SOUTHERN AFRICA GLOBAL COMPETITIVENESS HUB

INSIDE SOUTHERN AFRICAN TRADE

ISSUE 14 OCTOBER 2008

Madagascar, the world's fourth largest island nation, lies a mere 400 kilometers from Africa's east coast, yet seems more closely connected to its island neighbours and France than to the continent.

Although still one of the poorest nations in the world, Madagascar is growing fast, experiencing economic growth of around five percent on average for each of the past five years. Our Madagascar Fact Sheet on page 10 provides a brief overview of the country and its economy.

In 2005, the country became a member of SADC and last year it joined the SADC Free Trade Area. In our 'In Focus' article we look at how these developments are viewed within Madagascar, where some see opportunities while others feel threatened by the prospects of increased competition.

We also discuss these issues, as well as the country's overall economic policies, international trade and competitiveness, with the country's Trade Minister, Ivohasina Razafimahefa, who believes Madagascar can become the bread basket of SADC.

In the Guest Perspective, John Hargreaves, vice-president of the Madagascar Economic Processing Zone Association writes about the great successes of the country's textile and apparel sector, warning also about some of the challenges that the future may bring.

We hope you will enjoy this issue of INSAT and we invite you to share your opinions and suggestions with us by writing to *insat@satradehub.org*.

INSIDE THIS ISSUE

USAID | SOUTHERN AFRICA
FROM THE AMERICAN PEOPLE

Published by the Southern Africa Global Competitiveness Hub as part of its Trade Facilitation and Capacity Building Activities, and sponsored by USAID.

AROUND SOUTHERN AFRICA

COUNTRIES IN THE REGION FACE RENEWED PRESSURE TO SIGN FAR-REACHING EPAs

The European Union is hoping to finalize an Economic Partnership Agreement (EPA) with several countries in Southern Africa, in what is known as the SADC-EPA grouping, by the end of this year. European negotiators are pushing for a far-reaching agreement that would cover, in addition to trade in goods, trade in services and the so called "Singapore issues" (investment, competition, government procurement and trade facilitation). But analysts say the EU is facing an uphill battle and whether it can convince countries in the region to include the new generation issues in the final EPA remains to be seen.

Neither Ready nor Interested

Throughout last year, the seven countries that make up the SADC negotiating group – Angola, Botswana, Lesotho, Mozambique, Swaziland, Namibia and South Africa – battled to limit the negotiations to trade in goods. South Africa eventually withdrew from the talks in part because of the Agreements' reference to trade in services and some of the Singapore issues. Botswana, Lesotho, Namibia and Swaziland signed bilateral interim deals under which they agreed to include trade in services and the Singapore issues in future EPA negotiations.

But with the deadline for concluding final EPAs less than three months away, governments in the region do not appear any more ready or willing to make firm commitments on these issues than they were a year ago. They say they do not have the institutional capacity to deal properly with competition policy, for example, at the national or regional levels. They also argue that with services and investment, it is necessary to ensure that a proper regulatory environment is established before liberalization takes place. But establishing such a framework for various services sector in such a short time span would be very difficult.

Many of these new generation issues have been removed from multilateral negotiations in the WTO at the behest of developing countries. The EU's insistence on including the Singapore issues in multilateral trade negotiations led to the walk out by African and Asian delegates at the WTO's Ministerial Meeting in Cancun in 2003.

And many fear that forcing these issues on the region in the absence of the necessary institutional and technical capacities would undermine national development objectives in both developing and least developed countries (LDCs), not just in the region, but throughout Africa.

"While all will depend on how the agreements will be shaped, the main issue of concern is that the region lacks the negotiating, policy and regulatory capacity to adapt their economies to the proposed changes," says one official with the United Nations Conference on Trade and Development (UNCTAD), who spoke on condition of anonymity.

"There is always a difference between an agreement in Geneva or Brussels among trade negotiators and the capacity of poor countries to derive the presumed benefits at home. What will end up happening is that the EU's draft will be adopted wholesale or with minor changes. I don't see it changing much. The risk is that the final agreement will not have as much operational value to SADC countries as to the EU," the official added.

The EU says it will provide countries that agree to include the Singapore issues in EPAs with additional capacity building assistance and technical support that will enable these countries to comply with their obligations. But regional officials say the aid the EU is promising with respect to the Singapore issues would not be designated through a newly created fund, but rather would be provided through the existing European Development Fund.

While lack of institutional capacity is often cited by governments as the reason for not making firm commitments on the extended list of issues proposed by the EU, it is not the only or even the most important factor.

The more important reason, analysts say, stems from concerns among governments in the region that including some of these issues in the EPAs would limit their ability to pursue domestic policy objectives. Moreover, governments see some of the provisions proposed by the EU as an unacceptable intrusion into national sovereignty.

Take for example the issue of government procurement, which is one of the more contentious issues in the negotiations. The EU would like regional governments to open their procurement markets, simplify tender procedures and grant European firms national treatment. In principle, the proposed provisions would do African countries a lot of good. They would pave the way for transparent and fair procurement practices and would limit anti-competitive practices. They would also lead to establishing regulatory frameworks and agencies to deal with competition issues.

Regional analysts say that while complying with such provisions would improve efficiency and spur economic growth, it would also limit governments' ability to use fiscal policy to stimulate their domestic economies when needed.

Hussein Kamote, a policy research analyst with the Confederation of Tanzanian Industries (CTI), says during an economic slowdown governments usually use public spending to stimulate domestic production by contracting local companies. He argues that provisions proposed by the EU on government

ARTICLE 67 OF THE INTERIM EPA

Second stage of negotiations

The Parties agree to continue negotiations in 2008 to extend the scope of the present Agreement. For the purpose of this Title, the SADC EPA States will be constituted of Botswana, Lesotho, Mozambique and Swaziland. The remaining SADC EPA States may join the process of negotiation on a similar basis. To this end, they will notify in writing the EC Party and the other SADC EPA States.

I.a) Trade in Services

1. The Parties recognise the growing importance of trade in services for the development of their economies and reaffirm their respective rights and obligations under the General Agreement on Trade in Services (GATS).

2. No later than 31 December 2008 the Parties will complete negotiations on services liberalisation, on the basis of the following:

- liberalisation schedule for one service sector for each participating SADC EPA State;

- commitment to a standstill as specified in Article V.1.b(ii) GATS, for all services sectors;

- agreement to negotiate progressive liberalisation with substantial sectoral coverage within a period of three years following the conclusion of the full EPA.

I.b) Cooperation in Services

1. The Parties recognise that trade capacity building can support the development of economic activities, in particular in services sectors. To this end, the EC Party agrees to support capacity building aimed at strengthening the regulatory framework of the participating SADC EPA States.

2. By the time of laying down the necessary arrangements for the liberalisation of trade in services, the Parties will define the specific cooperation objectives, principles and procedures that will accompany trade liberalisation.

II.a) Investment

1. The Parties agree to negotiate an Investment chapter, taking into account the relevant provisions of the SADC Protocol on Finance and Investment, no later than 31 December 2008.

II.b) Cooperation on Investment

1. The EC Party agrees to provide adequate technical assistance to facilitate negotiations and implementation of the Investment chapter.

III. Competition and Government Procurement

1. The EC Party agrees to cooperate with a view to strengthening regional capacity in these areas. Negotiations will only be envisaged once adequate regional capacity has been built.

procurement would "limit the powers of LDC governments to use fiscal expenditure as a key tool."

In many developing countries, government procurement accounts for as much as half of Gross Domestic Product. In Tanzania, for example, government procurement in 2003 constituted about 70 percent of public expenditure.

But some observers argue the concerns about government procurement are not justifiable because the Interim Agreements call only for cooperative arrangements and do not require negotiating government procurement any further in the final EPA.

The EU is also demanding market access concessions on investment, including commitments to grant national treatment to European investors and remove some restrictions on sectors that may currently be reserved for national investors/citizens. For example, the EU would like governments in the region to remove restrictions on the number of foreign companies allowed in one sector and the size of shares held by foreign investors in a company. Also, this may include setting of minimum investment values, and requirement of joint ventures, amongst others. The EU also wants governments to abolish restrictions on movements of capital and allow repatriation of profits by foreign-owned companies.

But many say that while some of these provisions would enhance the investment climate in the region, they are too focused on investors' rights and overlook investors' obligations to host countries, or obligations that EU countries have towards their investors.

Resisting the Pressure

As the end of the year approaches, countries in Southern Africa, like other ACP countries, are likely to face pressure from the EU to conclude deals that may contain some items on the EU's wish list of issues.

But that would not be new to governments in the region. They went through a similar process last year and they ended up with deals that they were not happy with due to the last minute inclusion of some controversial issues. This time around many governments are hoping to negotiate limited provisions on these issues, if any.

"…the degree of detail of any [provisions on Singapore issues] in the full EPAs to be concluded remains to be determined. Furthermore, in principle, it is possible to include varying degrees of commitment on services and trade-related issues by different members of the region within one full regional EPA, though deeper integration in these areas may ultimately require common regional undertakings," says a report released earlier this year by the UK-based Overseas Development Institute.

Many observers say that African negotiators have learned the lesson and will be better at resisting pressure and defending their interests. Perhaps they will be even better at coordinating their negotiating positions.

FOOD CRISIS BRINGS REGIONAL TRADE AND GMOs TO THE FORE

In June, African agriculture ministers agreed during the Food and Agriculture Organization of the United Nations (FAO) regional meeting for Africa that they need to boost agricultural production and expand regional trade to bring an end to the food shortage that is threatening millions all over the continent.

