



# The usage of EPA Tariff-Rate Quotas (TRQ) by South Africa and the EU

***Draft report***

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**DISCLAIMER**

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## Acronyms

<b>ACP</b>	African, Caribbean and Pacific
<b>AGOA</b>	African Growth and Opportunity Act
<b>DAFF</b>	Department of Agriculture, Fisheries and Forestry
<b>DALRRD</b>	Department of Agriculture, Land Reform and Rural Development
<b>DFQF</b>	Duty-free, quota-free
<b>EBA</b>	Everything but Arms
<b>EPA</b>	Economic Partnership Agreement
<b>EPASA</b>	Ethanol Producers Association of South Africa
<b>EU</b>	European Commission
<b>FPEF</b>	Fresh Produce Exporters' Forum
<b>GHG</b>	Greenhouse gas emissions
<b>GI</b>	Geographical Indication
<b>GSP</b>	Generalised System of Preferences
<b>LDC</b>	Least Development Country
<b>PPECB</b>	Perishable Products Export Control Board
<b>SADC</b>	Southern African Development Community
<b>SAFVCA</b>	South Africa Fruit and Vegetable Canners Association
<b>SARS</b>	South African Revenue Authority
<b>SASA</b>	South African Sugar Association
<b>SPS</b>	Sanitary and phyto sanitary
<b>TCDA</b>	Trade, Co-operation and Development Agreement
<b>TRQ</b>	Tariff-rate quota

## Executive Summary

The Economic Partnership Agreement (EPA) between the Southern African Development Community's (SADC) six member states (South Africa, Botswana, Lesotho, Namibia, ESwatini and Mozambique) and the European Union's 28 member states was signed in June 2016 and came into effect on 1 October 2016. Whereas the EPA provides for the full liberalisation of tariffs on most product lines, for certain goods, the absolute amount of trade that benefits from duty free access is limited by a tariff-rate quota (TRQ).

Tariff-rate quotas adopt a two-step system that combines import quotas (limit on quantities) and tariffs (duties) to facilitate preferential access. The TRQ system allows imports within the quota to be charged a lower tariff than imports outside the quota. TRQs granted to SA are detailed in Annexure I: Section B, while those granted to the EU are detailed in Annexure II, Section B of the SADC-EU EPA.

Since the implementation of the EPA, some exporters have leveraged the preferential access that the TRQs provide, while other industries have not exploited these opportunities. To understand the factors behind the different levels of TRQ utilisation, this report aims to:

- Assess the level of tariff-rate quota utilisation to date
- Identify the factors constraining the usage of the tariff-rate quota for selected agri-products i.e. the sugar-to-bioethanol value chain, the fruit-to-can value chain and mortadella bologna
- Suggest remedial actions that can be implemented to address the existing constraints to utilising the TRQs contained in the EPA

### Usage of TRQs granted to South Africa by EU

As shown in the table below, South African exporters have utilised the TRQs to varying degrees. The sugar, frozen orange juice and (bulk) wine industries have nearly, if not completely, exhausted the TRQs since 2017. Increased TRQ utilisation has also been recorded for apple juice and bottled wine over the same period: apple juice increased from 19% to 86% and bottled wine increased from 64% to 84%.

At the same time, active yeast and ethanol also show a relatively low level of utilisation. Moreover, the take-up is consistently zero for processed products in the dairy industry, some fruit products, and white crystalline powder.

Table E. 1: TRQ utilisation for SA exports to the EU, TRQ allocation (tonnes) and TRQ utilisation (%)

Product	TRQ, 2017	TRQ, 2018	TRQ, 2019	TRQ %, 2017	TRQ %, 2018	TRQ %, 2019*
Frozen orange juice	1,057	1,078	1,099	100%	100%	100%
Cane sugar for refining	100,000	100,000	100,000	87%	100%	99%
Refined sugar of cane sugar for re-fining	50,000	50,000	50,000	34%	99%	66%
Wine Quota B (bulk wine)	33,953	33,635	33,953	98%	95%	100%
Apple juice	3,595	3,712	3,829	19%	86%	4%
Wine Quota A (bottle wine)	77,741	78,483	79,224	64%	84%	63%
Canned fruit, except tropical canned fruit	57,156	57,156	57,156	52%	44%	42%
Active yeast	350	350	350	24%	21%	18%
Ethanol	80,000	80,000	80,000	14%	16%	12%
Tropical canned fruit	3,020	3,080	3,140	0%	8%	0%
Skimmed milk powder	500	500	500	0%	0%	0%

Butter	500	500	500	0%	0%	0%
Frozen strawberries	385	393	400	0%	0%	0%
White crystalline powder	500	500	500	0%	0%	0%
Citrus jams	100	100	100	0%	0%	0%

**Source: TARIC**

**\* TRQ utilisation until 6 November 2019**

There are two plausible explanations for the low TRQ usage for some products.

First, difficulties in accessing the EU market are well documented. Stringent technical, quality or safety standards can present a significant barrier to exports from developing economies that are ill-equipped to meet these requirements. The challenge is more acute among small and medium enterprises that cannot afford the high costs and specialised data collection and traceability requirements associated with the certification and compliance process.

In addition to these legislative measures, there are a range of voluntary and private standards such as those related to social and environmental concerns that SA exporters are expected to meet e.g. Ecolabel, GlobalGAP and BRC Global Standards. While private standards are voluntary, in practice these are mandatory in supplying major buyers in certain markets.

Second, in order to export animal products (including bovine, poultry, meat, eggs and honey), the EU must first approve a country's residue monitoring plan for specific animal products.<sup>2</sup> South Africa's exports of wild game and farmed game already have such a monitoring plan in place. However, milk products have not received this level of approval, and therefore would prevent South African skimmed milk powder and butter from entering the EU.

#### *Key lessons from the sugar-to-bioethanol value chain*

South Africa has a small yet well-established ethanol industry primarily producing sugar-based and synthetic ethanol. The ability of the industry to increase production has been hamstrung by the delay in legislating the Biofuels Regulatory Framework, which was finally concluded in December 2020. This approval provides the industry with a significant incentive and much-required certainty to invest in capital expenditure. As such, we should see increasing investment along the biofuels value chain in the near future. Discussions between government, fossil fuel producers, fuel distributors and bioethanol producers to initiate the blending of bioethanol into fuel should continue to ensure that the implementation occurs swiftly.

The weak performance of the sugar and bioethanol industries in South Africa has been exacerbated by recent drought spells in South Africa. Moreover, with the decrease in demand for traditional downstream products (especially in sugary beverages) on the back of the health promotion levy, the industry faces tremendous challenges.

A significant proportion of the country's current ethanol output is processed into various products by a few large and vertically integrated companies, e.g. Illovo and Sasol, while the balance is sold into the domestic market. Various ethanol-based products are exported to the rest of Africa, Asia and the USA. Despite the TRQ, relatively little exports go to the EU market, largely because of depressed prices in the EU.

#### *Key lessons from the fruit-to-can value chain*

South Africa has a large and competitive fruit industry that has developed strong export capabilities over time. This has occurred at a time when there is increasing demand for fresh produce, while demand for processed fruit is declining. This shift in demand has contributed to a decline in canned

<sup>2</sup> More detail regarding EU's monitoring plan requirements and processes can be accessed via this link: [https://ec.europa.eu/food/sites/food/files/safety/docs/cs\\_vet-med-residues\\_animal-imports-non-eu\\_brochure\\_en.pdf](https://ec.europa.eu/food/sites/food/files/safety/docs/cs_vet-med-residues_animal-imports-non-eu_brochure_en.pdf).

fruit production. Moreover, changes in weather patterns have had an adverse impact on fruit production in South Africa.

Together, these factors have reduced the export of processed canned fruit from SA. As a result, the downstream industry has consolidated significantly, largely through acquisitions by the dominant processors, and re-capitalisation has been low. Thus, despite the awareness and use of the TRQ, exports are unlikely to increase without improvement in underlying industry and climatic conditions.

In response to the industry's challenges, the DTI has proposed activities focused on improving production efficiency in the vegetable and canning industries, though it is not clear what these interventions may entail.<sup>3</sup>

### Usage of TRQs granted to the EU by SACU

As shown below, most of the TRQs for EU export products are currently well utilised. Only three products have a TRQ utilisation of zero percent: barley, cereal-based food preparations (other corn flour, in immediate packaging of a content of 5 kg or more) and Mortadella di Bologna.

Table E. 2: TRQ utilisation for EU exports to SA, 2017 – 2018

Products	TRQ 2017	TRQ, 2018	TRQ, 2019	TRQ %, 2017	TRQ %, 2018
Pork	1,250	1,250	1,250	99%	102%
Butter and other dairy fats	350	350	350	8%	100%
Pig fat	130	140	140	95%	100%
Wheat	248,495	248,495	251,495	100%	99%
Ice Cream	105	105	105	0%	76%
Cheese	5,285	5,315	5,345	109%	45%
Barley	8,970	8,970	8,970	0%	0%
Cereal based food preparations	1,610	1,610	1,610	0%	0%
Mortadella di Bologna	70	70	70	0%	0%

Source: SACU reporting and (Tralac, 2018)

The lack of usage on the barley TRQ is explained by the fact that there is currently a zero percent duty rate on barley. This implies that importers can use the normal channels of importing and avoid the additional administrative hurdle of importing through the TRQ system. Engagements with the European Union Delegation to South Africa (EUD) indicated that having the TRQ in place ensures that should the rate of duty for barley increase, then the EU will continue to have preferential access to the SA (and SACU in general) market.

The reasons behind the lack of uptake for corn flour and Mortadella di Bologna is unclear. Anecdotal evidence suggests that importers of cereal-based preparations and Mortadella di Bologna are not well-versed with the preferential access opportunities afforded under the EPA. Without this information, companies rely on historical knowledge and use the same systems and processes when processing import permits. In other words, companies rely on the Ordinary Customs Duty (as outlined in Schedule 1 / Part 1 / Section IV) without consulting the General Notes in Schedule 1 that details the opportunities under the EPA. These documents, and others, make up the Scheduled to the Customs and Exercise Act, 1964 (Tariff Book).

<sup>3</sup> [http://www.dti.gov.za/industrial\\_development/agro\\_processing.jsp](http://www.dti.gov.za/industrial_development/agro_processing.jsp).

In instances where importers do not utilise the TRQ system, SARS provides an avenue to rectify this error through the Voucher of Correction system.<sup>4</sup> The Voucher acts as a rebate system, allowing importers to claim back the duties paid when importing within the quota. For this, importers would need to be aware of the TRQ utilisation per annum to gauge whether they qualify for the rebate. Currently, information on the usage of the TRQ is only available upon request from SARS.

## Findings and Recommendations

This study considered the performance of South African agriculture exports to the EU, and specifically, the usage of the TRQs allocated to specific processed agriculture products through the SADC-EU Partnership Agreement. Despite the generous preferences provided in both the EU and South African markets in terms of these TRQs, the utilisation rates for South African exports of ethanol and canned fruit, and EU exports of Mortadella di Bologna, are relatively low and in cases declining.

The study finds that the main reasons for the low uptake by South African exporters of the specified products are supply constraints in the domestic market. For ethanol, most domestic production is sold locally, and exports are therefore directed at higher-value markets outside of the EU. Moreover, a lack of progress in the implementation of domestic regulatory reforms, has stifled new investment in bio-ethanol production. Similarly, the production and export of South African canned fruit is constrained by changes in consumer taste and climatic conditions, rather than limitations in the EU market. The reason for the non-use of the TRQ for exports of Mortadella di Bologna to South Africa is less clear, but seems to reflect a lack of awareness from importers and insufficient pressure from consumers.

Based these findings, the recommendations can be grouped into three broad categories. Easy wins require the minimal effort to increase uptake and largely involve disseminating information about the TRQs to a wider audience. Technical recommendations speak to the need to bolster SPS requirements and establish a monitoring plan for milk products. Lastly, there are several structural issues that have a direct impact on the capacity and competitiveness of the industries within South Africa, and currently limit South Africa's to the EU.

Most of these issues can only be addressed by the South African industry with support from its Government, though there are areas where the EU may be able to provide insight and technical support.

### A. Easy wins

**Recommendation 1:** Increase awareness among companies that import Mortadella di Bologna and cereal-based preparations.

**Recommendation 2:** Increase awareness about market opportunities in the EU for targeted SA exporters. In the case of ethanol, provide country-level information on demand and the requirements to enter these markets. The establishment of an approved service provider, similar to the Perishable Produce Export Certification Agency, might be beneficial for other exporters.

**Recommendation 3:** Educate South African retailers and restaurants about the availability and benefits of the TRQ on niche products. If local consumers are fully aware of the cost benefits associated with the TRQs, they are more likely to demand preferential prices from importers and distributors. A dedicated knowledge workshop with importers, retailers and restaurants in South Africa to promote EU food products provided for under the TRQs could be considered.

**Recommendation 4:** Inform importers of EU products that have not used the TRQs about the Voucher Correction System, that allows them to claim back on the duties paid, provided they were within the TRQ.

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<sup>4</sup> The Voucher of Correction can be accessed here: <https://www.sars.gov.za/AllDocs/OpsDocs/SARSForms/SAD%20614%20-%20Voucher%20of%20Correc-tion%20SA%20products%20Ex%20warehouse%20or%20fuel%20levy%20goods%20ex%20duty%20paid%20stocks%20-%20External%20Form.pdf>.



## B. Technical recommendations

**Recommendation 5:** Prioritise the development of technical capabilities for exporting in South Africa e.g. developing a monitoring plan for dairy products and ramping up the SPS technical capacity at DALRRD.

**Recommendation 6:** Support South Africa (SADC) in the implementation of a diagonal accumulation system that allows movement of inputs across SADC EPA states.

## C. Addressing structural challenges

**Recommendation 7:** Now that the draft Biofuels Regulatory Framework has been approved subject to amendments, there is need to advocate for its urgent implementation to encourage firms to invest in expanding biofuel production, and simultaneously attract new entrants. Here South Africa may be able to learn more from the EU regulatory experience through study tours or knowledge-sharing events.

**Recommendation 8:** The fruit industry (and agriculture in general) is already suffering from the impact of climate change. A climate mitigation strategy is needed by the industry, and this may include investing in yield varieties that are less vulnerable to the effects global warming.

