scrutinise the specific compensation programmes that accompany already accomplished FTAs. This study places compensation in the above-described context of North-South trade liberalisation and asks how these payments have been used to advance trade liberalisation in the case of the BLNS states and the EU-South Africa FTA. Because compensation payments as a subset of trade relations are not always very transparent to the outside world, studying the exact way aid is used in the process of introducing trade liberalisation can be difficult. This study draws on official documents and personal interviews with public officials to fill this gap.

Amongst the existing research on North-South trade liberalisation, assessments of the use of financial compensation are underdeveloped. This might be due to a prevailing focus on and the popularity of liberal thinking. Liberal thinking assumes that international support for trade liberalisation is easily accepted by states seeking development through trade. However, liberalism

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17 Prowse (2002), Jacquet (2002), World Bank (2002), WTO/OECD (2004).
18 Wong (1997), Davidson & Matusz (2004).
19 Solignac Lecompte (2003), Szepesi (2004), Powell (2002).

does not always explain the particular ways in which both the EU and South Africa have used financial compensation to offset the drawbacks of the TDCA as experienced by the BLNS states. This study aims to assess this emerging relationship between trade liberalisation and financial compensation. Including financial compensation as a factor in the process of BLNS countries' trade liberalisation and explaining the aims of such compensation provides a more complete image of trade relations between the EU, South Africa and the BLNS countries.

Intended contribution

Two opposing views can be used to position and understand compensation for North-South trade liberalisation. Financial support can be regarded as easing transitional economic adjustment costs that accompany the introduction of liberalisation, such as the transformation of taxes, domestic industries and judicial regimes. The opposite perspective, rather than focussing on economic adjustments, emphasises the role of financial compensation in creating political compliance. A high dependence on foreign funds makes it difficult for developing country governments to refuse these compensation payments.[20]

The former view, which considers compensation as easing transitional costs, fits well within a liberal perspective. The theory of liberalism argues that the bulk of economic development is accomplished by the introduction of free trade itself. Financial compensation is necessary only temporarily and is linked to overcoming specific problems of economic adjustment.

The other interpretation of compensation corresponds closely with a realist perspective. According to realism, trade liberalisation is a highly politicised process in which states seek access to foreign markets, while conceding as little access as possible to

[20] Kanbur (1998), Elbadawi (1999), Mshomba (2000).

their domestic market. Here financial compensation serves mainly as a political 'sweetener' to gain acceptance of a trade agreement by one or more states that might otherwise see that agreement as unpalatable.

In the past, both political and economic objectives have influenced the disbursement of aid.[21] In similar ways both sufficient political support and accommodating required institutional adjustments are essential when introducing free trade. This study shows to what extent compensatory payments reflect this dichotomy. It examines four different EU and South African compensation programmes to the BLNS states and seeks to find how these payments serve either or both objectives. Since both a lack of economic adjustment and non-compliance in their own ways hamper the successful implementation of trade liberalisation, the specific design of compensation payments can have a direct bearing on economic development. Especially when adjustment aims are replaced by political motives, economic development becomes contaminated.

Research approach

Compensatory aid can supply funding for specific economic adjustment measures or function as a political sweetener for those who lose out because of trade liberalisation. To determine how compensation to the BLNS countries conforms to these two roles, this research looks at four characteristics of these payments: the term at which compensation is offered; its targeting to specific areas; how much money is involved; and the issue of being tied to the EU-South Africa Trade, Development and Cooperation Agreement (TDCA).

21 Schraeder, Hook & Taylor (1998), Alesina & Dollar (2000).

The term at which compensation payments are offered is one criterion that helps to determine the approach best suited for explaining the nature of compensation payments. If financial assistance only helps the BLNS countries get through a specific period of adjustment after which these payments will be discontinued, easing economic adjustment seems to be the more prominent goal. This approach loses credibility when the term of compensatory aid is not decided on the basis of a calculated adjustment period. In such situations, the term of funding is either open-ended or too short to accomplish the goals of economic adjustment. When the term is decided on the basis of accomplishing political acceptance for free trade, compensation is provided either on a one-off or on an open-ended basis depending on the specific political demands.

Similar inferences can be made concerning the targeting of compensatory payments. The more the funds are directed to specific sectors that are adversely affected by the implementation of free trade, the stronger the economic adjustment argument. However, if compensation is supplied as a lump sum of money transferred to the respective BLNS governments, the opposite idea of the EU obtaining political support for a free-trade relationship becomes more plausible.

Regarding amount, a realistic match between the size of compensation and the economic objectives of a compensation programme supports the economic adjustment view. When a compensation programme holds economic adjustment aims for which the amount is inadequate or excessive, compensation comes more in line with conditions for securing political support.

According to liberal theory, the economic benefits of more open trade alone, perhaps supported by minor forms of policy adjustment, should be sufficient to create the acceptance of trade liberalisation. If compensation is offered on the condition of free trade acceptance, it should be done in combination with a well-defined commitment to targeted adjustment measures. However, when compensation payments are disbursed solely on the condition of free trade acceptance, independent of other criteria such as economic targeting, the opposite view gains credibility. Linking compensation to TDCA acceptance without attaching a commitment to targeted adjustment measures means using financial pressure directly to enforce the acceptance of free trade.

If a compensation programme's main purpose is to ease economic adjustment, its term, targeting and amount are calculated and specifically determined on the basis of economic adjustment goals. Its linkage to TDCA acceptance is accompanied by adjustment policies. These characteristics indicate the EU's and South Africa's intentions of using compensation payments as a form of additional economic support to help pave the way for creating free trade with the developing world. They showcase a North-South relationship in which the importance of the developmental aspects of free trade is promoted by the advanced industrialised states and willingly accepted by the developing world. This outcome corresponds with a political theory of liberalism. A compensation programme that conforms to these criteria also implies that the 'aid for trade' paradigm, which sees aid as having to provide economic support for free trade development, would be endorsed. Since institutional support for economic adjustment to trade liberalisation is greatest under these circumstances, the possibility that free trade will create economic development is also enhanced.

If compensation payments match a political acceptance approach, then the term, targeting, amount and tie to the TDCA are unrelated to economic adjustment. These aspects are more closely related to attracting the political support of governments. Correspondence with this interpretation indicates that, to a certain extent, governments in the BLNS states have objections to the introduction of free trade. Support for free-trade thinking as propagated by western actors is not fully shared by the BLNS governments. Such resistance is overcome by offering financial aid to those that make the decisions on economic policy in the developing world. This perception fits well within a theory of realism. Within a perspective that focuses on securing political acceptance, the role of aid to stimulate economic changes, which the ‘aid for trade’ paradigm promotes, would be contradicted. If the majority of compensatory funding goes on creating political acceptance, less money will be left for institution building. A solid basis for the introduction of free trade will thus be affected, making it more difficult for free trade to effectively add to economic development. Finally, a certain design would also signal an important political vulnerability of BLNS governments.

The possibility exists that these two views overlap between various TDCA-related payments or between different criteria of a single compensation programme. The four criteria mentioned here help to determine how the two theories relate to each other and what the exact nature of this compensation is.

Methodology

Botswana, Lesotho, Namibia and Swaziland are all part of SACU and are thus experiencing the same sudden access of the EU into their economies. The BLNS states are therefore treated equally for the purpose of this study. Their shared dependence on South Africa as a major regional economic actor and SACU partner with a strong influence on their economic policies in the past and the present adds to this belief. Their exemplary position as a whole for other ACP regions further justifies why the four BLNS countries are regarded as one case as far as possible. However, in those situations in which differences are relevant to the argument this research tries to make, it differentiates amongst the four states.

With the help of the method of process tracing this study shows how the EU and South Africa have acted in recent trade negotiations with each other and with the BLNS states. In process tracing the chain of events that links the causal factor of a hypothesis to its outcome is studied. Evidence is provided for each step within that chain.[22]

The information for this case study derives from personal interviews with public officials, primary government documents and existing studies. For information on trade liberalisation in the BLNS states and EU and South African influence thereon, this paper draws mainly on existing studies. Regarding compensation payments, primary EU, South African, BLNS states and SACU government documents are used. Existing research and media documentation help to further underpin this information. Finally, personal interviews with EU and South African government officials involved with the negotiation and implementation of the TDCA and with independent researchers on Africa's political economy help to add new views and support existing opinions.

The BLNS states can be considered both typical and atypical for a larger group of countries. They are atypical regarding their long history as a customs union and the remarkable effectiveness of that union. This places the BLNS countries ahead of other regions in the ACP area in terms of regional economic integration. On the other hand, all ACP members are currently renegotiating their trade relationships with the EU towards more enhanced reciprocity, functioning along regional lines. Their stronger and further developed relations with the EU and South Africa make the BLNS countries a good test case for large parts of the rest of the continent. Their customs union with South Africa is

[22] Van Evera (1997: 64).

also regarded by some as a building block for the larger SADC area.[23] This makes a study of the BLNS countries relevant to a broader set of cases, particularly to other ACP countries.

The appendix presents a technical framework for the methodology used for this study. It divides the case study into a number of variables and discusses their relationship to each other on the basis of a causal diagram. The methodological framework also expands on the class of relevant cases and the positioning of the BLNS states within that group.

Chapter 2 examines the impact of Western economic pressure to liberalise on the shifts in BLNS states' trade policies. An overview is given of the past and present relationship between the EU, South Africa and the ACP states. The main focus is on the effects of the TDCA on the BLNS states. The following chapter examines the relationship between compensation payments and international pressure to liberalise. It outlines four different compensation programmes and scrutinises their contents. Finally, Chapter 4 uses the two opposing models to assess the compensation programmes and their implications for trade and aid relationships between the EU, South Africa and the BLNS states.

[23] Gibb (1997: 68).

2

Trade liberalisation and Western pressure

Trade policies since the 1980s have shifted globally towards enhanced forms of liberalisation. This chapter examines the impact of Western economic pressure to liberalise on the shifts in the BLNS states' trade policies. A discussion of the role of various BLNS partners in the international trading system and an assessment of their visions, instruments and actions gives an impression of how western leverage operates. This chapter begins with an assessment of how trade liberalisation since the 1980s has shifted globally. It then examines the relationship between the EU and Africa. An overview of the history and nature of EU development cooperation helps to determine the pressure on ACP countries to liberalise over time. Whether South Africa uses inducements to achieve the relaxation of trade barriers is assessed thereafter. The effects of the TDCA and the new SACU agreement on Botswana, Lesotho, Namibia and Swaziland further discloses the impact of trade liberalisation pressure by the EU and South Africa.

Trade, aid and the neo-liberal era

From the mid-1980s onwards, western countries have increasingly emphasised greater and a more reciprocal reduction of trade barriers. At roughly the same time a change in global economic structures occurred that is often referred to as the globalisation of the world economy. New communication technologies, easier transport and faster financial flows made national borders less relevant. Transnational corporations working in a system of free trade became the focus of economic activity. And the liberal doctrine of non-intervention and the free play of market forces have received new interest.[1]

When the relaxation of border restrictions on trade and investment occurred in the 1980s, the remaining regulatory differences between developed countries suddenly became more significant. Advanced industrialised countries therefore sought to improve the integration of 'behind the border' policies. This more enhanced form of liberalisation, often referred to as deep integration, adjusts policies at a national level around an internationally negotiated norm and ranges from the harmonisation of standards to macroeconomic policy coordination.[2] Especially in Europe, the idea of deep integration has found a strong foothold.

As a result of this shift in trade policy, liberalising western powers have also come to consider free trade as a new basis for their relationship with the developing world.[3] The macroeconomic position that the developing states found themselves in during the 1980s laid the foundations for this movement. High balance of payments deficits and extensive amounts of foreign debt first created the need for policy change. When help was

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1 Burchill (2001).
2 Haggard (1995: 1-14).
3 Draper (2003: 6).

called in from the international financial institutions, a second incentive for reform, called conditionality, was introduced. The conditionality norm was used to promote further measures of trade liberalisation by developing nations in exchange for development assistance. This helped developed countries to enhance economic integration in the South.

Simultaneously, changes in the international regime governing world trade and investment also made it necessary for developing countries to start offering more concessions towards reciprocal forms of free trade. The emerging economic dependence that the 1980s brought about and the shifting trade relations resulting from this made deep integration become more salient in the South. Sub-Saharan Africa's relative economic unimportance has, however, stopped the North from stimulating high levels of deep integration in this region.[4]

The removal of trade barriers, or shallow integration, in Sub-Saharan Africa has by now reached a higher position on the agenda of the advanced industrialised states. It is argued that when trade restrictions are removed, the developed and the developing world economies can converge more easily than under a system of highly protected economies. These more highly integrated economies will then accelerate economic growth in the South. Those who want to overcome their position of underdevelopment, liberals argue, should follow the pace of globalisation and trade liberalisation.[5] The aforementioned financial dependence on international financial institutions during the 1980s has contributed importantly to the enhancement of free trade in the developing world. The structural adjustment programmes of the IMF and the World Bank that have been implemented in many developing countries since the 1980s have

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4 Haggard (1995: 12).
5 Lindert & Williamson (2001).

tended towards a neo-liberal approach.[6] By allowing nearly eighty per cent of all Structural Adjustment Loans to hinge on the concession of trade policy reform and macroeconomic stabilisation, the IMF and the World Bank have, more than most other actors, contributed to a higher level of shallow integration in the South.[7]

Following on from the ascendance of neo-liberal thinking, insufficient results from donor-related funding to Africa and the successful way Asian economies have managed to develop over the past twenty-five years without the help of large amounts of aid, development policies have gained popularity in which the improvement of trade, rather than the effectiveness of aid, is the focus of attention.[8] The so-called 'trade not aid' advocates that came to prominence in the 1980s argue that focusing on cash and project assistance is at best a distraction and possibly even harmful in terms of promoting prosperity. Keeping their markets open is therefore considered the best strategy the developed world can follow in order to support developing nations' economies. Governments of poor countries, in this view, should participate more actively in the global economy by removing barriers to trade and by eliminating government-imposed distortions in the economy.[9] Such measures of shallow integration could take place at the bilateral, regional or multilateral level. Constructing regional economic integration schemes amongst African countries is a prime objective of western countries that should help liberalise Third World trade policies and strengthen their economies.[10]

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6 Leonard & Straus (2003: 25).
7 Haggard (1995: 22-23).
8 Riddell (1987: 157).
9 Osborne (2002: 314).
10 Goldstein (2002: 12).

More recently, the donor community has made adjustments to its stance on the relationship between trade and aid and the 'trade not aid' debate. While free trade is still considered the main driver for development, the perception of aid as an instrument to accomplish trade liberalisation in the developing world has received more attention. Development aid is increasingly targeted towards the strengthening of export capacities. This means that development assistance now goes to trade-related essential services such as providing insurances, upgrading standards and assisting developing countries with certification. The maintenance of roads, ports and other transport infrastructure has also gained priority.[11] Even though the idea of an enhanced role for free trade is still eminent, practical considerations have meant that aid is considered an important driver of liberalisation. Stemming from this view, the motto 'aid for trade' is often heard.

Changes in EU and South African trade policies

An important western power that has promoted the liberalisation of trade over the last few decades is the European Union. Both between countries that are part of the EU and towards those outside the union, a strong move in the direction of the opening up of markets has emerged. Inside its boundaries, the free movement of capital, labour and products has constituted an enhanced form of deep integration. But also with regard to its external trading partners, the EU has pushed for free trade.[12] Stimulation to liberalise trade by the World Trade Organisation (WTO) has contributed significantly to this behaviour. The WTO demands the liberalisation of global trade in goods and services of all its members. Although the EU is generally seen to pursue

[11] Jacquet (2002).
[12] Lamy (2001: 15-16), McQueen (1998).

higher levels of free trade with other regions, it is also often blamed for its protective nature. Such criticism has come to focus especially on its Common Agricultural Policy (CAP).[13]

EU development cooperation

In post-colonial times, the European Union and its forerunners have been of great influence on the economic development of Third World countries, especially those in Africa.[14] Through its European Development Fund, it has awarded African countries substantial amounts of development assistance.[15] The EU has tried to spur economic development in Sub-Saharan Africa using direct financial donations, project and programme assistance, and preferential trading systems. Soon after the period of decolonisation, trade agreements on the basis of non-reciprocity became part of the larger development policy for the ACP region.

