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Economy Watch Namibia – July 2016

The SADC EPA, impact of Brexit on Namibia (page 2), currency update (page 4)

EPA signed – the actual work starts now

After some ten years of negotiations the SADC EPA Member States and the EU finally signed the Economic Partnership Agreement (EPA) on 10 June 2016 in Gaborone, Botswana. The EPA negotiations were necessitated by the need to bring the trade-related stipulations under the Cotonou Agreement in line with World Trade Organisation requirements. The Cotonou Agreement is a comprehensive treaty between the group of 78 African, Caribbean and Pacific states and the EU covering a broad spectrum of topics including trade. At the same time the SADC EPA was signed, the EU and ACP countries started discussions in Windhoek about a new comprehensive development agenda and agreement to replace the Cotonou Agreement that expires in 2020.

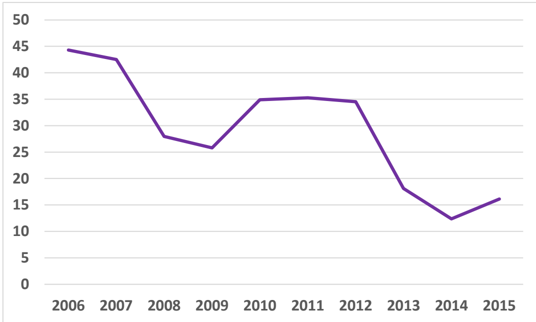
The term 'SADC EPA' might be misleading since the configuration includes only six of the 15 SADC Member States, namely the five SACU countries – Botswana, Lesotho, Namibia, South Africa and Swaziland – and Mozambique. Initially, Angola and Tanzania were part of the SADC EPA, but have withdrawn to trade under the unilateral 'Everything but arms' arrangement with the EU (Angola) or to be part of the negotiations between the East African Community, which is a customs union, and the EU (Tanzania).

The EPA provides duty-free quota-free access for 100 percent of goods from the SADC EPA Member States (for South Africa 98.7 percent) to the lucrative EU market (with the exception of arms), but provides for reciprocal treatment for EU goods into their markets over time. The asymmetric trade liberalisation offers companies in the SADC EPA member states time to adjust to potentially rising competition. While SACU member states will finally grant duty free access to 86 per cent of imports from the EU, Mozambique will open her market to 74 percent of EU imports. The agreement provides for safeguards, meaning SADC EPA member states can apply and or increase import duties in case imports of certain goods increase quickly and substantially and hence threaten domestic producers. Furthermore, value addition between SADC EPA member states can be cumulated - meaning that the various stages of production can take place in more than one member states. Cumulation therefore, can support the creation of regional value chains.

While the EPA provides improved and secured access to the EU market, the benefits to the SADC EPA countries depend on a number of factors: First, the economies have to produce tradeable goods in sizable quantities that are in demand in the EU. Supply side constraints have often hindered African countries exploiting trade preferences offered by developed countries, be it under the Cotonou Agreement or the African Growth and Opportunity Act of the USA. Expanding the production capacity is hence a necessary step for a number of companies. Furthermore, products have to comply with standards applicable in the EU, which in turn requires setting domestic standards and strengthening domestic standards institutions responsible for ensuring adherence to these standards. Social and environmental standards are becoming more relevant than tariffs regarding market access.

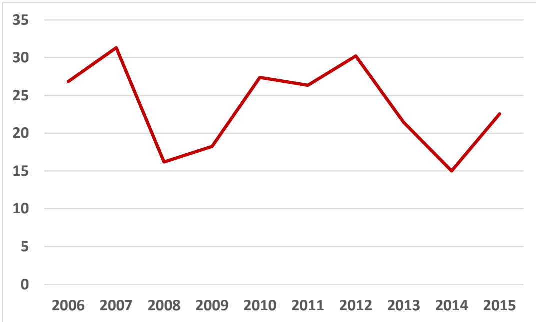
However, the EU has granted preferential market access to a number of countries and regional groupings and is negotiating further trade and investment agreements, which will increase competition on the EU market further and erode relative trade preferences for SADC EPA member states over time.