**Recommendation 9:** For those products where sugar content is influencing consumption and prohibiting exports i.e. citrus jams, information or support may be needed to encourage the industry to diversify into products that have a low sugar content.

# 1 Introduction

The Economic Partnership Agreement (EPA) between the Southern African Development Community's (SADC) six member states (South Africa, Botswana, Lesotho, Namibia, ESwatini and Mozambique) and the European Union's 28 member states was signed in June 2016 and came into effect on 1 October 2016. Whereas the EPA provides for the full liberalization of tariffs on most product lines, for certain goods, the absolute amount of trade that benefits from duty free access is limited by a tariff-rate quota (TRQ).

Since the implementation of the EPA, some exporters have leveraged the preferential access that the TRQs provide, while other industries have not exploited these opportunities. To understand the factors behind the different levels of TRQ utilisation, this report aims to:

- Assess the level of tariff-rate quota utilisation to date
- Identify the factors constraining the usage of the tariff-rate quota for selected agri-products
- Suggest remedial actions that can be implemented to address the existing constraints to utilising the TRQs contained in the EPA

## 2 Methodology and structure

The paper adopted a mixed-methods approach, relying on primary and secondary sources for quantitative and qualitative information. The initial phase of the study involved a desktop review of industry-level studies, government reports and trade data (from the International Trade Centre Trade Map). Data on tariff-rate quota usage was sourced from EU Taxation and Customs Union Databases - TARIC – for products exported to the EU; and secondary sources that relied on South African Revenue Services data for products imported from the EU. This information was validated through engagements with selected industry associations, government departments, importers and exporters (see Annexure 1).

In order to identify the factors constraining the usage of the tariff-rate quota, three agriproducts were selected for deeper analysis: (i) ethanol, (ii) canned fruit and (iii) Mortadella di Bologna. For ethanol and canned fruit, the study employs a value chain approach to understand the competitiveness and constraints faced by exporters of these products. In the case of Mortadella di Bologna, a more qualitative approach was adopted to describe the challenges faced by South African importers, including the extent to which importers know about the preferences provided by the EPA.

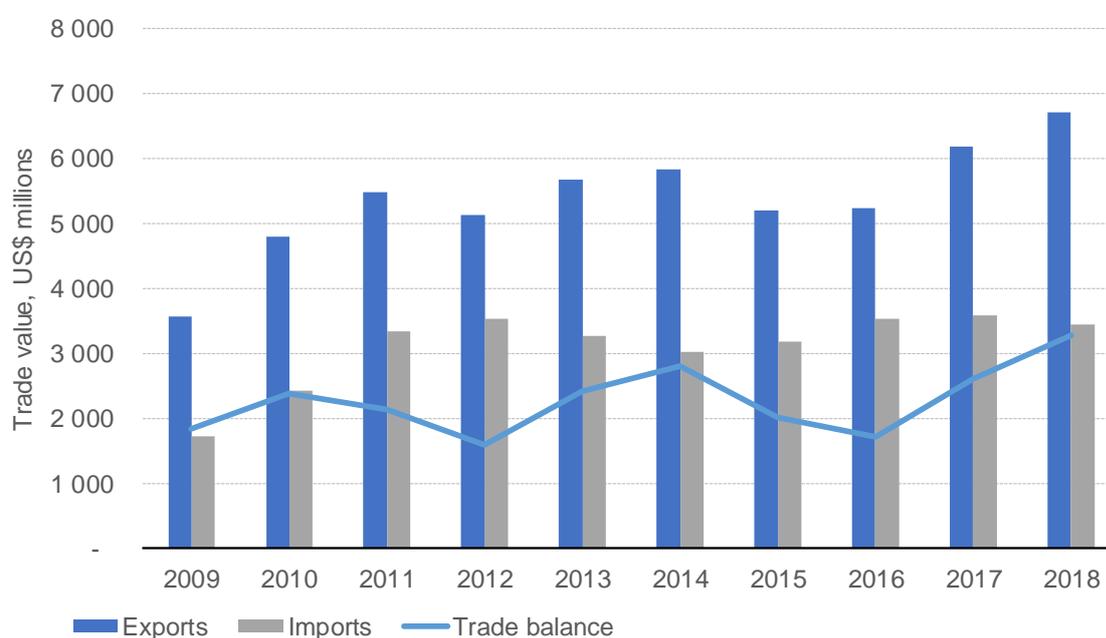
The rest of the paper is structured as follows: [Section 2](#) provides an assessment of South Africa's key markets for agriculture and agro-processing products, highlighting the importance of trade with the European Union. [Section 3](#) discusses the key aspects of the Economic Partnership Agreement and how its approach varies from the EPA's predecessor, the Trade, Development and Cooperation Agreement (TDCA). This is followed in [Section 4](#) by an analysis of the rate of TRQ utilisation to date for the all agricultural products in the EPA. [Section 5](#) interrogates the level of TRQ utilisation among three products – ethanol, canned fruit and Mortadella di Bologna, and explains the factors driving TRQ utilisation. [Section 6](#) then concludes with a set of recommendations that can be implemented to enhance the utilisation of TRQs by exporters in the EU and SA.

### 3 South Africa's trade in agricultural and agro-processing products<sup>5</sup>

South Africa has consistently maintained a positive trade balance for agriculture and agro-processing products, recording a surplus of US\$2.8 billion and US\$349 million respectively in 2018. The country's trade in these two product groups is discussed in more detail below.

In the last three years, agriculture exports (i.e. animal products, field crops, horticulture, wool and fine hair) have grown strongly from US\$4.8 billion in 2016 to US\$6.2 billion by 2018. This growth has been propelled by the increase in edible fruits exports, which grew by 27% over the same period. At the same time, exports of field crops have also shown strong growth, despite the drought in 2015/16. Notably, maize and sugarcane exports grew by more than 100% between 2015 and 2016.

Figure 1: South Africa's trade in agriculture products<sup>6</sup>



Source: ITC Trade Map, 2019

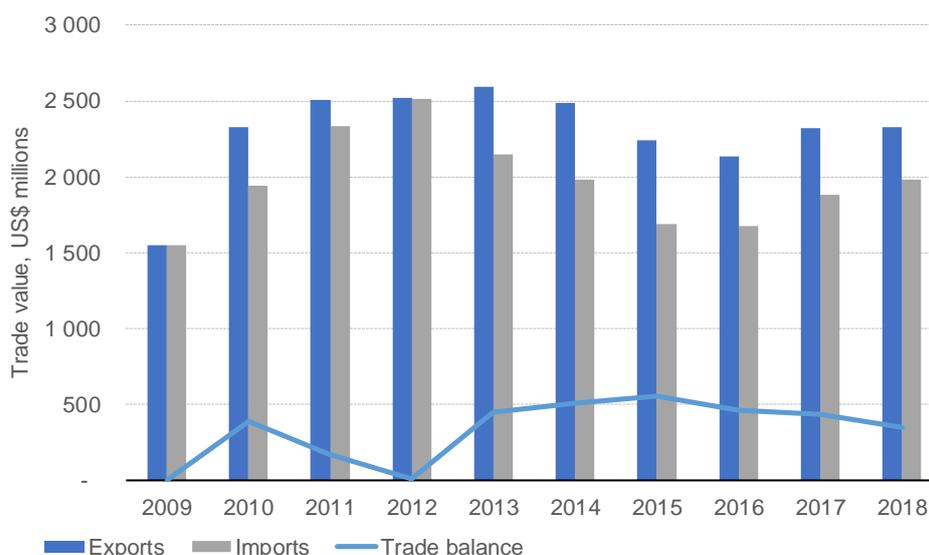
Trade in agri-products is comprised of various goods. Beverages, spirits and vinegar account for the largest proportion of exports in processed agri-products (61% in 2018), and this includes wine, ethanol, water and beer. This is followed by processed food products (30% in 2018) e.g. oil products, dairy, fish, meat and cereal-based food preparations, and tobacco and tobacco products (9% in 2018).

Like the agriculture sector, South Africa's exports of processed agri-products have risen in recent years, from US\$2.1 billion to US\$2.3 billion between 2016 and 2018. However, imports have also been increasing, at an even faster rate, resulting in an overall worsening of the trade surplus (see Figure 2).

<sup>5</sup> The trade data analysis is based on trade data from the international Trade Centre's Trade Map, which is based on United Nation's Comtrade's (until January 2018) and South Africa Revenue Services (since January 2018) calculations.

<sup>6</sup> Here agriculture products refers to animal and fish products (HS 01-03, HS0401, 0407, 0408, 0409, 04010, and HS05); field crops (HS10, HS12 and HS1701); Coffee, tea, maté and spices (HS09) and Horticulture (HS07-08 & HS13-14) and wool and fine animal hair (HS5101-5105).

**Figure 2: South Africa's trade in agri-processed products<sup>7</sup>**



Source: ITC Trade Map, 2019

Generally, the rest of Africa is South Africa's main export market for agriculture and agriculture-based preparations (see Table 1). This is followed by the European Union (28 members) and Asia. The diversity and growth of food-related exports into the Africa market has been driven by the spread of South African supermarkets into the region, which are a primary conduit for exporting these products. Within the EU market, the high demand for fruit and fish products has been supported by trade agreements (including the previous TCDA and now EPA), which provide preferential access for South African exports. Interestingly, a very low proportion of agriculture and agriculture-based preparations enter the American market, despite the AGOA arrangement. The Asian market is a key destination for cereals, fruit and meat products.

**Table 1: SA' Export destinations for products produced in 2018 by region\***

HS Code	Product	2018 (nominal US\$ million)	EU (28)	Africa	America	Asia	Other
'08	Edible fruit and nuts	3,673	45.7%	7.4%	7.7%	32.2%	6.9%
'22	Beverages, spirits and vinegar	1,414	34.4%	43.2%	8.4%	10.6%	3.3%
'20	Preparations of vegetables, fruit & nuts/plants	670	27.4%	42.2%	6.7%	15.1%	8.6%
'10	Cereals	555	8.3%	42.1%	1.5%	47.8%	0.3%
'03	Fish & aquatic invertebrates	547	63.4%	8.3%	5.8%	18.3%	4.1%
'17	Sugars & sugar confectionery	480	12.4%	60.9%	3.5%	20.9%	2.2%
'19	Preparations of cereals & pastry products	270	1.2%	92.9%	0.3%	2.7%	2.8%
'02	Meat and edible meat offal	266	0,7%	62.5%	0.3%	36.2%	0.4%
'15	Animal or vegetable fats and oils	247	9,7%	87.9%	1.0%	1.3%	0.2%
'04	Dairy produce	247	0,0%	99.5%	0.0%	0.3%	0.2%

Source: ITC Trade Map, 2019

\* The top destination is highlighted in grey.

<sup>7</sup> Here processed products captures food products (HS0402-0406, HS11, HS15-16, HS1703-1704, HS18-21); beverages, spirits and vinegar (HS22); and tobacco and tobacco products (HS24).

## 4 The SADC-EU Economic Partnership Agreement

The EPAs date back to the signing of the Cotonou Agreement and the need to ensure WTO compliance in the trade relations between the EU and the African, Caribbean and Pacific (ACP) states (Ramkolowan, Forthcoming). Like the Trade, Development and Cooperation Agreement (TDCA), that previously governed trade between South Africa and the EU, the SADC EPA therefore provides for reciprocal preferences between the member parties. Its overriding purpose is to drive sustainable economic development through deepening trade between selected SADC countries and the European Union (European Union Commission, 2016).

Of the 16 countries in the SADC regional bloc, the EPA was signed by six member states – Botswana, Lesotho, Mozambique, Namibia and eSwatini and South Africa. The agreement provides for asymmetric liberalisation - while Botswana, Lesotho, Mozambique, Namibia & eSwatini are provided full duty-free, quota-free (DFQF) access to the EU market, South Africa, because of its middle-income status, was provided substantive (but not full) DFQF access. Reciprocally, the EU received full liberalisation on most tariff lines in the SADC region, though a much larger proportion of EU exports was partially liberalised or excluded (Table 2).

**Table 2: SADC – EU Economic Partnership Agreement summary of trade liberalisation levels**

	Trade in Value		
	Full liberalisation	Partial liberalisation	Excluded
EU offer to BLMNE	100% (except arms and ammunition)	<b>N/A</b>	<b>N/A</b>
EU offer to South Africa	96.2%	2.5% (incl. TRQs)	1.3%
SACU + Mozambique offer to EU	74.1%	12.1% (incl. TRQs)	13.8%

*Source: DG Trade, 2019*

Over and above tariff liberalisation, the EPA provides for flexible rules of origin, development cooperation, and tariff rate quotas on selected products. These features are summarised below:

### 4.1 Flexible rules of origin<sup>8</sup>

The EPA rules of origin allow for diagonal and bilateral cumulation, as indicated in Protocol 1 of the Rules of Origin of the agreement. This means that non-originating materials can be considered as originating provided that certain conditions are met. The aim is to provide some leeway for party states to use non-originating materials when such materials are not readily available in the territories of the parties. Such a flexible approach to rules of origin is crucial in developing regional value chains and deepening regional integration.

Bilateral cumulation applies to inputs sourced by a SADC EPA state from the EU (or vice versa), provided that the processing undertaken is not minimal. With diagonal cumulation, materials originating from SADC EPA states; African, Caribbean and Pacific (ACP) EPA countries; or Overseas Countries and Territories<sup>9</sup>; and EU countries are considered as originating, under the condition that sufficient processing and working is undertaken. The same cumulation rules apply to the EU states, where materials originating in a SADC EPA State, other ACP EPA States or in OCTs can be considered as originating.

In order to benefit from these flexible rules of origin there is need to have administrative procedures in place between the countries to ensure that the origin of material can be tracked to determine the

<sup>8</sup> For more detailed information on Rules of Origin in the SADC EU EPA please download [https://sadc-epa-outreach.com/images/files/SADC\\_EU\\_EPA\\_rules\\_of\\_origin\\_briefing\\_note\\_February\\_2018.pdf](https://sadc-epa-outreach.com/images/files/SADC_EU_EPA_rules_of_origin_briefing_note_February_2018.pdf).