The 1963 and 1969 Yaoundé Conventions were the first major trade and development agreements to be forged between the EU and a large group of African nations. Under these conventions the European Economic Community (EEC) offered eighteen of the former French and Belgian colonies in Africa a combination of development aid and favourable trade policies.[16] In return, the EEC asked for reversed trade preferences and for the right to own commercial enterprises in these countries.

In 1975 African nations blocked attempts by the EU to negotiate a successor to the Yaoundé agreements. Many of them

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13 Halderman & Nelson (2004), Borell & Hubbard (2000: 18-26).

14 Grilli (1993: xiv).

15 However, this was not the beginning of development aid in general. Since the end of World War II individual countries in Europe had already started supplying development funds to countries which at that stage were still their colonies.

16 In 1992 the Maastricht Treaty transformed the European Economic Community (EEC) into what came to be called the European Union (EU).

Photo 1 Trade in Africa: Takoradi, Ghana
[Source: Audiovisual Library of the European Commission]

had grown sceptical about their economic bonds with the western world, which they perceived as a relationship of dependency based on the legacy of colonialism.[17] African plans for a New International Economic Order (NIEO) called for a change in the international economic system that would increasingly favour African and other Third World countries' economies.[18] In 1975 the first of four Lomé Conventions was thus signed between the

[17] Moshoeshoe (2003: 28).
[18] Haggard (1995: 101).

EU and forty-six African, Caribbean and Pacific (ACP) countries. This group would eventually expand to include seventy-eight members. Besides offering financial and technical cooperation through the European Development Fund and the European Investment Bank, the treaty now contained non-reciprocal provisions for free exports going from ACP states to the EU. This form of unilateral self-imposed free trade by the EU was introduced as a way of encouraging economic development in the ACP region. This trade relationship of non-reciprocity would eventually continue for twenty-five years, until the signing of the Cotonou Agreement in 2000.

The preferential conditions under Lomé extended progresssively with its three successors, Lomé II, III and IV. However with the beginning of the financial crisis in the 1980s, a shift away from project-based to policy-based financial assistance developed.[19] The 1984-1985 Lomé III negotiations showcased the initial steps in this process. A resolution on structural adjustment in Sub-Saharan Africa was adopted in 1988.[20] But only with the inception of Lomé IV in 1990 did it become clear that structural adjustment, instead of project purposes, as well as the development of the private sector were gaining ground as part of development cooperation policies.[21] When Lomé IV expired in 1999 and a new trade and development treaty had to be negotiated, the EU called for serious changes that matched a more liberal stance on trade and development. The non-reciprocal free-trade relationship that had been introduced in the 1970s was now to be abandoned. This eventually resulted in the Cotonou Partnership Agreement of 2000.

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19 Mailafia (1997: 86).
20 Ibid: 94.
21 Haggard (1995: 102).

Photo 2 Paul Nielson, European Commissioner for Development and Humanitarian Aid from 1999 to 2004

[Source: Audiovisual Library of the European Commission]

The Cotonou Agreement

The Cotonou Agreement is a framework for future negotiation, not a long-term trade and development treaty, which the Yaoundé and Lomé conventions were.[22] During negotiations it was agreed that the EU and the ACP nations would start developing a relationship on the basis of complete trade liberalisation. This primarily meant a shift towards more reciprocal methods of trade.

The foundations for the Cotonou Agreement had been laid four years earlier, in 1996. In that year the European Commission published a document under the title *Green Paper on Relations between the European Union and the ACP Countries on the Eve of the 21st Century: Challenges and Options for a New Partner-*

22 ECDPM (2001d).

ship.[23] The paper formulated new guidelines for the EU's trade and development policies with the ACP. It then became clear that the EU was to adopt enhanced forms of neo-liberal thinking. It pursued the liberalisation of trade relations with its developing world trading partners. Trade and a relationship of enhanced shallow integration became its primary strategy for the enhancement of economic development and the fight against poverty in Africa.[24]

With the emergence of globalisation and the popularity of neo-liberal thinking in the 1980s, the EU came to consider it essential that a shift in trade and aid relations with the ACP region occur. Many ACP countries had by then grown highly dependent on the trade and development aid provisions of the Lomé treaties.[25] As large groups in the North came to consider past aid-flows as mainly unsuccessful – a phenomenon sometimes referred to as 'donor fatigue' – a call for changing relations developed. Alongside the then-burgeoning 'trade not aid' debate, the EU called on ACP countries to take greater responsibility for managing their own economies. This was to reduce their dependency on the large sums of development aid that they had received since the beginning of Lomé I.

Global sentiments on the enhanced liberalisation of trade that then emerged shifted the rules of the multilateral trading system. This again influenced EU-ACP relations. The General Agreement on Trade and Tariffs (GATT), and later the WTO, requested a new EU-ACP trade agreement that was compatible with many of those rules. Article XXIV of GATT, which deals with trade arrangements between developing and developed

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23 European Commission (1996).
24 EU (2003).
25 Bocquet & Guiltat (1998: 7).

nations, called for the introduction of trade on a basis of reciprocity.

During the mid-1990s these various incentives led the European Commission to fundamentally reconsider its relationship with the ACP region.[26] Eventually, in 1996, the Green Paper on relations between the European Union and the ACP was released, launching a new vision of trade after Lomé IV.[27] The paper's primary focus was on the need for WTO compatibility and reciprocal trade.[28] Succeeding the provisions under GATT, all WTO members agreed to strive for higher levels of global free trade. Binding commitments were made to improve market access between states within a set time-frame. Therefore, when talks about a successor to the Lomé treaty started in 1998, the Green Paper formed the basis from which to negotiate for the EU.

In June 2000 the EU and ACP states signed the Cotonou Partnership Agreement in Cotonou, the capital of Benin. This was not an actual agreement but instead a framework for negotiations to be continued at a later stage. It focuses on the issue of moving from non-reciprocal to reciprocal trade, as is compatible with WTO requirements. Both parties, the EU and the ACP region, have requested a waiver from the WTO to last until January 2008, when a new WTO-compatible agreement must be in place.[29] Till then, the current non-reciprocal tariff preferences shall remain in place.

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26 Le Pere (2000: 1-4).

27 The European Commission publishes Green Papers and White Papers. The former are discussion papers on a specific policy area and are meant to open up a debate amongst all interested parties. White Papers contain specific proposals for EU action in a certain area and are meant to lead directly to policy development.

28 Thomas (1997).

29 Van Hove & Bilal (2002).

In the intervening time the EU aims to gradually establish reciprocal free trade with the ACP region. All ACP countries may opt for either an individual trade relationship with the EU or a collective trade relationship under which they operate as a regional grouping, the so-called Economic Partnership Agreements (EPAs).[30] The latter option has received most attention and is preferred by the EU.[31] The EU considers most African economies too small to be able to effectively compete with those of developed countries.[32] EPAs, it argues, enable developing countries to confront the problems of exclusion caused by globalisation more effectively. These regional agreements stimulate the economic, regulatory and institutional reforms that improve the investment climate in ACP countries and enable private-sector development. The EU also expects EPAs to enhance the involvement of women in economic, political and social life. They encourage sustained economic growth, increased competitiveness, the creation of productive jobs and better access to social services such as health, education and training.[33]

Least Developed Countries (LDCs) are exempted from the shift towards reciprocity. They may choose either to accept the new standards of trade or to stay with the old non-reciprocal preferences. Whichever the LDCs opt for, they will maintain free access to the EU market for all products except arms.[34] Although the LDCs might seem better off under non-reciprocity, the benefits are likely to outweigh the costs. Besides market access, EPAs also include agreements on services and other trade-related

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30 Economic Partnership Agreements (EPAs) were initially called Regional Economic Partnership Agreements (REPAs). There is, however, little difference in the form and function of the two. See ECDPM, ‘Regional Economic Partnership Agreements’. See ECDPM (2001c).

31 ECDPM (2001d).

32 Asante (1997: 17).

33 Le Pere (2000: 4).

34 ECDPM (2001c).

issues, which are not included under the non-reciprocal provisions. Benefits typical to regional integration, such as attracting investors, can also improve economic conditions for LDCs.[35]

Besides a trade chapter, the Cotonou Agreement also offers an aid protocol. The European Development Fund (EDF), the EU's main financial instrument for development cooperation, and the European Investment Bank (EIB) will provide funding for the ACP region's economic adjustment to trade liberalisation. In July 2003 for instance, a €50 million trade capacity-building programme called Trade.Com was launched for the ACP countries.

Negotiating the transformation towards a reciprocal EU-ACP trade agreement is likely to continue until the end of 2007. This process has been divided into two phases. During Phase I the various parties negotiated a broad framework at the all-ACP level. Phase II, which started in 2003, is now being negotiated at the regional level. By 2008 the Lomé Agreement should be replaced by reciprocity for all non-LDCs and the group of LDCs that have chosen to join the EPA plans.

EU liberalisation pressure

Economic integration with advanced industrial states means having to adjust profoundly to developed countries' economic policies. Developing states have therefore not always wholeheartedly embraced trade liberalisation.[36] ACP countries too have often uttered their disapproval of the EU's intention to relinquish non-reciprocal trade. They have been reluctant to abandon the trade preferences that they received for more than twenty-five years under the various Lomé treaties. Open borders were considered tantamount to enhanced competition from the technologically more advanced economies in the North. Fearing the

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[35] Van Hove & Bilal (2002).
[36] Haggard (1995: 4-5).

global move towards trade liberalisation and possible exploitation, ACP governments initially expressed their desire to broaden preferences with the EU.[37]

The EU, however, pursuing the acceptance of its reciprocity plans, has had the advantage of several leverages. One concerns the aid component that traditionally accompanies trade agreements between both parties. During the Cotonou negotiations it soon became clear that the EU intended to scale down its budget for development assistance, which has been substantial since the beginning of Lomé. Many developing countries are in dire need of financial help but their high dependence on foreign funds often creates a situation in which they are willing to abide by the policy demands of developed countries.[38] Tying aid to policy changes has been called the conditionality norm.[39] At the 1990 Lomé IV Agreement a strong form of conditionality was introduced in EU-ACP relations and when the Cotonou negotiations began, the EU expanded its use. Not immediately deciding how seriously to cut its aid programme, it offered the ACP states the possibility of keeping reductions low in return for concessions in the trade chapter.[40]

To promote ACP acceptance of the new trade provisions, the EU has often argued that WTO compatibility is imperative. If no agreement was signed, a new waiver from the WTO would no longer be obtainable. However, since the conclusion of the agreement, this argument has repeatedly been contested. Former WTO Deputy Director Miguel Rodriguez Mendoza declared in 2000 that no existing WTO rule would make it necessary for EU-ACP trade relations to shift from the Lomé conventions to

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[37] Libreville Declaration: adopted by the first summit of ACP heads of state and government. Libreville (November 1997).

[38] Mshomba (2000: 188).

[39] Haggard (1995: 21).

[40] Schilder (2000: 24).

reciprocal free trade agreements.[41] The EU has, therefore, been said to uphold self-defined criteria for WTO compatibility. Its focus on the EPA initiatives makes it difficult for ACP states to determine what opportunities for WTO-approved reciprocal trade exist outside these agreements.[42]

During the negotiating process the EU hardly diverged from the propositions that it initially made in its 1996 Green Paper.[43] It was in the position to do so as the ACP group in many respects formed a disparate negotiating partner. The EU's political bargaining power had accumulated over a period of almost forty years and by the time of the Cotonou talks significantly outperformed that of ACP countries.

The various strengths and leverages constituted a powerful tool which the EU could use to influence ACP trade policies. Within an environment of high financial dependence on the North, stemming from the debt crisis of the 1980s, developing countries in Africa have become seriously vulnerable to developing-country pressure. The EU thus effectively advanced shallow integration by the ACP region. Although not always preferred, the ACP states were left little choice but to accept most EU propositions. Many similarities exist with the trade and aid relationship which South Africa has developed with its African partners.

South African trade liberalisation after apartheid

After South Africa's first free elections in 1994, the newly formed government faced important decisions regarding reshaping its economy. The apartheid regime had introduced a system of import substitution industrialisation under which South

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41 Ibid: 12.
42 Bilal & Rampa (2006).
43 Moshoeshoe (2003: 98).

African industries were protected by high tariff structures.[44] Exclusion from several Preferential Trade Agreements and international trade sanctions stemming from global anti-apartheid policies led to the need to do so.[45] After 1994, when South Africa was released from the apartheid-era trade restrictions, the new government had to redefine its future trading relations. Choosing a policy that was closer to free trade or one that favoured protectionism became the main topic of debate.[46]

Since that time, South Africa – with the Department of Trade and Industry (DTI) as its prime driving force – has clearly opted for a trade policy with liberalisation influences.[47] To promote its integration in the global economy, from which it had long been ostracised, the DTI considered scaling down South Africa's high trade barriers as a priority. In 1996 the Growth, Employment and Redistribution (GEAR) strategy was thus launched. GEAR is an export-oriented macro-economic programme that has tariff liberalisation as one of its main objectives.[48] South Africa actively pursues the implementation of WTO trade rules and it has been said to execute these even faster than is required.[49] The Trade, Development and Cooperation Agreement (TDCA) that was concluded with the European Union in 1999 serves as a good example of South Africa's efforts towards enhanced free trade.

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[44] Draper (2003: 19).
[45] Bezuidenhout (2002).
[46] Draper (2003: 1).
[47] Ibid: 2, COSATU (2000), Hentz (2005).
[48] COSATU (2000: 113).
[49] Others, such as Peter Draper, argue that South Africa is not pursuing trade liberalisation any faster than it is obliged to according to the provisions of the Uruguay Round of the WTO. Draper does, however, agree that South Africa is supporting the lowering of trade barriers in the SADC region. See Telephonic interview with Peter Draper, research fellow of the 'Development through trade project' at the South African Institute of International Affairs (SAIIA). Pretoria, Leiden (August 2004).

The advent of a new South African government also marked a new beginning for enhanced African economic cooperation. In recent years, South African government officials have increasingly travelled the continent to settle violent disputes and to forge stronger political and economic links in Africa. In 1998 South African President Thabo Mbeki gave a speech at the United Nations University in Tokyo entitled 'The African Renaissance, South Africa and the World',[50] in which he spoke of new ambitions for Africa's development that were to be pursued through a communal African economic programme. This would help the continent to lift itself out of its position of economic exclusion from the rest of the world.

Photo 3 South African President Thabo Mbeki and President of the European Commission Jose Manuel Barosso
[Source: Audiovisual Library of the European Commission]

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50 Mbeki (1998).

Mbeki's ideas of an African Renaissance formed an important stepping stone for the New Partnership for Africa's Development (NEPAD).[51] This action plan, presented in 2001 and for a large part designed by South Africa, also aims to bolster African economies by bringing the continent into the world trading system and the global economy.[52] The main areas that NEPAD focuses on are peace and security, democracy and governance, economic and corporate governance, human resource development, infrastructure and the diversification of production and exports.[53] Economic models closely related to neo-liberalism are considered to form the basis of these ambitions.[54]

During the 1980s, similar programmes to revitalise Africa's economy focused mainly on extensive forms of collective self-reliance. NEPAD, however, sees the solution for Africa's problems in a market model with high levels of free trade at its core. The globalisation of the world economy is considered to have made it both possible and necessary to integrate further into the global economy.[55]

The renewed western development strategies of open trade and further economic integration with the developing world have meant that NEPAD has received extensive political support from western donor countries.[56] Various initiatives that the programme mentions correspond with EU plans to enhance economic development in the ACP area. Its regional integration initiatives clearly correlate with the EU's goals for Economic Partnership Agreements (EPAs). Although many African leaders foresaw large potential for new financial support through NEPAD, the

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[51] African Union (2001).
[52] Ibid: paragraph 28.
[53] Goldstein (2002: 25).
[54] Melber (2003: 4).
[55] Hope (2002: 394).
[56] Group of Eight (2002).

substantial promises for larger aid packages have so far failed to materialise.