Exports to the EU as share of total exports in percent, 2006 to 2015



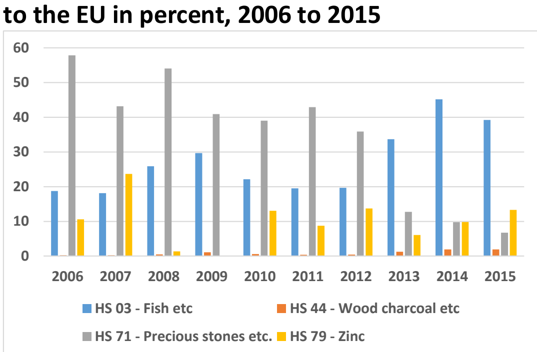
Source: Namibia Statistics Agency

Exports to the EU as share of total exports in percent – excl. diamonds (HS71), 2006 to 2015



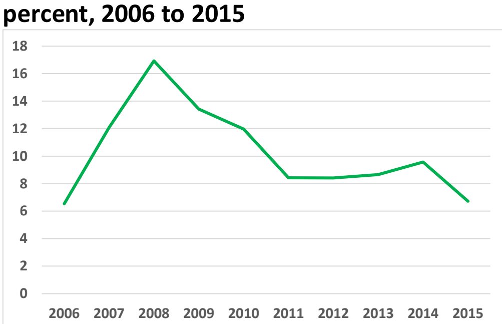
Source: Namibia Statistics Agency.
Note: HS – Harmonised System. The analysis is based on two-digit HS codes.

Main exports to the EU as share of total exports to the EU in percent, 2006 to 2015



Source: Namibia Statistics Agency.

Imports from the EU as share of total imports in percent, 2006 to 2015



Source: Namibia Statistics Agency.

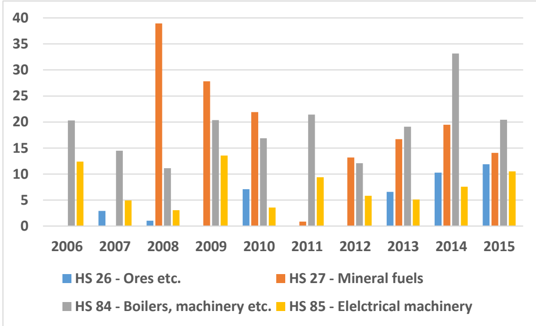
Hence, not only quality assurance is of essence, but also product differentiation and the building of brands. It allows consumers to associate products with a certain country or region and make these products their preferred choice. Companies will compete not only on price, but on other product attributes.

Cumulation of origin provides the opportunity of creating regional value chains but requires harmonisation of regulations and standards across the region so that components of a final product can be sourced from within the region. It also requires the availability of efficient, reliable and competitive services such as transport, communication and financial services that impact on the competitiveness of the manufacturing sector. Functioning regional integration schemes play an important role here as well in order to create a conducive trading environment.

The reciprocity of trade preferences often invokes fear about increased competition from EU producers on the domestic market. However, because of trade liberalisation between South Africa and the EU as agreed upon in the Trade and Development Cooperation Agreement, EU companies already have access to the markets of other SACU member states. Moreover, the reduction or removal of import duties increases the competitiveness of domestic producers that import inputs from the EU and will put them on par with their South African competitors that benefit already from lower import duties.

The work for the private sector starts now to identify new export opportunities to the EU, increase the supply capacity, and to develop new products and brands. The private and public sectors have to work together to strengthen the competitiveness of the economy in general and of companies in particular to exploit new market opportunities and to be prepared for potentially increasing competition on the domestic market.

Main imports from the EU as share of total imports from the EU in percent, 2006 to 2015



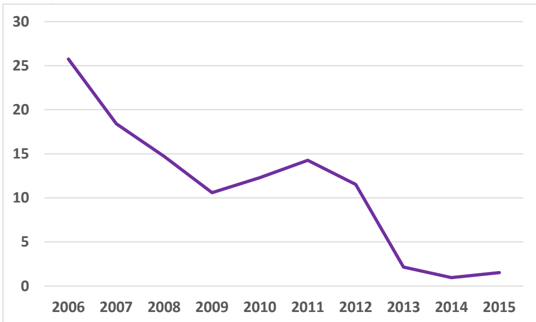
Source: Namibia Statistics Agency.

Brexit – possible impacts on Namibia and lessons learnt

On 23 June 2016 a majority of voters in the United Kingdom voted for the country to leave the European Union after joining the predecessor, the European Economic Community, 43 years ago. The UK is the only member state to ever decide to withdraw from the world's most advanced regional integration project. The popular vote to withdraw has surprised markets, politicians, analysts and apparently the advocates of the 'Leave' camp as well. The results have caused substantial uncertainties which are expected to remain for the near future. The British pound dropped to historic lows against the US dollar and Euro as well as other currencies. Stock markets tumbled as investors moved to safe havens, such as gold, the Japanese yen, Swiss franc and some government bonds with yields consequently plummeting into negative territory.