<sup>9</sup> The Overseas Countries and Territories of the EU includes 25 members from countries and territories in the Caribbean, Indian Ocean, Pacific region and other isolated territories e.g. Greenland, Falkland Islands. See [https://ec.europa.eu/europeaid/regions/octs\\_en](https://ec.europa.eu/europeaid/regions/octs_en).

level of transformation. The level of transformation is measured through a combination of value-added rules, special technical requirements and changes in the tariff heading.<sup>10</sup> As of December 2019, diagonal cumulation was not yet possible given that there was no agreement or arrangement entered into among the relevant parties to ensure compliance and correct implementation of the rules of origin, as required in the SADC-EU EPA. Implementing this administrative process would allow member states to issue the movement certificate EUR.1, an origin declaration or the supplier's declaration.

In addition to allowing for cumulation, the Protocol on the Rules of Origin relaxes the rules of origin requirements for certain sectors, such as clothing and textiles. In this case, a single transformation rule is applied under the EPA i.e. regardless of the fabrics origin, local manufacturing is enough for origin status. This is different from the double transformation requirement that was previously provided for under the TDCA and for non-LDC GSP countries (Naumann, 2018).

Given South Africa's status as middle-income country and its export strengths in certain commodities, South Africa does not have access to some of the flexibilities afforded under the EPA. Materials originating from South Africa that do not have DFQF access to the EU, cannot be cumulated with other countries. In other words, South African products that attract a duty when exported to the EU, are not automatically granted originating status when included in the exports of any other SADC member state. Box 1 provides an example of how cumulation rules are applied in the EPA.

#### **Box 1: Example of the Application of the Rules of Origin with SADC EPA member states**

The rules of origin for jam in the SADC EPA (HS 2007) indicate that in order for non-originating materials to be considered as originating, sufficient processing must take place. Specifically, all the material inputs used in the manufacture of jam must be classified in an HS heading other than that of the final product; and the value of any sugar (HS1701 99 10) used cannot exceed 30% of the ex-works price<sup>11</sup> of the product.

This means that if Botswana were to produce jam using local marula fruits and South African sugar, in order to meet the rules of origin, the value of the sugar cannot exceed 30% of the price of the jam. This is because South African sugar does not have duty-free, quota-free access into the EU, and thus cannot receive a derogation from these rules through cumulation.

If the Botswanan manufacturer uses sugar from eSwatini, the manufacturer does not face a sugar content limit since Eswatini has duty-free, quota-free access for sugar into the EU.

If a South African jam producer were to use marula fruit from Botswana and sugar from eSwatini, they could apply for originating status through cumulation if the production steps carried out go beyond the minimal operations listed in the agreement (article 9.1 of the Protocol), such as packaging, cleaning, adding sugar or simple mixing of ingredients. This is because both countries enjoy duty-free, quota-free access into the EU for these products.

## **4.2 Developmental approach**

Chapter II of the SADC-EU EPA on trade and sustainable development commits the member countries to support trade liberalisation in a way that contributes towards sustainable development, and to cooperate fully to implement the EPA. The sustainable development provisions seek to promote three key pillars namely economic development, social development and environmental protection.

Chapter III then outlines the areas of cooperation, including development cooperation through which the EU (and EU member states) commit to providing development assistance (financial and

<sup>10</sup> According to article 6 of the EPA, all the countries involved in the acquisition of the originating status have entered into an arrangement or agreement on administrative cooperation with each other.

<sup>11</sup> The EPA defines ex-works price as “the price paid for the product ex works to the manufacturer in the EU or in a SADC EPA State in whose undertaking the last working or processing is carried out, provided the price includes the value of all the materials used, minus any internal taxes paid which are, or may be, repaid when the product obtained is exported.”

non-financial) to the SADC EPA states in order to maximise the benefits of the EPA. This includes support in the implementation of rules of origin systems, addressing technical barriers to trade measures and ensuring customs cooperation between EPA states. The EPA also commits parties to cooperate in increasing SADC EPA states' competitiveness and to develop business enhancing infrastructure. These priority areas directly impact on SADC EPA states' ability to maximise preferential access to the EU.

### 4.3 Tariff-rate quotas (TRQ) allocations

Tariff-rate quotas combine import quotas (limits on quantities) and tariffs (duties) to facilitate preferential access for a limited number of sensitive goods. The TRQ system allows imports within the quota to be charged a lower tariff than imports outside of the quota. TRQs granted to SA are detailed in Annexure I: Section B, while those granted to the EU are detailed in Annexure II, Section B of the SADC-EU EPA.

#### 4.3.1 TRQs granted to South Africa by the EU

As the BLNME<sup>12</sup> countries have DFQF access into the EU, TRQs in the EU apply only to exports from South Africa. Following on from the TCDA, the EPA improved the level of trade liberalisation for canned fruit, frozen orange juice and wine, that were already exported by South African companies to the EU through TRQs. In addition, South Africa was granted new quotas for some agricultural products such as sugar, ethanol and butter. The TRQs provided under the TDCA and the EPA are summarised in Table 3. The 'EPA TRQ duty' represents the proportion of the MFN duty that can be deducted within the quota (i.e. the level of the preference).

Table 3: Changes to agricultural TRQs for South Africa under the EPA

Product*	HS Code	TDCA (tonnes)	EPA, 2017 TRQ (tonnes)	EPA TRQ duty**
<b>New TRQs</b>				
Refined sugar or cane sugar for refining	1701.99.10	0	50,000	100% MFN
Cane sugar for refining	1701.13.10 & 1701.14.10	0	100,000	100% MFN
Ethanol	2207.10.00 & 2207.20.00	0	80,000	100% MFN
Active yeast	2102.10.90	0	350	100% MFN
White crystalline powder	1702.30.50	0	500	100% MFN
Citrus jams	2007.91.30	0	100	50% MFN
Skimmed milk powder	0402.10.19; 0402.10.11; 0402.10.99 & 0402.10.91	0	500	100% MFN
Butter	0405.10.50; 0405.10.90; 0405.10.30 & 0405.10.11	0	500	100% MFN
<b>Expanded TRQs</b>				
Canned fruit, except tropical canned fruit ( <b>duty-phase down</b> )	2008.40.51; 2008.40.59; 2008 40 71; 2008.40.79; 2008.40.90; 2008 50 61; 2008.50.69; 2008.50.71; 2008 50 79; 2008.50.92; 2008.70.61; 2008 70 69; 2008.70.71; 2008.70.79; 2008 70 92; 2008.70.98; 2008.97.59; 2008 97 74; 2008.97.78; 2008.97.98; 2008 50 98	27,102	57,156	41% MFN
Frozen orange juice ( <b>TRQ increases annually by 21t</b> )	2009.11.99	1,036	1,057	50% MFN

<sup>12</sup> Botswana, Lesotho, Namibia, Mozambique and eSwatini

Wine Quota A i.e. bottle wine	85 headings under 2204.21 except: 2204.21.93; 2204.21.94; 2204.21.96; 2204.21.97 & 2204.21.98	50,126	79,224	100% MFN
Wine Quota B i.e. bulk wine			33,953	100% MFN
Frozen strawberries ( <b>TRQ increases annually by 7.5t</b> )	0811.10.90	370	385	100% MFN
Tropical canned fruit ( <b>TRQ increases annually by 60t</b> )	2008.97.72	2,960	3,020	50% MFN
Apple juice ( <b>TRQ increases annually by 117t</b> )	2009.79.11; 2009.79.91; 2009.41.92; 2009.49.30; 2009.71.20; 2009.71.99; 2009.79.19; 2009.79.30; 2009.79.98		3,595	50% MFN

**Source:** (European Union Commission, 2016; Ramkolowan, Forthcoming)

\* Information in parenthesis represents additional considerations under the EPA.

\*\* The percentage reduction from the MFN rate.

In South Africa, the allocation of the TRQs are administered through three main avenues (see Table 4): in all three instances, SARS is tasked with issuing the movement certificate EUR 1 that validates the proof of origin, and ensures that the cumulation principles are applied as per the SADC-EU EPA.<sup>13</sup>

- Some products are administered on a **first-come, first-served basis by the South African Revenue Service (SARS)**: SARS processes applications for products.
- Some products require an **export permit from the Department of Agriculture, Land Reform and Rural Development: the DALRRD** (previously Department of Agriculture, Forestry and Fisheries the) receives export permit applications in October of each year, processes the applications and notifies the exporters of their annual TRQ allocation by early December, ahead of the next year's quota. These permits are awarded based on a number of criteria, including the company's B-BEEE status, market share and historical export performance
- Sugar products receive an **export permit from the South African Sugar Association**: the sugar industry is the only sector in which the industry association is tasked with processing TRQ allocations.

<sup>13</sup> <https://www.chamber-international.com/exporting-chamber-international/documentation-for-export-and-import/eur-1-certificates/>

**Table 4: SA Export TRQ administration**

Product	Conditions for exports under preferential duties
<b>ADMINISTERED BY SASA</b>	
Refined sugar or cane sugar for refining	TRQ administered by <b>SASA</b> . Apply for EUR1 Certificate from SARS until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
Cane sugar for refining	
<b>ADMINISTERED BY SARS</b>	
Skimmed milk powder	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
Butter	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
Frozen strawberries	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
White crystalline powder	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
Citrus jams	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
Active yeast	Apply for EUR1 Certificate from <b>SARS</b> until the TRQ is fully utilised on the EU side on a first-come, first-served basis.
<b>ADMINISTERED BY DALRDD</b>	
Canned fruit, except tropical canned fruit	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised. DAFF can re-allocate the provisional quotas if not utilised.
Tropical canned fruit	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised.
Frozen orange juice	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised. DAFF can re-allocate the provisional quotas if not utilised.
Apple juice	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised.
Wine Quota A	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised. DAFF can re-allocate the provisional quotas if not utilised.
Wine Quota B	
Ethanol	TRQ administered by DALRRD, issuing annual export permits until the TRQ is fully utilised.

Source: See No. 40379 GOVERNMENT GAZETTE. DALRRD publishes a gazette annually, which includes the process allocation, an updated quota allocation, where applicable and the deadline for TRQ allocation applications.

#### 4.3.2 TRQs granted to the EU by SACU

The TRQs granted to the EU by SACU are allocated between the member states on an annual basis. South Africa is allocated a significant proportion of the SACU TRQ (usually 80%), while the remainder is divided among the other member states (Table 5). The TRQs are managed on a first-come, first-served basis in each country, except for Namibia, where the Namibian Revenue Agency allocates the quota. The Agreement makes provision for any unused TRQ allocation by 1 September of each year to be re-allocated to the other SACU member states.

**Table 5: SACU Tariff Rate Quota allocation for 2019, in tonnes**

Products*	HS Code	EPA annual TRQ	SA TRQ allocation	SACU TRQ Allocation	EPA TRQ duty**
Barley	1003.10; 1003.90	10,000	8,970	1,030	100% MFN
Butter ( <b>annual duty phase-down</b> )	0405.10.10; 0405.90.00	500	350	150	50% MFN
Cereal based food preparations	1901.90.40	2,300	1,610	690	25% MFN
Cheese ( <b>TRQ increases annually by 150tonnes</b> )	0406.10.00; 0406.20.00; 0406.30.00;	7,850	5,345	2,505	100% MFN

	0406.40.00; 0406.90.12; 0406.90.22 & 0406.90.99				
Ice Cream	2105.00.10; 2105.00.20; 2105.00.90	150	105	45	50% MFN
Mortadella di Bologna	1601.00.20	100	70	30	100% MFN
Pig fat	0209.10.00	200	140	60	100% MFN
Pork ( <b>annual duty phase-down</b> )	0203.22.00; 0203.29.90	1,500	1,250	250	50% MFN
Wheat and meslin	1001.19	300,000	251,495	48,505	100% MFN

Source: SACU TRQ Tracker

\* Information in parenthesis represents additional considerations under the EPA.

\*\* The percentage reduction from the MFN rate.

For a product to qualify for the TRQ duty in SACU at the time of presenting a valid Bill of Entry, the document needs to be supported by a valid proof of origin, a movement certificate EUR1, and a valid import permit from the DALRRD. The proof of origin and movement certificate EUR1 are issued by the respective EU member states' customs authority.

According to SARS' General Notes:

*"For the purposes of entry of any imported goods at the lower rate of duty specified in the EU column the importer shall at the time of entry for home consumption of any consignment -*

*(i) produce together with any documents required to be produced in terms of section 39 a valid proof of origin and proof of compliance with the territorial requirement in accordance with provisions of Part A of the Schedule to the General Notes to Schedule No. 1;*

*(ii) only be entitled to payment of such lower rate of duty in respect of goods subject to a TRQ, if such quota is allocated in accordance with the provisions of the rules for section 49 relating to tariff quotas."*

## 4.4 Trade defence instruments

Chapter II of the EPA also includes a provision of a series of trade defence instruments, in which anti-dumping and countervailing measures in the EPA are subject to the existing WTO Agreements. However, there are several safeguard measures that protect the member states in the event of a surge of imports that are likely to distort the domestic market, and pose a threat to an industry (Berends, 2016).

Safeguard measures assists industries that are threatened by giving the industry time to improve competitiveness and participate internationally. Figure 3 provides a summary of the safeguard measure available, along with the beneficiaries, products covered, intervention and duration of the measure and provision in the EPA. Different from traditional safeguard measures, the agricultural safeguard duties are not triggered by providing evidence of harm. Rather, the agricultural safeguard is volume-based and activated when a threshold of imports exceeded. The BLNS safeguard stands to protect BLNS countries that adjust the protection levels to match those existing to SA as per the TDCA, thereby standardising SACU's level of liberalisation as a customs union. New industries are vulnerable to import competition, and this safeguard is in place to protect new industries for as long as the injury can be ascribed to the reduction of the duties (Berends, 2016).