There are various reasons why NEPAD envisages enhanced regional economic integration in Africa. Regional integration enlarges markets, which makes it easier to attract foreign investment. Intensified regional cooperation is also likely to improve the infrastructure between countries, creating a better environment for trade between African trading partners. With larger markets, competition increases, thus lowering production prices. Larger markets also allow African countries to gain political and economic power, rendering governments less dependent on the developing world. Lastly, working together on a regional basis decreases the chances of national and international conflicts.

South Africa, in conjunction with a small group of other African states, has taken the lead in developing the NEPAD initiative, making it one of NEPAD's strongest adherents.[57] The present government is encouraging states continent-wide to implement NEPAD and regional integration is one of South Africa's priorities within NEPAD. The regional cooperation agreement that it is focusing most on concerns the group it is a member of itself, the Southern African Development Community (SADC). In 1996 a free-trade protocol was signed between eleven of the SADC countries. A Free Trade Agreement (FTA) between the member states was scheduled to be established within a period of eight years.[58] There are plans are to install a customs union by 2010, a common market by 2015, a monetary union by 2016 and a single currency by 2018.[59]

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57 Gelb (2001: 25).

58 As of 2006, the FTA has still not been established. Estimates are that it will take until 2008 for 85% of goods within the region to become tariff-free. The Free Trade Area is now supposed to be fully in service by 2012. *Mail & Guardian* (2006b).

59 *Mail & Guardian* (2006c).

Map 1 The Southern African Development Community (SADC) area

Enhancing the efficiency of SADC – to which the BLNS states also belong – matches South Africa's liberalisation objectives as well as its regional development goals. By introducing asymmetrical free trade in the SADC region and by offering support to the strengthening of neighbouring economies, South Africa synchronises growth throughout the region with its national growth objectives.[60] South Africa regards support for regional integration as an incentive for economic development in the entire region, a phenomenon sometimes called developmental regionalism.[61] It has called market integration the 'key driver for development'.[62] This type of development through trade shows a clear link with the 'trade not aid' philosophy.

Enhancing regional integration directly benefits South Africa's national interests. Since SADC is South Africa's largest export market, lowering trade barriers through regional integration can be very advantageous. It enlarges South Africa's domestic market, giving producers greater potential for exporting to countries within the region.[63] The SADC FTA could also lead South Africa to pursue trade agreements with other developed and developing regions. Such objectives, however, would not necessarily benefit the rest of the SADC members.[64] Because South Africa is relatively wealthier than its partners in SADC, it is better protected from the effects of open trade barriers than the rest of the region.

These risks for other SADC members, as well as the perception that South Africa is primarily concerned with its own well-being, have led some to argue that South Africa's regional

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60 Nkuhlu (1997: 80).
61 Tsie (2000: 11).
62 *Mail & Guardian* (2006b).
63 Draper (2003: 10-11). Between 2001 and 2005 South African exports to other Southern African states rose from Rand 215 billion to Rand 320 billion. *Mail & Guardian* (2006b).
64 Goldstein (2002: 12-13).

integration attempts are, in fact, a way of dominating the continent.[65] South Africa's GEAR strategy shows a strong preference for private-sector capital in the region and is supported by various regional integration programmes. Its relative abundance of corporate capital has led to fears of South Africa dominating regional economies.[66] Meanwhile, Structural Adjustment Programmes (SAPs) – agreed by the World Bank, the IMF and six of the fourteen SADC countries – are also promoting trade liberalisation throughout the region.[67]

South Africa plays an influential role within the Southern African Customs Union. With its history of economic dominance in the region, South Africa has long exercised substantial control over SACU trade policies.[68] Since the end of apartheid, the South African government has pushed for trade liberalisation in the entire SACU area.[69]

South Africa's economic power in comparison with its regional partners enables it to have extensive influence over the region's economic policies. This is irrespective of whether South Africa's ideological intentions are focussed on its own national or on regional interests. Support from the EU further increases such pressure.[70]

In June 2006 the EU and South Africa adopted a Strategic Partnership agreement that, according to the EC, would 'move political relations between the EU and South Africa from regular

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65 See, for instance, Bond (2002), Melber (2003), Tsie (2000) and Gelb (2001).
66 Tsie (2000: 17).
67 Besides Lesotho, the Southern African Customs Union countries were exempted from having to implement adjustment programmes by the World Bank. See Clapham (1996: 171).
68 McCarthy (2003: 618).
69 Gibb (1997: 84), Kalenga (2000: 6).
70 For instance, in the 2000 Multi-Annual Indicative Programme between the EU and South Africa, the EU promises funding to South Africa for increasing regional cooperation initiatives.

dialogue to intense strategic cooperation, as both share many objectives on regional, pan-African and international issues'.[71] The agreement reflected their intention to strengthen communal efforts in promoting economic development on the rest of the continent. European Development Commissioner Louis Michel was quoted as saying that 'Together, we promote, for instance, peace, good governance and regional integration through the African Union. This strategic partnership between the EU and South Africa will allow us to work even more closely together at regional, continental and global levels to support Africa meet its development goals.'.[72]

Since South Africa maintains trade policies that are quite liberal, it regards similar liberal programmes preferable for the entire SADC region.[73] The signing of the Trade, Development and Cooperation Agreement (TDCA) with the EU can be seen as one such step in pressurising the region to enhance trade liberalisation.

The Trade, Development and Cooperation Agreement

The liberalisation policy that South Africa adopted after 1994, and which was formalised most clearly in the 1996 GEAR programme, has importantly influenced its trade policy. One prominent spin-off has been the EU–South Africa Trade, Development and Cooperation Agreement (TDCA).

During long stretches in the apartheid years, South Africa faced measures of trade discrimination by its foreign trading partners. Imports were boycotted internationally and embargoes were imposed on the trade of arms and oil. South Africa's shift to

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71 European Commission (2006), Commission proposes to upgrade EU's relations with South Africa to a Strategic Partnership. Press release, Brussels (28 June 2006).

72 Locit.

73 Tsie (2000: 17).

a democratically elected government in 1994 meant an end to these boycotts. A strong will emerged amongst European countries to support the Mandela leadership and to encourage economic growth. A new EU–South Africa trade relationship, so it was argued, would help the young democracy develop.[74] As the EU was then, and still is, South Africa's largest trading partner, constituting a new trade agreement with the EU was considered pivotal.[75] Therefore, in 1995, shortly after the elections, trade negotiations started.

Because both parties adhered to tariff-liberalising policies, it was logical that the new agreement would be based on these same principles. Although initially South Africa expressed its desire to be included in the Lomé treaty and hence be offered terms of non-reciprocity, it soon had to drop these intentions because of resistance from the EU. South Africa's dependence on the economically dominant EU gave the EU sufficient leverage to enable the acceptance of reciprocity. Both the EU's importance as a trading partner and the large amounts of funding it was to offer South Africa enhanced the conditionality norm. Reciprocal free trade became the point of departure for the EU and South Africa, although both parties soon began to strive for various exceptions. During the four years that followed many changes to the original negotiation mandates were made.

At the start of negotiations the EU had five main negotiating directives. The trade agreement with South Africa had to be WTO compatible; to cover development objectives; to respect the EU common policies; to be in coherence with other preferential agreements; and to take into account the impact it would have on the Southern African region.[76]

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[74] Davies (2000: 5).

[75] At the beginning of the TDCA negotiations in 1996, trade with the EU constituted 44% of South Africa's trade. See Jachia & Teljeur (1999: 21).

[76] Lowe (2000: 39-45).

The Trade, Development and Cooperation Agreement was to have both a trade and a development component. On the trade side, the EU agreed to remove approximately 95 per cent of tariffs on South African exports. The elimination of these tariffs, mainly on industrial products, would develop only gradually. A period of ten years was foreseen, beginning from the start of the TDCA in the year 2000. On agricultural products, however, the EU insisted on a relatively strict policy. Although it did offer some concessions, the Common Agricultural Policy, which grants large subsidies to EU agricultural exporters, would still seriously affect South Africa's trade in agricultural products.[77] On the South African side, approximately 86 per cent of tariffs were to be phased out within a maximum period of twelve years. Because the parties faced very different levels of development, the final agreement contained a structure of asymmetry and differentiation. The European Union was to phase out its tariffs sooner and to a higher extent than South Africa.

The TDCA has opened up new trading possibilities for South Africa and many opportunities for trade expansion have emerged, especially for industrial products. This has created a more favourable environment for establishing new industries and for attracting investors who are looking for a platform to enter the European Union. In theory, this means that the region and SADC and SACU in particular also have new opportunities. However, disadvantages also loom. South Africa, SACU and SADC have now been forced to open up their economies to competitive EU products.

The EU holds that the TDCA's development component is the main reason for forging a trade agreement.[78] It expects direct economic benefits from free trade for South Africa. But besides

[77] Davies (2000: 9).
[78] Lowe (2000: 42).

free trade, the European Commission has also offered €125 million annually to South Africa under the European Programme for Reconstruction and Development (EPRD). It does so in addition to bilateral donations made by the individual EU member states. Most financial support comes in the form of grants and loans for development programmes. This aid marks the assistance side of the conditionality norm and demonstrates what South Africa has gained in return for its policy changes. The asymmetrical implementation of free trade can, of course, also be considered as part of the development programme.

Since the conclusion of the trade talks, much has been said about the contents of the EU-South Africa FTA. While both parties are breaking down barriers – the EU doing so more and faster than South Africa – critics say the influence of EU imports on South Africa’s market is much larger than that of South African imports on the EU market. They expect South Africa to experience its new vulnerability much more than the EU.[79] Moreover, many consider the differentiation in implementing reciprocity essentially unfair. Although the EU bans tariffs on more products, South Africa does so for more sensitive products. Furthermore, products excepted through the Common Agricultural Policy could also continue to harm South Africa.

The South African government realises that these economic changes can have detrimental effects. It, however, argues that the dynamic and geopolitical benefits of entering into a FTA with the EU outweigh the costs.[80] This might not be the case for the countries that South Africa already holds trade agreements with in its own region. Because of their economic integration agreement with South Africa, Botswana, Lesotho, Namibia and Swaziland face excessive damage from the TDCA.

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[79] Davies (2000: 10).
[80] Goodison (1999: 38).

TDCA effects on SACU

The Southern African Customs Union (SACU) is considered the oldest Customs Union in the world. Founded in 1910, SACU encompasses South Africa, Botswana, Lesotho, Namibia and Swaziland. The SACU countries experience free trade within the region and maintain common tariffs for external trade. To promote the domestic production of goods inside the customs union, these external tariffs until recently were kept relatively high.

One of the major concerns that critics of the Trade, Development and Cooperation Agreement expressed during the negotiations with the EU was the potential damage for Botswana, Lesotho, Namibia and Swaziland.[81] Their economic integration with South Africa through SACU meant that these countries are *de facto* incorporated into the TDCA. The BLNS countries expected various direct and indirect negative effects of the TDCA. The trade-related concessions that South Africa was to make to the EU, were considered relatively more harmful to the BLNS. The liberalisation of trade with the EU is a much bigger shift for the BLNS countries than it is for South Africa.

The TDCA forced the BLNS states to eliminate thirty per cent of tariffs on products coming from the EU. Meanwhile, the non-reciprocal Lomé trade agreement already provided them with very favourable arrangements for exports to the EU.[82] Therefore, unlike South Africa, access to the EU market would not improve for the BLNS states.[83] Lower tariffs on EU products would make the BLNS countries lose the ability to compete with cheaper EU products, especially in the highly subsidised agricultural and agro-processing sectors.[84] Stronger competition from EU products could also force SACU industries to lower their prices.

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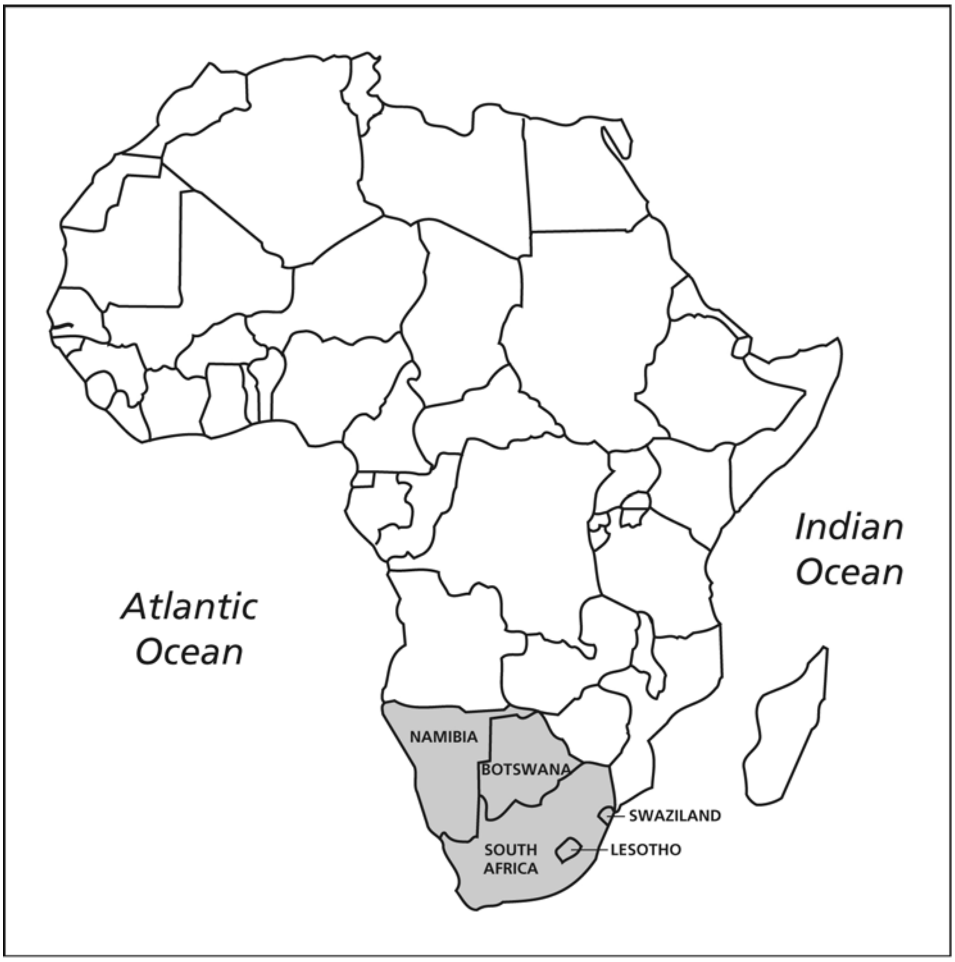
81 Panos (1998: 15-16), Goodison (1999), Mbekeani (1999), ERO (2001).
82 Ibid: 27.
83 Ibid: 41.
84 Ibid: 45.



Map 2 The five countries of the Southern African Customs Union (SACU)

That would drive investors towards foreign industries and markets with higher price levels. All this would lead to production, employment and income losses. Besides enhanced competition from the EU, South Africa – now facing the same tariffs for trade to the EU as the BLNS countries – potentially became a larger competitor as well.

