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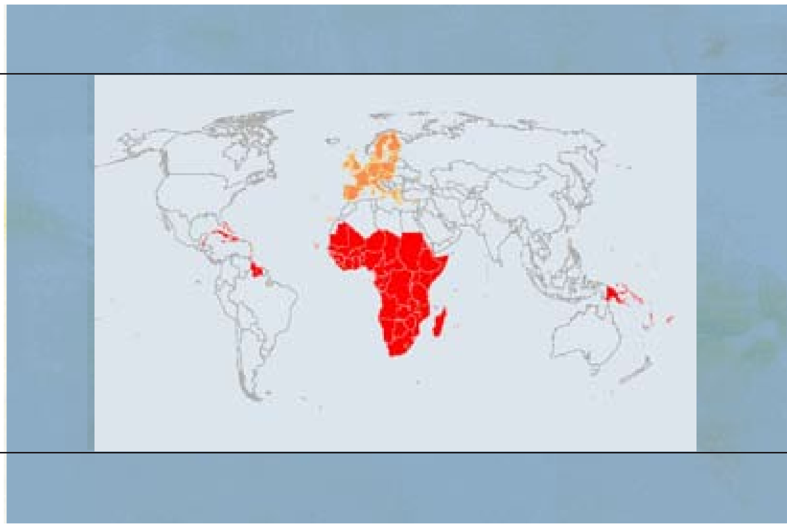
The agricultural dimension of the ACP-EU Economic Partnership Agreements



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The agricultural dimension of the ACP-EU Economic Partnership Agreements

Edited by
Suffyan Koroma
and
J.R. Deep Ford

Commodities and Trade Division

FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS
Rome, 2006

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Foreword

Overview

The African, Caribbean and Pacific (ACP) countries are facing several major sets of closely interlinked forces that are likely to have significant impacts on the development of their agriculture (including fisheries) sectors and their food security situations. The possible conclusion and outcome of both the negotiations for Economic Partnership Agreements (EPAs) under the Cotonou Agreement (with the European Union (EU)) and the World Trade Organization (WTO) Doha Round pose serious concerns on the future of their agricultural trade and development. Furthermore, the ongoing Common Agricultural Policy (CAP) reform which will determine the nature of EU agriculture over the next few years, and the process of EU enlargement have also created additional challenges for ACP States as to how to address these multi-faceted forces so as to reap the maximum benefits for their mostly agrarian economies.

This study is one of the outputs of a programme of assistance provided by FAO to the ACP Secretariat and member states in preparing for the detailed phase of negotiations on Economic Partnership Agreements (EPAs) with the EU. It provides an introduction to some of the most critical aspects of the agriculture and fisheries negotiations including feasible approaches and options for the ACP to ensure that their agricultural and fisheries sectors reap maximum and sustained benefits with a view toward enhancing their food security situation.

The report consists of seven chapters. The first chapter presents an introduction to the ACP, its negotiating groups and the importance of the agricultural sector. It emphasises the dependency on primary exports with low income elasticity and high price volatility, high production variability and relatively low yields. It identifies the major issues that would need to be addressed to ensure that as global agriculture markets become further integrated, ACP agriculture does not become uncompetitive and marginalized. It also provides a summary on the status of EPA negotiations.

Chapter 2 examines issues of compatibility between the EPAs and the WTO, including the implications for ACP-EU trade relations. It presents detailed assessments of the options for the EPAs, the requirements and implications for the ACP of the “substantially all of the trade” clause in GATT Article XXIV, the pros and cons under the WTO legal system of having EPAs as custom unions or free trade areas, the link with the Enabling Clause, issues related to asymmetry, reciprocity and the transition period. It also assesses the possible impacts on specific products and the future of the commodity protocols for ACP agriculture under the EPAs. In Annex 2.1 to Chapter 2, the existing framework of legal instruments that regulate Intellectual Property Rights (IPRs) relating to agriculture of relevance to the EPAs is presented. Finally, options are suggested for ACP negotiators drawing on lessons from previous agreements negotiated by the EU and the positions taken in the Doha Round.

Chapter 3 examines the potential role of EPAs in supporting food security in ACP states. It assesses the current dynamic of ACP–EU trade, the effects that the preferences have had on the value chains associated with ACP exports and the extent to which this relationship may change in the coming years as a result of “preference erosion”. It also examines challenges and options for the ACP in meeting new and emerging EU Sanitary and Phytosanitary Standards (SPS). In this way it complements the parallel chapters on the effects of the CAP reform and EU enlargement on the ACP, the WTO interface with the ACP–EU relationship and on the challenges facing the ACP in the effective management of their fisheries resources. Finally it presents options for the ACP drawing on lessons from the EU-South Africa Trade and Development Cooperation Agreement (TDCA) and the EU-Chile trade agreement.

Chapter 4 describes the background to the recent CAP reforms and the implications that these reforms will have for ACP states. These reforms are relevant to the EPA negotiations because they affect the value of the preferential access, which the ACP states are trying to safeguard through EPA agreements. Also, drawing on results from impact analysis, it examines the commodity sectors that are likely to be affected by the CAP and the implications for the relevant ACP states.

In Chapter 5 the issue of EU enlargement and how this process is likely to impact on ACP agriculture is evaluated. The chapter provides an assessment of possible agricultural trade policy and other changes that are likely from the recent accession of the ten new member states to the EU. It examines the channels and mechanisms by which third countries, including ACP countries, might be affected by these changes, focusing mainly on their trade flows.

Chapter 6 focuses on the fisheries sector. It examines challenges and options to the ACP in both the WTO fisheries negotiations and the Fisheries Partnership Agreement between the ACP and EU.

The final chapter (Chapter 7) evaluates the shortcomings in the EC's negotiating objectives as set out in its mandate and assesses the implication for ACP agriculture using an illustrative scenario based on the assumption that its terms are no more onerous than is the South Africa–EU TDCA. It further extends and assesses options of how issues in the WTO relevant to food security could be made more development friendly. Finally, it examines the issue of resource mobilization for agriculture and rural development in the ACP countries along with estimates of the amount of funds required to enhance agricultural productivity and food security in ACP states.