Earlier that month, the FAO forged a partnership with a number of key players in agricultural development, including the International Fund for Agricultural Development (IFAD) and the World Food Program (WFP), to boost food production in Africa in part by linking highly productive agricultural regions to areas suffering from food shortages.

The renewed push to expand agricultural production and trade in Africa is putting fresh pressure on African governments to rethink their regional trade policies, including those on Genetically Modified Organisms (GMOs).

Intra-African Trade: One Key to Food Security

African policy makers agree that expanding intra-African trade and integration is key to overcoming Africa's food shortages. Yet despite years of trade liberalization and a plethora of regional agreements, intra-African trade still accounts for a very small share of total trade between African countries and the rest of the world.

Part of the reason for limited intra-African trade dates back to colonial times when African countries traded primarily with their colonial rulers rather than with each other. Breaking this pattern is not easy especially since most countries in Africa export a limited range of products.

Another part of the reason has to do with poor trade policies. Many governments in Africa still restrict cross-border trade in food staples. For example, in the Southern African Development Community (SADC) many countries use import bans and import and export licenses on strategic commodities such as maize, maize meal, meat, poultry and sugar, even at times of domestic food shortages.

Licenses are also required for the export of agricultural inputs like oil seeds and fertilizers. Such restrictions on trade flows not only lead to price volatility and higher consumer prices, they also diminish farm prices and, consequently, incentives for production.

Poor infrastructure, administrative barriers and corruption at border posts have also been important factors in hindering intra-African integration.

A recent study that looked at trade along the Gaborone-Durban transport corridor, which links Botswana to the South African Port of Durban, estimates the additional costs associated with toll roads, customs clearance procedures and delays at the two border posts in Botswana and South Africa at 25 percent of total transport costs. In other parts of Africa these costs can be significantly higher.

As a result of all these factors, agricultural markets in Africa are extremely fragmented along sub-regional, national and sub-national levels. This means that African food markets can not ensure profitability for sizeable private investment in the different stages of the commodity chain. It also means that farmers in highly productive regions of Africa can not have easy access to growing markets across national borders.

Jones Govereh of Michigan State University argues in a policy note that production of food staples for the growing urban markets and regional cross- border trade is "the largest growth opportunity available for African farmers" and that facilitating access to the these markets is "critical for efforts to stimulate agricultural production growth." Furthermore, he argues that "failure to facilitate expansion of national and regional trade in food staples risks stalling production, growth and private investment in agriculture. In thin national markets, without export outlets, production surges lead easily to price collapses."

GMOs: Modifying the Debate

Another trade-related issue that has acquired renewed interest in light of the food crisis is the policy around GMOs. In Africa, some countries have embraced GMOs as a way to increase food production. GMOs tend to be more pest-resistant and give better yields than conventional crops. In South Africa for example, biotech maize, soy, and cotton planted areas increased by 30 percent to approximately 1.8 million hectares between 2006 and 2007 according to a U.S. Department of Agriculture report.

But many African governments have banned GM crops partly as a health precaution and partly on the grounds that they could contaminate their own crops, thus hurting future exports to Europe, Africa's largest export market. The concern is that exports of GM crops could lead to cross-pollination in the EU, which has zero tolerance for GM traces in non-GM imports.

Resistance to GMOs in Africa made the headlines in 2002 and triggered a contentious debate when Zambia rejected GM food aid at a time of critical food shortages in the country.

The varying GMO policies within Africa have hampered trade between countries that have accepted GMOs and those that have not. A study by the Food, Agriculture and Natural Resources Analysis Network (FANRPAN) on eight countries in Southern Africa confirms that, among other non-tariff barriers, disparate policies on GMOs have constrained food trade within SADC.

But observers say with soaring food prices and food shortages threatening millions in Africa, resistance to GMOs in Africa is likely to break down, especially since many important players in global agricultural trade, including Brazil, India and China, have forged ahead with the technology.

Pressure is also mounting on the European Commission to speed up GM crop approvals to counter soaring food prices. A recent report by the Joint Research Centre, the European Union's scientific and technical research laboratory, on the health impact of GM foods said that foods made with GM ingredients are safe to eat. According to recent press reports, the European Commission will soon propose relaxing the zero tolerance policy on food imports in response to pressure from the food industry and farmers who demand allowing imports of GM animal feed.

But no matter what position African governments take on GM crops, analysts say, they will face the same challenge: developing a framework for regulating GM trade, especially among regional groupings many of whom have launched or are planning free trade areas.

Most African countries lack technological capacity to screen and detect GMOs or deal with safety requirements necessary for approving general GMO. Therefore, reaching a meaningful agreement on the issue would be difficult.

Jonathan Mafukidze, a research fellow with the Human and Social Research Centre (HSRC), a regional research institute based in South Africa argues that the absence of harmonized sanitary and phytosanitary (SPS) and bio-safety regulations, among other barriers, trade in agricultural products within SADC's newly established free trade area will remain low.

"Common bio-safety regulations are particularly important at this point because of the high incidences of genetically modified food products in the region brought about by the hunger situation in the SADC," he says.

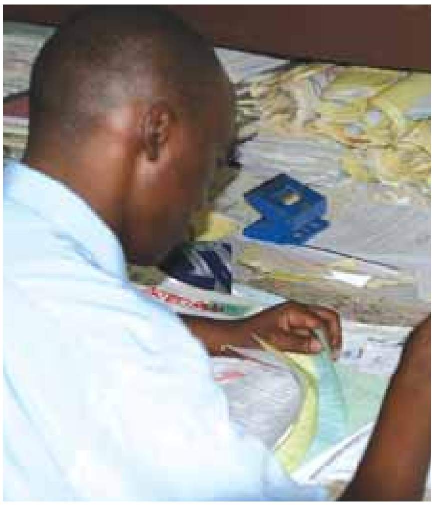
ZAMBIA, ZIM TO LAUNCH THE REGION'S FIRST ONE-STOP BORDER POST

One year after the initial deadline, the Common Market for East and Southern Africa (COMESA) will launch the region's first one-stop border post at Chirundu between Zambia and Zimbabwe, one of the busiest inland ports in the Eastern and Southern African region later this year.

The border post, which will be supported by UNCTAD's Automated System for Customs Data and Management (ASYCUDA), is expected to speed trade flows between the two countries and cut landed costs by nearly 40 percent. Both Zimbabwe and Zambia said that they finalized the requisite legislative framework to launch ASYCUDA.

Sources say the one-stop border post will be an important test of COMESA's preparedness to launch a free trade area later this year. Improvements in ports and border crossings are critical to increasing intra-regional trade within the proposed COMESA customs union.

The nineteen-member regional grouping first launched efforts to link the national customs systems of Member States through a harmonized electronic management system in 1999.



"The training of customs officials and clearing agencies on the new transit procedures started in June 2008," says Joseph Musariri, the president of the Shipping and Forwarding Agents Associations of Southern Africa.

According to shipping and forwarding agents, freight clearance at one border post in COMESA has been taking as long as five days owing to customs red-tape, lack of a harmonized customs management system and stringent regulatory requirements.

In September last year, Donald Kaberuka, the president of the African Development Bank, said these long clearance time lags at Africa's ports and border posts constituted an "unwritten tax on exporters."

A 2005 World Bank Trade Note shows that for a majority of sub-Saharan African countries, transport delays accounted for quite a sizeable proportion of their international shipping costs as a ratio of the value of trade.

ONE-STOP BORDER POST BETWEEN MOZAMBIQUE AND SA PROMISES INCREASED TRADE

Construction of a 24-hour one-stop border post between South Africa and Mozambique began in early August, raising hopes for increased trade along one of the region's most important transport corridors.

The US$100 million border post is expected to significantly cut time and cost of trade along the Maputo Corridor, which links South Africa's most industrialized and productive region, Gauteng province, with Maputo's sea port in Mozambique. The corridor, which includes road, rail, port and terminal facilities, is also vitally important for Mozambique's economy given the country's close economic and trade ties with South Africa.

Brenda Horne, CEO of Maputo Corridor Logistics Initiative, one of the driving forces behind the project, says the new border post will use simplified procedures and an EDI (electronic data interchange) system that will link the customs administrations in the two countries to accelerate customs clearance.

"Relevant support systems such as EDI across both countries and all departments…[will] ensure the benefits of the huge investment of more than 600 million Rands will serve our corridor and the region and ultimately bring down the cost of doing business, transportation costs and support regional integration," she said.

Business people, who often complain of the inefficiencies and mounting congestion at border crossings between South Africa and Mozambique, are pinning high hopes on the new border post.

"For many years we have been waiting for a 24-hour joint border at Ressano Garcia and Komaatipoort borders. [The 24-hour border post] will mean speeding up imports to take one day compared to four days or more, fewer documentation processes and less costs," says Jim Lafleur of Mozambique's Confederation of Business Associations.

The one-stop border post is expected to be operational in the first quarter of 2010.

NEWS BRIEFS

SUMMIT LAUCHES SADC FREE TRADE AREA

SADC officially launched its free trade area (SADC FTA), in the making since 2000, at the group's annual summit in August. Under the FTA, 85 percent of the tariff lines of SADC countries will be exempt from customs duties but Value Added Tax (VAT) will still be payable at domestic rates.

The twelve countries that are signatories to the SADC Protocol on Trade agreed to reduce customs duties over a 10-year period starting in September 2000. Countries will reduce customs duties according to the so-called tariff offers, with more developed countries eliminating their duties faster than their lesser developed counterparts.