Perhaps the most substantial effect of lower tariffs was the expected decrease in BLNS states' customs revenue. At the time of the TDCA negotiations, SACU contained a common customs and excise revenue pool. For levying customs no distinction was made between trade to South Africa or to any of the other SACU countries. South Africa was responsible for the collecting of these funds and their disbursal to the SACU members according to a fixed distribution code. Since in reality the majority of trade to the region goes to South Africa – the vast majority of BLNS imports come in via that country – the BLNS states have always been very dependent on South African trade customs.[85]

The BLNS countries rely heavily on the SACU revenue pool. In 1998, during the negotiation process, SACU customs were calculated to amount to 17.1 per cent of total government revenues for Botswana, 27.6 per cent for Namibia, 44.8 per cent for Swaziland and 41.7 per cent for Lesotho.[86] The implementation of the TDCA was expected to result in revenue losses of between Rand 1.6 billion and Rand 5.7 billion per year for the whole SACU region.[87] While for Botswana this meant a decrease of revenue of only 5.3 per cent, Namibia would be affected with an

85 Meyn (2003: 2).

86 Mbekeani (1999: 55). By 2001 these numbers had changed to 13% for Botswana, 28% for Namibia and 51% for both Lesotho and Swaziland. See Meyn (2003: 2).

87 Jachia & Teljeur (1999: 22).

8.6 per cent loss. Swaziland and Lesotho were expected to lose out by 13.9 and 12.9 per cent respectively.[88]

To cope with these potentially severe effects, the BLNS countries were forced to amend their trade policies. The domestic tax systems were to be reformed so that the losses in customs revenue would be moderated. To withstand the increased competition from EU and South African products, industrial enterprises were required to become more competitive and to develop new products. Strong regulatory and judicial regimes also had to be encouraged to attract foreign investment.[89] Especially least-developed Lesotho risked detrimental effects as a result of the TDCA. Although technically offered the possibility of maintaining non-reciprocal treatment by the EU, SACU's communal revenue collection system meant that in effect Lesotho would benefit minimally from its preferential LDC treatment.

Facing these detrimental effects and having to carry out such drastic reforms has triggered much TDCA-related criticism amongst the BLNS countries. The EU and South Africa have, however, always claimed to have considered the BLNS states' interests during TDCA negotiations. They argue that the damage done to the BLNS states is less serious than stated above and that the existing effects have been catered for properly by the implementation of safeguard clauses and compensation payments.[90]

The new SACU agreement

In October 2002, after seven years of negotiations, a new customs union agreement was signed between all five SACU countries. Much of the criticism by the BLNS states seemed to have been heard by South Africa. BLNS concerns with the effects of

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88 Mbekeani (1999: 55).
89 Ibid: 56.
90 Lowe (2000: 44).

South African regional dominance were largely met. The BLNS countries were given a larger revenue share, with Lesotho and Swaziland receiving the highest increases.[91] They also gained greater authority in SACU's decision-taking structure. This attempt at democratisation was meant to balance South Africa's economic and, therefore, decisional hegemony within SACU.[92] However, in return for these concessions the BLNS countries were to accept higher standards of trade liberalisation.[93]

In the new SACU agreement, all members promise to strive for further integration into the global economy.[94] This confronts the BLNS states with all the risks of increased competition and revenue losses that were mentioned earlier as coming from the TDCA. Besides liberalising trade towards outside parties, SACU members have also taken further steps towards intra-SACU market integration.[95] Harmonising policies in various areas and achieving higher standards of deep integration amongst its members has become an important SACU objective.[96] Agricultural marketing regulations in SACU countries are scheduled to be geared to one another while on industrial matters a common industrial policy for the whole customs union is envisaged.[97]

Many signs show that the BLNS countries have taken their promises seriously. They have decided to pursue higher levels of

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91 McCarthy (2003: 625).
92 Ibid: 621-23.
93 Ibid: 626.
94 Southern African Customs Union Agreement between the governments of the Republic of Botswana, the Kingdom of Lesotho, the Republic of Namibia, the Republic of South Africa and the Kingdom of Swaziland, signed October 2002. Gaborone: Tralac.
95 Southern African Customs Union Agreement between the governments of the Republic of Botswana, the Kingdom of Lesotho, the Republic of Namibia, the Republic of South Africa and the Kingdom of Swaziland, signed October 2002. Article 2 (f). Gaborone: Tralac.
96 Erasmus (2004).
97 McCarthy (2003: 628).

trade liberalisation, both through more shallow forms of integration with the advanced industrialised countries and through deep integration amongst its members. In various reports and interviews, BLNS government officials have stated stepping up to an enhanced removal of tariffs on trade.[98] The WTO, in its 2003 Trade Policy Review, argues that 'since the last Review of their trade policies in 1998, SACU countries have continued their economic reform programmes, where trade and investment liberalization have played key roles'.[99] The same report mentions that SACU members 'urge for more initiatives which will multilaterally liberalize trade in areas of particular interest to developing countries'.[100] SACU is currently also forging a FTA with the United States. A FTA with the European Free Trade Association (EFTA) was concluded in 2005. SACU also signed a preferential trade deal with Mercosur at the end of 2004. Trade deals with India, China and Nigeria are expected in the near future and also Singapore, Thailand, Sri Lanka and Turkey have expressed interest in free trade with SACU.[101] These activities clearly suggest a move by the BLNS countries towards enhanced trade liberalisation. Compensation payments, which the BLNS states were offered in return for their concessions, are the topic of discussion hereafter.

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98 See European Research Office (2001), Irving (1999) and government of Lesotho (2004).

99 WTO (2003a: vii). All SACU countries are original WTO members. Three of them have resident delegations in Geneva and participate actively in the WTO while the two other members plan to open missions in Geneva soon.

100 WTO (2003a: x).

101 Business Day, 3 October 2005.

Chapter findings

The decision by the BLNS states to introduce a more liberal direction to their trade policies seems harmful and therefore may look somewhat out of place. However, the different forms of pressure that the advanced industrial states exerted explain how this decision originated. Within an environment of growing economic globalisation, in which the dominant western powers strongly promote trade liberalisation, developing countries have found it hard to maintain policies that are independent of more open trade. Powerful external economic and political constraints, first introduced by the advanced industrialised states during the 1980s, have given the North greater bargaining power over the South. Besides individual countries and a trading block such as the EU, the WTO and international financial institutions have also pushed for shifts in the direction of free trade.[102] The 1980's debt crisis enabled these actors to provide assistance on the basis of policy adjustment in the developing countries, the so-called conditionality norm.

The EU has pursued enhanced free trade with the developing world through the introduction of reciprocity under the new Cotonou trade agreement and the TDCA. South Africa, being the other partner to the TDCA and making use of the new SACU treaty, must be held accountable for this impact too. International pressure, originating largely from the EU and South Africa, has made it increasingly difficult for the BLNS countries to withstand a move towards enhanced trade liberalisation. The various forms of pressure, stemming mainly from economic shocks, expanding conditionality and changes in the multilateral trading system, have created this environment. The next chapter examines more specifically one such pressure instrument that has been

[102] Harvey (2000: .84).

used to accomplish trade liberalisation in the BLNS countries; compensation payments.

3

Compensation payments

The relationship between western pressure to liberalise and a shift in BLNS countries' trade policies, as the previous chapter discussed, forms a background against which one such form of pressure can be placed. This chapter focuses on compensation payments. It scrutinises their presence and form, as well as the extent to which they have been used to promote further trade liberalisation.

The first section examines generic forms of development assistance, as used by the EU to stimulate trade liberalisation by the ACP countries. There, the burgeoning of a system in which aid is offered in return for trade adjustment is assessed. The same section discusses the forms of conditionality that have existed since the mid-1980s. Thereafter, the chapter focuses on the EU-South Africa TDCA. Non-financial concessions that were made to the BLNS states to curb the effects of the TDCA are addressed. Finally, various compensation payments that were given to the BLNS states by the EU and South Africa are scrutinised.

In studying financial pressure on the BLNS states, the chapter focuses on three possible forms: pressure from the EU through

ACP agreements; pressure from the EU and partly from South Africa through the TDCA related compensation payments; and pressure from South Africa through the SACU agreement. Assessing the compensation programmes that fit within these categories reveals the extent to which each of them is capable of carrying out the objectives for which they were officially designed.

EU-ACP conditional aid

Historical overview

The European Union has a long history of offering trade agreements in combination with financial assistance to African countries. Currently nearly half the money spent on development assistance comes from the EU and its individual member states. Together they provide more than €30 billion worth of aid annually, which places the EU amongst the world's biggest donors.[1] EU cooperation traditionally focuses on both economic and development cooperation.[2] The 1963 and 1969 Yaoundé Conventions and since 1975 the various Lomé treaties were based on a strong belief that the EU had an obligation to help the African, Caribbean and Pacific (ACP) countries to overcome their state of underdevelopment. During the 1960s and 1970s former colonising powers sought to replace formal colonial structures by trade arrangements that would maintain European influence in Africa.[3] The principle of combining trade agreements with development aid stood at the centre of all these agreements.

1 EU (2004).
2 EU (2001a).
3 Mailafia (1997: 36).

The Lomé III negotiations of 1984-1985 introduced the concept of conditionality, albeit at a relatively low level.[4] When in 1989 Lomé IV was signed, a stronger understanding amongst the donor community had emerged that financial aid and economic support programmes were ineffective if not tied to economic reforms. The EU encouraged countries to undertake structural adjustment programmes with the help of financial support from developed nations.[5] These measures of tying aid to adjustment requirements reflected what Chapter Two called the conditionality norm. Aid recipients were encouraged to design policies that promoted economic integration in order to receive financial assistance. Under Lomé IV, special structural adjustment support programmes to ACP countries were thus introduced.[6]

The main financial and technical instruments of the Lomé agreement were, and still are, within the Cotonou partnership, the European Development Fund and the resources of the European Investment Bank. These are allocated in various forms, such as grants and risk capital.[7] Most EU aid comes in the form of non-repayable grants.[8] During the 1986-1998 period, the ACP countries received €22.8 billion from the European Development Fund in grants, risk capital and loans to the private sector. This represented 77 per cent of all EU aid to ACP countries. Sixteen per cent of aid to the region, or €4.9 billion, was allocated from the European Community budget. This mainly encompassed food aid and humanitarian aid (particularly in 1994 and 1995). The remaining seven per cent was provided from the 'own resources' of the European Investment Bank, the EU's long-term funding

4 Haggard (1995: 102).
5 Mailafia (1997: 46).
6 Ikiara (1997).
7 EU (2001a).
8 EU (2004).

body, in the form of concessional loans.[9] Most of these loans went to infrastructure projects and utilities.

Under Lomé IV, funds were made available through ten different cooperation instruments. During the Cotonou negotiation process, the EU tried to reduce this number and sought to introduce a new programming system. The integration of the different development cooperation aspects – politics, trade and aid – became a major objective of this new programming system.[10] Providing risk capital and loans on concessional terms remained an important aspect of the new aid cooperation instrument.[11]

Conditionality provisions under Cotonou

Combining the politics, trade and aid sectors within one cooperation instrument, and making it a focal point of its new cooperation agreement has reshaped EU development assistance. Under the new Cotonou directives, aid has received a closer relationship with trade objectives.[12] As the EU is focussing its trade relationship with the ACP region increasingly on conceptions of trade liberalisation and reciprocity, it is likely to base the nature of its development assistance on similar conceptions. Linking aid to policies that promote trade liberalisation implies enhancing the conditionality norm which started under Lomé III.

Article 67 of the Cotonou Agreement discusses the intention to 'provide support for macroeconomic and sectoral reforms implemented by the ACP States'. One form of development assistance that the EU has initiated after the conclusion of the new Cotonou Agreement supports the integration of the ACP states into the

9 ECDPM (2001a).
10 ECDPM (2001e).
11 ECDPM (2001b).
12 European Commission (2002).

multilateral trading system of the WTO.[13] Extra attention is also given to regional integration. Regional activities that have an influence on national development have received substantial support.[14] The plans for constituting Economic Partnership Agreements in the ACP region seem to be of direct influence on the nature of EU aid. In 2002 the SADC region received €101 million to promote regional integration. A year later Trade.Com was approved, which was to support the ACP countries in their transition towards EPA regions. A €20 million Project Management Unit was also funded to prepare the ACP countries for the EPA negotiations.[15] In April 2006 the European Commission again donated an amount of €18 million to the SADC bloc to modernise their customs systems and improve border posts. The grant intended ‘to put in place a legal and institutional framework for a future SADC customs union envisaged for 2010’.[16]

Much of the EU funding currently goes into technical assistance and capacity building. EU aid increasingly focuses on areas such as the restructuring of government agencies, the privatisation of public companies and the training of officials. It also helps to supply ACP negotiators with knowledge and skills that are needed in international negotiations.[17] The conditionality norm has overtly gained much ground within EU aid disbursements.

TDCA-related compensation

In Chapter Two the potential harm that South Africa’s partners within the Southern African Customs Union faced as a result of the EU-South Africa TDCA was discussed. Increased competi-

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13 European Development Fund (2003).
14 European Commission (2000).
15 Szepesi (2004).
16 *Mail & Guardian* (2006a).
17 European Commission (2002).

tion from both the EU and South Africa, combined with a drastic decline in revenue, formed the major threats for Botswana, Lesotho, Namibia and Swaziland. For the EU and South Africa, however, adopting a free trade relationship was essential. Both were determined to find solutions to external impediments such as the concerns of the BLNS states. The newly revised – and in many ways trade liberalisation promoting – aid programme that the EU used through its agreement with the ACP met these goals in many ways. Donating development assistance in the form of adaptation schemes to WTO standards, but also supplying money for regional integration, strongly encouraged the objectives of deeper integration within the SACU region. It also enhanced shallow integration with the outside world.

Even more effective support for creating acceptance of the TDCA was included in the TDCA itself. These forms of support were related more directly to the BLNS states' concerns with the agreement. Various non-financial adjustments to the TDCA were made to comply with BLNS complaints about their economic well-being. For example, a special mention of the BLNS countries was included in the safeguard clause of the agreement. These safeguard clauses ensure that if any product is imported in quantities and under conditions that would threaten to cause serious injury to BLNS states' producers, appropriate measures may be taken.

Sensitive products such as beef and sugar were already excluded on the South African side of the agreement. The 'full cumulative' provision was included in the rules of origin of the TDCA to protect the industries of the BLNS countries. This allowed South Africa to export goods produced in the other SACU countries as 'South African' if the final stage of processing was undertaken in South Africa. Finally, the possibility of special EU assistance to the BLNS states under the cooperation programme with South Africa was mentioned in the TDCA.[18]

TDCA-related financial compensation

Besides the various trade adjustments that were made in the final draft of the TDCA, the BLNS states also requested assistance outside the agreement to curb the detrimental TDCA effects. The decline in revenue was particularly alarming and needed to be dealt with. To keep government income at a stable level, addressing fiscal reform was urgent. Introducing new taxes, such as a system of Value Added Tax (VAT) and strengthening existing tax collections were considered priorities. At the same time, public expenditure needed to be restricted by accelerating commercialisation and privatisation reform in BLNS countries.[19] While these reforms were costly, they were regarded as symptoms that the BLNS states had not themselves created. The EU was therefore seen as the actor that should supply appropriate funding.

In an interview conducted for this study, South African Member of Parliament and Chair of the Parliament's Trade and Industry Committee, Rob Davies, mentions that at the time of the TDCA negotiations the BLNS states' concerns led to a political conflict.[20] A SACU liaison group, representing Members of Parliament from all SACU countries, clashed with the EU on the need for compensation to the BLNS states. In spite of considerable pressure by the liaison group, the EU refused to acknowledge that the TDCA's adverse effects on the BLNS countries were serious enough to merit compensation. According to

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[18] Lowe (2000: 44).

[19] Bank of Namibia Research Department (2002: 14).

[20] Telephonic interview with Rob Davies, member of parliament and chair of the South African parliament's trade and industry committee, Johannesburg, June 2004.