**Figure 3: SADC-EU EPA safeguard measures**

	Bilateral safeguard	Agricultural safeguard	Food security safeguard	BLNS safeguard	Infant industry
Beneficiary	All parties	SACU	SADC EPA States	BLNS countries	BLMNS countries
Coverage	All products	23 agricultural tariff lines	All products	60 tariff lines	Infant industry produce
Measure	<ul style="list-style-type: none"> <li>• suspension of further reduction of the duty; or</li> <li>• increase in duty up to MFN rate; or</li> <li>• - introduction of tariff quotas</li> </ul>	A duty which shall not exceed 25% of the current WTO bound tariff or 25 percentage points, whichever is higher. Such duty shall not exceed the MFN rate	Not specified	Increase in duty up to the MFN rate or a zero duty TRQ, with duty outside the quota not exceeding the MFN rate	Suspend further reductions of the duty or increase in duty up to the MFN rate
Duration of the measure	For the EU, 2 years with possible extension of 2 years. For SADC EPA countries, 4 years, with possible extension of 4 years	For the remainder of the calendar year or 5 months, whichever is the longer	As soon as the circumstances leading to its adoption cease to exist	Four years, with possible extension of four years	Eight years
Duration of the provision	Indefinite	12 years from entry into force	Indefinite	12 years from entry into force	As long as injury is a result of a reduction of the duties

Source: (Berends, 2016)

## 5 An assessment of TRQ utilisation

The previous section highlighted the growth in South African agricultural exports, including to the EU, and the role of the EPA in supporting such trade. It also noted the importance of flexible rules of origin, development cooperation and TRQs in supporting trade in specific agricultural products. This section assesses the extent to which exporters in South Africa and the EU have actually been able to take advantage of the preferences provided through the TRQs; and identifies three products for deeper analysis.

### 5.1 Usage of TRQs granted to South Africa by EU

As shown in Table 6 below, South African exporters have utilised the TRQs to varying degrees. The sugar, frozen orange juice and (bulk) wine industries have nearly, if not completely, exhausted the TRQs since 2017. Increased TRQ utilisation has also been recorded for apple juice and bottled wine over the same period: apple juice increased from 19% to 86% and bottled wine increased from 64% to 84%.

At the same time, active yeast and ethanol also show a relatively low level of utilisation. For processed products in the dairy industry, some fruit products, and white crystalline powder, the take-up is consistently zero.

**Table 6: TRQ utilisation for SA exports to the EU, TRQ allocation (tonnes) and TRQ utilisation (%)**

Product	TRQ, 2017	TRQ, 2018	TRQ, 2019	TRQ %, 2017	TRQ %, 2018	TRQ %, 2019*
Frozen orange juice	1,057	1,078	1,099	100%	100%	100%
Cane sugar for refining	100,000	100,000	100,000	87%	100%	99%
Refined sugar of cane sugar for re-fining	50,000	50,000	50,000	34%	99%	66%
Wine Quota B (bulk wine)	33,953	33,635	33,953	98%	95%	100%
Apple juice	3,595	3,712	3,829	19%	86%	4%
Wine Quota A (bottle wine)	77,741	78,483	79,224	64%	84%	63%
Canned fruit, except tropical canned fruit	57,156	57,156	57,156	52%	44%	42%
Active yeast	350	350	350	24%	21%	18%
Ethanol	80,000	80,000	80,000	14%	16%	12%
Tropical canned fruit	3,020	3,080	3,140	0%	8%	0%
Skimmed milk powder	500	500	500	0%	0%	0%
Butter	500	500	500	0%	0%	0%
Frozen strawberries	385	393	400	0%	0%	0%
White crystalline powder	500	500	500	0%	0%	0%
Citrus jams	100	100	100	0%	0%	0%

**Source: TARIC**

**\* TRQ utilisation until 6 November 2019**

There are two plausible explanations for the low TRQ usage for some products.

First, difficulties in accessing the EU market are well documented. The key EU regulations and standards include, but are not limited to:

- Quality and marketing (including labelling) – measures related to the quality of imported goods and the associated standards for labelling of these goods.
- Sanitary and phytosanitary (SPS) issues – measures related to agricultural, fish and food produce to minimise the spread of disease and related health risks.
- Packaging – measures related to the type of materials and form that packaged goods imported into the EU can take.

Stringent technical, quality or safety standards can present a significant barrier to exports from developing economies that are ill-equipped to meet these requirements (Grote, Froberg, & Winter, 2006; Tralac, 2010; Fernandez-Stark, Bamber, & Gereffi, 2011). The challenge is more acute among small and medium enterprises that cannot afford the high costs and specialised data collection and traceability requirements associated with the certification and compliance process (Ramkolowan, Forthcoming; de Klerk, 2019).

Engagements with DARLDD highlight that insufficient regulatory and institutional capacity at the department also exacerbates the ability of SA exporters to meet EU requirements, especially when it comes to sanitary and phytosanitary requirements. To mitigate this, the EU established a fund of

€10 million<sup>14</sup> to support the development of SPS infrastructure and processes within DALRRD's animal and plant divisions. This funding will partially meet the infrastructural and technical requirements for bolstering SPS capacity in the country, and the SA government has also committed to funding this process.

In addition to these legislative measures, there are a range of voluntary and private standards such as those related to social and environmental concerns that SA exporters are expected to meet e.g. Ecolabel, GlobalGAP and BRC Global Standards (OTGS, 2019). While private standards are voluntary, in practice these are mandatory in supplying major buyers in certain markets.

Second, in order to export animal products (including bovine, poultry, meat, eggs and honey), the EU must first approve a country's residue monitoring plan for specific animal products.<sup>15</sup> South Africa's exports of wild game and farmed game already have such a monitoring plan in place. However, milk products have not received this level of approval, and this would prevent South African skimmed milk powder and butter from entering the EU (European Union Commission, 2016).

Other products, such as canned fruit and juice concentrates face less stringent export requirements compared to dairy, meat and poultry. The reasons for the relatively low usage of the TRQs for non-tropical canned fruit and tropical canned fruit, which were sitting at 44% and 8% respectively in 2018, deserves further exploration.

## 5.2 Usage of TRQs granted to the EU by SACU

As shown in Table 7, most of the TRQs for EU export products are currently well utilised. Only three products have a TRQ utilisation of zero percent: barley, cereal-based food preparations (other corn flour, in immediate packaging of a content of 5 kg or more) and Mortadella di Bologna.

Table 7: TRQ utilisation for EU exports to SA, 2017 – 2018

Products	TRQ 2017	TRQ, 2018	TRQ, 2019	TRQ %, 2017	TRQ %, 2018
Pork	1,250	1,250	1,250	99%	102%
Butter and other dairy fats	350	350	350	8%	100%
Pig fat	130	140	140	95%	100%
Wheat	248,495	248,495	251,495	100%	99%
Ice Cream	105	105	105	0%	76%
Cheese	5,285	5,315	5,345	109%	45%
Barley	8,970	8,970	8,970	0%	0%
Cereal based food preparations	1,610	1,610	1,610	0%	0%
Mortadella di Bologna	70	70	70	0%	0%

Source: SACU reporting and (Tralac, 2018)

<sup>14</sup> As part of the EPA, the EU also committed to enhance cooperation on capacity building and technical assistance especially in relation to aligning legislation and regulation with international developments in SPS and technical barriers to trade and strengthening risk analysis and assessment capacity for pest control and food safety.

<sup>15</sup> More detail regarding EU's monitoring plan requirements and processes can be accessed via this link: [https://ec.europa.eu/food/sites/food/files/safety/docs/cs\\_vet-med-residues\\_animal-imports-non-eu\\_brochure\\_en.pdf](https://ec.europa.eu/food/sites/food/files/safety/docs/cs_vet-med-residues_animal-imports-non-eu_brochure_en.pdf).

The lack of usage on the barley TRQ is explained by the fact that there is currently a zero percent duty rate on barley. This implies that importers can use the normal channels of importing and avoid the additional administrative hurdle of importing via the TRQ system. Engagements with the European Union Delegation to South Africa (EUD) indicated that having the TRQ in place ensures that should the rate of duty for barley increase, then the EU will continue to have preferential access to the SA (and SACU in general) market.

Anecdotal evidence suggests that importers of cereal-based preparations and Mortadella di Bologna are not well-versed with the preferential access opportunities afforded under the EPA. Without this information, companies rely on historical knowledge and use the same systems and processes when processing import permits. In other words, companies rely on the Ordinary Customs Duty (as outlined in Schedule 1 / Part 1 / Section IV) without consulting the General Notes in Schedule 1 that details the opportunities under the EPA. These documents, and others, make up the Scheduled to the Customs and Exercise Act, 1964 (Tariff Book).<sup>16</sup>

In instances where importers do not utilise the TRQ system, SARS provides an avenue to rectify this error through the Voucher of Correction system.<sup>17</sup> The Voucher acts as a rebate system, allowing importers to claim back the duties paid when importing within the quota. For this, importers would need to be aware of the TRQ utilisation per annum to gauge whether they qualify for the rebate. Currently, information on the usage of the TRQ is only available upon request from SARS.

### 5.3 Products identified for further analysis

There are several factors that may explain the low level of utilisation of TRQs for some products, including a lack of awareness, stringent technical requirements, and the weak institutional capacity in SA required to support SA exporters in entering the EU market. To explore these factors in more detail, and to consider how these utilisation rates may be improved, the following products were selected for further investigation:

- Two SA export products:
  - Ethanol (from sugar)
  - Tropical and non-tropical canned fruit
- One EU export product:
  - Mortadella di Bologna.

The South African products were identified for three reasons. First, all the products have very low TRQ usage rates. Second, the sugar and fruit value chains contribute significantly to domestic economic growth and employment, such that an increase in exports would have substantial economy-wide benefits. Third, for all of these products, it would seem that there are non-administrative issues (beyond SPS requirements) that are constraining trade and need to be understood.

In terms of the SA TRQ allocation, cereal-based food preparations (corn flour) and Mortadella di Bologna are the only EU export product with an effective zero percent usage rate (given that barely is currently imported duty free). Mortadella di Bologna has a higher general rate of duty (40% or 240c/kg, whichever is higher) compared to corn flour (20%), which implies that importers would have a higher incentive to use this TRQ. Their reasons for not doing so is uncertain.

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<sup>16</sup> The tariff code book can be accessed here: <https://www.sars.gov.za/Legal/Primary-Legislation/Pages/Schedules-to-the-Customs-and-Excise-Act.aspx>

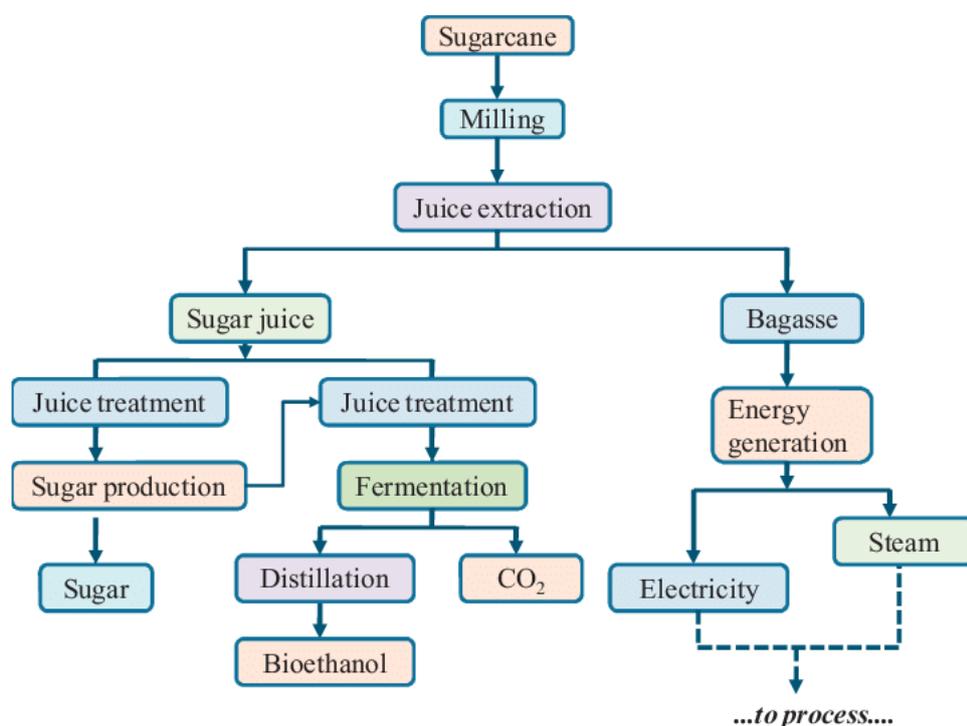
<sup>17</sup> The Voucher of Correction can be accessed here: <https://www.sars.gov.za/AllDocs/OpsDocs/SARSForms/SAD%20614%20-%20Voucher%20of%20Correc-tion%20SA%20products%20Ex%20warehouse%20or%20fuel%20levy%20goods%20ex%20duty%20paid%20stocks%20-%20External%20Form.pdf>

## 6 Product case studies

### 6.1 The sugar-to-bioethanol value chain

In order to understand the reasons why South Africa has been unable to take advantage of the TRQ on ethanol exports into the EU, it is important to understand the structure and competitiveness of the domestic sugar-to-bioethanol value chain. The sugar value chain is quite complex, with different processing methods resulting in various downstream products. From the milling process, sugar juice can be produced into sugar, which is directly used by households or by industry in the preparation of confectionary and baked goods. Alternatively, molasses can be fermented into bioethanol, a key input in the production of fuel, solvents, paints and other industrial purposes or animal feed. Bagasse, another by-product from sugar production, can be used to generate electricity (Figure 4).

Figure 4: Sugar Value Chain



Source: (Vohra, Manwar, Manmode, Padgilwar, & Patil, 2013)

In a season, the South African sugar industry produces approximately 2.2 million tonnes of sugar, with some of the sugar exported to neighbouring countries, Europe and Asia. The sugar is produced by a combination of large-scale growers (82%), small-scale growers (10%) and sugar estates owned by sugar milling companies (8%). In total, the sugar industry is made up of close to 21,000 cane growers, and six millers. The millers are vertically integrated in that they have upstream and downstream operations along the sugar value chain (DAFF, 2017).