With the exception of products not covered in the Protocol (such as sugar, arms, ivory and second hand cars), all goods will be traded freely by January 2012. Goods originating in SADC countries, other than certain excluded products, already enter the Southern African Customs Union (SACU) free of duty. Non-SACU countries have been allowed to retain tariffs against South African producers for longer than for the other SACU countries; Botswana, Lesotho, Namibia, and Swaziland (BLNS).

Angola has acceded to the SADC Protocol on Trade, but has not yet submitted its tariff offer. It had been expected to do so during the summit this year, but postponed its offer on the basis that its producers are not yet ready for competition from products from other SADC countries. The Democratic Republic of the Congo (DRC) has not acceded to the protocol and the Seychelles, which rejoined SADC in August, has not yet indicated whether or when it will be joining the FTA.

TANZANIA: TOURISM LEADING EXPORT SECTOR IMPROVEMENT

The low-cost high-volume tourism strategy pursued by Tanzania appears to be paying off. The Standard Bank Research Department in August reported that tourism has become Tanzania's leading foreign exchange earner. According to figures released by the Bank of Tanzania, tourism trade – hotels and restaurants – accounted for about 25 percent of the country's foreign exchange earnings.

But infrastructural bottlenecks will have to be addressed if the tourism sector is to reach its full potential, Standard Bank economists argue.

BOTSWANA HARMONIZES VEHICLE AND AXLE LOAD LIMITS

In a move that will facilitate the movement of goods within the SADC and COMESA region, Botswana in July announced that it will implement new axle and vehicle load limits of 9 tons, 18 tons, 24 tons and 56 tons,which is in line with its neighbours, Namibia and South Africa.

"This is good news. We have been fighting for this for the past ten years and now it has finally happened," says Barney Curtis, Executive Officer of the Federation of East and Southern African Road Transport Associations (FESARTA).

According to Curtis, a few related issues still need to be addressed: the harmonization of load limits on the Tete corridor and other roads in Mozambique, which are still on 48 tones, with the SADC and COMESA limits; the ban on interlink vehicle combinations in Tanzania; the harmonization of weighbridge allowances; and the harmonization of load limits on super single tires.

EXPORTS UNDER AGOA INCREASE SIGNIFCIANTLY IN 2008

Year on year exports from all AGOA beneficiares to the US grew by 62 percent in July according to data published on AGOA.info, a website that tracks AGOA-related developments. Nigeria and Angola continue to dominate overall exports by value, although South Africa – the third largest exporter under AGOA – has more than doubled its exports to the US during this period (from US$1.1 billion over the same period last year to US$2.26 billion this year). A weaker Rand/Dollar exchange rate indicates that this increase translates into an even larger increase in local currency terms.

MAURITIUS ALLOWED TO USE THIRD COUNTRY FABRICS UNDER AGOA

The US Senate in early October passed legislation that will see Mauritius declared eligible to use third country fabrics and still qualify for duty-free exports under AGOA. Until now, this derogation had been blocked due to protests from Lesotho, another AGOA beneficiary which competes with Mauritius in the American market.

CAPE TO CAIRO FREE TRADE AREA ON THE HORIZON

At the end of a historic tri-partite summit between SADC, COMESA and the East African Community (EAC) in October in Kampala, Uganda, participants issued a communique expressing their intention to merge the three regional economic communities into 'one regional economic grouping'.

"This is an important step towards the formation of the African Economic Community," Jerry Vilakazi, president of the SADC Employers Group responded in a press release. "Our members welcome the political commitment shown towards increasing intra-regional trade and economic linkages between the countries of Southern and Eastern Africa. This commitment must now be matched by a focus on effective implementation."

According to the e-COMESA newsletter, the merger of the three blocks will create an economic grouping comprising 26 countries with a combined population of 527 million and a combined GDP of US$624 billion.

INSIDE THE PRIVATE SECTOR

NEW CEMENT FACTORY IN TANZANIA TO MEET GROWING DEMAND

Nigeria's industrial conglomerate Dangote Group will soon begin building Tanzania's biggest cement factory in the Mtwara region in the Southern part of the country.

The plan to build the factory comes amid surging demand for cement and soaring prices - primarily as a result of increases in freight costs - both in Tanzania and throughout the region. Earlier this year, Tanzania faced a serious cement shortage which drove cement prices sharply higher and led the Government to waive duties on imported cement.

The growing demand for cement together with the high prices have spurred interest within Tanzania, and in many other cement producing African countries, in investment in local cement production.

Nigeria's Dangote Group, which operates a chain of companies in the cement, food transport and agriculture industries, was quick to seize on the conducive market conditions.

In July, Dangote Group reached a US$1.45 billion agreement with China National Materials Co., or Sinoma, under which Sinoma will build six cement production lines in Tanzania, Congo, Ethiopia, Zambia, and Equatorial Guinea, the statement said.

Sources with Dangote Group say the US$400 million factory in Tanzania will have an annual output capacity of five million tons, most of which will be exported to other countries in the region such as Burundi, Democratic Republic of Congo, Rwanda and Uganda. Currently, Tanzania has three cement plants with a combined output of 1.5 million metric tons per annum.

Plans are also well advanced to provide the necessary infrastructure to facilitate production and exports from the factory.

A 300MW gas-fired power plant that is being built will provide the factory with a reliable source of energy while ongoing rehabilitation of the Mtwara Corridor will improve the region's access to the Port of Dar es Salam.

The Tanzanian President Jakaya Kikwete expressed hope that the factory will benefit the construction industry and the economy as a whole.

"When this investor finishes construction of the cement plant in Mtwara which will produce five million tons per year, our construction industry will benefit a lot so too will the economy," he said. "We need to sustain current economic growth for ten years in order for the common man in the street to feel the impact and manufacturing is a very important area of the economy."

STATE-OF-THE-ART PASTA FACTORY OPENS IN BOTSWANA

South Africa's Southern Foods Group, through its subsidiary Prima Foods Botswana, has launched production of a new pasta plant with hopes to increase its share in regional markets. The plant, which is being co-financed by the Botswana Development Corporation, is part of a broad drive by the Botswanan Government to reduce the country's dependency on the diamond industry by diversifying the economy:

The US$3 million state-of-the-art plant, situated at Ramotswa, south of the capital Gaborone, has the capacity to produce 2.25 metric tones per hour of pasta products and biscuits, as well as other food products.

Prima Food's General Manager Johann Swanepoel says that at the fore of Prima Foods efforts to establish a strong foothold in the domestic and regional markets are plans to produce a variety of high quality products to cater to the upper segment of the food market.

"The factory is the only manufacturer of high quality pasta and biscuit products in Botswana. The plan is to diversify later with complementary pasta products by expanding the range of products," Swanepoel says, adding that the company is planning to export to sub-Sahara African countries including the Democratic Republic of the Congo, South Africa, Zambia and Zimbabwe.

Swanepoel acknowledges that conditions in the food market are less than ideal but also speaks confidently about his company's ability to compete.

"With the current rises in food prices against cheaper imports, we are likely to experience a decrease in sales and loss of revenues," he says, "to survive the market challenges, we have to become more efficient, proactive and competitive. Furthermore, local retailers can add value to our operation if they promote local brands."

Botswana Assistant Minister of Trade and Industry Mr. Duke Lefhoko expressed hope at the opening of the factory that the factory will not only create more employment but will also facilitate transfer of skills and knowledge to locals.

INSIDE THE DONOR COMMUNITY

MCA MADAGASCAR RE-PLANTS OPPORTUNITIES

Louis Velonjara proudly shows off his patch of tomatoes, green peppers, lettuce, beans and other vegetables. His little 'farm', located near Hellville, the capital of Nosy Be, covers less than a hectare. Yet its produce will allow him to buy a future for his son, Aristide, who dreams of becoming a mechanic.

Since shortly after starting this farm in April, Louis has been harvesting nearly 40kg of tomatoes a week, earning him around 350AR (US$8) – a respectable return in a country where the average annual per capita income is only US$320. And luckily for Louis, the climate of Nosy Be is such that he can cultivate his crops all year round. He also managed to secure (at least temporarily) a spot close to a stream which allows him to irrigate his crops when necessary.

Louis' efforts are supported by the Agricultural Business Investment (ABI) Project of the Millennium Challenge Account in Madagascar (MCA-Madagascar), which is financed under the US$110 million Millennium Challenge Compact signed between the US and the Malagasy Government in March 2005 as the first of its kind.

According to the MCA-Madagascar website the project aims 'to stimulate the rural market economy by developing new opportunities for market-based income growth'. The ABI project is implemented through a network of Agricultural Business Centres (ABCs) that 'work with a broad set of partners and stakeholders to provide information regarding agribusiness, technology, finance and management, the lack of which constrain growth of the agricultural business sector.' Johanesa Rasolofoniririna, director of the project, says in particular the centres support farmers in order to improve the quality and quantity of production, better manage their farms and to access markets for their products.

For the purpose of project implementation, Madagascar is divided into six regions and activities are primarily aimed at rice, butterbeans, maize and lychees for the export market and vegetables for domestic trade.

But the project is particularly pertinent in a place like Nosy Be, a little island off the north coast of Madagascar, where nearly the entire island population was left destitute after SIRAMA, the government-owned sugar producer, collapsed in 2002. At the height of SIRAMA's operations, around 80 percent of the population of Nosy Be was either directly or indirectly dependent upon the company. "Essentially they [SIRAMA] owned half the island and after nationalization and subsequent mismanagement, it completely collapsed," explains Simon Bell, a consultant with the Economic Development Board of Madagscar (EDBM). "Most of [the former SIRAMA employees] have turned to just growing their own food and vegetables and now people like MCA are trying to organize them to supply quality vegetables to the tourism industry."