Davies, ideological reasons for introducing reciprocal free trade with the SACU region prevented the EU from acknowledging the negative effects of the TDCA. Since the FTA with the SACU region was to function as a precedent for the rest of the ACP, this acknowledgement would have had serious implications for future EPA negotiations.[21]

While the BLNS countries insisted on being compensated and the EU refused to acknowledge the adverse TDCA effects, the EU found alternative ways to create BLNS acceptance. Davies mentions that the BLNS states were offered various adjustment payments by the EU within the framework of existing and new aid programmes. Because this aid is not earmarked as compensation, it does not force the EU to acknowledge any damage from the TDCA that could set a precedent for the rest of the ACP region.[22] However, since the aid is directly related to curbing the TDCA effects, the nature of these payments is in reality similar to fully fledged compensation payments. Various TDCA-related adjustment programmes appear to exist.

The Economic Integration Support Programme to the BLNS

In 2000 the EU launched its Economic Integration Support Programme to the BLNS. This three-year, €6 million programme aims to help support the BLNS countries benefit from the EU-South Africa FTA.[23] More specifically, the programme seeks to assist the BLNS countries adapt trade and trade-related policies and restructure their means of revenue collection. It also supports private-sector development in the BLNS countries and encourages them to take advantage of the TDCA.[24] By providing technical assistance, equipment and resources, the institutional

21 Ibid.
22 Ibid.
23 European Research Office (2002b: 16).
24 See European Union in South Africa.

frameworks and the human capacity of the BLNS states are thus developed.

The Economic Integration Support Programme (EISP) has been divided into three phases. Phase One consists of preparatory work and an analysis of adjustment issues arising from trade liberalisation. Phase Two includes the designing of appropriate transitional budgetary support programmes. It also aims to assist the private sector in enhancing competitiveness. Phase Three includes the financing of the transitional budgetary support programmes.[25]

Reception of the EISP

Since its launch, the Economic Integration Support Programme has received substantial criticism from BLNS governments and NGOs. Various arguments have been used in formulating this critique.

The BLNS states consider the EISP to be insufficiently targeted at the individual problems of the separate countries. The programme plans to base a Project Management Unit at the Swaziland Ministry of Finance, from which the programme will be conducted. However, the BLNS countries fear that this Management Unit will not properly cater for their individual concerns.[26] They argue that problems are addressed more effectively when using staff that are familiar with country-specific issues on the impact of the EU-South Africa TDCA. By requiring personnel to work with governments and the private sector in separate BLNS countries, concrete initiatives should develop more efficiently.[27]

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25 European Research Office (2004a).

26 In June 2004 the EISP was redesigned. The new Project Management Unit is now likely to be located in Namibia.

27 European Research Office (2001: 22).

Since all transitional budgetary support measures will be prepared within the framework applicable to the EU's Structural Adjustment Support Programmes, some worry that only Lesotho will be able to claim this aid.[28] There would be a problem for Botswana, Namibia and Swaziland to receive funding under the present EISP structures. The EC is thought to be reluctant to sufficiently cushion the impact of free trade on government revenues in non-LDCs. Some believe it fears the precedent this might set in the context of wider ACP-EU trade negotiations.[29]

Complaints about the EU downplaying the scale of future revenue losses have been voiced from the onset.[30] Financial differences exist between EU programmes that focus on economic development in individual BLNS countries. The so-called EU-Lesotho Co-operation Agreement and Financing Programme for the Period 2002-2007 is granting €110 million to Lesotho alone. Meanwhile, the EISP plans to use €6 million for a three-year programme that has the enormous task of both revising trade policies and a revenue collection system and supporting private-sector development in four different countries. This programme thus seems heavily underfunded when one considers that Swaziland's revenue losses, resulting from enhanced free trade with the EU, are estimated at seven times the annual EU aid budget to the country.[31]

In an interview, Eva Bursvik, Trade and Regional Integration Officer at the EC delegation in Namibia, challenged the argument of insufficient funding for the EISP. Bursvik mentioned that 'the problem is [not] that too little funds have been allocated to this support […] given that virtually no funds have been util-

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28 European Research Office (2002b: 24).
29 Ibid.
30 Goodison (1999: 85).
31 European Research Office (2002a).

ized under this programme to date'.[32] According to her, the main problem has instead been 'to spend/invest the funds wisely and effectively'. She argues that 'It is difficult to identify the needs, design a programme to assist, find the right people to manage it and provide TA (technical assistance), and for the cooperating partner to absorb and make use of the support'. However, these difficulties enhance the perception that the EISP has been poorly designed.

Moreover, the €6 million designated for this project do not seem to be extra aid for the BLNS countries. Half of this amount comes from the intra-ACP facility, which has similar objectives.[33] The other €3 million are to come from the European Programme for Reconstruction and Development in South Africa (EPRD). The EU has been said to shift the burden of most adjustment costs for the BLNS states to South Africa.[34] This might not affect the outcome of the programme itself but it could affect the donation of alternative South African support for BLNS adjustment.

Another important aspect of the EISP that has received substantial criticism is the term in which it has been offered. As mentioned earlier, restructuring trade policies, revenue collection and enhancing private-sector development is relatively ambitious for a three-year timeframe. Five years after its launch, the EISP was still not operational due to fundamental flaws in the design of the project.[35] Some have raised the question about how successful reform and the building of new fiscal capacity can be measured. They wonder what will be done if, after the prescribed

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32 Questions answered electronically by Eva Bursvik, trade and regional integration officer at the EC delegation in Namibia. Windhoek, Tokyo (November 2004).

33 See European Union in South Africa.

34 Goodison (1999: 86).

35 European Research Office (2002b: 24).

term of three years, its capacity remains low.[36] The amount of criticism the EISP is receiving makes any continuation in the case of failure unlikely.[37] There have been requests for the EU to make firm and binding commitments to support the process of fiscal restructuring not only in the short but also in the medium and long term.[38]

Finally, one other controversial feature of the programme has been the issue of linkage. Since South Africa and the BLNS countries together form a customs union, they have certain obligations to one another. When any of the SACU partners pursues an economic agreement with an outside party, approval is required from all the other parties in the customs union. South Africa needs the BLNS states' agreement to implement its TDCA with the EU. The EU has therefore made the disbursal of EISP funds conditional on the formal agreement of the BLNS states with the TDCA.[39]

As was mentioned in the introduction, tying payments to free trade acceptance does not necessarily render the EISP a less-effective programme. It is in line with the conditionality norm, which the EU has increasingly adhered to since Lomé III. The EU considers the economic integration objectives of the TDCA a necessity for the BLNS countries. Offering development assistance through the EISP would be senseless without acceptance of that programme. However, if a second-order commitment to targeted adjustment measures is absent, the goals of the EISP change. The programme's lack of effectiveness, as described above, casts doubt as to whether policy adjustment served as the prime motive underlying this linkage.

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[36] In a 2005 overhaul of the EISP, the timeframe was extended to five years, provided that a mid-term review showed sufficient progress.

[37] ECDPM (2000).

[38] European Research Office (2003c: 8).

[39] European Research Office (2001: 22).

With the signing of the new SACU agreement in 2002, the issue of BLNS countries' acceptance of the TDCA came to a conclusion. In the new treaty all parties agreed that 'No Member State shall negotiate and enter into new preferential trade agreements with third parties or amend existing agreements without the consent of other Member States'. With the last part of this sentence the TDCA became *de facto* accepted by the BLNS states.[40] Although this ratification has in a way made the linkage issue of the EISP redundant, the observed EU intentions at the time of the EISP launch in 2000 still help to determine the main objectives of compensation payments.

The EISP lacks specific targeting, sufficient resources and a realistic timeframe. This is seriously affecting its effectiveness in seeking to adjust BLNS trade-policy structures to the TDCA. The linkage factor, in combination with poor targeting standards, suggests that EU concerns with TDCA acceptance might limit concerns for efficient adjustment.

After remaining idle for five years, the EISP was relaunched in January 2005. The programme was expanded by including the enhancement of SACU's regional integration agenda and the strengthening of the SACU secretariat's capacities.[41] The new EISP has redirected the management of its projects to the SACU secretariat, with activities and interventions suggested through National Bodies and Technical Liaison Committees. The actual implementation of activities is executed by these Technical Liaison Committees, by National Bodies, Member States' governments and possibly the private sector. These changes clearly tackle an important part of the aforementioned targeting problems. However, they leave untouched the effects of the

[40] Questions answered electronically by Aloys Lorkeers, resident adviser to the EC delegation in Swaziland. Johannesburg (June 2004).

[41] Namibian (2005).

initial EISP at the time of its launch in 2000. Its initial design still reflects the EU's previous intentions. Also, the newly added regional integration as well as the SACU secretariat support targets render the size of the programme increasingly insufficient to achieve all its goals.

Other compensation

Besides adaptation programmes such as the EISP, other forms of financial support to the affected BLNS countries have in the past also been disbursed.[42] In September 1999 the European Commission's Director-General for Development, Philip Lowe, promised to secure funds to cushion the negative impact of the EU-South Africa FTA.[43] Although the EU made a commitment to supply this accidental funding, it gave no guarantee that it would continue such contributions to BLNS countries on an annual basis.[44]

Several months before Lowe made his promises, in May 1999, the EU had already granted €1.2 million to Swaziland under its eighth EDF programme for Swaziland. The aim of this funding was the 'strengthening of Government of Swaziland capacity in trade policy analysis, external trade relations and trade promotion'.[45] In an interview with the Resident Adviser to the EC delegation in Swaziland, Aloys Lorkeers, these payments were said to have been 'programmed well ahead, and independent from whether a TDCA would be agreed or not'.[46] According to Lorkeers this assistance was not directly related to the TDCA and not intended to facilitate the acceptance of the TDCA by Swaziland. However, at the time of disbursal the EU did mention that

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[42] Goodison (1999: 84), European Research Office (2002b: 24).
[43] Namibian (1999a).
[44] Locit.
[45] Questions answered electronically by Aloys Lorkeers, resident adviser to the EC delegation in Swaziland. Johannesburg (June 2004).
[46] Locit.

this money was meant ‘to help Swaziland cope with any fall-out or effects from the South Africa-EU free trade agreement’.[47]

Photo 4 Prime Minister of Swaziland Themba Dlamini and European Commissioner for Development Louis Michel, 22 November 2005
[Source: Audiovisual Library of the European Commission]

In September 2000 the European Union awarded Swaziland a 5.6 million euro grant to help the government reform its revenue collection system. One of the main objectives was to reduce Swaziland’s dependency on trade-related taxation.[48] In the light of Swaziland’s expected loss of revenue at that stage, resulting from the EU-South Africa FTA, the payments can hardly be seen as being independent of the TDCA. Although this adjustment fund as well as the €1.2 million fund might not have been directly tied to TDCA acceptance, they have almost certainly

47 Irving (1999: 1).
48 ANC (2000).

facilitated the acceptance of the agreement by BLNS states. Both programmes support Rob Davies's statement that to cushion the TDCA effects, adjustment payments under existing aid programmes instead of TDCA-related budgetary compensation payments were implemented. This prevented the creation of a precedent for other regions.

Similar aid disbursals as for Swaziland can be found for Lesotho and Botswana. In the Country Strategy Paper and Indicative Programme for the Period 2001-2007 between the EU and Lesotho, attention is drawn to 'the possible impact that the TDCA will have on the customs revenues received through SACU'. It then continues by arguing that: 'In this regard [i.e. the TDCA impact], the proposed EC support for the development of institutions with a medium and long-term policy planning capacity and the strengthening of Lesotho's analysis and negotiating capacity in trade related issues, particularly for the envisaged Regional Economic Partnership Agreements (REPA) with the EU, will be important'.[49] This excerpt indicates that EU support has been disbursed to Lesotho for the direct purpose of curbing the negative TDCA effects.

Under the eighth EDF just over €2 million have been allocated to Lesotho's Department of Economic Cooperation and its Department of Economic Policy. This money has been spent on Advisor, Economic Planning and Budget Support.[50] All beneficiaries correlate with the aims of cushioning TDCA-related effects. This counters a claim by the head of the EC delegation in Lesotho, Daniel Aristi, that no payments have been made to help cushion the impact of the TDCA on Lesotho.[51]

49 Kingdom of Lesotho & the European Community (2000: 12).
50 Ibid: 38.
51 Although it does not necessarily imply that the entire amount was meant to compensate for the TDCA.

Within EU-Botswana relations TDCA-related aid has also been granted. As with Swaziland, EDF funds to Botswana have supported a process of fiscal reform too. The European Commission has used three separate EDF projects to provide long-term tax-related technical expertise, short-term consultancy, training and minor equipment.[52] The money associated with these exercises amounts to almost €800,000.[53]

All the aforementioned payments to Swaziland, Lesotho and Botswana have been launched within the framework of adjustment programmes and therefore reflect a form of conditionality.[54] In a September 2002 EC report on trade and development, the Commission stated that the EU 'has experience with assisting the fiscal adjustment process in the form of advisory services and training'.[55] However, it continues by mentioning that it has done so 'also in the form of temporary budget support to contribute to covering transitional shortfalls (for example in West Africa and in Eastern and Southern Africa)'. This suggests the existence of yet another form of compensation: budgetary support.

Budgetary support

Under the EISP, a commitment for additional budgetary support was made to Lesotho.[56] Responding to this issue, Daniel Aristi, Head of the EC delegation in Lesotho, mentions that these funds

52 Republic of Botswana, European Community (2003: 21).
53 Ibid: 53.
54 Interestingly, the recent SACU-US free trade negotiations showed similar occurrences of adjustment assistance. When SACU asked compensation for expected losses in revenue income resulting from a FTA with the US, its call was turned down. Instead, the US offered US$2 million for capacity-building support. See Telephonic interview with Peter Draper, research fellow with the development through trade project at the South African Institute of International Affairs (SAIIA). Pretoria/Leiden (August 2004).
55 Commission of the European Communities (2002: 23).
56 European Research Office (2004a: 6).

have in fact not been allocated.[57] This does not necessarily render these payments less important. The initial plans for budgetary support still reflect the EU's intentions. However, similar commitments were also made outside the EISP, stating that where enhanced free trade with the EU created fiscal difficulties, LDCs would be eligible for additional budgetary support.[58] Cancellation of the EISP payments does not seem to have been due to a change in aid directives. The same 2002 EC report on trade and development states that 'to facilitate the adjustment process resulting from multilateral and regional trade agreements, the Commission intends to continue and extend this kind of [budgetary] support'.[59]

Photo 5 Former President of the European Commission Romano Prodi and Botswana President Festus Mogae
[Source: Audiovisual Library of the European Commission]

[57] Questions answered electronically by Daniel Aristi, acting head of the EC delegation in Lesotho. Johannesburg (June 2004).
[58] European Research Office (2003b: 7).
[59] Commission of the European Communities (2002: 23).

From the mid-1980s onwards, the EU has increasingly applied measures of conditionality to its financial assistance to Sub-Saharan Africa. All the above-mentioned aid flows were set up to facilitate higher standards of trade liberalisation in the BLNS states. The Economic Integration Support Programme to the BLNS, the adjustment funds for Swaziland, Lesotho and Botswana under the eighth EDF and the budgetary support for Lesotho were initiated to offer the BLNS states compensation for their enhanced integration in the global economy.

South African aid to the BLNS states

South Africa has only been in the position to offer development assistance to the wider SADC region since its move to democracy in 1994. SADC's forerunner, the Southern African Development Coordination Conference (SADCC), was formed in 1980 with the purpose of being a direct opponent of the South African apartheid regime. It pursued larger regional independence from, and the isolation of South Africa.[60] Logically, the SADC countries accepted almost no development assistance from South Africa. When international sanctions were dropped after 1994, South Africa quickly developed into a strong regional player. Actively interfering with the economic development of surrounding countries had become much easier. As previous sections explained, South Africa has since encouraged the implementation of trade liberalisation continent-wide. It has used regional integration schemes, amongst others, as a means to accomplish this.