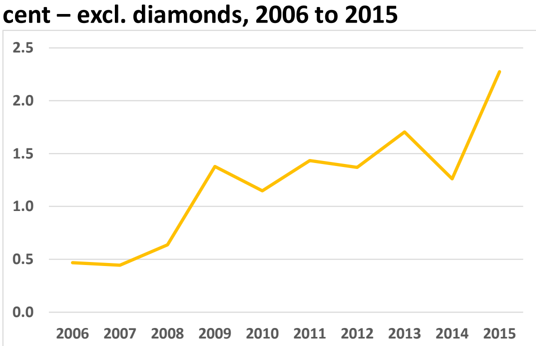
Although the referendum is not binding, politicians have vowed to respect the result that saw the two camps separated by a rather small number of votes - 1.2 million votes. Article 50 of the Lisbon Treaty provides for the withdrawal of Member States from the EU in line with their own constitutional requirements. These remain unclear in the UK, since there is no written constitution. Discussions are ongoing on whether it is the Prime Minister or the Parliament that formally decides on the withdrawal. If Parliament is to decide, it seems unlikely that MPs would overrule the public vote - even though the majority of parliamentarians were in favour of remaining in the EU. After official notice is given to the European Council about the intention to withdraw, the EU Treaty will cease to apply once a withdrawal agreement has been reached. Withdrawal is supposed to take place within two years of the official notice being given unless all parties agree on an extension. Hence, the UK's new relationship with the EU will only be fully known, once agreement between the parties about all the details of the withdrawal has been reached. Furthermore, it remains to be seen,

Exports to the UK as share of total exports in percent, 2006 to 2015



Source: Namibia Statistics Agency

Exports to the UK as share of total exports in percent – excl. diamonds, 2006 to 2015



Source: Namibia Statistics Agency.

how Scotland and Northern Ireland are going to respond to the withdrawal from the EU since their voters voted overwhelmingly in favour of remaining.

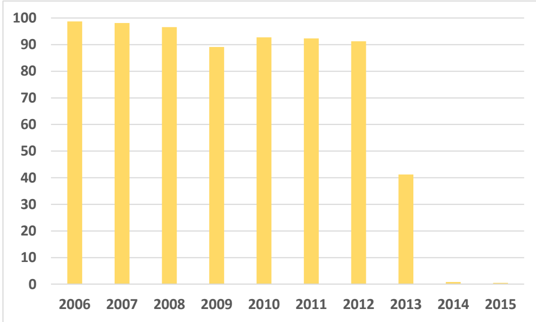
The Brexit has direct and indirect impacts on the Southern African region and Namibia. Globally, such uncertainties result in companies reviewing and postponing investment decisions, which in turn will lead to lower than expected economic growth, reduced consumer demand and reduced demand for commodities. The UK is apparently not in a rush to invoke Article 50 of the treaty which will prolong existing uncertainties. Downward revisions of economic growth are expected to result in more monetary easing. The UK economy might enter into a recession by the end of 2016. The US Federal Reserve Bank has already kept interest rates steady, partly because of disappointing labour market data in May. Although labour market data improved substantially in June markets do not expect an interest rate hike before the end of the year – if at all this year. The Bank of England is expected to halve the interest rate to 0.25 percent in August for the first time since 2009. The monetary easing has led to a strengthening of emerging market currencies, such as the Brazilian real, Russian rouble and South African rand (see below). Gold is again regarded as a safe haven and is one of the best performing minerals this year (see graph below). The gold price increased by 28 percent this year and is 17 percent higher than a year ago. The bullion was trading at USD1,354.25 per ounce on 8 July.

If the UK exits the EU, she will need to re-negotiate all trade arrangements she is currently part of as an EU member including the just signed, but not yet implemented SADC EPA. It can reasonably be expected that the country will prioritise trade negotiations, which absorb substantial yet limited human resources, with the most important trading partners. It is therefore advisable for the SADC EPA member states to already seek clarification from the UK about the way ahead and discuss their own expectations regarding the future relationship with the UK.

The trade impact on Namibia if the UK does not implement the SADC EPA will remain limited since Namibia is not strongly exposed to the UK market. Namibia's exports to the UK accounted for 26 percent of total exports and some 58 percent of exports to the EU market in 2006. The share has declined continuously since then and stood at 1.5 percent of total exports and 9.5 percent of exports to the EU in 2015. Diamonds accounted for 98 percent of Namibia's exports to the UK in 2006, but their share dwindled to 0.5 percent a decade later because of the relocation of the Diamond Trading Company from London to Gaborone. However, the UK remains an important market for Namibian meat and grapes. Some 23 percent of Namibia's total meat exports and almost 100 percent of meat exports to the EU were destined for the UK in 2015, while 21 per cent of fruit exports (grapes) ended up on the UK market accounting for 27 percent of fruit exports to the EU market. Meat contributed 31 percent and fruits 12 percent to Namibia's total exports to the UK in 2015. The UK is also a major market for Namibia's charcoal absorbing 22 percent of Namibia's total charcoal exports and 50 percent of charcoal exports to the EU market. Charcoal exports made up 10 percent of total exports to the UK in 2015. While the UK has been an import export destination for beef and grapes, new market opportunities are opening up for Namibian beef exporters. Namibia has been cleared for beef exports to China through Hong Kong and is expected to be allowed to export to the USA by the end of 2016. This could mitigate against any possible disruption of meat exports to the UK.