Rasolofonirina says there is a considerable potential for farming on land that was previously used for growing sugar but points out that property rights issues still hamper agricultural expansion in the area. He goes on to explain that much of the land on Nosy Be would be ideal for redevelopment into small-holder farms

and the replanting of sugar cane, but is unattainable to those who have been tilling it for decades. The titles for the land remain with SIRAMA and farmers like Louis are reduced to 'illegal' farming which prevents them from further investing in expanded operations - they can be thrown off the land at any moment.

MCA-Madagascar is also running a program on property rights to improve access to title deeds for land and increase the efficiency of land service administration, but much still remains to be done. These efforts are expected to bring an end to land disputes, improve access to finance and increase rural enterprise investment.

The ABI project is slated to be completed in 2009. That leaves little time to address some of the challenges that Louis still faces. In addition to living in perpetual fear of being thrown off the patch of land he has been so devotedly cultivating, he still struggles to consistently access high quality seeds and fights an endless battle against pests attacking his crops. Finding a market for his produce is also not always easy.

AROUND THE WORLD

HURDLES TO BIOFUEL GROWTH BIGGER THAN EXPECTED STUDY FINDS

Although ethanol and biodiesel have captured a share in the global fuel market, their transition to a global industry will be more painful than analysts had expected, according to a new study by Accenture, a global consulting firm.

The study, Biofuel's Time of Transition, said the challenges facing the industry will be manifested in four areas: distribution and integrating biofuels into the established fuels value chain; infrastructure investment because of the difficulty of justifying investment up front when the future size of the market is uncertain; financial markets where there is a need to develop markets for biofuels with liquidity and risk management tools to enable industry growth; and consumers' perception which deteriorated as a result of the debate over the impact of biofuels production on food supplies.

The study also argues that the impact of biofuels on food supplies has been exaggerated. Citing bioethanol which accounts for 90 percent of the biofuels market the study notes that increases in the price of corn, one of the two sources of ethanol, have been the smallest among those of grains – up 31 percent compared with the 78 percent rise in rice. Similarly, the study says, prices of raw sugar, the other source of ethanol, fell in early 2007 and struggled for many months to recover.

US SENATE CLEARS WAY FOR NUCLEAR TRADE WITH INDIA

The US Senate endorsed a historic US-India nuclear agreement paving the way for resumption of civilian nuclear trade between the two countries after more than 30 years.

The Senate voted 86-13 to approve the deal and to lift a civilian nuclear trade ban the US imposed on India after the latter conducted a nuclear test explosion in 1974. India says the agreement will help provide energy to fuel its booming economy.

CHINESE EXPORTS WEAKEN AS A RESULT OF GLOBAL SLOWDOWN

The global economic slowdown which is weakening demand for Chinese exports will drag the country's economic growth down this year into single digits, according to economists polled by Reuters in September.

The poll showed that a combination of weakening demand in the main industrial economies and a slowdown in China's property sector due to tight credit will push growth down to 9.9 percent this year.

Economists expect the Chinese Government will ease monetary policy through the end of next year to support growth in the face of economic slowdown.

But despite the poor export outlook, economists expect that China's trade surplus will remain at an elevated US$247 billion this year and US$231 billion in 2009. The surplus in 2007 was US$262 billion.

NEW GM STUDY SPURS FRESH CALLS FOR SPEEDY APPROVALS

The European Union's scientific and technical research laboratory has released a study saying that foods made with genetically modified (GM) ingredients are safe to eat prompting fresh calls for Europe to speed up GM crop approvals to counter soaring food prices, the Financial Times (FT) reported last month.

According to the FT, the study, while admitting that little is known about the long term health effects of GM foods, said GM foods that have been put forward for regulatory approval have not had harmful effects. It also said GM crops approved in the EU were not found to have caused allergies such as skin reactions.

INSIDE THE WTO

DOHA TALKS REMAIN STALLED

Doha Round talks on agriculture and non-agricultural market access (NAMA) have failed to produce any progress over the past three months, according to sources familiar with the negotiations.

Sources say the surprise resignation of European Trade Commissioner Peter Mandelson last month and the appointment of Catherine Ashton of the UK, who has little trade negotiating experience, have contributed to the stalemate and further dimmed the prospects of a breakthrough in the negotiations in the near future.

In agriculture talks, the chairperson of the agriculture negotiations group, Crawford Falconer, announced that he will not call any meetings of all members until about the third of week of November. Instead, he held private informal consultations with some members, which some referred to as "walks in the woods" to signify the fact that they took place away from the WTO.

In NAMA, the new chair of the negotiating group, Swiss Ambassador Luzius Wasecha, announced that he was not going to tackle critical issues in the talks, such as sectoral negotiations and formula cuts, but will use the old negotiating text issued before the failed July ministerial as a "starting point" for talks.

Meanwhile, and in an effort to demonstrate her commitment to reviving the Doha Round, the new EU Trade Commissioner, Catherine Ashton, travelled to Geneva to meet Pascal Lamy, just after she was confirmed by the European Parliament.

Ashton expressed her optimism about concluding the Doha Round despite the failure of the WTO ministerial earlier this year. Ashton said that her meetings in Geneva confirmed to her that Doha is still "very much alive", and she promised that Europe will continue to play a central role in "pushing the talks forward."

COUNTRY FACT SHEET…

MADAGASCAR
ISLAND OF OPPORTUNITIES

Madagascar is the fourth largest island in the world and perhaps best known for its unique flora and fauna; especially its famous lemurs.

The Malagasy population is largely non-urbanized, with only about 25 percent settled in the industrial zones around Antananarivo, Toamasina and Antsirabe. The rest are almost entirely dependent on subsistence farming and over 70 percent of the population lives in poverty.

Madagascar gained its independence from France on June 26th, 1960. During 1992-93 free presidential and National Assembly elections were held, ending 17 years of single party rule. On February 22, 2002, the opposition candidate, Mark Ravalomanana, a businessman, declared himself president in a close election. Supporters of Didier Ratsiraka, president since 1975, refused to accept Ravalomanana's claim and a period of political and economic crisis ensued. A recount of the votes, mediated by African leaders, declared Ravalomanana victorious. In the face of a divided opposition, he was re-elected with a clear majority in December 2006. Recent changes to the Malagasy constitution, which also made English the country's third official language, will allow Ravalomanana to extend his tenure for a third term should he win the 2011 election.

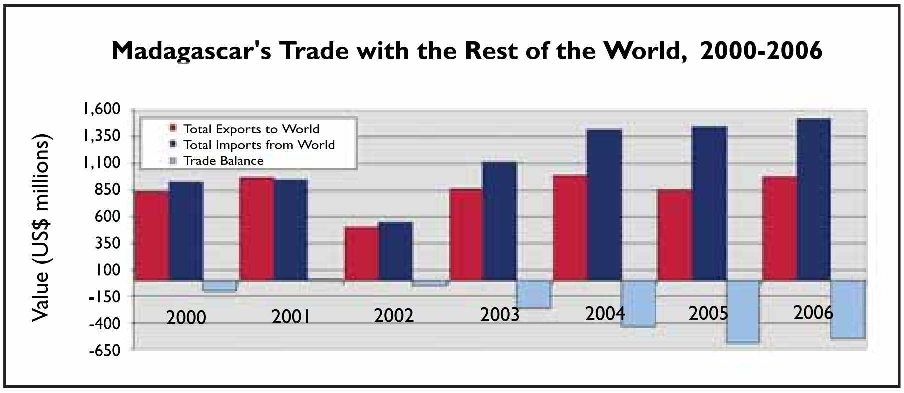
With his promises of liberal economic reform and modernisation, Mr. Ravalomanana is a favourite of the Bretton Woods institutions, donors and other foreign observers.

Indeed, early reforms have already borne fruit as the country has, for example, become one of the top three exporters of apparel under AGOA.

However, the country remains highly dependent on imports and donor support. Foreign aid accounts for over 10 percent of GDP, and Madagascar continues to run a large trade deficit.

Due primarily to the socialist policies of the Ratsiraka era, Madagascar's mineral riches, believed to include oil, have been largely unexploited. Recent high prices on international markets and increased opening up of the economy have seen huge investments into the country. Overall foreign direct investment (FDI) into Madagascar has jumped from an average of around 1 percent of GDP between 1996 and 2005 to around 12 percent of GDP by 2007.