Summary of findings

The main findings and conclusions of the study are the following:

a) Current agriculture and livestock policy and strategies should be better integrated and reflected in the ongoing EPA Negotiations and by ACP countries in their other negotiating arenas, especially in the WTO Doha Round. It is essential to ensure that all these negotiations conclude agreements that further national objectives related to the agricultural sector.

b) ACP preferences will continue to be eroded - by WTO liberalization, Everything-but-Arms (EBA), CAP Reform, EU enlargement and EU Regional Trade Agreements (RTAs). However, beneficial preference opportunities still exist and ACP countries should negotiate with the goal of strengthening these, using them effectively and making them permanent in the context of EPAs.

c) The structure and patterns of trade are changing rapidly, influenced heavily by private sector investment and standards. ACP countries need to prepare at the national level to accommodate and adjust to these changes in order to expand their own trade. These regulations (SPS) and other private standards (traceability) point to the need for promotion of strategic alliances between firms of all sizes and increased cross border integration in order to be competitive and sell in premium markets.

d) Adjustment assistance is an accepted dimension of the ongoing negotiations and should be pursued by ACP countries jointly and in the context of specific products. Preference erosion will be different for different commodities, for instance, beef may be less negatively affected than rice.

e) An assessment of the impact of CAP reform on product markets indicates that sugar and rice will be by far the most negatively affected: *sugar* because of the significant price reduction (approximately 33 percent) and a sharp fall in production induced by a quota reduction; *rice* because of a 50 percent cut in the support price. One way of offering compensation on rice would be to remove the remaining (35 percent) duty on TRQ amounts and expand the size of the quota. On sugar, the accompanying measures, including both trade and development measures, should be fully agreed before completion of EPA negotiations, including how Least Development Countries' (LDC) EU EBA commitments will be accommodated.

f) The immediate impact of EU enlargement on ACP agricultural trade will be limited. Both changes in the basis of quota allocations and removal of the production incentive of coupled payments lead to this conclusion. However, ACP countries need to project how future production growth in each country can affect its market opportunities and negotiate access and assistance that will maintain stable conditions while facilitating change in their own countries.

g) Fish trade preferences are also being eroded but the major obstacles for ACP countries are the relatively more stringent food safety and quality requirements that their exports face. This underlines the need for continuous capacity-building and institutional strengthening in ACP countries in the area of fisheries production and marketing management. Assistance from, and cooperation with importing countries and international organizations will be needed.

h) ACP Small Island Developing States (SIDs) dependent on fish exports should consider placing greater emphasis on fresh and frozen products, where the market is growing, and away from the stagnant and/or falling demand for canned and cured products.

i) A waiver through Article IX of the WTO Agreement would not meet the Cotonou commitment "to conclude new WTO-compatible trading agreements." Also, extending the Generalized System of Preferences (GSP) would not be an acceptable option because an extension to all other developing countries would automatically erode any benefit of preferences under an EPA framework. One option might be to try to define the uniqueness of the ACP relationship (history with the EU) and qualify the EPA under the current GSP as a programme only for the ACP.

j) Attaining WTO compatibility for EPAs seems most likely by amending Article XXIV, through introducing a Special and Differential Treatment (SDT) exception. This is being pursued in the WTO by both the ACP and EU, arguing that the Doha commitment should "take into account the development aspects of regional trade agreements". This would allow the asymmetry needed in an EU/ACP regional trade agreement. The ACP and the EU are a formidable block in the WTO and they should find greater commonality in their positions and pursue them jointly in the WTO before the completion of the Doha round to enable the compatibility of EPAs with WTO regulations.

k) The EU will require some liberalization by the ACP under EPAs. Therefore, a similar process as is being engaged in for Special Products in WTO framework should be completed for the EPA agreement. This should be detailed by tariff lines for each country in the regional grouping and treatment phased appropriately.

l) CAP reform will further diminish the value of preferences, and also reduce revenue to EU farmers. In the Cotonou Agreement the EU commits to maintain benefits enjoyed by ACP states relative to third countries. While EU farmer compensation is clear, this is far from the case with ACP producers. This commitment should be fulfilled as a part of the EPA negotiations.

m) Regional and sub-regional cooperation should also be encouraged in the field of fisheries management and in monitoring, control and surveillance. This element will take on a larger role in the future as funds paid by the EU for access to ACP fishing grounds will be increasingly directly allocated, at least in part, for this purpose in the Fishery Partnership Agreements (FPAs).

n) ACP coastal countries should assess and accordingly develop its capabilities in critical areas such as: research paying due attention to broader environmental concern, fishery monitoring, control and surveillance capacities, and management policies that include effective participation of stakeholders.

THE ACP STATES BY REGION AND ECONOMIC CLASSIFICATION

Least Developed Countries (LDCs)				**Non-LDCs**		
Africa (34)		**Caribbean (1)**	**Pacific (5)**	**Africa (15)**	**Caribbean (15)**	**Pacific (9)**
Angola	Liberia	Haiti	Kiribati	Botswana	Antigua and Barbuda	Fiji
Benin	Madagascar		Samoa**	Cameroon	Bahamas*	Papua New Guinea
Burkina Faso	Malawi		Solomon Islands**	Congo	Barbados	Tonga
Burundi	Mali		Tuvalu*	Côte d'Ivoire	Belize	+Marshall Islands*
Cape Verde*	Mauritania		Vanuatu**	Gabon	Cuba***	+Cook Islands*
Central African Republic	Mozambique			Ghana	Dominica	+FS of Micronesia*
Chad	Niger			Kenya	Dominican Republic	+Nauru*
Comoros*	Rwanda			Mauritius	Grenada	+Niue*
Democratic Republic of the Congo	Sao Tome and Principe**			Namibia	Guyana	+Palau*
Djibouti	Senegal			Nigeria	Jamaica	
Equatorial Guinea*	Sierra Leone			Seychelles**	Saint Kitts and Nevis	
Eritrea*	Somalia*			South Africa***	Saint Lucia	
Ethiopia**	Sudan**			Swaziland	Saint Vincent and the Grenadines	
Gambia	Togo			Zimbabwe	Suriname	
Guinea	Uganda				Trinidad and Tobago	
Guinea-Bissau	United Republic of Tanzania					
Lesotho	Zambia					

* Not a WTO member

** Observer status at WTO. Observers must start accession negotiations within five years of becoming observers.

*** Cuba is a Member of the ACP group but not part of the Cotonou Agreement

**** South Africa is formally joined the ACP group in April 1998. It dose not benefit from Lomé trade preferences. It has concluded a separate FTA with the EU. Under the WTO it is considered as a developed country.

\+ Joined the ACP group in June 2000.