As opposed to its relationship with most SADC countries, South Africa had provided its SACU partners with development

[60] Gelb (2001: 11).

assistance from long before the end of apartheid. Most of these payments were compensatory in nature.

Prior to the new 2002 SACU agreement, the BLNS countries had felt that South Africa benefited disproportionately from the customs union agreement. During the apartheid era, South Africa had always been in the position to set the communal tariff and excise duties, which it did in such a way as to meet its own goals of industrial development. As a result, the BLNS states lost fiscal autonomy and experienced restricted sovereignty over trade and industrial policy. In many cases they were forced to pay higher prices for goods imported from outside the union.[61] Moreover, the BLNS states until 1994 regarded the political damage caused by close ties with an internationally ostracised nation as justification for being compensated.

The 2002 SACU renewal: BLNS states' concerns for TDCA

Under the 1969 SACU agreement, South Africa promised to make certain concessions that would balance its relationship with the BLNS states. Since South Africa was highly dependent on SACU for cheap resources and the export of continuous flows of its products to the BLNS states, it offered various forms of compensation.[62] The most important was the customs revenue allocation system, which assured BLNS governments of a guaranteed minimum in customs revenues.

In 1994, partly because of South Africa's complaints that the revenue-sharing system was becoming unaffordable, the negotiations for a new SACU agreement were initiated.[63] The treaty that was eventually signed in 2002 showed a structure in which the majority of the communal revenue earnings would be divided

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61 McCarthy (2003: 615-16).
62 Gibb (1997: 73).
63 Ibid: 80.

amongst the SACU members in the form of a customs, an excise and a development component. The latter component, to which South Africa is the only net contributor, was established to protect Lesotho, Namibia and Swaziland in particular against the adverse effects stemming from bilateral and multilateral trade liberalisation.[64] The free-trade agreement between South Africa and the European Union must be regarded as the main example of such liberalisation.

Rob Davies mentions that similar mechanisms cushioning the BLNS states from the polarising effects of being in a customs union with South Africa already existed in the previous SACU treaties. However, he says, these payments' rationale has shifted with the new SACU agreement. Davies argues that, instead of curbing trade liberalisation within the SACU region, the aim of the development component is now to help the BLNS states in dealing with trade liberalisation with outside partners.[65] Others have come to similar conclusions.[66]

The development component of the new treaty was initially set at 15 per cent of all revenue coming in through the total SACU excise pool. Since this part of the agreement will only 'be reviewed from time to time and will be adjusted if agreed to by all Member States' the percentage and its disbursal seem somewhat arbitrary and open-ended.[67] No mention is made in the agreement of the conditions attached to the allocation of the funds. Unlike the EISP, a policy adjustment programme has not

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64 McCarthy (2003: 626-27), Kirk & Stern (2003: 15).

65 Telephonic interview with Rob Davies, member of parliament and chair of the South African parliament's trade and industry committee. Johannesburg (June 2004).

66 Kirk & Stern (2003: 14-15).

67 Southern African Customs Union Agreement between the governments of the Republic of Botswana, the Kingdom of Lesotho, the Republic of Namibia, the Republic of South Africa and the Kingdom of Swaziland, signed October 2002, Annex A: Revenue sharing formula. Gaborone: Tralac.

been scheduled to direct these funds.[68] Both the terms and the targeting of the development component are therefore unspecified. Adjusting BLNS states' trade policies to higher levels of economic integration is difficult within this framework.

The development component was set up to curb the negative effects from bilateral and multilateral trade liberalisation. It is highly unlikely that this funding would have been disbursed without the BLNS states' approval of the most important liberalisation initiative in the region, the TDCA. After all, had the TDCA not been ratified, hardly any reason would have existed for cushioning the BLNS states against trade liberalisation. It is therefore reasonable to assume that, during the SACU negotiations, the South-Africa-funded development component was linked to the BLNS states' acceptance of the TDCA. Eventually, the chapter of the SACU agreement that deals with third party involvement created *de facto* acceptance of the EU-South Africa FTA.[69]

Just as the EISP and the various alternative TDCA-related payments by the EU, the development component of the new SACU agreement aims to cushion any adverse effects of the TDCA. Whereas the EISP speaks of specific targets and of a specific term, the funding of the new SACU agreement lacks these criteria. The SACU agreement also linked its payments to TDCA ratification without requiring specific targeting.

Besides support through the SACU development component, South Africa has also promised to help the EU in assisting the BLNS states deal with the TDCA. Within the EU-South Africa FTA it was agreed that South Africa would provide adjustment assistance for its neighbouring states.[70] The main effect of this has been the Economic Integration Support Programme that was

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[68] Kirk & Stern (2003: 10).

[69] Questions answered electronically by Aloys Lorkeers, resident adviser to the EC delegation in Swaziland. Johannesburg (June 2004).

[70] Eurostep (2000).

set up in cooperation with the EU. As mentioned earlier, South Africa was to provide half of the amount that was assigned for this project. Indirectly, however, these funds come from the EU through its Programme for Reconstruction and Development for South Africa. In the year 2000 South Africa and the EU also agreed within their Multi-Annual Indicative Programme that enhanced cooperation and integration with the SACU region was one of the main indicators of European support to South Africa.[71]

Chapter findings

In Chapter Three it was argued that the BLNS states are moving towards higher standards of free trade as a result of EU and South African pressure. Reciprocity through the Cotonou Agreement and *de facto* free trade through the TDCA have been the EU's tools to accomplish this. South Africa has stimulated further trade liberalisation in the BLNS countries with the help of the TDCA and the new SACU agreement. The implementation of these programmes has created higher levels of trade liberalisation in the BLNS states.

The current chapter has demonstrated that there is a connection between aid and economic adjustments in the ACP area. Financial compensation, a specific form of the pressure that Chapter Two addressed, has importantly influenced the acceptance of the TDCA by the BLNS states. The EU has offered compensation through the ACP agreements, the TDCA, the EISP and the eighth EDF. South Africa has provided similar funding through the EISP and the SACU development component.

The shift towards trade liberalisation that Chapter Two assessed can now be put into better perspective. The conditionality

[71] Government of the Republic of South Africa & The European Commission (2000: 15).

norm that emerged in the 1980s under Lomé III gained further support under Lomé IV and eventually became essential with the signing of the new Cotonou Agreement in 2000. This conditionality norm has recently also been used for the BLNS states. Compensation payments are leading the BLNS countries to adjust their economies to enhanced free trade with the EU. The tying of the EISP – and arguably the SACU agreement – to TDCA acceptance has acted as a stimulus for the BLNS countries to accept further reciprocity.

In assessing the workings of these four compensation programmes, most have turned out to be incapable of reaching their official objectives. Of the EISP, the eighth EDF, the budgetary support payments and the SACU development component, some have offered money while failing to install effective elements of economic adjustment. This raises the question as to whether the EU's and South Africa's priorities do in fact lie with the full adjustment of BLNS states' economic policies. The following chapter uses this programme analysis and compares the design of all four compensation programmes to both an economic adjustment and a political acceptance model.

4

The aims of compensation: Economic integration vs. political acceptance

Two opposing views can be discerned to determine the relationship between the introduction of trade liberalisation and financial compensation in dealings between the BLNS countries and the EU and South Africa. If compensation payments supported economic adjustment, the point at which adjustment aid was offered would be of a temporary and well-defined nature. Payments should also be targeted at removing the economic impediments to trade liberalisation. The size of compensation would ideally be based on exact economic studies of what is necessary to achieve trade liberalisation. Tying the disbursement of compensation payments to political concurrence with a trade policy shift would not be possible without a second order commitment to proper targeting.

Compensatory aid programmes could also be aimed at building political support for trade liberalisation. Financial support for policy changes would then be fixed to a term that was either too short or open-ended. In similar ways, compensation would have to be targeted not so much at the sectors of an economy that were damaged by trade liberalisation but at the demands of people, who are, after all, the most important to creating political acceptance. Also, the amount of money which is offered should be based on a political rather than an economic study of what is needed to achieve free trade. Compensation payments within these objectives are tied to the acceptance of free trade without including a commitment to targeted adjustment measures.

This chapter seeks to determine which model each of the compensation programmes encountered best correspond with. The outcome of this assessment has important consequences for the relationship between trade and aid in the case of the EU, South Africa and the BLNS states as well as for development objectives in the Southern African region.

It is possible that one programme, or parts of it, may correspond with an economic adjustment model, while others correspond with a political acceptance model. The four above-mentioned criteria help determine how these models interrelate and what possible combinations mean for the workings of each payment. And finally, this chapter examines the aims of compensation from a realism and a liberalism perspective. It assesses which of these two theories the compensation payments and their main objectives correspond with.

Objectives of BLNS compensation

The EISP

The first form of TDCA-related compensation payments that Chapter Three discussed concern the Economic Integration Support Programme to the BLNS. If viewed in terms of economic adjustment, the EISP should cater for the economic transition to free trade. As mentioned earlier, the initial EISP should be seen as being independent from the EISP that was redesigned in 2005. The first design still reflects the EU's intentions at the time when the TDCA was not yet officially accepted by the BLNS states.

The EISP shows a demarcated term of three years, sub-divided into three well-defined stages. After these three years, the adjustment mechanisms are meant to create swift policy adjustments. Secondly, the aim of providing technical assistance, equipment and resources – and the plans to do so one at a time in distinct phases – indicates a specifically designed and carefully targeted approach. All these facets are likely to stimulate economic changes that ease a move towards free trade.

If the EISP is regarded otherwise, its objective should be to create political acceptance for the TDCA amongst the BLNS states. Little seems to affect that perception. The €6 million that were invested in technical assistance, equipment and resources to develop institutional frameworks and human capacity can also serve a second aim, namely to create political adherence. Adjustment aims and the aim of creating political support are not necessarily mutually exclusive. However, the economic returns of these investments matter less within a political acceptance model.

Chapter Three discussed elements of the EISP which do not always fit the economic adjustment presumptions. They do, however, fit the political acceptance model. The EISP's three-year term proved too short for its high ambitions. The programme's targeting proved ineffective because of a centralised rather than locally directed structure. The amount of €6 million was too low in view of its many goals and cast doubt on whether the EISP was designed on the basis of how much was in fact needed for economic adjustment. Together, these elements make the EISP ineffective in adjusting the BLNS states' trade policy structures to the TDCA. Although in theory the EISP seems to match some of the adjustment beliefs, closer assessment shows that the programme is insufficiently effective for building transitional structures that prepare the BLNS countries for more open trade. Chapter Three discussed how the linkage factor and the absence of a second order commitment to proper targeting put the EISP's intentions under pressure.

Tying the disbursal of EISP money to TDCA agreement would be suitable within a political acceptance model. Linking the programme to ratification without imposing a requirement for sufficient targeting increases the chances of political acceptance for the TDCA. Its failure to achieve economic adjustment to free trade becomes understandable when TDCA concurrence proved to be its primary goal. Both a transition term that is too short and imprecise targeting matter less if the priority of the EISP lies with political acceptance instead of economic adjustment. A lack of funding is more easily understood if the programme intends mainly to signal EU sensitivity to the BLNS states' concerns. The EISP has been presented as exactly that: a programme that assesses BLNS concerns and explores possible solutions. The two-year delay of the programme and its failure to consider possible problems beyond the three-year period also support the interpretation that a short-term signal rather than a long-term adjustment aim is most important.[1]

The EISP may in fact have mitigated initial concerns about the TDCA effects to create sufficient goodwill for TDCA acceptance at the 2002 SACU renewal. That the EU was predominantly interested in taking away political concerns is further supported by the fact that it did not propose the EISP of its own initiative. It

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[1] The redesigned EISP has a five-year timeframe, and a mid-term review. However for the purpose of this study, the design of the initial EISP is more relevant.

merely reacted to a strong call by BLNS governments to set up the programme.[2]

The interpretation of the EISP functioning as a 'sweetener' and aiming to build political support instead of economic adjustment thus gains credibility. Naturally, this does not rule out the presence of all economic adjustment objectives. Despite its discussed ineffectiveness, the EISP has been revised and new structures for effective BLNS states' adjustment will possibly emerge. However, looking at the initial design of the programme, political acceptance goals help to understand important parts of the EISP at moments when an economic adjustment model seems less capable of doing so.

The eighth European Development Fund

Chapter Three also looked at adjustment payments to Swaziland, Lesotho and Botswana which were disbursed under the eighth European Development Fund. As these payments were directed towards the economic areas that the TDCA affected most, a relationship with that agreement was indicated. Both the 2002 EC report and the statement by Rob Davies that such EDF funds were in fact disguised compensation payments further linked the origins of this compensation to the TDCA.[3] The relationship between EDF aid and trade liberalisation again brings to the fore the debate between the economic adjustment and the political acceptance interpretation.

At least one important point of criticism that was mentioned for the EISP seems not to hold for the eighth EDF payments. Whilst the EISP insufficiently addressed individual BLNS states'

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[2] Personal interview with anonymous representative of the EC in South Africa. Pretoria (June 2004).

[3] Telephonic interview with Rob Davies, member of parliament and chair of the South African parliament's trade and industry committee. Johannesburg (June 2004), Commission of the European Communities (2002).

adjustment needs because of a centralised set-up, EDF aid was managed at a national level. This has made it easier for the Swaziland, Lesotho and Botswana governments to target the eighth EDF payments to their own problems and solutions. Contrary to the EISP, the EDF payments have also been divided into smaller, more manageable projects.

Regarding amount, term and the issue of tying, EDF support to Swaziland, Lesotho and Botswana also differs from the EISP characteristics. The amount of both EDF programmes to Swaziland totals €6.8 million, which exceeds the total EISP budget.[4] However in this case, the entire amount has been distributed to one state instead of to four. The term in which the projects are meant to be executed is not any more strictly determined than that of the EISP. But, since the targeting is specified and manageable and since more money is involved, the timeframe, which for both projects is between two and three years, has also become more realistic. Finally, the EC representative to Swaziland, Aloys Lorkeers, confirmed that a tying chapter was not included for EDF funds.[5] Other available information provides no reason to doubt this assertion.

Judging by its term, targeting, amount, as well as from the absence of linkage to TDCA acceptance, the eighth EDF payments to Swaziland, Lesotho and Botswana are probably more effective in supporting trade policy adjustment than the EISP was. This does not automatically imply that the EDF funds lack the aim of creating political trade policy acceptance. However, since there seems to be a relatively high level of effectiveness, a strong case can be made that the economic adjustment model explains

4 ANC (2000), Irving (1999: 1).

5 Questions answered electronically by Aloys Lorkeers, resident adviser to the EC delegation in Swaziland. Johannesburg (June 2004).

many aspects of these payments at least as well as a political acceptance model would.

EU budgetary support

In spite of various indications of TDCA-related budgetary support to BLNS countries, only a commitment for additional budgetary support to Lesotho can be traced under the EISP. But this aid was eventually never allocated to Lesotho. Its initial purpose as well as the EC directives for similar future budget support make it nonetheless an important aspect of TDCA-related aid.

The initial purpose of the budgetary payments was to cushion the government's revenue shortfall which arose as a result of lower customs incomes. The objectives of economic adjustment to this new situation and those of enhancing political support could theoretically both be served within a certain programme.

However, targeting within budgetary support is considerably vaguer then under normal programme support. Budgetary support payments, although normally accompanied by spending directives, give recipient governments greater control over their own policies.[6] Some civil-society organisations have expressed concern over budget support not meeting donor objectives. They argue that such funding primarily accommodates the priorities of those in power in African countries.[7] In the case of Lesotho, the EC temporarily suspended its budgetary support because of difficulties in both tracking the final destinations of 40 per cent of the Lesotho government budget and in properly assessing the impact of these funds.[8]

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6 Cordella & Dell'Ariccia (2003: 10), Unwin (2004: 16-17).

7 Unwin (2004: 25).

8 Questions answered electronically by Daniel Aristi, acting head of the EC delegation in Lesotho. Johannesburg (June 2004).