As a result, the Government faces the challenge of ensuring that appreciation of the currency, a likely outcome of rising investment, does not stifle export growth. The Government also needs to ensure that economic growth is broad-based



Source: World Trade Organization 2008 Trade Policy Review of Madagascar

Population: 19.7 million (growing at 2.6% per annum)

Land Area: 587,000 km^2

GDP: US$7.3 billion

GDP Growth: 6.5%

GNI per Capita: US$320 (Atlas method, current US$)

HIV/AIDS Prevalence: 0.1% of population ages 15-49

Inflation Rate: 9.5% (GDP deflator)

Currency: Malagasy Ariary (MGA) 1,800 = 1US$

Literacy Rate: 69% (CIA World Factbook)

Life Expectancy: 59 years (2006)

(Data Source: World Bank for 2007 unless otherwise indicated
Madagascar Map: http://www.wordtravels.com
est. = estimate

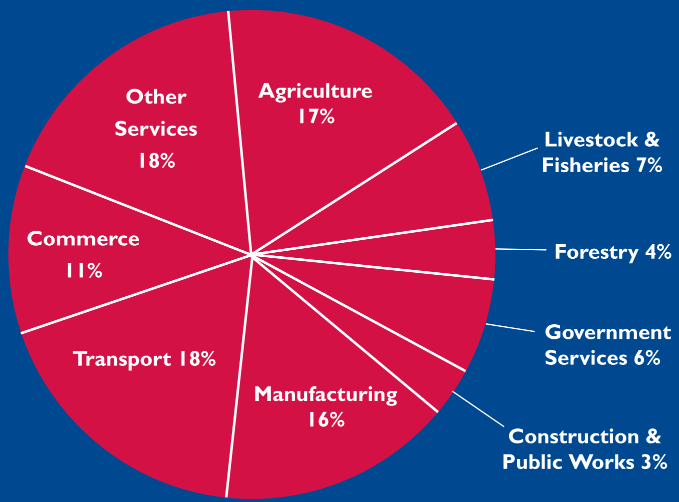
and that local industries are not crowded out by cheap imports and exports remain competitive.

Expanding its tax base and drawing the large informal economy, estimated at up to 30 percent, into the mainstream pose further challenges.

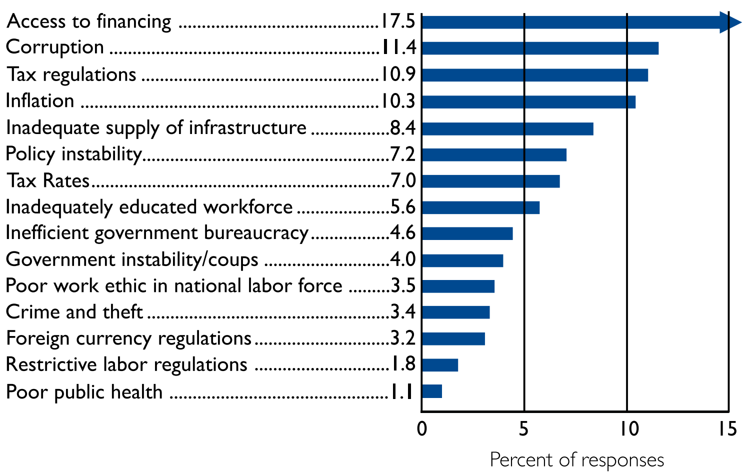
The Economic Development Board of Madagascar (EDBM), established in 2007, aims at providing a one-stop shop for setting up companies and aims to attract US$500 million of (non-mining) FDI and improve the country's Doing Business ranking from 144th place in 2009 to 80th place by 2012.

COMPOSITION OF MADAGASCAR'S ECONOMY - GDP BY SECTOR IN 2005

(Source: World Trade Organization 2008 Trade Policy Review)

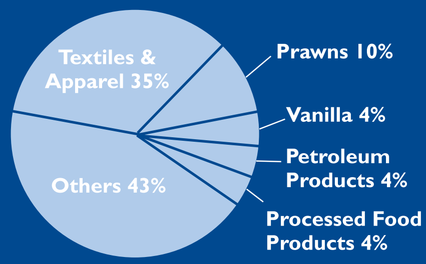


The Most Problematic Factors for Doing Business

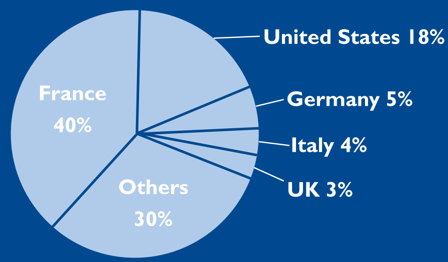


Source: World Economic Forum Global Competitiveness Report 2008-2009

TOP EXPORTS 2007



TOP EXPORT MARKETS 2007



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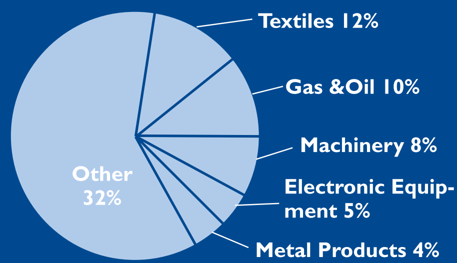
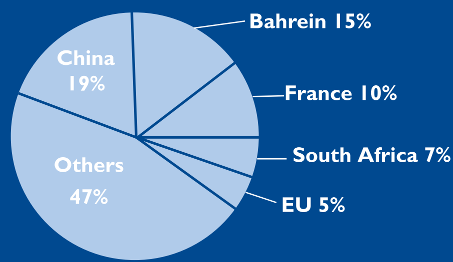


TOP IMPORT MARKETS 2007



The above data was provided by INSTAT (Institut National de la Statistique Malgache)

INSAT FOCUS

LOOKING TOWARDS SOUTHERN AFRICA FOR GROWTH

Madagascar became the 14th member of SADC on August 18, 2005; something that the country's president, Marc Ravalomanana, had been promoting since he took office in 2003. When it joined the regional grouping Madagascar seemed motivated by the opportunity to expand its export market by gaining access to the potentially lucrative South African market. Based on the country's agricultural potential, many politicians maintain a vision of Madagascar as the breadbasket of SADC. But three years on, the business community in the country remains divided on whether joining SADC was a good move or a premature one. Most Malagasy businesses know very little about markets in SADC, and those that do know find more reason to worry, rather than rejoice, given the prospects of stiff competition from mainland producers, especially from South Africa.

Ready for Competition?

Until recently, Malagasy businesses operated in a cocoon with little internal and foreign competition. Production costs in Madagascar tend to be high and the quality of locally produced goods variable. As a result, many Malagasy producers are now daunted by the prospect of an influx of cheaper, better quality goods from the continent.

"As an island country, we have a different psychology and we are a little closed on ourselves and that is one of the problems with regional integration – they should show more interest in what is happening outside. Operators see it as a small catastrophe," explains Daniel Raremby, deputy secretary general of the Groupement des Entreprises de Madagascar (GEM).

To date, most of Madagascar's exports have been going to France, the US and other EU countries. In 2007, only about half a percent of Madagascar's exports were destined for South Africa. Most of its regional trade has been with its close neighbour Mauritius, with whom it trades duty and quota free under the COMESA Free Trade Area as well as a bilateral agreement. (It will also be able to trade freely with Mauritius under the SADC Protocol on Trade).

Malagasy businesses have already started feeling the impact of increased competition." The main competitor is South Africa and there are more and more South African products imported by Madagascar," says Alain Pierre Bernard, a Malagasy development consultant. Bernard sees this not as a threat though, but as an opportunity for Malagasy producers to improve the quality of their products: "They can compare South African foods with Malagasy foods, the quality, the type of standards, the variety. I think for some people it was a pretext for them to think about how to improve their own quality – it is learning by doing – by buying in Shoprite, and I think it is an opportunity."

But Hanta Rakotovao, executive secretary general of FIVMPAMA, an association of Malagasy entrepreneurs argues that most businesses in Madagascar lack information, not only about market opportunities, but also about the standards that businesses will have to respect in target markets.

The Chambers of Commerce and Industry of Antananarivo (CCI-A) share this concern. "Of course there are many opportunities, but the problem before us is that we are a [former] French colony so we don't have any relations with African companies…so… we don't know really well the detail of what happens, what is the opportunity in the other countries," says Njaka Rajaonarison, head of the office of information and partnerships at the CCI-A.

Vast Potential

But despite the concerns and uncertainty, the Government and some businesses see significant opportunities in the SADC market.

Textile and clothing manufacturers for example are excited at the prospects of expanding exports of clothing to South Africa, where a 40 percent tariff is currently applied to clothing imports from non-SADC countries.

"Madagascar last year exported almost US$2 million to South Africa in clothing whereas Mauritius exported about US$100 million - and the cost of labour in Mauritius is about four times what it is here. So if Mauritius could do a hundred million, we could do at least that. And if you look at the figures we did US$670 million last year all together so 10 percent more; that would mean 10 percent more jobs. It is a good opportunity and it is only 3-4 days by ship so I think it is interesting," explains John Hargreaves, vice-president of the Madagascar Export Processing Zone Association.

Other Malagasy manufacturers see great potential in the form of cheaper inputs – especially steel from South Africa.

Malagasy politicians also have high hopes of turning Madagascar into the breadbasket of Southern Africa.

"SADC is roughly at 300 million people – roughly 15 times the Malagasy population. So in terms of number people, we have 15 times bigger market for the Malagasy people. But also in terms of GDP – the GDP of the SADC region is roughly US$200 billion – which is 40 times the GDP of Madagascar, so you can imagine how big the potential is for the Malagasy producers while going into the FTA," said Madagascar's minister of the economy and trade and industry, Ivohasina Razafimahefa, in an interview with INSAT.

"[W]e think that we will be able to be the supplier of food for the SADC region under the FTA," he added.

Indeed, the potential is immense. Madagascar has ideal climatic conditions, abundant fresh water and at least 18 million hectares of cultivable land of which only about two million is currently under crops.

According to the Economic Development Board of Madagascar (EDBM), "the soil diversity allows the exploitation of different types of crops. For instance, fruits and vegetables in the central regions, oleaginous cultures (nuts, soya), cotton and sugar cane in the South-West and North-West, and cash crops (vanilla, coffee, clove, pepper and litchis) on the East coast."