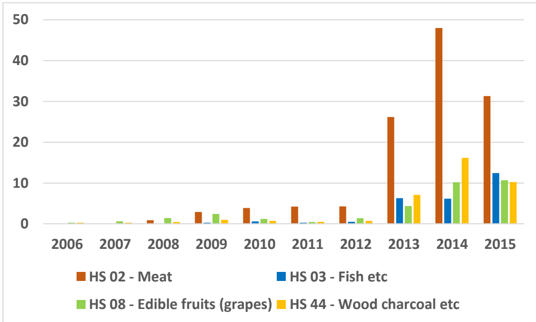
Imports from the UK followed a similar trend as exports. While imports rose sharply from 0.7 percent of total imports in 2006 to 7.2 percent in 2008 mainly because of substantially higher imports of fuels and diamonds from the UK, the share declined continuously thereafter to not even 0.5 percent by 2015. Boilers

Diamond exports to the UK as share of total exports to the UK in percent, 2006 to 2015.



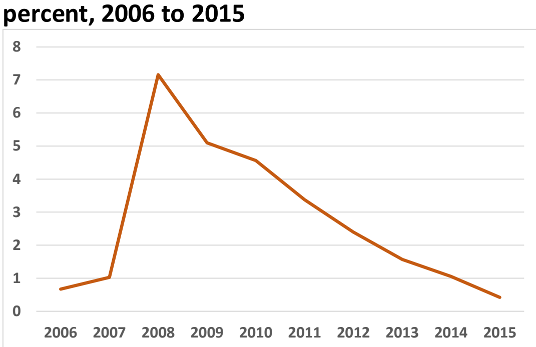
Source: Namibia Statistics Agency.

Other main exports to the UK as share of total exports to the EU in percent, 2006 to 2015



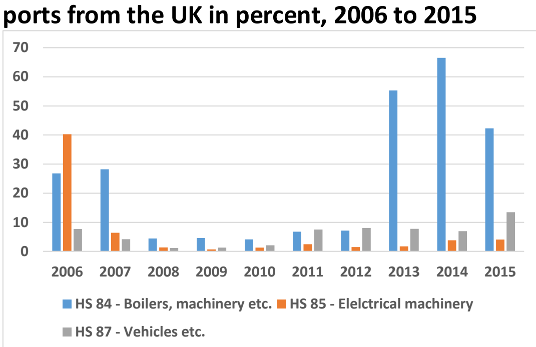
Source: Namibia Statistics Agency.

Imports from the UK as share of total imports in percent, 2006 to 2015



Source: Namibia Statistics Agency.

Main imports from the UK as share of total imports from the UK in percent, 2006 to 2015



Source: Namibia Statistics Agency

& machinery and vehicles contributed more than 50 percent of total imports from the UK in the past three years.

There are a few lessons we could learn for our own regional and continental integration ambitions. In order to place regional or even continental integration on a strong foundation the private sector and civil society should be part of the process. Information could be shared about progress being made with the implementation of regional protocols and about ongoing negotiations be it at SACU, Tripartite FTA or Continental FTA level. This would ensure that the private sector and the population at large is aware of the implications of regional integration and the opportunities and challenges. Last but not least, there is need to build a regional identity and strengthen common regional interests.