The two leading millers in South Africa, Tongaat Hulett and Illovo Sugar, process molasses into two main products – animal feed by Tongaat and bioethanol by Illovo (DAFF, 2017; Chisoro-Dube, das Nair, Nkhonjera, & Tempia, 2018). Tongaat planned on investing in one large-scale bio-ethanol plant at one of its mills in 2014/15, but it is unclear whether investment has come to fruition.<sup>18</sup> Illovo retains a significant proportion of the molasses for bio-ethanol production, processing it further to manufacture potable ethanol used in alcohol production, anhydrous alcohol used in the pharmaceutical industry and other ethanol derivatives used in the production of solvents, methylated spirits,

<sup>18</sup> See [http://www.hulett.co.za/prod/renewable\\_energy.asp](http://www.hulett.co.za/prod/renewable_energy.asp).

natural laxatives and printing ink.<sup>19</sup> The remaining molasses is sold to the market, effectively rendering Illovo the key supplier of molasses in the domestic market.<sup>20</sup>

The sugar industry is governed by sector-specific legislation embodied in the Sugar Act of 1978 and Sugar Industry Agreement (SIA) of 2000. The South African Sugar Association ensures that the industry operates within the confines of the SASA constitution. SASA's mandate includes determining the notional price of sugar (often used as the floor price) and the division of proceeds between the growers and millers.<sup>21</sup> At the bioethanol level, there is an industry association, the Ethanol Producers Association of Southern Africa (EPASA), which supports agricultural and synthetic ethanol producers through engaging with government on behalf of the industry, among other activities (EPASA, 2012).

### 6.1.1 The development of the ethanol industry

Historically, ethanol has been produced from sugar-based processes in South Africa. The same chemical structure in bioethanol (plant-based) can be manufactured through the refining of coal (Vohra, Manwar, Manmode, Padgilwar, & Patil, 2013). Different from the sugar industry, synthetic ethanol has constant (predictable) production given that it is a guaranteed by-product from the refinery process. Within these ethanol variations, there is a distinction between denatured and undenatured ethanol. Denatured ethanol can be used in the manufacture of fuel, blended with gasoline or neat. Undenatured (or potable) ethanol is used for beverage and industrial organic chemical production.

Sugar-based ethanol is less harmful to the environment, and is increasingly being blended with fuel to minimise greenhouse gas emissions (Schuenemann & Kerr, 2019; Braude, 2014). Using biofuel also reduces reliance on oil imports, which has a direct impact on foreign exchange savings (Braude, 2014). Bio-ethanol also offers diversification opportunities for the sugar industry, which is especially important in SA given the concomitant impact of the health promotion levy and surplus sugar production in the EU on downstream demand for sugar.<sup>22</sup> Diversifying into bio-ethanol might also curb job losses currently being experienced in the sugar industry<sup>23</sup>, and create new downstream employment opportunities.

The aforementioned benefits of bioethanol (and biofuel more generally) have driven the growth and development of the biofuels industry across different economies. The European Union has increasingly encouraged the use of biofuels, targeting transport fuel uses (see Box 2). In South Africa the National Biofuels Strategy was approved in 2007, however, bioethanol production for blended fuel has stalled due to the country's failure to conclude the Biofuels Regulatory Framework. The Draft Biofuels Regulatory Framework was only approved by Cabinet in December 2019 subject to amendments.<sup>24</sup> The main objective of the Framework is to introduce regulations and standards for the mandatory blending of biofuel by October 2015, using sugarcane and vegetable products (e.g. canola and soyabeans) as a feedstock (Braude, 2014).<sup>25</sup> The implementation of this strategy would automatically increase downstream demand for sugarcane, given that 400 million litres per annum of biofuel would be required.

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<sup>19</sup> <https://www.illovosugarafrika.com/Products/Furfural-and-Derivatives>.

<sup>20</sup> Based on an interview with the Ethanol Producers Association of Southern Africa in October 2019.

<sup>21</sup> <http://www.nda.agric.za/doiDev/sideMenu/Marketing/Annual%20Publications/Commodity%20Profiles/field%20crops/Sugar%20Market%20Value%20Chain%20Profile%202016.pdf>.

<sup>22</sup> South African Sugar Association see <https://pmg.org.za/files/170531SASA.pdf>.

<sup>23</sup> Tongaat Hulett announced company restructuring that will affect about 5,000 jobs. See <https://www.iol.co.za/business-report/companies/union-concerned-about-sugar-farm-workers-plight-over-looming-retrenchments-24472784>.

<sup>24</sup> <https://www.gov.za/speeches/cabinet-approves-draft-biofuels-regulatory-framework-19-dec-2019-0000>

<sup>25</sup> Maize was omitted from the list of allowed biofuel sources for food security reasons.



## Box 2: Development of Biofuels

Internationally, bioethanol has developed in response to substantial government support through blending mandates, pricing formulae (tariffs) and import protection. For the biofuels sector, a stable regulatory framework is a pre-requisite in order to provide investors with certainty, especially given the entrenched interests of the fossil fuel industry.

Moreover, the emergence of blending mandates is increasingly being driven by rising (and volatile) international crude oil prices that naturally reduce demand for petrol and diesel fuels. Furthermore, environmental and climate change mitigation considerations are becoming more important in the wake of global warming (Schuenemann & Kerr, 2019).

The EU Biofuels Policy dates back to the early 2007s, with a biofuels strategy that aimed to stimulate demand for biofuels in the EU as a way of lowering GHG emissions; encouraging sustainable production of feedstock by diversifying fuel sources and developing long-term replacement fuels; as well as using biofuels as a mechanism to support developing countries capable of producing and supplying biofuel to the EU (Henley & Fundira, 2019). To support increased uptake of renewable energy, EU policy targeted EU's overall energy mix to include 20% renewable energy by 2020, and ensure that the transport sector had a renewable energy blending rate of 10%. A report released in 2017 indicates that EU was on track to meet the 20% energy mix target, while they were falling short on the 10% blending rate (GAIN, 2018).

The Policy also imposes stringent requirements for producers in the EU and importers. First, biofuel installations starting production on or after 1 January 2017 must offer GHG savings of 60% or more compared to fossil fuels (if produced with no net carbon emissions from land-use change).<sup>26</sup> Second, evidence must be provided that biofuels were not produced from raw materials obtained from land with high biodiversity value or high carbon stock (Indirect Land Use Change and Direct Land Use Change). Lastly, raw materials (feedstock) must be produced in accordance with "Environmental" provisions of the Public, Animal and Plant Health in Council Regulation (EC) No. 73/2009.

### 6.1.2 The status of South Africa's ethanol industry

South Africa's ethanol industry has the capacity to produce 405,000 kilo litres of absolute alcohol (klaa) ethanol from a combination of plant-based and synthetic ethanol (Table 8). The local market absorbs 160,000 klaa per annum, split between potable (25,000 klaa) and industrial (135,000 klaa). The balance (about 240,000klaa) is exported.<sup>27</sup>

Table 8: SA ethanol capacity

SA Company	Capacity (klaa) to date	Ethanol type
Glendale Distilling Co.	5 000	Sugar Based
Illovo Sugar - Merebank	50 000	Sugar Based
NCP Alcohols	65 000	Sugar Based
Sasol South Africa	285 000	Synthetic
Total	405 000	

Source: Ethanol Producers Association of Southern Africa

Of the total industry production, Sasol accounts for 70%, as a by-product from its coal refineries. According to EPASA, legislation that was passed in the early 1980s prohibits the use of synthetic ethanol for potable uses i.e. alcohol production. The legislation stated that potable ethanol must be plant-based. Consequently, Sasol produces the following types of ethanol<sup>28</sup> for industrial purposes:

<sup>26</sup> For more information refer to Annex V Directive 2009 / 28 / EC found here <https://eur-lex.europa.eu/LexUriServ/LexUriS-erv.do?uri=OJ:L:2009:140:0016:0062:EN:PDF>.

<sup>27</sup> Based on data collected by the Ethanol Producers Association of Southern Africa.

<sup>28</sup> See Sasol description on products <https://products.sasol.com/pic/products/home/categories/denatured-ethanol/index.html>.

- ethanol 95E5 used in the preparation of liquid printing inks for flexographic and gravure printing;
- ethly alcohol, a solvent in domestic burners, cleaning agents, lacquers and varnished and fuel additive; and
- ethylol 95, a solvent in lacquers and lacquer thinners, etch primers, liquid printing ink and foundry dressings.<sup>29</sup>

Illovo accounts for 14% of the market through the Illovo Sugar – Merebank plant and Glendale Distilling Co., a subsidiary of Illovo. The balance is produced by NCP Alcohols, a subsidiary of a Belgian-based company that is part of the AlcoGroup. NCP uses ethanol grades in the manufacture of pharmaceuticals, cosmetics, alcoholic beverages, toiletries, homecare products, industrial products, essences (as an intermediate in chemicals manufacture such as esters and acrylates) and vinegar (acetic acid).<sup>30</sup>

The document review and engagement with industry identified two key factors that are affecting the growth and development of the local sugar-to-bioethanol value chain. These include the failure to finalise the regulatory framework and access to steady input.

### **Pending regulatory framework**

The failure to legislate the Biofuels Regulatory Framework presents an obstacle to the growth and development of the South African bioethanol market. Absent of this regulatory framework, the on-going production of ethanol intended for industrial and potable purposes will continue, but capacity expansions to meet the intended fuel blending requirements will remain on standby. The recent approval of the Draft Biofuels Regulatory Framework should address this “standstill” and encourage firms to invest in capacity expansion for local consumption or export purposes.

### **Access to steady inputs**

The industry relies on essential inputs from two industry players i.e. Sasol and Illovo. Given that the uses of synthetic ethanol are constrained, the primary source of ethanol for non-industrial purposes is sugar cane molasses. During unfavourable agricultural seasons, downstream users of molasses in South Africa face significant constraints in the domestic market and must rely on imports. For exporters of alcohol products to the EU, diagonal cumulation therefore becomes important in that it enables them to source and use molasses from other EPA countries, and to still benefit from tariff preferences.

## **6.1.3 Trade patterns**

As discussed in Section 5.1, South African exporters utilised just 16% of the 80,000 tonne TRQ opportunity in 2018, which is equivalent to 12,726 tonnes. In order to understand whether there are opportunities to increase TRQ usage, it is useful to consider SA’s historical trade in ethanol. Importantly, the HS nomenclatures do not distinguish between sugar-based and synthetic ethanol. Rather, a distinction is made between undenatured ethanol (HS220710) and denatured ethanol (HS220720). Of these two, South Africa primarily trades undenatured ethyl alcohol (about 80%). Both qualify for the TRQ.

South Africa is a net exporter of ethanol (HS2207), with the country’s trade surplus growing from US\$95 million in 2009, to US\$148 million by 2018 (illustrated in

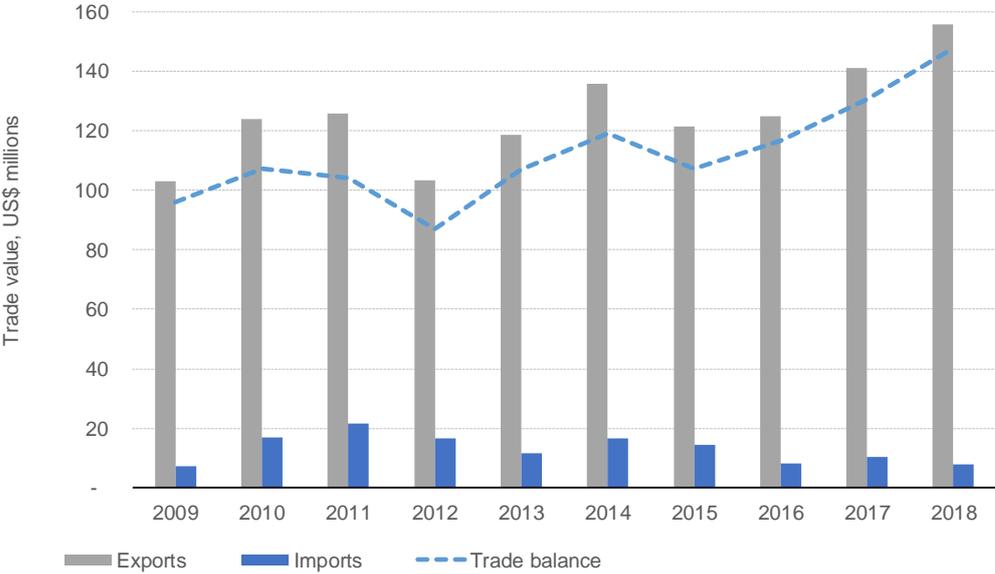
Figure 5). The improvement in the trade balance can be explained by the simultaneous growth in exports, and the decline in imports. In 2012, South Africa experienced a drought, which affected

<sup>29</sup> According to Ethanol Producers Association of Southern Africa, there is legislation that was implemented in the early 1980s that did not permit Sasol to use ethanol for potable purposes i.e. alcohol. Legislation stated that everything consumed should be from vegetable matter.

<sup>30</sup> See more detail here: <https://www.ncpalcohols.com/products-ethanol.html>.

sugar production, thereby having a knock-on effect on ethanol exports. Since then ethanol production has recovered, peaking in 2018.

**Figure 5: South Africa’s ethanol exports and imports, nominal US\$ millions**



Source: ITC Trade Map

The sugar-to-bioethanol industry benefits from three key trade agreements, namely SADC, AGOA and SADC-EU EPA, which provide sugar and ethanol with preferential access into the SADC, USA and the EU markets respectively.<sup>31</sup> These trade arrangements are somewhat reflected in the major export destination for South African ethanol, as summarised in Table 9. Together, these 10 countries account for more than 75% of the country’s total exports of these products.