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Abbreviations and acronyms

ACP	African, Caribbean and Pacific
AoA	Agreement on Agriculture
AP	Appellant Body
CAP	Common Agricultural Policy
CAR	Central African Republic
CARICOM	Caribbean Community and Common Market
CARIFORUM	Caribbean ACP States
CEC	Commission of the European Community
CEEC	Central and Eastern European country
CEMAC	Economic and Monetary Community of Central Africa
CET	Common external tariff
CN	Combined Nomenclature
COMESA	Common Market of Eastern and Southern Africa
COMEXT	Eurostat’s Commerce extérieur intra- and extra-EU trade database
CRNM	Caribbean Regional Negotiating Machinery
CRTA	Committee on Regional Trade Agreements (WTO)
CU	Customs union
EAC	East African Community
EBA	Everything but Arms
EC	European Community
ECOWAS	Economic Community of West African States
EEC	European Economic Community
EEZ	Exclusive Economic Zone
EFTA	European Free Trade Association
EPA	Economic Partnership Agreement
ESA	Eastern and Southern Africa
EU	European Union
FAPRI	Food and Agricultural Policy Research Institute
FEOGA	European Agricultural Guidance and Guarantee Fund
FMD	Foot-and-mouth disease
FP	Financial perspective
FPA	Fishery Partnership Agreements
FTA	Free Trade Agreement
FTA	Free Trade Area
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
GNI	Gross national income
GSP	Generalized System of Preferences
HS	Harmonized System
IDS	Institute of Development Studies
LDC	Least developed country
MFN	Most favoured nation
MRL	Minimum residue level
MTR	Mid-term review
NIS	Newly independent states

OECD	Organisation for Economic Co-operation and Development
Pacific Forum	Pacific ACP States
PSE	Producer subsidy equivalent
RoW	Rest of world
RTA	Regional Trade Agreement
SACU	Southern African Customs Union
SADC	Southern African Development Community
SDT	Special and differential treatment
SIDS	Small Island Developing States
SMP	Skim milk powder
SP	Special Product
SPS	Sanitary and phytosanitary standards
TBT	Technical barriers to trade
TDCA	South Africa Trade, Development and Co-operation Agreement
TRAINS	Trade Analysis and Information System
TRIPS	Trade-Related Aspects of Intellectual Property Rights
TQ	Tariff quota
UNCTAD	United Nations Conference on Trade and Development
US	United States of America
WAEMU	Western African Economic and Monetary Union
WTO	World Trade Organization

Chapter 1
Introduction

The Cotonou Agreement of June 2000 between the African Caribbean and Pacific (ACP) States and the European Union (EU) included a comprehensive framework for establishing the future of ACP-EU relations in the post Uruguay Round Period. The primary focus of this agreement is economic development, regional integration, poverty reduction and the smooth and gradual transition of the ACP into the global economy. To achieve these objectives, the Agreement provides for an approach for concluding of new World Trade Organization (WTO) compatible trading arrangements between the ACP States and the EU. This is to be accomplished through the conclusion of Economic Partnership Agreements (EPAs) to be negotiated during the period starting from September 2002 to December 2007. The ACP States are Negotiating EPAs as regional groups as follows: CEMAC (Economic and Monetary Community of Central Africa; ECOWAS (Economic Community of West Africa States; ESA (Eastern and Southern Africa); SADC (Southern Africa Development Community); CARIFORUM (Caribbean Forum); and the Pacific Forum. Table 1.1 presents a summary profile of each of these groups.

The basic arguments concerning the pros and cons of EPAs are over seven years old. They date back to the EU's proposal made at the outset of negotiations for a successor to Lomé IV that the trade regime be revised. The European Commission's arguments for and against such a change were set out in a Green Paper to which the ACP (as well as civil society and research organizations) subsequently responded (EC, 1997). On the positive side, the EC's arguments included the points that a new trade regime should do more to foster the integration of ACP states into the world economy and should be more easily defensible in the WTO. On the negative side, the ACP states were concerned that the new arrangements would reduce the benefits enjoyed by them under Cotonou and earlier Agreements.

It was not possible to agree on such a new trade regime from the outset of the Cotonou Agreement. Instead, Cotonou extends the Lomé trade regime, but with the proviso that negotiations must commence in 2004 for a successor regime that will come into effect in 2007. It is the scope of this post-2007 trade agreement that is the subject of the negotiations that began formally in September 2002.

TABLE 1.1: ACP GROUPS NEGOTIATING EPAs

Africa Group					
CEMAC	**ECOWAS**	**ESA**[7]	**SADC**	**CARIFORUM**	**Pacific Forum**
Cameroon[2]	Benin[2]	Burundi[1,5]	Angola[1,4]	Antigua and Barbuda[2,6]	Cook Islands[3,4,6]
Central African Republic[1,2,5]	Burkina Faso[1,2,5]	Comoros[1,3,6]	Botswana[2,4,5]	Bahamas[2,3,6]	Fiji[4,6]
Chad[1,5]	Côte dÍvoire[2]	Djibouti[1]	Lesotho[1,2,4,5]	Barbados[2,6]	Kiribati[1,3,4,6]
Republic of the Congo[2]	Guinea-Bissau[1,2,5]	Eritrea[1,3]	Mozambique[1,4]	Belize[2,6]	Marshall Islands [3,4,6]
Democratic Republic of the Congo[1]	Mali[1,2,5]	Ethiopia[1,3,5]	Namibia[4]	Dominica[2,6]	Federated States of Micronesia[3,4,6]
Gabon[2]	Niger[1,2,5]	Kenya[8]	United Republic of Tanzania[1,8]	Dominican Republic[4,6]	Nauru[3,4,6]
Equatorial Guinea[1,2,3]	Senegal[1,2]	Madagascar[1]	Swaziland[2,4,5]	Granada[2,6]	Niue[3,4,6]
Sao Tome and Principe[1,3,4,6]	Togo[1,2]	Malawi[1,5]		Guyana[2,6]	Palau[3,4,6]
	Cape Verde[1,3,4,6]	Mauritius[6]		Haiti[1,2,6]	Papua New Guinea[4,6]
	Gambia[1,4]	Rwanda[1,5]		Jamaica[2,6]	Samoa[1,3,4,6]
	Ghana[4]	Seychelles[3,6]		Saint Kitts and Nevis[2,6]	Solomon Islands[1,4,6]
	Guinea[1,4]	Sudan[3]		Saint Lucia[2,6]	Tonga[4,6]
	Liberia[1,3,4]	Uganda[1,5,8]		Saint Vincent and the Grenadines[2,6]	Tuvalu[1,3,4,6]
	Nigeria[4]	Zambia[1,5]		Suriname[2,6]	Vanuatu[1,3,4,6]
	Sierra Leone[1,4]	Zimbabwe[5]		Trinidad and Tobago[2,6]	

[1] Least Developed Country
[2] Has a common external tariff (Customs Union) with other members of group
[3] Not a WTO Member/in the WTO accession process
[4] Not a member of the Customs Union but has Preferential/Free Trade Agreement with other members of group
[5] Land-locked country
[6] Small Island Developing State
[7] Group does not represent a Regional Economic Community
[8] Belongs to a Customs Union with countries of other negotiating group