Besides targeting, a lacking term also affects economic adjustment purposes. As a result of its one-off disbursal, such undirected assistance stands less of a chance of adding to the long-term process of trade-policy adjustment than when funds are provided at different stages. Since the suspension of these payments only occurred after the approval of the TDCA, a political acceptance interpretation for the initial design remains relevant.

The cancelling of this budget support makes it difficult to establish how much money would have been allocated to Lesotho. Considering that Lesotho's estimated loss of revenue as a result of the TDCA amounts to 12.9 percent, on the basis of annual SACU-related customs of around €137 million, it can hardly be expected that the amount for budgetary support would have covered any substantial economic losses.[9] Since the budgetary support payments were part of the EISP, the inception of which was dependent on TDCA concurrence, these payments were also tied to TDCA acceptance.

With hardly any conditions attached and its targeting unspecified, this money would have lacked almost any economic adjustment aim. Its linkage with TDCA ratification enhances the thought that it would mainly have been used for persuading the Lesotho government to accept enhanced free trade. A neo-mercantilist or realist view, according to which the EU tries to buy its way into free trade, would have interpreted the nature of these payments much more adequately than liberalism would have.

The budgetary support payments to Lesotho, regardless of their suspension, form a strong example of side-payments. Holding relatively weak conditions, this money lacks a convincing economic adjustment aim. Its linkage with TDCA ratification in the absence of a second order commitment to targeted adjustment

[9] Kingdom of Lesotho & the European Community (2000: 60).

measures enhances this view. It thus becomes plausible that the budgetary support payments were designed to encourage the Lesotho government in going along with enhanced free trade. A view in which the EU tries to secure political acceptance of free trade interprets the nature of these payments more adequately than an economic adjustment model does.

A political acceptance approach raises questions as to why the other BLNS states were not mentioned in the EISP plans for similar aid. One argument could be that only Lesotho is considered a Least Developed Country and thus needs EU support more than the others. However, as mentioned earlier, Swaziland was expected to lose an even higher percentage of its revenue.

This preferential treatment, which it also experienced under the EISP, can again be explained by a political acceptance model. Lesotho already had the guarantee of ongoing non-reciprocal trade with the EU under the Everything But Arms (EBA) provisions for Least Developed Countries. Unlike Botswana, Namibia and Swaziland, who were expected to face a move towards reciprocal trade in the future, Lesotho did not have to worry about enhanced trade liberalisation if the TDCA was to be repudiated. In fact, the EBA option seemed to provide Lesotho with even better conditions than the TDCA. Responding to questions on this matter, the EC head of delegation in Lesotho mentioned that no changes in trade volumes had occurred as a result of the TDCA. However, he said, there was ‘scope for textile exports to Europe to take off under the EBA (not the TDCA)’.[10] Lesotho, theoretically a more persistent adversary to the TDCA, thus required larger compensation than the other BLNS countries. It is not unrealistic to regard the design of budgetary support to Lesotho in the light of greater financial pressure

[10] Questions answered electronically by Daniel Aristi, acting head of the EC delegation in Lesotho. Johannesburg (June 2004).

from the side of the EU. This scenario further strengthens the political acceptance interpretation for the budgetary support payments to Lesotho.

The SACU development component

The SACU development component was set up to protect Lesotho, Namibia and Swaziland against the adverse effects stemming from bilateral and multilateral trade liberalisation. The previous chapter discussed how the size of this component as well as its disbursal are relatively arbitrary and open-ended. As no conditions for its allocation are mentioned, terms and targeting are also not specified. This affects the possibilities for adjusting BLNS states' trade policies to higher levels of economic integration. The development component's objective to curb the negative effects from bilateral and multilateral trade liberalisation suggests that it was linked to the BLNS states' acceptance of the TDCA. Meanwhile, in the absence of well-designed targeting, this tying runs counter to an economic adjustment approach.

The term, targeting, amount and linkage to the TDCA all make the SACU development component incomprehensible within a narrow economic adjustment model. However, as was the case with the EISP, the programme's ineffectiveness does not impede the alternative interpretation. The SACU development component's lack of targeting and term pose no barriers if it intends to create political acceptance. Offering a relatively large sum of money without a specified purpose does not ease economic adjustment. However, this lack of specificity does make sense if the goal is to build political support. Finally, the linkage issue in combination with insufficient targeting also coincides with the latter perspective.

Interpreting the findings

In assessing the four TDCA-related aid components, aspects of both an economic adjustment model and a political acceptance model have been identified. The EISP is most easily understood within the latter framework. The economic adjustment model, however, helped account for the objectives of the eighth EDF payments as least as well as the political acceptance view. Budgetary support to Lesotho, even though eventually not disbursed, contained characteristics that were closer to a political acceptance interpretation. South Africa's payments through the SACU development component were also primarily compatible with the political acceptance model.

Overlapping objectives

The four aid programmes reflect elements of both views on trade and aid relationships. The findings in Chapter Three and Three therefore suggest that both perspectives have some applicability. Political acceptance and economic adjustment considerations can overlap and coexist within the same programme. Finding various explanations for the existence of these payments is less contradictory than would appear. The EU at the time of the TDCA negotiations consisted of fifteen member states, each tending towards the promotion of their individual interests. For the EU to run negotiations with outside partners effectively it always needs internal compromise between individual members first. Only then can it commence negotiations with third parties, which will often mean making further concessions.

This situation of negotiating at different levels with various individual state interests is what Robert Putnam has called a 'complex multi-level game'. At the domestic level, he argues, politicians are pressurised by interest groups. At the international negotiating level politicians have to satisfy domestic groups while simultaneously minimising any negative effects of foreign developments.[11] The bigger the overlap between domestic and international demands, the larger a negotiator's margin for reaching an agreement. Within the EU this means that its many different members first have to match domestic demands to international demands at the EU level. Only then can they match their common demands with outside trade partners, such as South Africa and the BLNS countries. Certain complex multi-level games within EU-ACP relations have existed since the Lomé Conventions in 1975.[12]

Parts of the 1999 TDCA negotiations illustrate the diverging interests that can emerge through multi-level EU trade negotiations. During the trade talks, Spain and Portugal requested that the terms 'port' and 'sherry' no longer be used for fortified wines from South Africa. These domestic issues were lifted to the supra-national EU level when third-party South Africa was confronted with them. Spain and Portugal's demands influenced the EU-South Africa talks and finally led to a situation where the TDCA negotiations threatened to stall.[13]

When deciding on an economic adjustment or a political acceptance interpretation for EU compensation payments to the BLNS states, similar multi-level interests must be considered. According to a European Commission representative in South Africa, such diverging motives were clearly present during the TDCA negotiations. Whereas the Nordic and Benelux countries seemed to be more concerned with the development aims of the TDCA, the Southern European countries mainly focused on the

11 Putnam (1988: 434).
12 Mailafia (1997: 97).
13 Namibian (1999b).

trade objectives of the agreement.[14] Similar controversies between an economic adjustment and a political acceptance approach could well have existed with regard to compensatory aid for the BLNS states.

The assessment of the four aid programmes to the BLNS states has shown that the two objectives can overlap and coexist, both between and within programmes. What this study has aimed to do is to establish the extent to which each perspective helps to clarify the nature of each payment.

Prevailing model and theoretical reflections

Notwithstanding the overlap between the two models, assessments of the individual compensation programmes show that often one perspective clarifies a programme better than another. The Economic Integration Support Programme to the BLNS, the budgetary support payments to Lesotho and the development component of the new SACU agreement all contained features that could be explained best with the help of a political acceptance model. Where economic integration could be used as a model to understand these programmes, it did so only to a certain level. Only for the eighth EDF payments did a more overt form of economic integration seem to match the evidence better than political acceptance did. Regarding the four TDCA-related aid programmes, concerns for political acceptance turn out to be crucial.

This means that within the analysis of EU compensatory aid to the BLNS states, the importance of state power must be recognised. The EU has tried to introduce reciprocal free trade with the BLNS region by offering payments that are based on political acceptance considerations. Compensation programmes have been

[14] Personal interview with anonymous representative of the EC in South Africa. Pretoria (June 2004).

oriented at least as much towards winning the political support of the BLNS governments as to addressing specific economic adjustment problems that are associated with lowering trade barriers in the BLNS countries.

The dichotomy between a state power interpretation and an interpretation that focuses on facilitating economic adjustment in fact resembles a juxtaposition of the theories of realism and liberalism within the trade liberalisation debate. Realism expects free trade to be introduced through a confrontation of powers in which parties concede as little access as possible to their domestic market.[15] Financial compensation serves mainly as a political 'sweetener' to gain acceptance of a trade agreement by one or more states that might otherwise not concur with that agreement.

Liberalism sees the bulk of trade liberalisation put in place by the lowering of trade barriers and through the powers of increased trade and investment themselves.[16] Financial compensation, according to liberals, is necessary only on a temporary basis and is meant primarily to overcome specific economic adjustment problems. Compensatory payments, they say, limit the benefits of economic integration, namely increased competition and efficiency. Liberal thinking therefore supports the view that if an FTA is not effective due to severe revenue losses for African states, that FTA should not or only gradually be installed.[17] Overdependence on foreign funds, many liberals argue, creates a situation in which governments shift their accountability from the domestic population to the international donor system. This creates a lack of political commitment and lowers the incentives to reform.[18]

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15 Nicholson (2002: 91-97).
16 Gunning (1999: 22), Jacquet (2002: 3-4).
17 Mshomba (2000: 199).
18 Leonard & Straus (2003: 30).

These two theories can now be placed against the backdrop of the economic adjustment model and the political acceptance model for compensation payments. Three out of four aid programmes appear to be in contrast with the liberal belief that trade liberalisation by developing nations should not be dependent on the creation of political acceptance. The argument that African states go along with more open trade mainly because of seductive assistance funds finds much support in the case of the BLNS states. This coincides importantly with a realist power model of free trade introduction. A purely liberal vision of the relationship between trade and aid in the case of the EU and the BLNS states becomes increasingly weak.

Chapter findings

The changes in levels of trade liberalisation, which the BLNS states experienced with the introduction of the new TDCA, resulted, to a large extent, from financial pressure from the EU and South Africa. This chapter focused on the objectives of TDCA-related aid to the BLNS states. It showed that the combination of trade liberalisation and compensation payments, discussed in Chapters Two and Three, can be structured according to two different models. An assessment was made for the four compensation programmes discussed in Chapter Three on the basis of these two models. The term, targeting, size of payments and the tying to TDCA acceptance constituted the four characteristics that helped to determine whether these payments better matched an economic adjustment or a political acceptance explanation.

Although the economic adjustment model proves viable for some elements of the payments, the political acceptance model explains the objectives of most of the aid programmes better. It can, therefore, be said that the specific payments that this study assessed have predominantly been designed to accomplish the political acceptance of higher levels of free trade. The EISP, the EU budgetary support payments to Swaziland and the SACU development component all fit this interpretation to a high degree. For at least three of the four compensation programmes, economic adjustment has not been the primary objective. Comparing this outcome to realism and liberalism theories gives strong support for the theory of realism. An interpretation in which state power is a dominant influence in the relationship between the EU, South Africa and the BLNS states best explains the behaviour of these actors.

5

Summary and implications

Overview

To present a background against which the origin of compensation payments could be explained, this study started off by assessing the changes in trade relations between the developed and the developing world since the period of decolonisation. From the 1980s, developing countries have increasingly moved towards enhanced levels of trade liberalisation as a result of pressure by advanced industrial states. The so-called 'conditionality norm' helps to explain how the North has managed to provide assistance on the condition of policy adjustment in developing countries. Western economic dominance, largely due to economic shocks in the developing world during the 1980s, an expanding conditionality norm resulting from this and increased reciprocity in the multilateral trading system constitute the main forms of liberalisation pressure that the developing world as a whole has experienced.

The BLNS states experienced such pressure to liberalise from the EU as well as from South Africa. The EU exerted pressure directly through the Cotonou Agreement of 2000, which was set up to change the existing EU-ACP relationship of non-reciprocal free trade into a relationship of full reciprocity. Indirectly, it exerted such pressure through its FTA with South Africa. By 2008 the ACP states are meant to have constructed regional Economic Partnership Agreements. That way the developing countries will profit more easily from the economic benefits of economies of scale, such as sustained economic growth, increased competitiveness, the creation of productive jobs and better access to social services. The EU-South Africa FTA *de facto* created one such relationship of free trade between the BLNS states, South Africa and the EU.

South Africa can be said to have pursued similar goals of enhancing free trade. It has done so not only through the TDCA but also through its SADC and NEPAD initiatives. The 2002 SACU treaty has also functioned as an important step in lowering trade barriers. The relationship between the BLNS states, the EU and South Africa resulting from these agreements reflects this link between western economic and political pressure to liberalise and the shift in BLNS trade policies.

Aid since the mid-1980s has increasingly been offered on the condition that trade barriers in the ACP region would be lowered. The TDCA can be regarded as an example of the so-called conditionality norm, according to which, trade liberalisation is introduced in exchange for financial assistance.

Besides various non-financial adjustments to the TDCA, three different TDCA-related financial compensation instruments have been introduced by the EU: the Economic Integration Support

Programme to the BLNS, the budgetary support payments to Lesotho and various TDCA-related payments granted to Botswana, Lesotho and Swaziland under the eighth EDF. A similar combination of trade liberalisation and compensation payments exists within the SACU agreement that the BLNS states and South Africa signed in 2002. The development component of this agreement provides financial compensation while simultaneously dealing with the issue of TDCA concurrence.

Two models can be turned towards to determine the nature and goals of each compensation programme. These are frameworks that offer different explanations for the way financial compensation is used to introduce trade liberalisation in the BLNS region. How the relationship between trade and aid is perceived is also affected by the extent to which the compensation programmes correspond with these two models.

The first model explains the function of compensation payments as a way to create political acceptance for a move to trade liberalisation. The second model focuses on the building of economic adjustment to facilitate the introduction of trade liberalisation. Since both models use financial support to spur economic policy changes, they both concur with the conditionality framework.

With the help of four different criteria – term, targeting, size of payments and tying to TDCA acceptance – it is possible to find which of these two models fits the design of the compensation programmes best. As a result, the EISP, the budgetary support programme for Lesotho and the development component of the new SACU treaty appear to fit the political acceptance framework better than the economic adjustment framework. Only those compensation payments that were disbursed under the eighth EDF do not meet any impediments to an economic adjustment point of view. Therefore, the model that explains the majority of the financial compensation programmes most suitably is the political acceptance model. This means that creating political concurrence with the TDCA has probably been the main aim of most payments. A theory of realism, which recognises the importance of state power, underlines many of the political acceptance ideas. A liberal theory, stressing the power of market forces while pursuing a minimum of state influence, corresponds more closely with the economic adjustment model. These liberal visions prove less persuasive in the case of trade and aid relations between the EU, South Africa and the BLNS countries.

Significance of findings and possibilities for future research

This study set out to assess the emerging relationship between trade liberalisation and financial compensation in BLNS countries' dealings with the EU and South Africa. In the introduction it was stated that determining the nature of compensation payments to the BLNS states would also clarify the current relationship between trade and aid in the case of the EU, South Africa and the BLNS countries.

The suitability of a political acceptance interpretation affects the relationship between trade and aid as perceived since the mid-1980s. If compensation payments to the BLNS states are primarily meant as political side payments, the 'aid for trade' approach – in which aid aims to strengthen developing countries' efforts to participate in the multilateral trading system by supporting liberal economic reform – is less persuasive. Although technically aid is still used to achieve free trade, how this is done diverges markedly from the existing view among donors. EU aid as assessed here aims mainly at accommodating free trade acceptance rather than improving structural reform. In the past the EU has stated that it is an important adherent of the ‘aid for trade’ debate.[1] It can thus be said to have acted in a contradictory way regarding most of its compensation payments to the BLNS states. South Africa can be seen to have done the same when judged by the SACU development component. It challenges the ‘aid for trade’ paradigm by using compensation that mainly intends to overcome political resistance to free trade by the BLNS countries. Because of their contradictory behaviour, both the EU and South Africa have disrupted the ‘aid for trade’ paradigm.