**Table 9: South African ethanol export destinations, by value**

Destination	2016-18 average exports US\$ ‘000	MFN duties (total AD)
Singapore	18,313	0%
United Arab Emirates	15,274	5%
Madagascar	13,947	20% (SADC)
Zambia	12,908	0% (SADC)
Angola	11,226	60% (SADC)
United States of America	11,035	0% (AGOA)
Rwanda	8,797	25%
European Union	8,536	0% (EPA)
Korea, Republic of	5,820	10%
Nigeria	4,668	5%
Other destinations	19,976	N/A
<b>Total</b>	<b>140,592</b>	<b>N/A</b>

Source: ITC TradeMap

*Madagascar and Angola are both SADC member states. Angola applies the duty on exports because it has not implemented the trade protocol. However, it is unclear why Madagascar has a duty on SA exports.*

Despite the preferential access provided for under the TRQ, exports to the EU are about 6% of total exports, much lower than those to Africa and USA. In 2018, exports to the EU amounted to

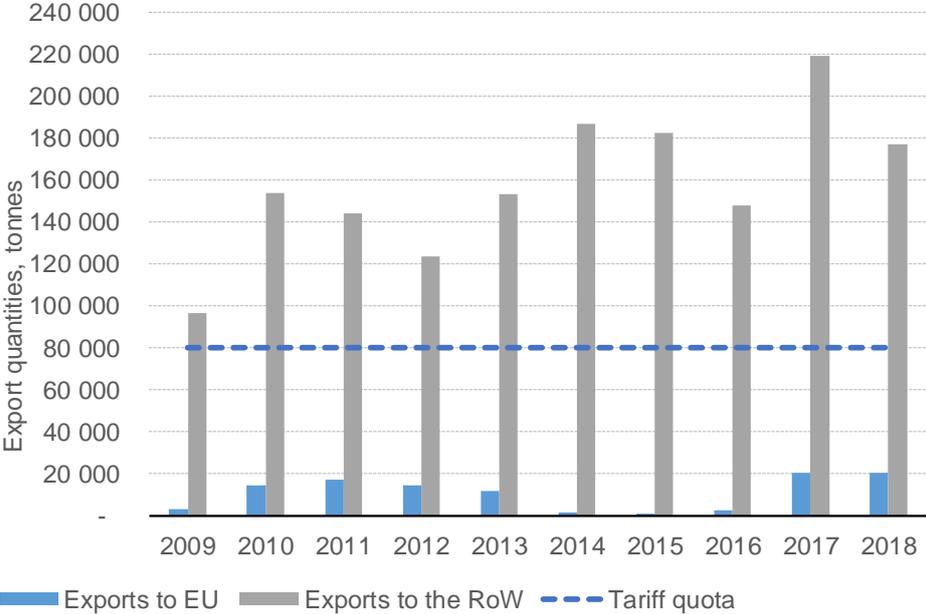
<sup>31</sup> [https://www.thedti.gov.za/trade\\_investment/ited\\_trade\\_agreement.jsp](https://www.thedti.gov.za/trade_investment/ited_trade_agreement.jsp).



20,474 tonnes (according to ITC Trade Map) and of these 12,800 (according to TARIC data) entered the market through the TRQ (see

Figure 6).

**Figure 6: South Africa’s ethanol exports against TRQ, by tonnes**



Source: ITC Trade Map

**6.1.4 Factors explaining TRQ uptake**

Based on the previous analysis and engagements with the industry, there are two factors that explain South Africa’s low uptake of the TRQ for ethanol exports to the EU. These are (i) depressed prices in the EU market for potable ethanol, and (ii) the EU’s regulatory requirements.

The ethanol export permit application process with DALRRD and the processing the EUR 1 Certificate with SARS was not identified as a bottleneck. In 2018, one of the major exporters forgot to submit their TRQ application, which partly explains why a significant amount of ethanol was exported outside of the TRQ in this year.<sup>32</sup> In response, DALRRD now sends reminders to industry representatives to ensure that manufacturers are aware of the application deadlines.

**EU market is not attractive**

South Africa primarily exports potable ethanol that is used in the manufacturing of beverages and industrial organic chemicals. Industry representatives indicated that pricing is the main pull factor for exports. For potable ethanol, the EU market is not as lucrative when compared to other major markets such as the USA and Asia. The removal of sugar quotas in the EU around the early 2000s led to increased production of sugar, which had a knock-on effect of ethanol production. Consequently, this reduced the general price of potable ethanol in the EU.

It is important to note that there are two companies that export to the EU, and this appears to be intra-company trade. Another company solely exports potable ethanol to the African market. The latter company is considering exporting to the EU on the back of the preferential access, though as indicated above, this will depend also on price considerations.<sup>33</sup>

<sup>32</sup> Interview with the Ethanol Producers Association of Southern Africa in October 2019.

<sup>33</sup> Based on industry engagements in October 2019.



## EU regulatory requirements

As explained earlier, ethanol derivatives can be employed to manufacture a wide range of products. Depending on the type of ethanol exported, and its intended use, there are different regulatory requirements in place in the EU.

For ethanol used in industrial processes, one local ethanol exporter shared their experience. To export ethanol intended for cosmetic and personal care use, a REACH Certificate of Compliance<sup>34</sup> is required, while for potable ethanol, an ISO9001:2000 is essential. Acquiring the REACH Certificate of Compliance required the company to go through an intensive evaluation process, including submitting product samples for review. The process took six months, and the company relied on its appointed representative in the EU to assist with the administration of the certification. The company did not cite any challenges with the processes and procedures.

To date, industry engagements indicate that South African companies have not ventured into exporting biofuel and as such, have not attempted to obtain the certification associated with exporting biofuels to the EU.<sup>35</sup> These regulations would include the RED 11 (Renewable Energy Directive) regulations & Fuel Quality Directive (FQD); and Indirect Land Use Change Requirements. From international experiences, securing these regulations is challenging and costly (Schuenemann & Kerr, 2019).

### 6.1.5 Conclusions

South Africa has a small yet well-established ethanol industry primarily producing sugar-based and synthetic ethanol. The ability of the industry to increase production has been hamstrung by the delay in legislating the Biofuels Regulatory Framework. Once this is concluded, it will provide the industry with a significant incentive and much-required certainty to invest in capital expenditure for expansion purposes. This will likely require further discussions between government, fossil fuel producers, fuel distributors and bioethanol producers to initiate the blending of bioethanol into fuel.

A significant proportion of the country's current ethanol output is processed into various products by a few large and vertically integrated companies, e.g. Illovo and Sasol, while the balance is sold into the domestic market. Various ethanol-based products are exported to the rest of Africa, Asia and the USA. Despite the TRQ, relatively little exports go to the EU market, largely because of depressed prices in the EU.

The performance of the sugar and bioethanol industries in South Africa has been exacerbated by recent drought spells in South Africa. Moreover, with the decrease in demand for traditional downstream products on the back of the health promotion levy, the industry faces tremendous challenges.

## 6.2 Fruit-to-can value chain

South Africa's fruit industry has strong capabilities in certain products. For example, the country is one of the major citrus exporters in the world (Chisoro-Dube, das Nair, Nkhonjera, & Tempia, 2018). The industry value chain is comprised of four distinct stages, which are closely interrelated (Figure 7). To compete internationally, there is need to ensure that all the necessary quality checks and traceability requirements are met at each level of the value chain. As a result, high levels of engagement and coordination are required by industry participants to enter the export market.

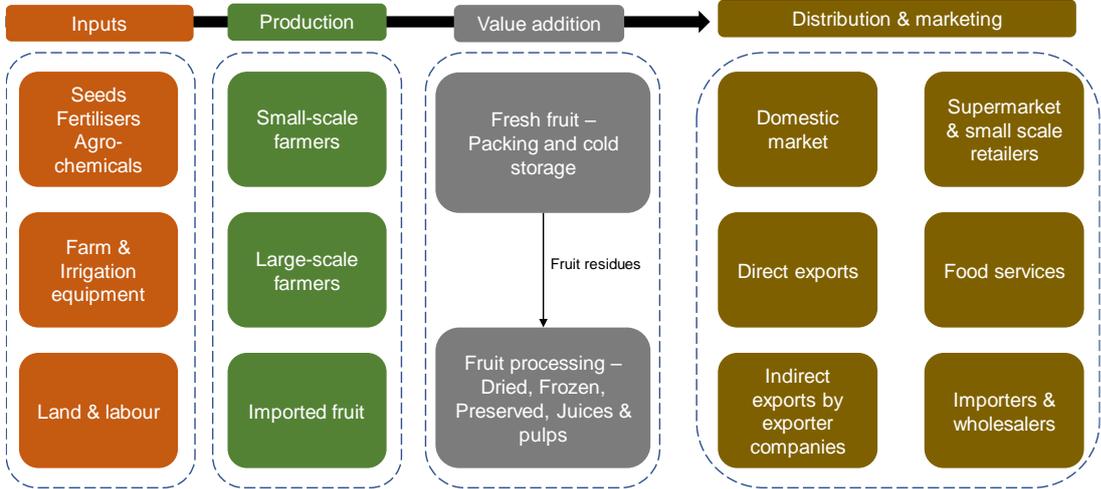
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<sup>34</sup> REACH Certificate of Compliance is a document certifying that a product is compliant with the EU REACH regulation (EC) No 1907/2006. It can be a testing report or statement issued by a third-party testing organization. It could also be a self-declaration. See [https://www.chemsafetypro.com/Topics/EU/REACH\\_Regulation\\_EC\\_No\\_1907\\_2006.html](https://www.chemsafetypro.com/Topics/EU/REACH_Regulation_EC_No_1907_2006.html)

<sup>35</sup> These regulations include the RED 11 (Renewable Energy Directive) regulations & Fuel Quality Directive (FQD); Indirect land use change (ILUC) requirements that can be certified by Bonsucro, ISCC (International Sustainability and Carbon Certification) and the RSB (Roundtable on Sustainable Biomaterials).

For fresh produce, cold chain storage facilities installed on air and sea freight are essential in ensuring that the fruit reaches the final destination in good condition. Processed fruit products, which is the study's focus, requires adherence to packaging, labelling and health requirements.<sup>36</sup> While certain farmers produce fruit for processing, residual fruit that does not meet international requirements can be channelled towards processing. In this way, farmers and processors can maximise the value of the fruit along the entire value chain.

Figure 7: Fruit value chain



Source: modified from (Fernandez-Stark, Bamber, & Gereffi, 2011)

### 6.2.1 The fruit canning industry

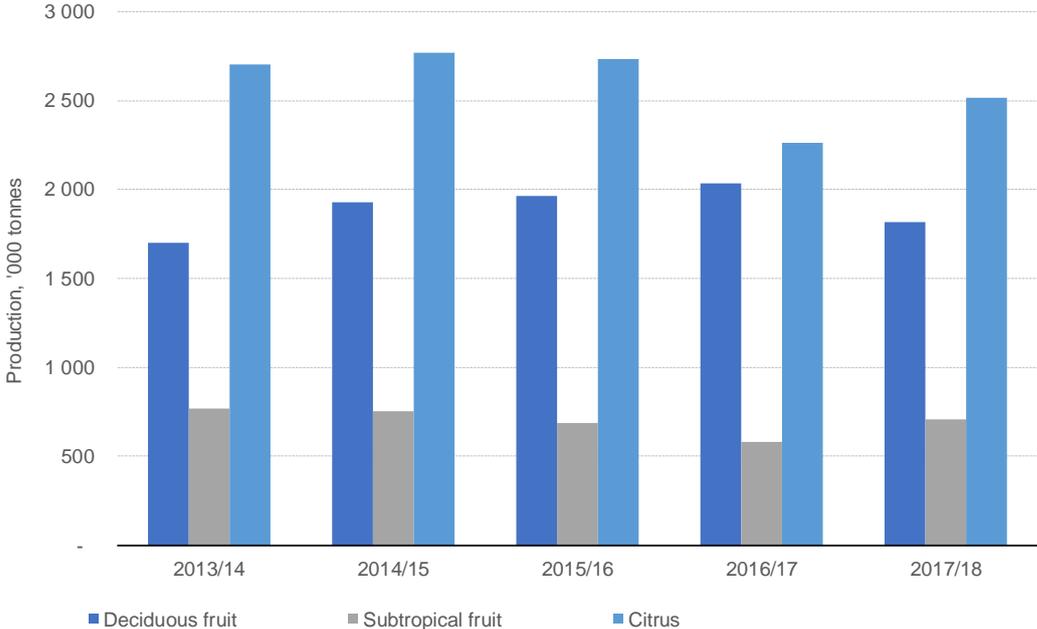
The SA Fruit & Vegetable Canners' Association, and Export Council, are voluntary industry association that support the fruit and vegetable canning industry, and serve the interests of their members through market promotion, assisting with market access, undertaking research into product competitiveness and promoting advancing the principles of transformation.

Fruit processing is labour intensive and employs more than 14,000 factory workers (SAFVCA, 2015), over and above the labour required at the primary production level. Total fruit production in South Africa declined between 2015 and 2017 due to a lack of sufficient rain, however citrus fruit and subtropical fruit have started to recover (Figure 8). Of the total domestic fruit production close to 75% is sold fresh, while the remainder is processed (25%) or dried (1%) (FPEF, 2019).

<sup>36</sup> <https://www.cbi.eu/market-information/processed-fruit-vegetables-edible-nuts/canned-fruit-vegetables/europe/>.



**Figure 8: Fruit production in South Africa, 2013 – 2017**

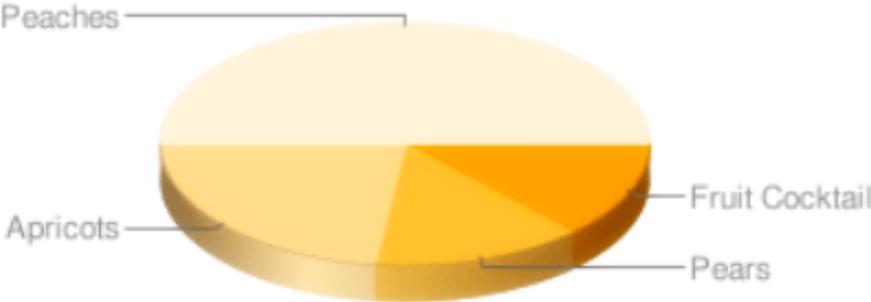


Source: (DAFF, 2018)

The South African fruit value chain is characterised by a highly disaggregated upstream level comprising over 6,000 commercial farmers, and a highly concentrated downstream segment. At the processing level, there are five fruit processors that account for 50% of total revenue (Chisoro-Dube, das Nair, Nkhonjera, & Tempia, 2018). The downstream segment also includes four fruit canning factories, two jam units, three fruit concentrate factories and one pineapple processor.

Canned fruit is laid in a sugar syrup or fruit juice and is either packed as single- or multi-fruit. Peaches, pears and apricots are single-canned, while fruit cocktails include variations of peach, pear, pineapple, grapes and red cherries. Figure 9 summarises the proportion of the canned fruit by type and shows that processed fruit is dominated by peaches. It appears that there is no separation of processing activities. In other words, the companies that manufacture the single-canned fruit are the same companies that produce fruit mixtures.