TABLE 1.2: ECONOMIC PROFILE OF ACP COUNTRIES

	Developing countries	ACP	ACP-A	ACP-C	ACP-P
Land area (2001) (1000 ha)	7 603 818	2 474 889	2 362 585	59 070	53 234
Total population (2002) (million)	4 900	727	684	35	8
Total population average annual growth rate (1990-2002) (%)	1.7	1.8	1.9	1.1	2.1
GDP per capita (1999-2001) (constant 1995 US$)	1 226	613	568	1 722	1 192
GDP per capita average annual growth rate (1990-2001) (%)	1.5	-0.2	-0.3	0.9	0.8
Agricultural GDP average annual growth rate (1990-2001) (%)	2.3	2.6	2.7	2.7	0.7
Trade/GDP (2001) (%)	52	54	55	46	82
Sectoral breakdown of economy (2001) (% of GDP)					
Agriculture	12.7	16.8	18.1	8.5	25.1
Industry	37.0	29.7	28.9	33.3	40.8
Manufacturing	23.5	13.5	13.6	12.8	7.7
Services	50.3	53.6	53.0	58.2	34.1

Note: ACP-A, ACP-C and ACP-P refer to the ACP countries in Africa, the Caribbean and the Pacific, respectively.
Sources: FAO and World Bank.

The ACP country group is demographically, geophysically and economically diverse. The total ACP country population, 727 million people, represents 15 percent of the total population of developing countries, with 94 percent living in Africa, close to 5 percent in the Caribbean and just over 1 percent in the Pacific countries.

Basic economic indicators vary significantly among the ACP countries, with per capita GDP ranging from more than US$9 000 in some Caribbean countries to less than US$100 in the poorest African countries. In the 1990s (1990-2001), the ACP countries averaged significantly lower rates of per capita GDP growth than the developing countries as a whole.

With regard to productive sectors, the ACP countries rely more on agriculture for income and employment generation than the overall group of developing countries, although this does not apply uniformly to all subgroups, the Caribbean countries being the exception. Large diversity exists among individual countries in the group. However, many of the industries or services are tightly linked to agriculture in numerous countries in the region. It is estimated that in most sub-Saharan Africa countries processing of agricultural products accounts for two-thirds of manufacturing value-added.

1.1 The importance of agriculture in the ACP countries

Agriculture’s role in promoting economic growth and alleviating hunger and poverty in most ACP countries is underscored by its importance in GDP, employment and trade, as illustrated in Figures 1.1(A) to 1.1(C). With the exception of the Caribbean subgroup, agriculture’s share in the GDP of ACP countries is higher than in developing countries as a whole and, although its role in employment generation has declined, agriculture still accounts for more than 60 percent of total employment in ACP countries compared to around 55 percent in developing countries as a whole. Agriculture also accounts for a larger portion of total trade for the ACP countries than for the developing countries as a group.

The agricultural sector’s relatively weak performance in the ACP countries is illustrated by Figure 1.2, which shows per capita food production over the last four decades for the developing countries as a whole as well as for the ACP countries in Africa, the Caribbean and the Pacific. While the developing countries have seen sustained increases in per capita food production throughout the period, in the ACP country group, food production on average, has not kept up with population growth. This is in stark contrast with the need to produce more food to cover a large part of the dietary needs of each ACP subregion both at present and in the future.

FIGURE 1.1(A): SHARE IN GDP

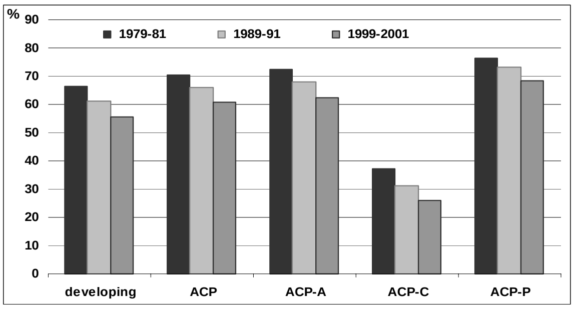


FIGURE 1.1(B): SHARE IN EMPLOYMENT

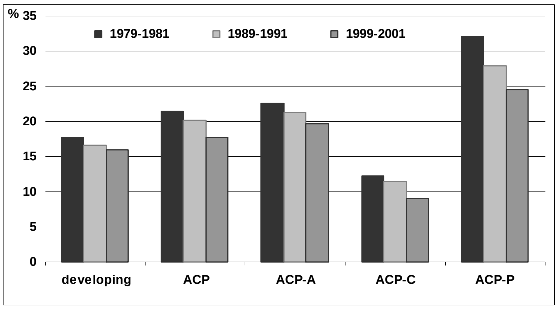


FIGURE 1.1(C): SHARE IN TRADE

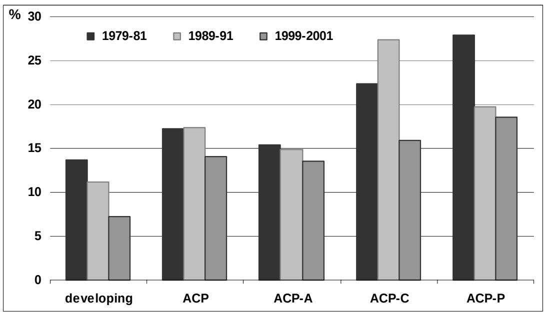


FIGURE 1.2: PER CAPITA FOOD PRODUCTION IN DEVELOPING AND ACP COUNTRIES (INDEX: 1989-91=100)

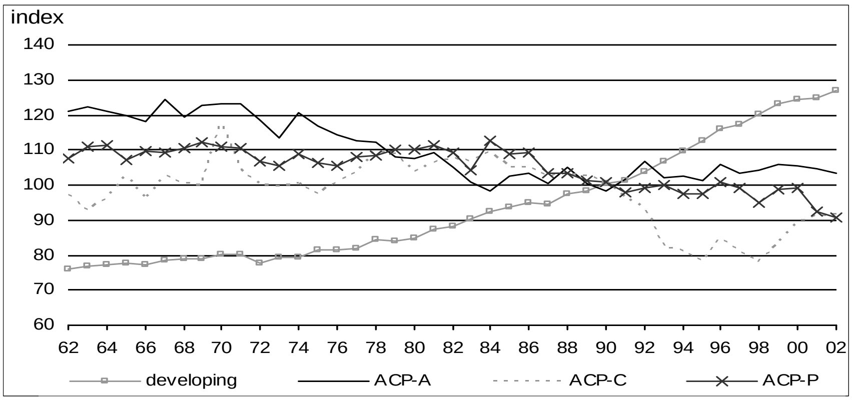


TABLE 1.3: AGRICULTURAL INDICATORS FOR ACP COUNTRIES

	Developing countries	**ACP**	**ACP-A**	**ACP-C**	**ACP-P**
Proportion of arable land irrigated (2001) (%)	11.0	4.9	4.2	22.7	0.5
Average added value in agriculture per worker (US$) (2001)	767	347	314	1 711	574
Per capita cereal production (2002) (kg/year)	242.3	129.3	132.9	81.5	23.6
Cereal yield (2003) (kg/ha)	2 837	1 137	1 123	2 101	2 082
Fertilizer use (2001) (kg/ha)	110.0	14.8	12.9	58.8	56.8

Data available only for Fiji, Papua New Guinea and Samoa.
Note: ACP-A, ACP-C and ACP-P refer to the ACP countries in Africa, the Caribbean and the Pacific, respectively.
Source: FAO and World Bank.