There is also significant potential in fisheries and aquaculture. Madagascar has some 2,000 km of rivers and a coastline of 5,000 km combined with an exclusive economic zone of more than 1.2 km^2, the 14th largest in the world.

Alain Pierre Bernard says Madagascar has an opportunity to expand its exports of natural and agriculture products to SADC. "Until now we are exporting mainly to Mauritius, but I think we can export to other countries, especially now with this issue of food security. That is why it is important for them [businessmen] to think strategically about markets and where they can perform; and that is why it is imperative for them to get better market information," he says.

Tourism also offers great opportunities. Over the past six years the number of tourists visiting Madagascar almost doubled, reaching 344,000 in 2007. Within SADC, South Africa is a fast growing tourism destination and itself also a significant regional source of business and leisure tourists. Madagascar stands to gain from linking into regional tourism packages, as well as from aggressively marketing its tourism products to South African and other regional tourists.

A Plethora of Challenges

While acknowledging the challenges some producers will feel as a result of opening local markets, economists say that the toughest challenges facing all Malagasy producers lie within the country.

Chief among these is poor infrastructure – particularly with regards to transportation, power and telecommunications services.

In the Malagasy Government's submission to the WTO for their 2008 Trade Policy Review, the Government estimates that "Madagascar's trade could increase by 20 percent with appropriate infrastructure support."

Another set of challenges to reaping optimum benefits from SADC membership are those associated with trade facilitation, in particular Customs. Apart from capacity weaknesses, the overuse of discretionary measures leads to a lack of uniformity in the application of measures, unpredictability and instability of regulations.

"The real problem is the customs because we really need to know whether they are ready for the opening of the market," laments Raremby. "[Businesses] want that customs are simple and effective, they want as little administrative problems as possible because the customs are terrible when they start looking through the products...If they don't want something to come in or go out, they will always find a reason and what they [business] want is a customs administration that is effective and simple."

Alain Pierre Bernard agrees. "First we have to improve Customs competencies and we have to improve confidence between customs and [the] private sector…when we discuss trade facilitation with customs and with the private sector, it is not the same level of understanding – that is the reason why it should be necessary to have training for both groups; specifically for trade facilitation."

Businesses also complain that, despite significant improvements at customs, in particular the automation of many processes, customs officers are not yet skilled in terms of customs valuations, leading to significant delays and over-charging of tariffs.

These constraints are exacerbated by the fact that business associations in Madagascar are weak and not sufficiently capable of defending the interests of the private sector in trade negotiations. The Chambers of Commerce, which constitutes the official forum for interaction between the government and the private sector, is directly dependent on the Ministry of the Economy, Commerce and Industry (MECI) for its operational budget.

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WE SPEAK TO...

IVOHASINA RAZAFIMAHEFA, MINISTER OF ECONOMY, TRADE & INDUSTRY

What is the philosophy and strategy of the Madagascar Government for trade and economic growth?

The center of the entire Government policy now is poverty reduction through economic growth based on development of the private sector as set forth in the Malagasy Action Plan (MAP). Everything that we are doing in the country is summarised there. The economy does not stand alone – it fits together with with education, with health, etc., because we need healthy, educated working people in the economy. That is the foundation.

The strategy for the economy is based on macroeconomic stabilization, regional intergration, development of SMEs, attractiveness of foreign direct investment and increasing competitiveness into the international markets.

We are also targeting the diversification of exports, which needs as a condition diversification of the economy. We want to reduce our reliance on traditional export products such as vanilla, apparel, paper, etc., and move more into diversified export products such as shrimps and fish products, as well as light industrial products and information services, with computer services or data processing services.

We are also still trying to move into higher value-added export products – instead of just exporting raw vanilla, raw paper, we are training to transform them to have larger value-added and in the future our aim is to transform the agricultural sector into an agricultural industrialized sector so that it actually will serve first the regional market and then the international market.

What is the Government doing to encourage domestic and international investment, particularly in export sectors?

Our first strategy is to have a level playing field for international and national investment so that there will not be any discriminatory treatment regarding the origin of the investment – that's the first condition that is needed. So we are not promoting FDI [foreign direct investment] at the expense of local investment; nor the other way around.

We recently adopted two new laws – an investment law and a law on the promotion of export processing zones. We are also working on an export promotion law. All of these initiatives are aimed at attracting FDI and to also developing domestic investment. We also set up a one-stop shop, the EDBM – Economic Development Board of Madagascar – this is both an investment promotion agency as well as an investment facilitating agency. We have also improved the procedures for setting up companies and for customs clearances. In addition, we are also improving the access of the private sector to finance. We are a member of MIGA (the Multilateral Investment Guarantee Agency), and we are a member of the African Trade Insurance Agency – so all this works to improve the business climate for both foreign companies and domestic companies to operate in.

Do you see reports like the World Bank's Doing Business and World Economic Forum's Global Competitiveness as important and do these influence the Government's policies?

Yes, because everyone is talking about Doing Business indicators (DBI) and everyone is talking about these competitiveness reports. I congratulate the people who are doing the work and I think it is good work. At least it provides some degree of comparison. I would say Madagascar has not improved it's rankings not because it has NOT improved in absolute terms, but because it has not improved in relative terms. The DBI and the competitiveness index, this is a dynamic competition, you do not have to improve only on your own in terms of where you were a year or two years earlier, but if you do not keep with the average base of improvement around the world, you will fall behind and it will appear as if you did not progress. We are making a lot of effort here in Madagascar. We have really worked to reduce the time it takes to set up a company. Where we were at around 20 days or even more before, now you will be able to set up a company in four days at EDBM where we have all the necessary ministries to help you.

The main weakness of Madagascar, which I myself am trying to work hard at addressing, is the time for closing an enterprise. Because of the legal framework in Madagascar, we have not reached the point of being able to close a company in a matter of one or two days yet. People still think that someone will close a company with bad intention, just to close a company and then get rid of the debt. So this is something that we still have to work on.

We also take the competitiveness report quite seriously, specifically focusing on the export sector because that is where we believe we should really strengthen our competitiveness. Of course the import substitution sector has to also be taken into account because when you work on the economy other products will flow into the country as well.

One specific thing that we also pay attention to is the industrial competitiveness index which is developed by United Nations Industrial Devcelopment Organization (UNIDO) because Madagascar is still predominantly an agricultural economy but we want to move into agro-industry, which is considered in this industrial compeitiveness index - so that is also something that we are very much working on.

How does the new law on the tax free zones differ from the previous one?

The new law which was recently adopted by parliament is less constraining than the earlier one. Under the previous law, companies operating in the export processing zone area were not allowed to subcontract with companies that were not in the area or within the treatment – either they sub-contracted with companies in the area or they subcontracted with companies based abroad because they were considered as companies in a kind of 'overseas area.' Under the new law they can subcontract with local companies so that they can have more integrated effect with the local economy.

Also, we have improved and facilitated the visa and the working licence for people working in the export processing zone area . We have introduced what we call the 'green line' for VAT reimbursement and also regarding the tax treatment as well as foreign currency repatriation - there is much, much more flexibility compared to the law we had before.

What, in your view, are the most critical challenges facing your efforts to diversify the economy and increase exports?

The major challenge is to increase our competitiveness – to be more competitive than the countries surrounding us, which would include: the ability of Madagascar to respond to the quality and quantity requested or required at the international level - we currently have production capacity constraints in many companies.

Information is a big challenge as well because most Malagasy companies are not well-connected to the international market yet; knowing the markets and the channels to get to these markets. Another major challenge is to find the lowest cost inputs for the production system; taking advantage of being in a free trade area or customs union we have to be able to find inputs at the best price for us to produce and then be competitive in the international market.

What are the respective roles of government and the private sector in addressing these constraints?

There is a role for government, there is a role for the private sector, but there is a joint role as well. Government has to provide the framework and the environment for the private sector to operate in – regulatory, procedural, legal, etc. This includes the infrastructure environment. The most important thing the private sector can do is reinvest – use the best equipment, and cutting-edge technology so that they can be and remain competitive in the international market. We also have to develop roads, build ports, and set up, for instance, the telecommunications system together with the private sector, probably in a PPP [public-private partnership] framework.

For example, we have a large mining investment in the south of Madagascar which needs a deep port. The Government is not able to build the port by itself, neither is the company – so we are putting our strengths together to create a PPP. PPP is something that we are putting much emphasis on and my ministry is the first responsible. Around 70 percent has been paid by the private sector, 30 percent paid by the Government, because the private sector believes that they will need it for their investments and the Government also feels that other people will be able to use the port as well. We expect this new port to become the highest performing port of the Indian Ocean in the coming years. This is just one example, but there are many other examples I can provide you with, showing this new way of working in terms of public-private partnership.

What are Madagascar's comparative and competitive advantages for possible export diversification?

In my view our advantages lie in the agro-industrial sector because we have the land and the climate to produce for the regional and international market. We are also trying to grow our aquaculture industry, because this is a sector where we believe we can be very competitive. There are particular opportunities at the high end of the market and niche markets like organic produce. Our competitiveness is in specific segments of the markets, rather than mass markets where we have to compete against countries like China, Brazil and others.

...continued on page 18

GUEST PERSPECTIVE

EPZ WORKS - LET IT CONTINUE

John Hargreaves, vice-president of the Madagascar Export Processing Zone Association and board director of 3 apparel companies employing 8,000 workers, comments on the challenges facing the Export Processing Zone regime and the textile and apparel industry in Madagascar

It has been almost 19 years since Madagascar's Export Processing Zone (EPZ) was established. The Zone was set up as a 'virtual' rather than a "fenced-in industrial estate", meaning that companies were able to enjoy its benefits regardless of their location.