**Figure 9: Canned fruit production by type, 2017**



Source: <https://www.safvca.co.za/safvcec.html>

Fruit processors must follow strict manufacturing processes to ensure that the canned fruit is manufactured in clean canning factories. The canners have their own quality checks, that are complemented by the third-party inspections offered by the Perishable Produce Export Certification Agency (PPECB) on the behalf of the DALRRD. Furthermore, the PPECB is recognised as an

approved service provider under the European Commission Regulation 543 of 2011. This recognition enables access into the EU, and minimises the checks at the port of entry into the EU.<sup>37</sup>

Recent difficulties in the fruit industry resulted in a significant consolidation in the sector, coupled with low levels of investment. Rhodes Food Group acquired Del Monte Foods and Boland Pulp in 2010 and 2015 respectively. As such, Rhodes' Food processing is split across these two subsidiaries, in addition to its own plant.<sup>38</sup> The other key processor is Tiger Brands, through its subsidiary Langeberg and Ashton Foods that it acquired in 2011.<sup>39</sup>

The main impediments to growth include escalating input costs (e.g. electricity and labour), the high cost of capital and the effects of climate change (SAFVCA, 2015). More pressing is a general decline in demand for canned fruit due to changing consumer preferences. These are discussed in turn below.

### **Limited capital investment**

The growth and development of the agro-processing industry requires high capital investment and scale in order to compete in the global market and meet export requirements. Access to skills and requisite technology for processing and traceability is necessary, yet comes at a high cost. At the moment, the industry is dominated by large food producers that account for a significant proportion of fixed capital investment, and are able to meet these requirements to some extent (Chisoro-Dube, das Nair, Nkhonjera, & Tempia, 2018). However, smaller companies with the potential to enter the export market will likely require external support to achieve economies of scale and meet international regulations and standards.

### **Effects of climate change**

In the upstream fruit industry, fresh fruit is the premium product, given the price differential between fresh produce and processed fruit. During periods of little rain, when total production is compromised, companies maximise the sale of fresh fruit, constraining inputs for the downstream processing market. Consequently, recent droughts in South Africa have had an adverse impact on the volume of fruit processed, and subsequently sales of fruit. As the effects of climate change worsen, this is likely to lead to further volatility (and shortfalls) in supply.

### **Changing consumer preferences**

The canned fruit industry is generally declining, leading to a reduction in canned fruit exports, while fresh fruit exports are increasing. Furthermore, there is declining demand for food stuffs containing high levels of sugar content. The canned fruit industry is penalised by these changing consumer preferences given that there is a perception of high sugar content in canned fruit.

## **6.2.2 Trade patterns**

As discussed in Section 5.1, South African exporters utilised 8% of the tropical canned fruit TRQ and 44% of the canned fruit TRQ (excluding tropical fruit) in 2018. To understand whether there are opportunities to increase TRQ usage, especially for tropical-canned fruit, it is useful to assess SA's historical trade in the following 6-digit HS code product groups:

- Canned fruit, except tropical canned fruit TRQ equal to 57,156 tonnes at 41% MFN:
  - 2008.40: Pears, prepared or preserved
  - 2008.50: Apricots, prepared or preserved
  - 2008.70: Peaches, incl. nectarines, prepared or preserved
- Tropical canned fruit TRQ equal to 3,140 tonnes at 50% MFN

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<sup>37</sup> See more information here: <https://ppecb.com/about/overview/>.

<sup>38</sup> Rhodes Food Group acquired Del Monte Foods and Boland Pulp in 2010 and 2015 respectively. See <http://www.rfg.com/about-us/history/> for more information.

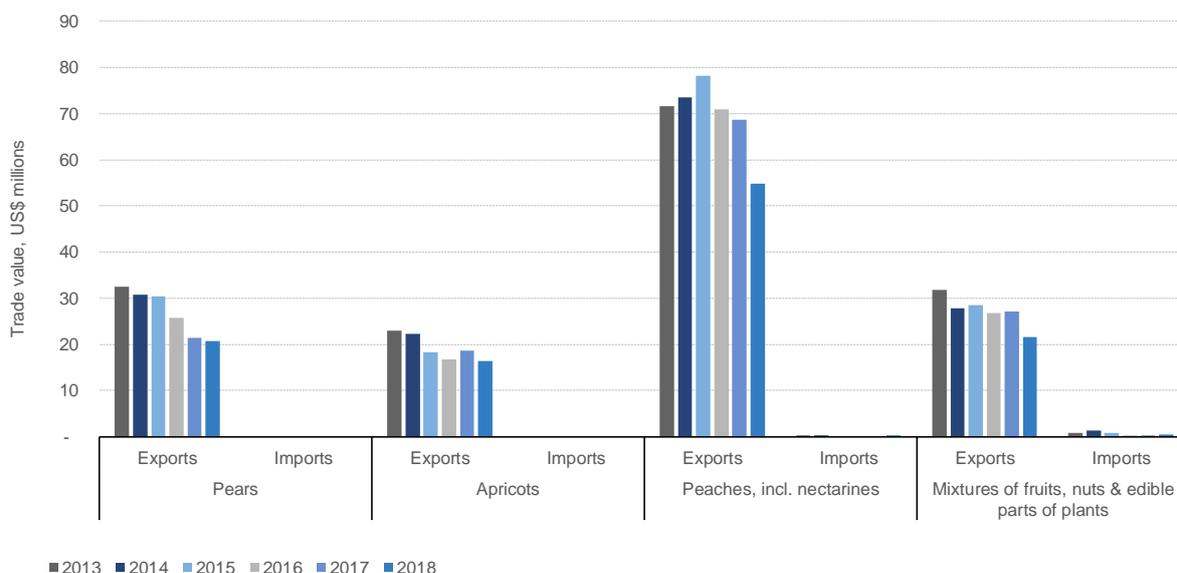
<sup>39</sup> <https://www.iol.co.za/business-report/companies/tiger-brands-buys-out-langeberg-1200861>.

- 2008.97: Mixtures of fruits (incl. nuts & edible parts of plants), prepared or preserved

Similar to the production structure shown in Figure 9, the largest component of canned fruit exports is accounted for by peaches (including nectarines), followed by pears, mixed fruit and apples.

The exports and imports for these products are illustrated in Figure 10. South Africa is a large net exporter of canned fruit, with very little imports, mostly from China and Germany, entering the country since 2013. The trade surplus has however been narrowing due to the rapid decline in some exports. Canned peach exports declined by 30% from US\$78 million in 2015 to US\$55 million by 2018. Pears have also decreased by 32%, to US\$21 million in 2018. Apricot exports have declined by 10% to US\$16 million over this same period.

**Figure 10: South Africa's trade in canned fruit, nominal US\$ millions**



Source: ITC Trade Map

Most canned fruit is destined for the EU, Japan, China and Australia. South African canned fruit is faced with significantly different tariffs across its major export markets. Whereas, Hong Kong and Singapore provide duty-free access for SA products, Viet Nam and Japan charge duties amounting to 15% and 40% respectively. In the EU and USA South African fruit exports receive some form of preferential access through the EPA and AGOA.

**Table 10: Top export destinations for canned fruit exported by South Africa in 2018 & average duty\***

Destinations	Average SA exports 2016-2018, US\$ mn	Average duty, 2008.40	Average duty, 2008.50	Average duty, 2008.70	Average duty, 2008.97
EU (28) – outside TRQ	35,398	23%	23%	23%	16%
EU (28) – within TRQ**		9%	9%	9%	8%
Japan	15,442	15%	15%	15%	15%
China	13,643	5%	5%	5%	5%
Australia	10,334	5%	5%	5%	0%
New Zealand	5,916	5%	5%	5%	5%
Hong Kong, China	5,643	0%	0%	0%	0%
Canada	5,150	9%	8%	7%	3%
Singapore	4,572	0%	0%	0%	0%
USA	4,399	0% (AGOA)	0% (AGOA)	0% (AGOA)	0% (AGOA)

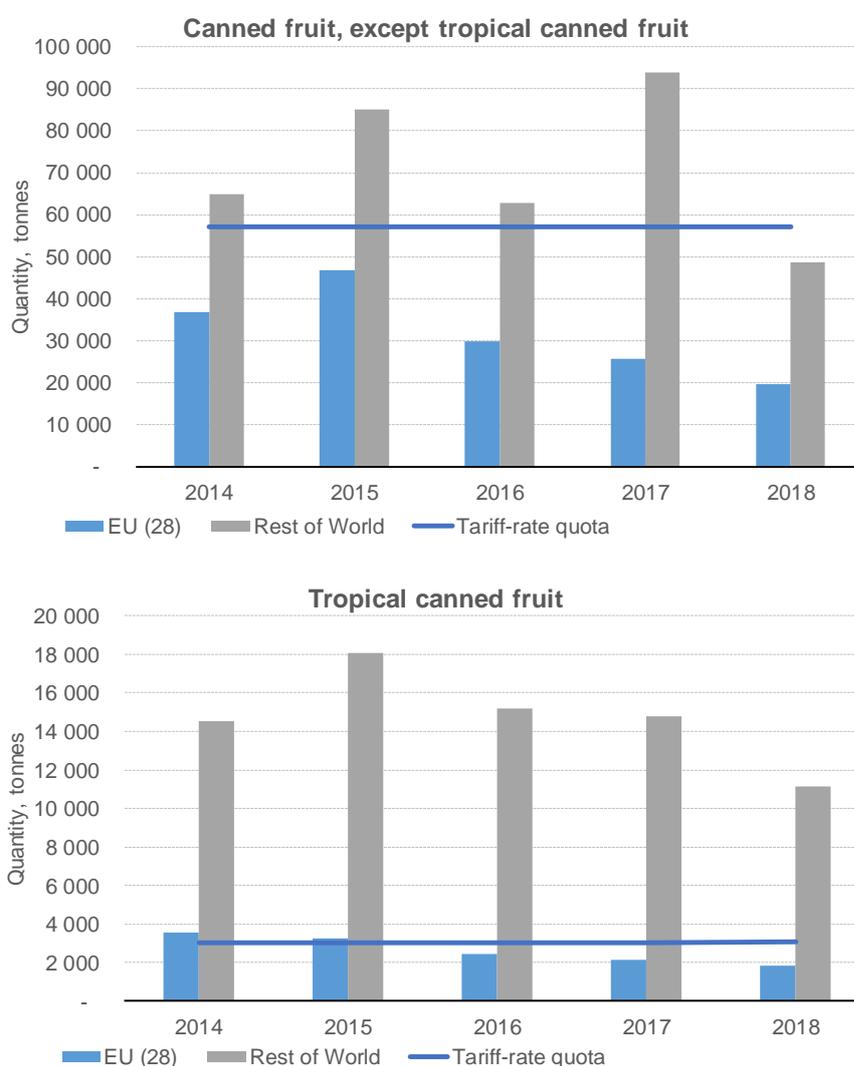
<b>Viet Nam</b>	3,816	35%	40%	35%	30%
<b>Other regions</b>	9,258	N/A			
<b>Total exports</b>	<b>113 571</b>	<b>N/A</b>			

Source: ITC Trade Map

\* The average duty for the 6-digit nomenclature represents the average duty product at the 8-digit nomenclature. \*\* Under the EPA, imports within the TRQ under HS codes 2008.40, 2008.50 and 2008.70 are given a 41% reduction from the MFN duty, while those under HS code 2008.97 are given a 50% reduction. Table 3 summarises the preference reductions under EPA.

In terms of volume, EU to the exports constitute 29% of single-fruit canning (peach, pear and apricot) and 14% of mixed-fruit canning. This is equivalent to 19,669 tonnes and 1,832 tonnes respectively. Figure 11 illustrates that current levels of canned fruit exports to the EU are well below what is provided for though the TRQs.

Figure 11: South Africa's canned fruit exports against TRQ, tonnes



Source: ITC Trade Map

Figure 11 also shows that there has been a shift in demand from the EU towards the rest of the world, and specifically, Africa, Australia and Asia. Exports to Africa increased from US\$20 million in 2014, to US\$30 million by 2018. Demand in Australia has also increased from US\$6 million to US\$16 million over the same period.

### 6.2.3 Factors explaining TRQ uptake

A key observation from the previous discussion is that South Africa's overall exports of tropical canned fruit have been declining in general (in value and volumes), with a severe contraction in 2018 where exports declined by 23% from the previous year. Exports to the EU have followed this same trend. As a result, South Africa is no longer able to meet its TRQ in the EU for this product. The main reasons for the country's utilisation of these preferences are considered below.

#### Awareness of the TRQs

One of the two exporting companies engaged with indicated that all their EU exports enter through the TRQ allocation. The company suspects that the falling uptake in the TRQ may be a result of lower canned fruit production, and not lack of awareness.

#### Awareness among the retailers

Retailers in the EU market are aware of the TRQ opportunities. As such, when procuring from the South African companies, the expectation is that the duty is factored into the selling price. This means that if the SA exporter does not take advantage of the TRQ, the EU retailer will request a discount regardless. Because of this, the one local manufacturer interviewed noted that all of their exports to the EU are processed through the TRQ.

#### EU regulations and standards

In order to ensure safety, quality and that health and sanitary standards are adhered to throughout the value chain, traceability is critical. Traceability, in the event of unforeseen risk, allows the processing company to track back to each level of the value chain and identify the root of the problem, and remedy accordingly. Generally, the large exporters are able to meet the international standards for exporting e.g. The International Featured Standards (IFS)<sup>40</sup> and BRC Global Standards.<sup>41</sup> Moreover, the presence of the PPECB authenticates the health standards and regulations in SA and eases entry into the EU market.

#### EU additional duties on composite agri-goods

The EU imposes an additional duty on "composite agri-goods" that have undergone some transformation depending on the content of four agricultural ingredients – milk fat, milk proteins, starch or glucose, or various forms of sugar. Based on industry engagements, this was not identified as a constraint in the canned fruit industry. Fruit canners use sugar-light syrups, thereby minimising the sucrose-content.

The additional duty may be an issue in the jam industry, where the jam is set in sugar. One of the processors in the jam industry indicated that in order to qualify for the quota, the sugar content in the jam needs to meet certain sugar specifications. Given that the jam processor does not meet this sugar threshold, they have not been able to access the citrus jam TRQ (the TRQ has not been utilised to date).<sup>42</sup>

### 6.2.4 Conclusion

South Africa has a large and competitive fruit industry that has developed strong export capabilities over time. This has occurred at a time when there is increasing demand for fresh produce, while demand for processed fruit is declining. This shift in demand has contributed to a decline in canned fruit production. Moreover, changes in weather patterns have had an adverse impact on fruit production in South Africa, favouring the fresh fruit industry.