Although agricultural conditions vary widely across ACP countries, many share worrisome characteristics and trends such as high production variability, relatively low yields, and dependency on primary exports with low income elasticity and high price volatility. This means that as global agriculture markets become further integrated, the ACP group's agriculture risks becoming uncompetitive and marginalized.

Table 1.3 presents a range of agricultural indicators highlighting how the ACP countries, on average (but with exceptions), fall below other developing country regions in the proportion of area irrigated, value added per worker, fertilizer levels and productivity. Agriculture's relatively weak performance is symptomatic of inadequate investments in human capital, agricultural infrastructure, research and extension networks. However, read differently, the table also underlines the potential which ACP countries have for developing their agriculture even in the context of existing technologies.

1.2 Issues for agricultural development in the African ACP countries

More than 90 percent of the ACP country population lives in Sub-Saharan Africa (SSA) where there is significant agricultural development potential. SSA has about 198 million hectares of arable land; some still unexplored or only partially used – which translates into 0.24 hectares of arable land per capita. This compares favourably with the corresponding figures for all regions except Latin America and the Caribbean. The region also experiences recurrent droughts and floods, yet withdraws only 1.6 percent of its available water, compared with 14 percent in Asia. About 4 percent of its arable land and land under permanent crops is irrigated, compared with 11 percent in Latin America and Caribbean, 33 percent in Asia and 11 percent for the developing countries as a whole.

Soils in sub-Saharan Africa tend to be highly weathered by relatively high rainfall and temperatures and are poor in nutrients. In western and central Africa, about 50 percent of farmlands suffer soil erosion and up to 80 percent of rangelands are degraded. With barely 4 percent irrigated land, there is an immediate need for a comprehensive water management programme to increase water use and improve the efficiency of water harvesting and conservation systems. Drawing on experiences of other regional programmes, it would generate substantial and sustainable increases in farm production as well as reduce vulnerability to future crises.

Countries that were formerly self-sufficient in, or exporters of, food have become net food importers. At the same time, they have become heavily dependent on one or two commodities for a large share of their export earnings (Box 1.1). A lack of modern inputs, high yielding crop varieties, vaccines and animal feed, and technology and facilities for post-harvest storage, processing and packaging has meant poor agricultural growth, the consequences of which are especially dire in the face of the food needs of the region's growing population.

For agricultural growth to occur there must be a system for taking goods from field to market, starting first and foremost with a well functioning rural road system. Africa's rural infrastructure is grossly insufficient its road system today compares unfavourably with that of India in 1950 in terms of kilometres of roads for every thousand square kilometres, adjusted for population density. Its rail freight is under 2 percent of the world total, its marine freight capacity is 11 percent and its air freight is less than 1 percent. Due to inadequate infrastructure, transport and insurance represent more than 25 percent of the value of exports in a third of the African ACP countries.

Africa also has difficulties accessing international markets for its agricultural products, because it lacks adequate mechanisms for ensuring sanitary, phytosanitary and quality standards.[1] Access could be increased if domestic markets were better regulated and standards of product safety and quality observed.

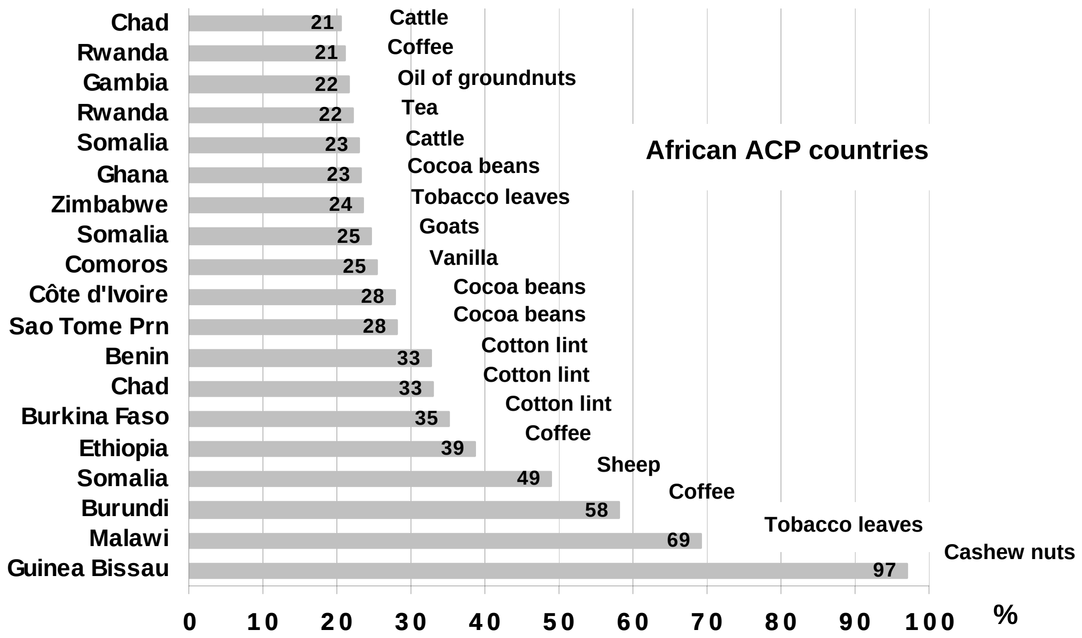
Despite their complexity, challenges facing agriculture in Africa are not insurmountable. The problems can be overcome if political will can be found and if resource mobilization for the sector is stepped up (see next section). There are already encouraging signs that the importance of agriculture in the region is being increasingly recognized.