Qualifying firms received a range of benefits including:

- exemption from rights and taxes on their inputs including equipment and raw material;

- exemption from income taxes for 5 years, and a 10 percent tax rate for life after that (the regular tax rate applied to firms in 2008 is 25 percent);

- free access to their foreign currency holdings.

According to Madagascar's Directorate-General of Revenue, 172 companies currently operate as part of the EPZ. The vast majority of these, about 90 percent, are in the textile and apparel industry. Other important sectors include aquaculture and more recently, business process outsourcing services such as call centres. There are also a few companies working in wood, leather and the craft industry.

Real Impact on Domestic Economy and Exports

The EPZ has been central to Madagascar's economic growth as an important source of job generation and foreign exchange earnings. EPZ companies directly employ more than 120,000 people. That is 30 percent of total employment in the private sector in Madagascar. Total wages paid by EPZ firms are estimated at 200 billion Ariary (US$120 million) annually.

It is also estimated that for each direct job in an EPZ company, three "indirect" jobs are created.

Therefore, the livelihood of 500,000 people depends on these companies, either directly or indirectly. But because the EPZ companies are located for the most part in Antananarivo, more than 50 percent of the working population of the capital depends on them for survival.

EPZ companies have also proven their ability to compete in global markets. Madagascar is now the second largest exporter of textiles and apparel in Sub-Saharan Africa and is on the way to becoming the largest. EPZ firms account for almost 70 percent of total Malagasy exports.

In 2007, exports of textiles and apparel hit US$700 million, accounting for 47 percent and 86 percent of total exports from Madagascar to the EU and the US, respectively.

Between 2006 and 2007 Madagascar had the third largest growth rate in exports to the US in the world after China and Vietnam.

And even as many countries in Africa and elsewhere saw their exports of textiles and apparel fall following the elimination of global textile quotas in 2005, the Malagasy industry held its ground in the global market. Madagascar is the only country in the region that enjoyed growth in its exports of textiles and apparel during the last two years.

In spite of the revaluation of the Ariary against the US dollar, and to a lesser degree, the Euro, during 2007, exports of textiles and apparel increased appreciably. Several large companies have plans to upscale their activities.

Some recent developments will also help the industry. For example, since January 2008, the EU has authorized the single textile transformation within the framework of the EPA (Economic Partnership

6 Largest Exporters of Textile & Apparel of Sub-Saharan Africa (US$ millions)

	Lesotho		Kenya		Madagascar		Mauritius		Swaziland		South Africa	
	US	EU	US	EU	US	EU	US	EU	US	EU	US	EU
2004	455.9	1.0	277.2	3.2	323.3	196	226.4	635.7	178.7	1.1	141.5	70.3
2005	390.7	0.8	270.6	2.9	277.1	215.2	166.6	524.8	160.9	0.1	67.2	48.2
2006	387.0	1.2	262.9	0.8	238.4	302.7	118.8	634.5	135.2	0.1	46.9	38.5
Total 2006	388.2 (3)		263.7 (4)		541.1 (2)		753.3 (1)		135.3 (5)		85.4 (6)	
2007	383.5	2.5	249.0	1.08	289.7	382.5	114.7	750.3	135.3	0.45	43.4	27.5
Total 2007	386		250.08		672.2		865		135.75		70.9	

Sources: AGOA.info, EU Comext

Exports of Textiles and Apparel from Madagascar						
Year	2003	2004	2005	2006	2007	Growth '06-'07
€ millions	138	171	191	240	255	+6%
US$ millions	196	323	277	238	290	+22%
Sources: ACT, CBP, EUROSTAT Comext						

Agreement). Moreover, the administrative problems that hindered access of Malagasy products to the markets of the SADC have been resolved. And the Southern African Customs Union said it is ready to allow apparel products that are made from third country fabric in Madagascar, (i.e., fabrics that undergo single transformation) to enter the Union duty free under the MMTZ (Mozambique, Malawi, Tanzania and Zambia) quota arrangement.

Lurking Challenges

In an ideal world, the strong performance of the Malagasy apparel firms and the fact that, unlike many other companies in Africa, these firms survived competition with giant Asian producers would mean that the industry is on solid ground.

Alas, the industry is facing many challenges that threaten to cast a shadow on its future.

First, the industry suffers from shortages in and unreliability of energy supply, which decreases its efficiency and hinders future expansion efforts. Such shortages also discourage new investment in the sector, particularly in textile production (yarn and fabric).

So far, there has been no clear strategy to increase energy generation capacity in the short or even medium-term.

Another challenge stems from the new law on exports which is expected to be passed by parliament soon. The law is primarily aimed at encouraging all companies to export. Yet the law could prevent the Government from conferring EPZ status to new companies. The EPZ suppression provisions were introduced based on demands by the IMF which argues that a single fiscal system is easier to administer. But this could be a first step towards eliminating the EPZ altogether.

A third challenge is the possible appreciation of the Ariary due to current investments in the mining industry. An appreciation of the Malagasy currency would render Madagascar's exports less competitive in the global market. The appreciation is likely to be temporary during the phase of implementation of the mines which will take two to three years that could be followed by a depreciation of the currency. But if the Government does not pay attention to this issue, the growth of the mining industry could lead to stifling the export sector, the paradox known as Dutch disease. If this happens, the mining sector will create 10,000 jobs to the detriment of 120,000 existing ones.

Why Fix What is Not Broken?

The EPZ companies have performed very well since the establishment of the zone 19 years ago and they achieved the goals that were set for them, namely creating jobs and generating foreign exchange. More importantly, these companies have excellent growth prospects if the Government can help them overcome some of the challenges mentioned above.

So why would the law abandon the EPZ now?

The law on exports should take provisions on EPZ as a starting point rather than replace them with new ones. It should encourage companies operating in the local market to export by facilitating exports and offering incentives.

Depriving new companies of EPZ status as proposed by the new export law and supported by the IMF would diminish investor confidence in Madagascar. This is just the opposite of what the Government and IMF are trying to achieve.

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Going Forward

Madagascar has huge potential to increase its exports to Southern and Eastern African countries; be it under COMESA or SADC. The greatest challenges to its producers lie within the country, rather than in the form of trade barriers.

To its credit, the Government is making significant progress in addressing many of these challenges.

To strengthen infrastructure, the Government is building a new port at Fort Dauphin in the south of the country; part of a joint effort with a mining company. And a second fixed line operator is being licensed and the costs of telecommunications are expected to be divided by 10 through linkages to SAFE (linking Indian Ocean Islands) and EASSy (linking Eastern African countries) submarine fibre optic cables in 2008.

But much remains to be done.

As the Government works to facilitate trade through improving infrastructure and the effectiveness of customs authorities, it also needs to guard against abuses of power by politicians and bureaucrats. In recent reports, Malagasy and foreign operators, as well as international observers, have raised concerns about governance issues in the country.

Finally, the great influx of foreign direct investment as a result of large-scale mining projects may lead to a sudden appreciation of the Ariary, negatively affecting the competitiveness of other export products. This will be another challenge for the Government to tackle head on.

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We also have a competitive advantage and comparative advantage in the industrial sector when productivity-adjusted labor costs are taken into consideration. Madagascar does not have the lowest labor cost, but we are probably the first or second in the world in terms of productivity-adjusted labor cost. Compared to China we are still competitive in terms of labor cost per unit of production.

What role do/can SMEs play in the Malagasy economy?

I believe that SMEs should be the basis of the economy. Of course we have some huge investments in Madagascar, such as mining investments. We also have other important investments that are coming in, but if those investments are not fully integrated in the economy they will have very limited impact on the economy – so what we need to try to do is make sure that there are a pool of SMEs that are able to tend to the needs of those huge investments. The idea of entrepreneurship is still not widespread in Madagascar and even worse than that, in past times, private initiatives and private business have been considered a bit in a prejorative way – these are 'the profit making people.' In the past young people would say 'I am going to look for a job', but now there is a larger and larger percentage of young people who say 'I am going to create my own business' and that is really satisfying for us. So we are seeking to build that kind of economy – which requires building the right skills. Many investors are saying that they cannot find the necessary skills locally - not only the human resources skills, but also they can also not find the companies that have the skills that can respond to their needs. We have to build those skills together with these huge mining companies so that we can fully integrate big firms, medium ones, and the small ones – all working together. But if the link between them is somehow missing then these large investment might not have any impact at all on the broader Malagasy economy. So we are trying to train people to respond to the needs of the market.

How does Madagascar plan to use regional and international trade agreements to increase trade-related growth?

Personally, I believe in international trade. I believe that international trade will make everyone better off. I also believe that everybody should be given the same strength to compete so that everyone can benefit equally from international trade. I push the agenda of international trade both at the regional and global level.

Speaking on behalf of my ministry, we have always done our best to conclude and even to bring other countries to move together towards achieving regional integration and international trade agreements. We want to maximize the benefits of trade for Madagascar and move the agenda. At the regional level we are negotiating the Economic Partnership Agreement (EPA) with the EU which has been stumbling a little bit at some points in time but we still believe that we should move on and conclude it because that will make everyone better off. I am just a bit worried that the products flowing from Europe will be much, much more than the other way around. So we have to make sure that Madagascar has the ability and the capacity to produce products that can be sent to Europe, otherwise the benefit of the EPA will not be fair and will not be just. To that end, I believe, and this is my personal belief, that the negotiation on market access should always be linked to the supply-side constraints, which is the discussion on development, otherwise this negotiation will not be concluded and otherwise the EPA will be a failure from its beginning. We are really trying to get the maximum out of the agreements that we are signing. Other agreements, like the AGOA initiative, have really pushed the economy of Madagascar.