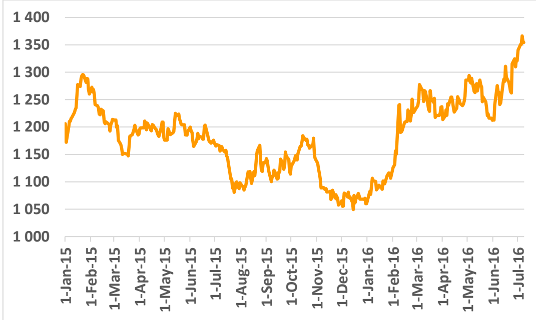
Namibia dollar gained ground again

The Namibia dollar (NAD) continued to depreciate against the USD, GBP and EUR at the beginning of the year when it was trading at NAD16.9 per USD, NAD24.5 per GBP and NAD18.4 per EUR, but has gained ground recently. The currency strengthened after Standard & Poor's decision at the beginning of June not to downgrade the sovereign rating of South Africa to 'junk' status and then made further gains in the aftermath of the Brexit decision. The NAD appreciated by 18.5 percent against the British pound that has fallen to historic lows vis-à-vis most currencies although recovering slightly after the swift and smooth hand over of power to new Prime Minister Theresa May. The NAD recovered some of the ground it lost last year and is trading 1.5 percent above levels in July 2015. The domestic currency appreciated against the USD (8.4 percent) and EUR (7.0 percent), but is still significantly weaker than at the beginning of July 2015. It was trading 15.4 and 15.5 percent lower respectively than in July 2015. On 12 July, one USD, GBP and EUR were worth NAD14.3199, NAD18.8106 and NAD15.9156 respectively.

The Brazilian real and Russian rouble have been the best performing currencies this year behind the Japanese yen. Consequently, the NAD depreciated against both currencies by 10.0 and 5.6 percent respectively this year. Compared to a year ago, the NAD was trading 12.3 and 2.6 percent lower respectively. On the other hand, the Chinese yuan and Indian rupee have both weakened against the NAD this year by 10.7 and 9.4 percent respectively. They remain, however, 7.2 and 9.0 percent stronger than a year ago. On 12 July the NAD was trading at 4.3253 (real); 2.1422 (yuan); 0.2133 (rupee) and 0.2239 (rouble).

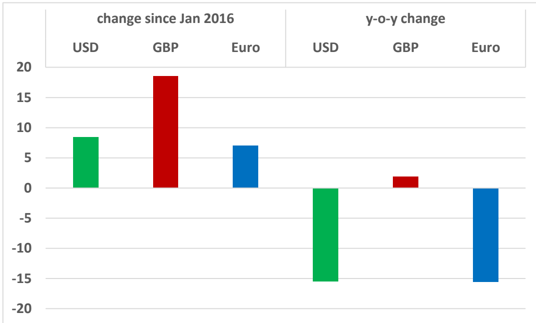
The prevailing uncertainties concerning the Brexit process, the timeline and its implications will dampen economic growth not only in the UK and Euro area, but in other parts of the world as well. Measures are being put in place in the UK and some other European countries such as Italy to stabilise the financial sectors. The Bank of England is expected to lower its repo rate in August after it kept it stable at 0.5 percent on 14 July and the Federal Reserve Bank will most likely not increase interest rates this year and could even lower the rate to provide some stimulus to the domestic economy. This could strengthen emerging market currencies including the South African rand. However, a downgrading of South Africa's sovereign rating is not off the agenda and the next review is due at the end of the year. Hence, while the ZAR/NAD have appreciated recently, we can expect continuous volatility over the next months as investors adjust their portfolios.

Gold price in USD per ounce, Jan. 15 to Jul. 16



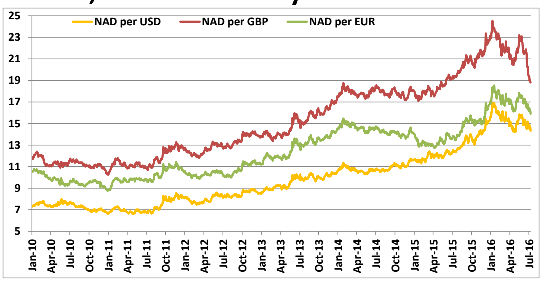
Source: World Gold Council

Appreciation (positive) and depreciation (negative scale) of the NAD against USD, GBP and EUR.



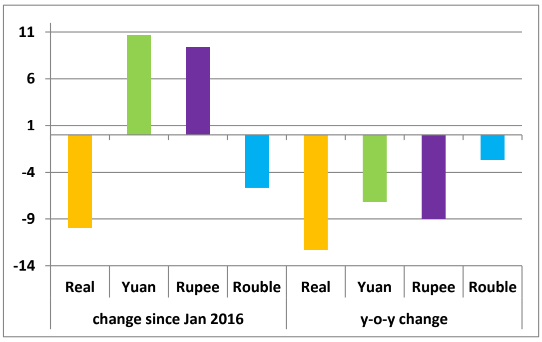
Source: South African Reserve bank, daily data

Exchange rates of the NAD versus major currencies, Jan. 2010 to July 2016



Source: South African Reserve bank, daily data

Appreciation (positive) and depreciation (negative scale) of the NAD against the BRIC currencies.



Source: South African Reserve bank, daily data

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