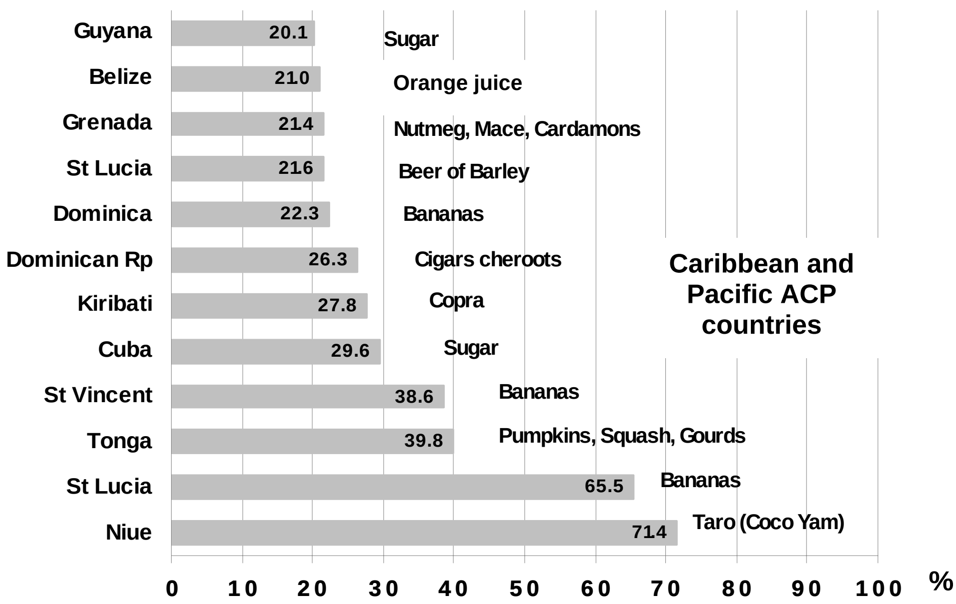
[1] This is not the sole reason for Africa's failure to benefit from international trade. This failure is also due to the effects of subsidies of US$1 billion a day; tariffs of 60 percent on raw materials and more that 100 percent on processed agricultural products; and technical barriers to trade imposed by developed countries.

BOX 1.1: DEPENDENCE ON SINGLE COMMODITY EXPORTS IN ACP COUNTRIES

High dependency on exports of one or a few agricultural commodities is a problem for many ACP countries. It makes their overall income, investment, employment and growth highly vulnerable to market fluctuations for these commodities. For these countries, diversification of the export base is a priority. The graphic below shows the ACP countries which rely on one agricultural commodity for more than 20 percent of their export earnings.

ACP countries relying on one agricultural commodity for more than 20 percent of their export earnings





Source: FAO

1.3 Issues for agricultural development in Caribbean and Pacific small island developing states (SIDS)

Small island developing states (SIDS) have very diverse economic profiles and levels of development. Table 1.4 categorizes SIDS into three groups by per capita income. A key issue facing SIDS is their degree of reliance on food imports compared to their local production. Cereal consumption covered by imports is around 80 percent on average for SIDS, with a higher dependency on imports in the richer group.

Exports from SIDS have benefited from EU/ACP agricultural trade protocols, which compensated them at higher levels than the world market. These protocols helped to maintain sugar and banana exports in many SIDS and their benefits are being eroded. However, under the EPAs the future of these protocols is being renegotiated. The economic, social and environmental impacts of this change will depend on the ability of producers to diversify production and gain competitiveness.

The rural economy of SIDS is dominated by a small number of commodities, such as sugar, copra and banana (Box 1.1). For example, around half of the countries of Group 1 are relying heavily on copra and banana exports. Two-thirds of the countries in Group 2 rely on sugar. In Group 3, only very few countries rely on a particular agricultural commodity for exports. SIDS has emphasized, as a priority, the promotion of local food supply and the expansion and diversification of their agriculture. Fruits and vegetables are a favoured area for diversification, in part to meet a growing demand for fresh products arising from tourism. About half of SIDS give priority to the development of traditional food crops to improve nutrition.

Some of the special challenges facing agriculture in the ACP SIDS are:

- Adapting to the new trade environment: SIDS' economies rely heavily upon agriculture, forestry and/or fisheries exports but they face challenges in the emerging global trade environment. Although the international trading system has not provided SIDS with any particular consideration as a group, they receive some form of preferential access to developed-country markets as beneficiaries of other agreements.
- *Food supply, nutrition and diversification:* Nutrition-related health problems and food-import dependency are growing concerns in many SIDS. When tourism is the dominant economic activity, 50 to 95 percent of foods and beverages are imported. In order to face the challenges of agricultural competitiveness and self-reliance, SIDS are seeking opportunities to diversify their agricultural systems.
- *Preserving marine resources:* While SIDS' land resources are limited, they govern large tracts of ocean. Capture fisheries have had upward trends but resource depletion and stagnant prices for some important species (such as tuna) threaten returns for both food and national income. The concepts of long-term sustainability and responsible fisheries should underpin development and management in SIDS.
- *Land, forests and mitigation of natural hazards:* Demands on forest and other coastal resources are endangering the ecosystems of SIDS, which are of major economic significance for settlement, subsistence and commercial agriculture and tourism. In addition, climate variability and change (including sea level rise) and vulnerability to natural disasters are of particular concern to SIDS.

TABLE 1.4: INDICATORS FOR SMALL ISLAND DEVELOPING STATES (SIDS)

	Agriculture in GDP %	Active population in agriculture %	Cereal dependency ratio %	Fruit-vegetable self-sufficiency ratio %
Group 1: below US$2 000/cap	29.2	62.5	63	107
Group 2: from US$2 000 to 9 000	8.5	20.8	89	94
Group 3: over US$9 000	3.2	6.4	95	55
Total	9.0	36.2	83	85

Source: FAO and World Bank

1.4 Status of the EPA Negotiations

Under four successive Lomé Conventions, ACP exports have benefited from non-reciprocal preferential access to the EU - and this is now under threat. In recent years, ACP preferences have been eroded as Most Favoured Nation (MFN) tariffs for other trading partners of the EU have been reduced. At the same time, food safety concerns in the EU have led to very strict food safety regulations which are proving very costly for ACP exporters. The WTO Doha Development Round, involving ACP countries as well, has reached a critical stage and although the WTO has granted the EU a waiver to maintain the non-reciprocal ACP preferences until December 2007, the scope of these preferences in the interim period up to the expiry of the waiver at the start of 2008 and beyond is of great concern to the ACP as they embark on these various negotiations. Furthermore, there are ongoing regional integration programmes in many parts of the ACP group, and free trade agreements are being negotiated by other Organisation for Economic Co-operation and Development (OECD) countries with groups within the ACP and their competitors elsewhere.

Submerged in the EPA and WTO negotiations, is the ongoing process of EU enlargement and reform of its Common Agricultural Policy (CAP) which involves moving away from a system of price support to that of direct aid to EU farmers. This reform is having two important effects on ACP countries which have traditionally enjoyed significant preferential access to the EU market; (i) it is reducing the value of preferential access to the EU market, by reducing the prices of EU agricultural products; (ii) it is making EU agricultural and value added food product exports more price competitive on domestic and overseas markets, thereby displacing ACP agricultural industry.