At the international level we have been a little disappointed, as everyone, at the – can you qualify it as a failure, probably not – probably the 'half-failure' of the WTO Doha Negotiations. We call upon everyone around the table to make some concession from their respective sides for it to move forward. Because again, people try to get the maximum out of it and then end up with nothing at all, and that is the risk for the entire world. We have been moving into this process and we believe we should carry on with the process.

Are you happy with the progress on implementation of the SADC FTA?

We are very much up-to-date and we are proceeding very well with the schedules that have been agreed. So we are very happy with that. We are happy with how it is being implemented and we look forward to full implementation of the FTA and hopefully after that going into a customs union and eventually a common market and monetary union – who knows, that is the calendar that we have set up for SADC for 2010 and 2015. So if everything goes well, everyone benefits fairly and equally from this framework. I personally find no obstacles for us to to achieve a customs union and eventually a common market and monetary union.

COMESA, of which Madagascar is also a member, will be establishing a customs union this year. Will Madagascar be a part of this customs union? Are you choosing between SADC and COMESA?

That is a very sensitive area. Many countries around the world are a member of two or even three regional frameworks at the same time. This is currently the situation with Madagascar – we are part of both SADC and COMESA. The fundamental consideration is where the benefits to the country can be maximized. We are trying to answer this question and are undertaking some analysis for COMESA, comparing that to SADC, and that analysis will allow us to conclude what direction we should go. At the same time we are moving into a FTA with SADC; that shows our commitment to work closely with the SADC framework as well. But as you know with other countries, it is possible to be a member of two groups at the same time. Personally I do not think that it is necessarily a contradictory situation, it can be a complimentary situation and we will try to make it so.

Where would you like to see Madagascar five years from now?

My wildest dream is for it to become another Singapore or Hong Kong. That is my wildest dream. Probably my wiser dream would be to achieve a GDP of US$520 to US$550 per capita – this would give the Malagasy people a much better standard of living. In the MAP we have set such goals, because ultimately that is what the government is for – to improve the standard of living of the people.

TRADE RESOURCES

In October the World Bank launched the sixth edition of its **Doing Business Report**.

As in the previous five years, the report evaluates "regulations that directly affect the ability of businesses to grow and create jobs and identifies good regulatory reform practices". This year's report looks at 181 economies around the world.

At the launch of Doing Business in Gaborone, Botswana, World Bank spokesperson, Dahlia Khalifa, emphasised the impressive reforms by African countries, saying that this year Africa recorded "the quickest and highest rates of reforms to date".

This year's top ten reformers included three African countries: Botswana, Senegal and Burkina Faso. The region's top performer, Mauritius, implemented further reforms to move up to 25th place. It is followed by South Africa in 32nd place (up from 35th), Botswana in 38th place (up from 52nd) and Namibia in 51st position (down from 48th place last year).

Overall, Eastern Europe and Central Asia again led the world in reforms – for the fifth year in a row. Doing Business recorded a total of 239 reforms by 113 economies that made it easier to do business between June 2007 and July 2008 – the most reforms recorded in a single year since the Doing Business project started in 2003.

Access the full report and other resources at *www.doingbusiness.org*.

The United Nations Conference on Trade and Development (UNCTAD) in September issued its 2008 Report on Economic Development in Africa entitled **Export Performance Following Trade Liberalization: Some Patterns and Policy Perspectives**.

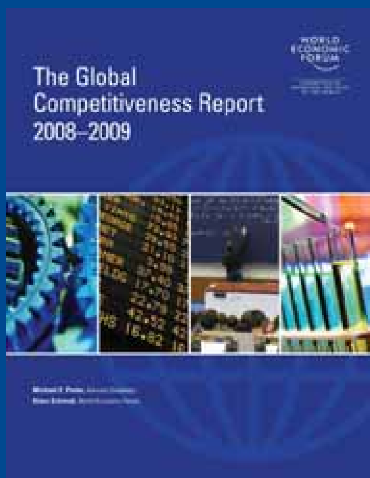
However, the report finds that African countries did not gain from trade liberalization. "Though there has been some improvement in Africa's export performance after trade liberalization, the level and composition of the continent's exports have not substantially changed…Africa as a whole has even lost export market share, which was down from 6 per cent of world exports in 1980 to about 3 percent in 2007."

Despite significant steps to liberalize trade since the late 1980s such as cuts in the number and value of tariffs, exchange rate liberalization and the removal of export barriers, African countries have effectively lost market share and still continue to mainly export primary commodities, which are prone to price instability.

The report identifies Africa's weak supply response as the most important impediment to the continent's export performance. It recommends that future export policies focus on increasing production for export and eliminating structural obstacles to increased supply capacity.

In terms of agricultural exports, the report blames the absence of complementary policies "to address the incentives and the structural and institutional constraints that are most critical for enhancing agricultural productivity, output and exports" for limited benefits from trade liberalization. In the face of a weak private sector, the authors suggest a bigger role for the state in developing agricultural exports especially as it identifies socio-economic issues and institutions as "preventing Africa from reaching its true potential in international agricultural trade."

The full report is available from *http://www.unctad.org/en/docs/aldcafrica2008_en.pdf*.



The World Economic Forum (WEF) **Global Competitiveness Report for 2008/9** was also released in October. The United States remained at the top of the competitiveness rankings followed by other European countries in the top 10. China has led the way among large developing economies climbing four places to 30th position. While several sub-Saharan African countries have 'measurably' improved their competitiveness, only three countries – South Africa, Botswana (moving up an impressive 20 places this year) and Mauritius – feature among the top half of the 134 economies ranked in this year's report.

Download the full report, highlights, summary, economy profiles, rankings and more at *http://www.weforum.org/gcr*.

INSIDE THE TRADE HUB

TRADE ADVISOR AUGMENTS CAPACITY

"Brussels was cold and wet," Leon recounts for the umpteenth time from behind his desk at the Ministry of Trade in Botswana's scorching heat. For much of the past two years, Leon has been shuttling between Botswana, the EU headquarters in Brussels and other meeting halls throughout the region to assist Botswana in obtaining the best possible deal with the EU during the ongoing Economic Partnership Agreement (EPA) negotiating process.

Leon Skarshinski was hired through the Southern Africa Trade Hub with money from the Botswana Trust Fund (a fund set up by the US Embassy in Gaborone) as a full-time Trade Advisor to Botswana's Department of International Trade (DIT). He is well qualified for this position, having previously served as a trade specialist in the U.S. Department of Commerce's International Trade Administration.

Since joining the DIT in January 2007, much of Leon's time has been spent on the EPA negotiations. "It has been long process," he laments, "but 2007 saw significant movement as we agreed on a tariff schedule that maintained a degree of protection for Botswana's sensitive product lines. However, things were quite rushed at the last minute and a number of issues were not fully resolved. The need to address these lingering issues, while moving forward in completing a full EPA, has led to a somewhat slower pace over the course of 2008."

In addition to trying to assist in resolving these 'lingering issues', Leon helped to formulate a number of national policy documents, served on reference groups, and commented on countless SACU, SADC and WTO position papers. He also forwarded recommendations for improved coordination of international donor projects and suggested a methodology for identifying and removing trade barriers on a domestic level – a process that is expected to complement the SADC initiative to implement a regional trade monitoring and compliance mechanism.

As his contract winds down, Leon hopes that he was able to make a lasting contribution to his department and the overall economic development objectives of Botswana. "Serving the Government of Botswana has truly been an honor. The Government's commitment to diversifying the economy and drive to participate fully in the global trade environment has already borne results. I look forward to following the country's progress and will eagerly await conclusion of a final EPA."

MORE MAGIC FOR AFRICAN APPAREL PRODUCERS

For the third year in a row, Southern African apparel producers had the opportunity to showcase their products and services to an elite U.S. audience.

Fifteen Southern African companies benefited from USAID Trade Hub support to attend the MAGIC Show, held from August 24-27, in Las Vegas, Nevada. Considered the preeminent show for promoting a brand or making sourcing contacts, the MAGIC Show attracted nearly 3,000 wholesalers representing over US$150 billion in U.S. consumer apparel sales.

Together with the East and West African Trade Hubs, Enterprise Mauritius and the DFID-funded ComMark Trust, the Southern Africa Trade Hub coordinated a 26-booth 'SOURCE Africa' Pavillion with 24 companies. The SOURCE Africa Pavilion is part of an ongoing effort to brand Africa as an alternative sourcing location in the apparel industry and included an information booth where Trade Hub staff provided information on Africa's textile and apparel sector and helped determine which of the companies attending might be the most appropriate for a specific buyer's needs.

To draw more buyers to the booth, buyers that filled out a sourcing information sheet received an organic cotton Edun Live T-shirt made in either Lesotho or Uganda for U2 rocker Bono and wife's company, Edun.

While it is too soon to determine what actual business will be generated by participation in the show, all participants considered the event a very useful investment of their time and money, and a critical networking and market linkage venue.

Over 100 contacts were made between Source Africa Pavilion exhibitors and show attendees. This included contacts (and potential business relationships) with major U.S. brands and retailers spending time with the Trade Hub team and a number of exhibitors. It is expected that millions of dollars of new business leads will transpire as a result of the event.