The existence of politically oriented compensation payments shows how determined the EU and South Africa have been to promote free trade with the BLNS countries. It reflects how important political cooperation is considered to be when trying to build higher levels of free trade. Yet such compensation payments also affect the popular vision among many advanced industrial states that the establishment of free trade is mainly promoted through a mutual lowering of trade barriers. In reality, pressure instruments such as compensation payments play an important role in trying to achieve trade liberalisation. The EU, South Africa and countries in the ACP area should seriously take into account the consequences of that notion when developing future trade and aid relationships.

In July 2006 the Doha Round of negotiations, which was to lower tariffs in trade at the multilateral level, was suspended. Gaps between some of the key players proved too great to overcome. Until a new round of multilateral trade negotiations is set up, establishing trade liberalisation is expected to focus mainly on bilateral and regional agreements.[2] In the case of the

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1 European Council & European Commission (2000).

2 The suspension of the Doha Round has been called ‘the starting gun for a race to conclude bilateral trade deals’. Euractiv (2006).

EU and the ACP area, enhancing free trade will move from a dual approach – through multilateral negotiations as well as the bilateral Cotonou agreement – to a single approach in which Cotonou will come to generate most of the attention. The EU's approach towards constituting higher levels of trade liberalisation is now likely to become of even greater importance to the ACP states, as alternative ways of negotiating trade have significantly been reduced.

As a result of the underdevelopment of economic adjustment measures, successful preparation for more open trade by the BLNS countries is possibly affected. That can have serious implications for economic development in the region. With expected production, employment and income losses combined with significantly lower customs revenue as well as insufficient instruments to curb these effects, the BLNS economies face serious economic losses. Donors focusing on trade liberalisation to fight poverty should consider these effects when making use of compensation payments.

There is little reason to consider the BLNS governments' acceptance of the TDCA as an indication that the implementation of free trade is gaining wider support in the ACP region. The policy of promoting free trade as well as serious resistance to it have existed for a long time. In light of the necessity of politically based payments to curb the BLNS governments' resistance to free trade, recent moves towards enhanced free trade are not necessarily the result of widely shifting economic perspectives among developing country governments. Instead they may largely reflect these countries' current political vulnerability. When cooperation by African countries mainly exists at the behest of compensation, scepticism is likely to remain dormant. As political leadership, ownership, accountability and a long-term vision are crucial for building sustainable institutions, a lack thereof affects the opportunities for economic development.

The findings of this research also make it easier to frame expectations regarding the FTAs which the BLNS countries are currently negotiating with the US, and Mercosur and regarding planned negotiations with India, China and Nigeria. As part of the negotiations, the US has already offered US$2 million of capacity-building support after SACU had requested compensation for revenue losses resulting from a future SACU-US FTA.[3] This confirms that similar structures as the ones that occurred in the TDCA situation can be expected elsewhere.

Another area for which this study has implications concerns the future EU-ACP negotiations that will deal with the Cotonou Agreement's successor. Both the ACP states and the EU, having promised in the Cotonou Agreement to start constituting future trade relationships on the basis of full reciprocity, can draw lessons from the intrusion of realist politics into the compensation programmes that were designed for the BLNS states. ACP countries will know better what to expect from the EU in terms of financial support. The size, required targeting and the conditions that are attached to financial compensation will be of special interest to them. The EU now has a clearer idea of how developing countries can respond to compensation payments. It is an example of what the effects could be of the realist approach when used for similar funding in alternative situations.

South Africa's role in the compensation payments to the BLNS states is also useful regarding its relationship with other

[3] Telephonic interview with Peter Draper, research fellow with the development through trade project at the South African Institute of International Affairs (SAIIA). Pretoria, Leiden (August 2004). The US in the past has mentioned that its plans for an FTA with the SACU region are a response to the EU's FTA with South Africa. This makes compensation schemes similar to the one the EU offered all the more understandable. USTR (2003a).

parts of Southern Africa and the rest of the continent. In view of its position as a forerunner and leader in many political and economic matters within Africa, South Africa can be a favourable partner for the EU in future EU-ACP negotiations. The relatively close cooperation between the EU and South Africa in reaction to the TDCA effects on the BLNS states offers lessons for the future. South Africa's current cooperation with the BLNS countries in various SACU FTAs can perhaps now be placed in a new framework. Its support for enhanced free trade with the EU in the entire SACU region might in fact have been a first step in the process of such wider SACU FTA building.

However, as stated in the introduction, this study was mainly set up to find information about the relationship between the BLNS states, the EU and South Africa. The findings provide a first glance at the role of compensation payments in general but further research is needed to decide whether similar forms of compensation in a comparable context exist in other situations and on a larger scale.

It is difficult to determine what the future possibilities are for the relationship between trade and aid in a broader scenario. The findings of this study, that the 'trade not aid' and the 'aid for trade' paradigms have become undermined as a result of the prevalence of a political acceptance framework for compensation payments to the BLNS countries, are in many ways case sensitive. The BLNS situation does not imply that the same can automatically be argued for the EU's trade and aid relations with other ACP countries, or for other donors. The BLNS states' situation can be regarded a forerunner to the scheduled EU-ACP negotiations on the introduction of reciprocal free trade. It is, therefore, easy to assume that the EU will hold on to similar political acceptance policies for all its aid recipients. However, further research is required to provide sufficient evidence for that hypothesis. This study should be seen as an introduction to further studies in wider contexts. It has provided the evidence for one piece of the puzzle, dealing primarily with the EU, South Africa and the BLNS states.

Appendix: Note on methodology

This study aimed to find out how efforts by the EU and South Africa to liberalise trade with the BLNS states operate via a system of financial compensation. It assesses the effects of compensatory payments on the relationship between trade and aid. In this appendix the methodology that was used for this research is outlined in further detail.

A method of process tracing was used to explain how EU and South African pressure have enhanced trade liberalisation in the BLNS states and how such pressure has led to a change in the relationship between trade and aid. Process tracing explores the chain of events that connects an independent variable to an outcome. It seeks to provide evidence for each individual step within that chain.[1]

This approach can be visually captured with the use of a causal diagram. In this diagram the independent variable is situated at the far left, while the dependent variable, or outcome, is on the far right. The variables in between, often referred to as intervening variables, represent the connecting chain of events. Arrows are used to refer to cause-effect relationships.[2] In the causal diagram below, the most important variables of this study, as well as their relationship to each other, can be found.

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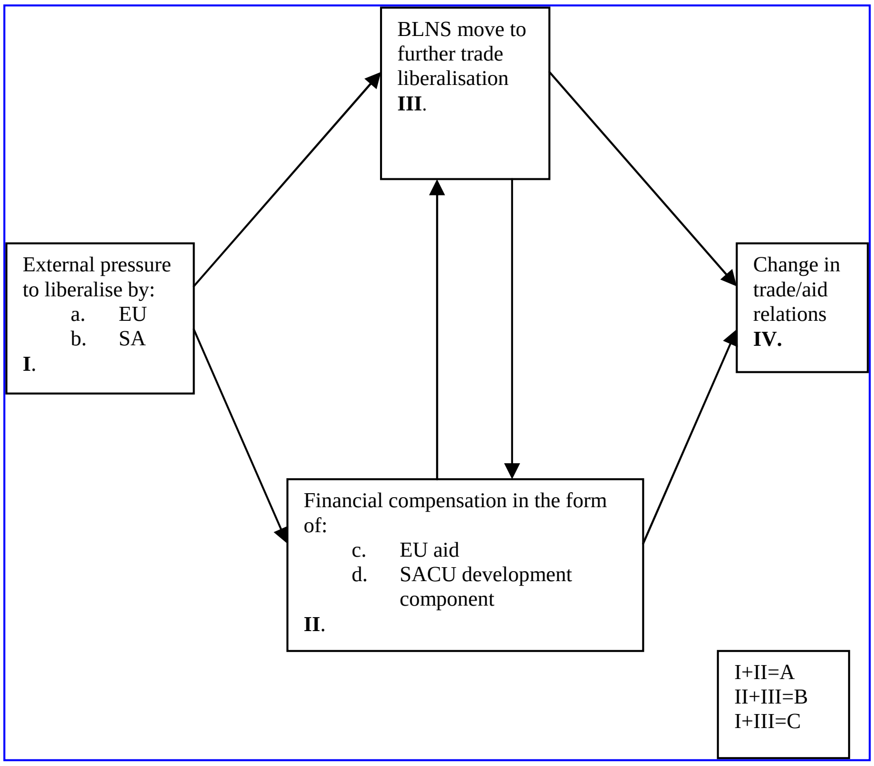
1 Van Evera (1997: 64).

2 Ibid: 10-15.



The outcome or dependent variable that this research paper assesses is the change in relationship between trade and aid (IV). The main causal factor of IV, the independent variable, is considered to be the external pressure by the EU (a) and South Africa (b). This factor is discussed in Chapter Two. As major intervening variables explaining the causal relationship between I and IV, two different factors can be discerned. On the one hand there is a move towards enhanced levels of economic integration with the EU and South Africa (III). And on the other hand, there is financial compensation in the form of EU (c) and South African (d) compensation payments to the BLNS states. These payments, it is argued, have influenced the level of trade liberalisation as implemented by the BLNS states, which makes variable II lead up to variable III. And, vice versa, the level of liberalisation also determines the nature of compensation payments. While the first intervening variable is assessed in Chapter Two, compensation payments are the focus of attention in Chapter Three.

To explain the interdependence of the two intervening variables, this study turns to what is called a conditionality framework. Conditionality emerged in the 1980s and is used to explain how the disbursement of aid in combination with trade adjustments operates in the case of the BLNS states. Together, these two intervening variables create the dependent variable, which shows that the relationship between trade and aid in EU-BLNS trade relations has shifted.

The causal relationships that this research assesses are threefold. First, Chapter Two discusses the way the EU and South Africa have recently used various inducements to influence the BLNS states' behaviour concerning the acceptance of trade liberalisation (C). Chapter Three assesses whether the EU and South Africa are doing so by offering financial compensation to these countries (A). Whether the compensation payments have influenced the level of the BLNS states' trade liberalisation and vice versa (B) is also discussed. The information concerning the nature of these compensation payments is taken from EU, South African, BLNS states and SACU government documents. This information is substantiated with the help of secondary sources. These include interviews that were conducted by the author with EU and South African government representatives and with independent experts on the research topic. Other academic research and newspaper articles have also been extensively used.

In Chapter Four, two different models help to determine how the EU and South Africa have used compensation payments to push for trade liberalisation in the BLNS countries. One model explains the aim of compensation as being to stimulate economic adjustments. The other considers such funding as a form of side-payments that have the primary aim of establishing political support for a move towards trade liberalisation. Focusing on four characteristics of the various compensation payments, Chapter Four assesses which model each payment corresponds best with and hence which best explains the objectives of each payment. Ultimately, this study formulates the extent to which the relationship between trade and aid has changed regarding the EU, South Africa and the BLNS states. It provides an answer as to whether the 'aid for trade' paradigm is still valid.

Class of relevant cases

The class of relevant cases from which the BLNS states were selected consists of a large group of ACP countries.[3] These countries all maintain trade-related aid programmes with the EU under the provisions of the Lomé IV Agreement. The vast majority of ACP states are classified as either lower-income developing countries or least-developed nations. Most receive official development support from the EU through the European Investment Bank and the European Development Fund. All ACP states have recently started negotiations for a new trade agreement with the EU. That agreement is to eventually succeed the provisions under Lomé IV, which officially ended in 2000. As opposed to the non-reciprocal trade relationship that the EU maintained with the ACP states from 1975, the new agreement is set to be built on a basis of reciprocity. The case of trade liberalisation pressure by the EU on the BLNS states fits well within that group.

As part of the successor treaty to Lomé, the EU plans to construct Economic Partnership Agreements (EPA) with regional groupings of states. There are various regional groupings on the African continent that are eligible for constructing these future

3 There are 78 ACP countries in Africa, the Caribbean and the Pacific region.

EPAs. The Southern African Development Community (SADC), which encompasses SACU, is one of those. Also the Economic Community of West African States (ECOWAS) and the Economic Community of Central African States (CEEAC) are existing economic communities that are considered as bases on which to construct EPAs.[4]

Besides their relationship with the EU, many of the African ACP countries also maintain strong ties with South Africa. Since 1994, South Africa has rapidly intensified its cooperation with other African states. Strengthening political and economic links in the region is considered a primary objective of the current government. The manner in which it pursues these goals is based on a market model of free trade and regional integration.[5] The New Partnership for Africa's Development (NEPAD), of which South Africa is one of the founding nations, stimulates similar cooperative plans for the entire continent. South Africa's trade liberalisation pressure on the BLNS states therefore also fits in the context of a larger group of African states.

Many of the economic adjustments that countries in the ACP region have made since the mid-1980s have been effected within a framework of conditionality. In exchange for development assistance, states have been encouraged to implement measures of enhanced trade liberalisation. Such conditioned aid has been an instrument for highly industrialised countries in the North to stimulate their developing partners towards greater economic integration. Since the beginning of Lomé IV in 1990, the EU has shifted its aid policy towards stronger conditionality.[6] The conditionality norm, which also occurs prominently in the case of the

4 European Research Office (2004b).
5 Nkuhlu (1997: 80).
6 Haggard (1995: 24).

BLNS states, has been expanded further with the Cotonou Agreement.

Both the independent variable and the two intervening variables which the diagram above outlines exist in a wider range of cases involving the EU, South Africa and the ACP countries. The pressure to liberalise as well as the combination of trade liberalisation and development assistance – the conditionality norm – are factors that exist in a larger African context.

Positioning within the class of relevant cases

Within this broader range of cases, the BLNS states occupy a ‘typical’ position. But even though typical, the BLNS states are not entirely representative of their class. Their long history as a union – SACU is the world’s oldest customs union – as well as their remarkable effectiveness form a contrast with many other regional groupings in Africa.

However, this effectiveness has made many believe that SACU should function as a building block for a bigger customs union comprising the fourteen SADC countries.[7] Because internal trade barriers within SACU do not exist, the Trade, Development and Cooperation Agreement with South Africa has introduced free trade with the EU for the entire SACU region. SACU is therefore the first regional organisation in Sub-Saharan Africa with which the EU maintains a reciprocal trade relationship. Consequently, it virtually qualifies as a member of an Economic Partnership Agreement.[8] SACU forms a good test case for other African states that are currently renegotiating their trade and development relationships with the EU.

Concerning their relationship with South Africa, the BLNS states also have characteristics that are typical of their class. The

7 Gibb (1997: 68).
8 ECDPM (2001c).

South African government has pushed for further trade liberalisation in the SACU area since 1994.[9] In view of its aims of introducing enhanced free trade and strengthening regional integration within Africa, South Africa's relationship with the BLNS states can be said to function as an exemplary model for the entire continent. By 2010 South Africa intends to have set up a Free Trade Area within the Southern African Development Community (SADC).[10] The well-developed and far-evolved Southern African Customs Union, all members of which are part of SADC, can be seen as a strong building block for South Africa's future relations with the SADC area.

Finally, the EU's close cooperation with South Africa in creating a *de facto* FTA for SACU through the TDCA can be seen as a test case for South Africa's position in future EU-ACP negotiations. South Africa's strong relationship with many African states as well as its African development plans make it a favourable partner for the EU. An assessment of South Africa's role in the BLNS countries' relationship with the EU therefore provides valuable information for the entire continent. Having made use of the conditionality framework, the EU and South Africa might both very well undertake similar efforts on a larger scale in the future.

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9 Gibb (1997: 84).
10 *Mail & Guardian* (2006a).

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