Furthermore, at the beginning of this decade, after several years of international debate about the magnitude and effects of subsidies in the fisheries sector, a consensus had emerged about the need to impose some discipline on their use. This consensus was recorded in the agreement reached in the Doha WTO Ministerial meeting. In the ongoing WTO discussions the special situation of developing countries is increasingly recognized. Nevertheless, ACP countries need to actively consider the role that subsidies have and might have in their own fishery sectors, in order to defend their interests in any future WTO agreement aiming to discipline the use of subsidies in the sector.

Given their already weak economies, the ACP countries are facing several major sets of closely interlinked forces that are likely to have significant impact on the development of their agriculture sectors and food security situation. If sound and proper positions are not in place during these negotiations, they are likely to be further weakened once the full effects of all the various forces are in place. It is therefore critical that the positions on all of these negotiations need to be coherent with each other and all need to be rooted in the overall economic and development strategy of the countries concerned.

After some years of initial preparation and talks on broad principles, the EPA negotiations are finally addressing concrete issues. Negotiations have been launched formally with the six ACP regional groupings but the pace and progress varies among them. Table 1.5 presents a broad timeline for the EPA Negotiations.

As the table shows, a process of substantive negotiations have been agreed to by the ACP and the EU to follow in four phases within the timeline based on priorities of the ACP negotiating region:

- *First Phase:* Establishing priorities (concerns and interest) of the EPA Negotiations for each ACP group and the EU;
- *Second Phase*: Convergence on strategic approaches to ACP regional integration – the objective during this phase of the negotiations is to establish a common understanding on the priorities for supporting regional integration and the targets to be attained by 1 January, 2008 and beyond;
- *Third Phase*: The objective of this phase is to consolidate the discussions and channel the points of common understanding into elements of a draft EPA.
- *Fourth Phase*: Finalization – negotiations during this final phase should concentrate on consolidating the results of the negotiations and complete the EPA negotiations by the end of 2007.

TABLE 1.5: TIMETABLE OF ACP-EU TRADE NEGOTIATIONS

Date	Negotiations	Trade Regime
2000 – to September 2002	Preparation of modalities for negotiations. EU granted waiver by WTO to maintain Lomé trade preferences until December 2007.	
September 2002 to December 2007	EU to negotiate “economic partnership agreements” (free trade agreements) with ACP countries, by regional groups, or country by country	
2004 - 2005	EU and ACP countries to study “all possible alternatives” for non-LDC countries which “decide (….) that they are not able” to sign free trade agreements. EU to revise its GSP	Maintenance with ACP countries, except South Africa, of non-reciprocal tariff preferences in force at present, i.e. the Lomé regime.
2006	EU and ACP countries to analyse agreements foreseen “to ensure that the calendar foreseen permits the adequate preparation of negotiations.	
December 2007	Conclusion of EPA Negotiations	
From 1st January 2008 until 2018-2020	Application (transitions period) of new Economic Partnership Agreements (EPAs).	End of the “all ACP” Lomé regime. ACP signatories of EPAs to progressively open their markets to EU products. LDCs which have chosen not to conclude EPAs to retain their non-reciprocal tariff preferences? Non-LDCs which have chosen not to conclude EPAs to benefit from new regime (still to be defined)

As of February 2006, negotiations are now in the third phase for three ACP regions – CEMAC, ECOWAS CARIFORUM. The other regions (ESA, SADC, Pacific) are somewhere between the first and second phase. It is worth noting the Pacific region has requested clarification from the EU on the legal status of development annexes to the EPA and the development support mechanisms, whether EBA market access will be granted to non-LDC EPA countries, alternatives to EPA and flexibility to address their specific needs.

In general, the negotiations so far have focused on the following issues:

- The progress and prospects of regional integration processes in all areas;
- Progress towards structural reforms in such key areas as public financial management, regulating and facilitating investment and the creation of new businesses, the working of judicial systems, education and vocational training, as well as training and education;
- Potential adjustment costs, such as the loss of tax revenue through lower customs duties; the scope for minimising those costs by continuing to protect sensitive products from liberalization, the phasing-in of changes, and the implementation of customs and tax reforms;
- Difficulties facing agricultural producers in rice, sugar and bananas, the related restructuring processes, and opportunities to secure future market access in a WTO-compatible EPA;
- Other vulnerable sectors, the sectors with the greatest competitive potential and the policies needed to back up the requisite changes;
- Trade policies’ compliance with WTO rules, making the most of the flexibility built in for regional trade agreements, and the progress of the Doha Development Agenda’s multilateral negotiations on issues such as agricultural support, market access and trade facilitation.

Chapter 2
EPAs and WTO compatibility: implications for ACP-EU trade relations

Introduction

For the last three decades, the trade relations between the EU as a bloc on the one hand, and the ACP countries as a bloc on the other, have been based on a series of "bilateral" treaties designed to provide non-reciprocal preferential terms of access for the products of the ACP to the markets of the EU – from Lomé I (1975-1980), to Lomé II (1980-1985), to Lomé III (1985-1990), to Lomé IV (1990-1995, later revised and extended to last until 2000, known as Lomé IV bis), and finally to Cotonou (2000 to 2020).[1] It is interesting to observe at the outset that prior to Lomé "a number of ACP countries had granted reverse preferences to the EEC".[2] The Lomé process was therefore not just about the creation of preferential market access for the products of ACP countries to the EC, but also about dismantling those pre-Lomé reverse preferences for EC products to access ACP markets, thereby establishing non-reciprocity as the core and distinctive principle of the *Lomé acquis* on trade matters.

This is set to change again in several important ways. The non-reciprocal EU preferences to the ACP countries have been generally challenged in the WTO framework and the EU is seeking to maintain its trade relations with the ACP and at the same time make these relations WTO compatible. Within the Cotonou Agreement it is intended that this will be achieved mainly through the negotiation of Economic Partnership Agreements (EPAs). The reintroduction of reverse preferences – also called "reciprocity" – is a fundamental feature of the (EPAs) that are to be negotiated by 2008.

The main purpose of this chapter is addressing the question related to the how ACP-EU trade relations can comply with WTO rules. Two WTO rules are most critical in this regard; Article XXIV of GATT 1994 on regional trade agreements and the Enabling Clause on special trading arrangements involving developing countries, and an examination of these for the establishment of EPAs form the core of this chapter. The first section of the chapter begins with an overview of the objectives and nature of EPAs as laid out in the Cotonou agreement. The second section addresses the legal issues related to establishing WTO compatible EPAs. The third section focuses on a series of conventions, treaties, protocols that are components of the governance of agriculture trade and as such are important to formation and operation of EPAs that regulate EU-ACP trade relations. The fourth section presents a summary of the main issues.