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<sup>40</sup> The IFS HPC is a standard for auditing safe and quality products/processes of suppliers concerning the manufacturing of household and personal care products. See <https://www.ifs-certification.com/index.php/en/standards/260-ifs-hpc-en>.

<sup>41</sup> Global Standards for Food Safety, Packaging and Packaging Materials, Storage and Distribution, Consumer Products, Agents and Brokers, Retail, and Gluten Free set the benchmark for good manufacturing practice, and help provide assurance to customers that your products are safe, legal and of high quality. See <https://www.brcgs.com/about/>.

<sup>42</sup> Email communication from a citrus jam processor in October 2019.

Together, these factors have reduced the export of processed canned fruit from SA. As a result, the downstream industry has consolidated significantly, largely through acquisitions by the dominant processors, and re-capitalisation has been low. Thus, despite the awareness and use of the TRQ, exports are unlikely to increase without improvement in underlying industry and climatic conditions.

In response to the industry's challenges, the DTI has proposed activities focused on improving production efficiency in the vegetable and canning industries, though it is not clear what these interventions may entail.<sup>43</sup>

### 6.3 Mortadella di Bologna

Mortadella di Bologna is a type of Italian sausage or luncheon meat made of finely hashed or heat cured pork.<sup>44</sup> The processing of Mortadella di Bologna is closely regulated and goes through a rigorous examination and approval process by the Istituto Nord Est Qualità (INEQ). INEQ also protects the quality of the product and the name as a Geographical Indication (GI).<sup>45</sup>

Over time, there has been a rise in the variations of mortadella (sausage) that can be found all over the world. Italian immigrants introduced the concept of mortadella in the South American region, especially in Argentina, Bolivia, Peru, Brazil, Ecuador, Chile, Colombia, Uruguay and Venezuela. During the stakeholder engagement, it was also established that there are now mortadella variations manufactured in South Africa.

There are two main companies that import mortadella di bologna into the country, namely Rialto Foods and Adriatic Ship Supply & Trading Company. These companies then distribute mortadella di bologna to retailers and restaurants in the country e.g. Old Town Italy, Cremalat and BM Foods.<sup>46</sup>

#### 6.3.1 Trade patterns

The 6-digit heading for "Sausages and similar products, of meat, offal or blood; food preparations based on these products" (HS1601.00) includes other sausage preparations *in other forms* (HS1601.00.90); *paté de foie gras and foie gras (goose liver paste)* (HS1601.00.10) and sausage *in paste form* (HS1601.00.20). The latter nomenclature applies to Mortadella di Bologna i.e. HS1601.00.20 i.e.

Over the last three years, there has been increased imports of sausages in "other" form, rising from US\$1.3 million to US\$2.3 million from 2016 to 2018. Over the same period, the imports *goose liver paste* declined sharply from US\$1,000 to \$0. The first import entry for Mortadella di Bologna was recorded in 2018, amounting to US\$19,000. The importers did not use the TRQ given that the TRQ usage for 2018 was zero percent. This was corroborated by industry participants that noted that they have been importing Mortadella di Bologna without using the TRQ.

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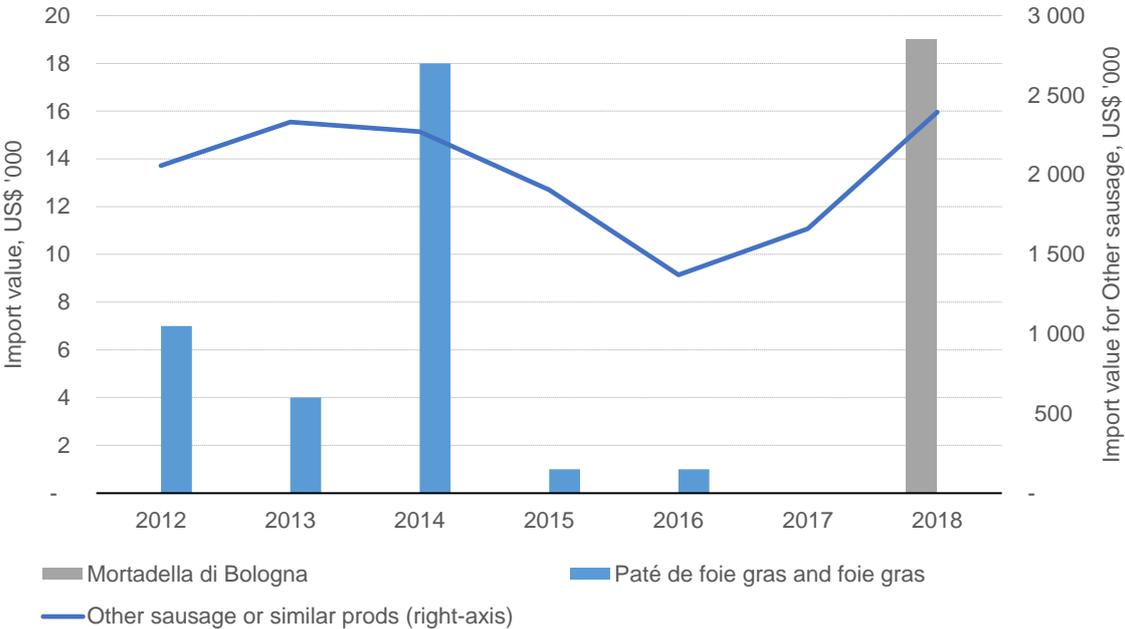
<sup>43</sup> [http://www.dti.gov.za/industrial\\_development/agro\\_processing.jsp](http://www.dti.gov.za/industrial_development/agro_processing.jsp).

<sup>44</sup> <http://www.weareitaly.net/en/product/Mortadella/emilia-romagna/Mortadella-Bologna-IGP.html>

<sup>45</sup> According to the Regulation, Mortadella Bologna IGP can be processed exclusively in Emilia Romagna, Piemonte, Lombardia, Veneto, Toscana, Marche, Lazio and in the province of Trento.

<sup>46</sup> Based on engagements with a company in the Italian Food industry, and verified by internet searches.

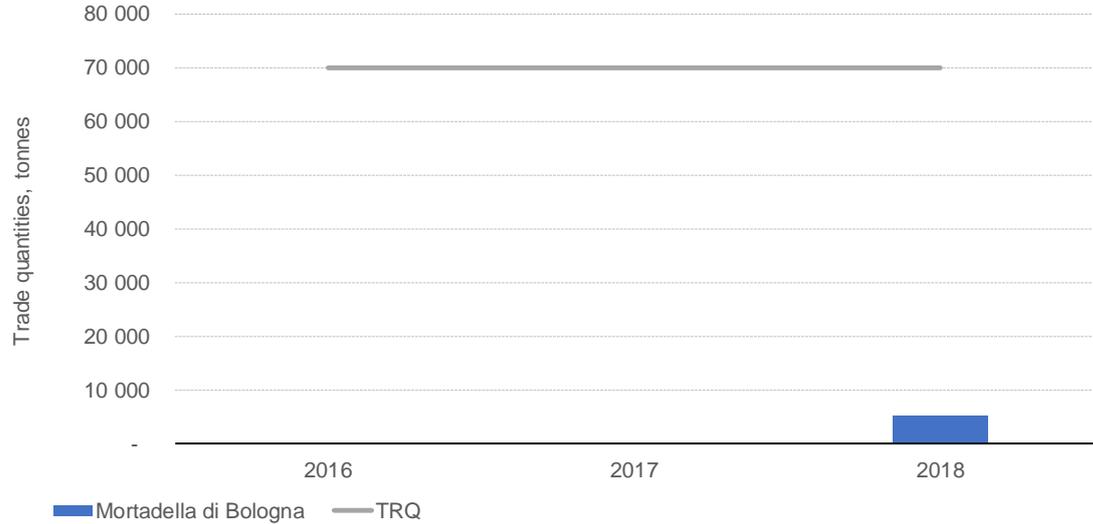
**Figure 12: South Africa’s imports of sausage varieties, in US\$ nominal values and tonnes**



Source: ITC Trade Map

In 2018, 5 tonnes was imported into South Africa (Figure 13). As expected, the Mortadella di Bologna imports were wholly sourced from Italy. The general rate of duty for Mortadella di Bologna imports is 40% or 240c/kg, whichever is higher. If imported within the quota allocation, Mortadella di Bologna can enter the SA market duty free (there is a 100% preference on the duty). In this case, none of the Mortadella di Bologna imports entered through the TRQ.

**Figure 13: South Africa’s Mortadella di Bologna TRQ usage, in tonnes**



Source: ITC Trade Map

**6.3.2 Factors explaining TRQ uptake**

Following an intensive attempt to engage with importers and distributors of Mortadella di Bologna (including other Italian products), two interviews were carried out. Based on these engagements,



the importation of Mortadella di Bologna through the TRQ dispensation has not occurred because companies are not familiar with the SADC-EU EPA in general, and the TRQ opportunities in particular.

During the stakeholder engagements, one key importer of Italian products (including Mortadella di Bologna) indicated that they supply all the requisite importing documents including a complete Bill of Entry, a valid proof of origin and movement certificate EUR1 when importing Mortadella di Bologna. Moreover, the importer has preferential supplier status for some imports from Italy, which indicates that the products have been wholly obtained or have undergone sufficient working or processing in Italy.<sup>47</sup> However, the importer is not familiar with the process of accessing the TRQ preferential tariff. As such, the company incurs the normal duty rate for importing. Generally, it appears as though SA importers of Mortadella di Bologna not aware of the TRQ, and therefore not utilising it.

### 6.3.3 Conclusion

The mortadella industry in South Africa is niche, with a handful of companies involved in the import and distribution of the product. These companies have been trading Mortadella di Bologna for a long period of time and continue to do so using established methods (and paying the full tariff). It would appear that there is a lack of awareness of the TRQ amongst importers, and no pressure from consumers (whether households or retailers) to secure the significant price benefits that would readily be gained from accessing this preference. Likewise, there is little interest from producers in the EU from increasing their market share in the small South African market for speciality meats using the TRQ.

## 7 Findings and Recommendations

This study considered the performance of South African agriculture exports to the EU, and specifically, the usage of the TRQs as per the SADC-EU Partnership Agreement. Despite the preferences provided, the utilisation rates for South African exports of ethanol and canned fruit are low and declining, while for EU exports of Mortadella di Bologna are zero.

The study finds that the main reasons for the low uptake by South African exporters of the specified products are supply constraints in the domestic market. For ethanol, most domestic production is exported, specifically directed at higher-value markets outside of the EU. Moreover, a lack of progress in the implementation of domestic regulatory reforms, has stifled new investment in bio-ethanol production. Similarly, the production and export of South African canned fruit is constrained by changes in consumer taste and climatic conditions, rather than limitations in the EU market. The reason for the non-use of the TRQ for exports of Mortadella di Bologna to South Africa is less clear, but seems to reflect a lack of awareness from importers and insufficient pressure from consumers.

Based these findings, the recommendations can be grouped into three broad categories. Easy wins require the minimal effort to increase uptake and largely involve disseminating information about the TRQs to a wider audience. Technical recommendations speak to the need to bolster SPS requirements and establish a monitoring plan for milk products. Lastly, there are a number of structural issues that have a direct impact on the capacity and competitiveness of the industries within South Africa, and currently limit South Africa's to the EU.

Most of these issues can only be addressed by the South African industry with support from its Government, though there are areas where the EU may be able to provide insight and technical support.

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<sup>47</sup> See more information on Preferential Origin here: [https://ec.europa.eu/taxation\\_customs/business/calculation-customs-duties/rules-origin/general-aspects-preferential-origin/introduction\\_en](https://ec.europa.eu/taxation_customs/business/calculation-customs-duties/rules-origin/general-aspects-preferential-origin/introduction_en)

## A. Easy wins

**Recommendation 10:** Increase awareness among companies that import Mortadella di Bologna and cereal-based preparations.

**Recommendation 11:** Increase awareness about market opportunities in the EU for targeted SA exporters. In the case of ethanol, provide country-level information on demand and the requirements to enter these markets. The establishment of an approved service provider, similar to the Perishable Produce Export Certification Agency, might be beneficial for other exporters.

**Recommendation 12:** Educate South African retailers and restaurants about the availability and benefits of the TRQ on niche products. If local consumers are fully aware of the cost benefits associated with the TRQs, they are more likely to demand preferential prices from importers and distributors. A dedicated knowledge workshop with importers, retailers and restaurants in South Africa to promote EU food products provided for under the TRQs could be considered.

**Recommendation 13:** Inform importers of EU products that have not used the TRQs about the Voucher Correction System, which allows them to claim back on the duties paid, provided they were within the TRQ.

## B. Technical recommendations

**Recommendation 14:** Prioritise the development of technical capabilities for exporting in South Africa e.g. developing a monitoring plan for dairy products and ramping up the SPS technical capacity at DALRRD.

**Recommendation 15:** Support South Africa (and SADC) in the implementation of a diagonal accumulation system that allows movement of inputs across SADC EPA states.

## C. Addressing structural challenges

**Recommendation 16:** Now that the draft Biofuels Regulatory Framework has been approved subject to amendments, there is need to advocate for its urgent implementation to encourage firms to invest in expanding biofuel production, and simultaneously attract new entrants. Here South Africa may be able to learn more from the EU regulatory experience through study tours or knowledge-sharing events.

**Recommendation 17:** The fruit industry (and agriculture in general) is already suffering from the impact of climate change. A climate mitigation strategy is needed by the industry, and this may include investing in yield varieties that are less vulnerable to the effects global warming.

**Recommendation 18:** For those products where sugar content is influencing consumption and prohibiting exports i.e. citrus jams, information or support may be needed to encourage the industry to diversify into products that have low sugar content.

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## Annexure 1

### Interview schedule

Industry / Stakeholder	Organisation	Interview conducted
Ethanol	South African Sugar Association	Yes
	Ethanol Producers Association of Southern Africa	Yes
	NCP Alcohols	Yes
	Illovo	Yes
Tropical canned fruit	SA Fruit & Vegetable Canners' Export Council	Pending
	Fresh Produce Exporters' Forum	Responded via email
	Tiger Brands	Yes
Mortadella Bologna	Adriatic Ship Supply & Trading Company	Yes
	Rialto Foods	Yes
	Old Town Italy	Yes
Government departments	Department of Agriculture, Land Reform and Rural Development	Yes
	South African Revenue Services	Yes