2.1 The Cotonou agenda, nature and object of EPAs

Cotonou is an agreement on trade and development relations between the EU and the ACP countries, and importantly an agenda for trade negotiations towards the creation of EPAs. One of the many innovations of the Cotonou Agreement is its vision of future trade relations between these two blocs. In a departure from decades of unilateral and non-reciprocal preferential terms of access for ACP products into the EU market, embodied in different treaties, protocols and conventions and accommodated by the multilateral trading system (more recently through a series of time-limited waivers), Cotonou set an ambitious agenda for the negotiation of EPAs. The hallmarks of which are to ensure that the trading relations between the EU and ACP are WTO compatible and thereby return to the traditional principle of reciprocity. The negotiation process was formally launched in September 2002 as required by the Cotonou Agreement and is set to be concluded by the end of 2007 with the creation of EPAs as of 1 January 2008.[3]

The overall objectives of economic and trade cooperation under the Cotonou Agreement include fostering the smooth and gradual integration of the ACP states into the world economy, eradication of

[1] The special economic arrangements between many of the ACP countries and the EC, which pre-date the 1974 Lomé I Agreement and the Association Agreements in the form of Yaoundé I (1963-69) and Yaoundé II (1969-75), are particularly notable.

[2] See WTO, *GATT Analytical Index: Guide to GATT Law and Practice* (updated 6th ed., Geneva, 1995, hereafter *GATT Analytical Index*) p. 826.

[3] See Article 37:1 of the Cotonou Agreement; Article 37 sets out detailed procedures for different phases of the negotiations together with their respective deadlines.

poverty and promotion of sustainable development. The establishment of EPAs has been identified as the route towards achieving those objectives.

The nature of EPAs

The Cotonou agreement sets out the basic principles and objectives of the EPAs and prescribes detailed modalities for their implementation. The EPAs are intended to be instruments for development, support ACP regional integration initiatives, improve ACP preferential market access into the EC, be compatible with WTO rules, and provide SDT to all ACP states, and in particular to the LDCs and vulnerable small, landlocked and island countries.[4] Although they are not defined anywhere in the Cotonou Agreement, EPAs are to be a new form of trading arrangement between the EU on the one hand, and individual ACP countries or sub-regional groupings on the other.

The EPAs will be different from all previous forms of arrangements between the EU and ACP countries in terms of, inter alia: the identity and configuration of the ACP-side of the partnership (individual ACP countries and/or sub-regions as opposed to the totality of ACP countries as a bloc); the substantive content and object of the agreements (more or less reciprocal trade liberalization compatible with WTO parameters, as opposed to unilateral preferences thus far legitimized under a waiver); and duration (permanent free trade arrangements phased-in over an agreed transition period as opposed to previous time-limited unilateral concessions). Some of these are briefly discussed further below.

Identity and configuration of parties to EPAs

All prior trading arrangements since Lomé I in 1975 were negotiated between the EC as a bloc and the ACP countries as a bloc, and the resulting EC import regime applied equally to all ACP countries, with an exception for LDCs, which was introduced later in the process. For purposes of the discussion here, we will exclude the LDCs,[5] as they are treated separately under Cotonou as well as the WTO, and ask the following question about the remaining group: Who are going to be the parties on the ACP side of the EPAs – the totality of ACP countries just like before? Individual ACP countries? Or ACP sub-regional RTAs (e.g. SADC and ECOWAS)? The question is crucial, yet among the least understood.

Article 37.5 of the Cotonou Agreement is the most relevant provision on this issue: "Negotiations of the economic partnership agreements will be undertaken with ACP countries which consider themselves in a position to do so, at the level they consider appropriate and in accordance with the procedures agreed by the ACP Group, taking into account regional integration process within the ACP." This implies that a single EPA would not be negotiated ACP-wide; rather, that the EPAs will be negotiated and concluded between the EU on the one hand, and each ACP country or groups of countries in a sub-region on the other. The Cotonou agreement does not set any limits on the level of aggregation of ACP countries, leaving the definition of geographical regions to the ACP states themselves. At another point, the Cotonou Agreement adds that, "to the maximum extent possible, regional integration programmes should correspond to programmes of existing regional organizations with a mandate for economic integration."[6]

The negotiation process is currently proceeding by sub-region. Right at the opening session of the EPA negotiations in September 2002, an agreement was reached to have a first phase in negotiations at an all-ACP-EC level addressing horizontal issues of interest to all parties and then move to a second phase which would be "at the level of ACP countries and regions, and would address specific commitments."[7] Furthermore, since the launch of the second phase in October 2003, negotiations in all six regions (Central Africa, West Africa, eastern and southern Africa, the Caribbean, the Southern African Development Community and the Pacific) have already commenced. From this one may conclude that a single EPA between all the ACP countries on the one hand, and the EU on the other, is no longer an option. Indeed, the EU Commission (draft) mandate to negotiate EPAs specifically

[4] See *ACP-EC EPA negotiations: Joint Report on the all-ACP–EC phase of EPA negotiations* (ACP/00/118/03 Rev.1, ACP-EC/NG/NP/43, hereafter *First Joint Report*) Brussels, 2 October 2003, para. 4(b).

[5] Yet, bear in mind that LDCs belong within all the sub-regional and regional groupings and have obligations therein that generally make them equal partners.

[6] Article 7 of Annex IV to the Cotonou Agreement.

[7] See *First Joint Report,* para. 1.

provides that the object of the negotiations is to establish EPAs "with ACP sub-groups defined in accordance with the provisions of Article 37(5) of the Cotonou Agreement".[8] Finally, speaking at the opening session of the SADC-EU negotiations towards EPAs in Windhoek, Namibia on 8 July 2004, the then EU Development Commissioner, Poul Nielson, confirmed that "negotiating at the regional level, rather than with all ACP, is an essential feature of this approach".[9]

This means that the whole process envisages any number of ACP countries as partners of the EU in as many future EPAs. Except in the one scenario where the EU could be negotiating EPAs with individual ACP countries, the negotiation of EPAs will therefore be done between two RTAs – the EU, which could be taken as a Customs Union (CU) for purposes of GATT Art. XXIV and ACP sub-regional RTAs or their intermediate versions. This is also what was envisaged by the Cotonou Agreement, which provides that "economic and trade cooperation shall build on regional integration initiatives of ACP States, bearing in mind that regional integration is a key instrument for the integration of ACP countries into the world economy."[10] The first Joint Report of the all-ACP-EC Phase of the EPA negotiations goes even further and provides that the "EPA's first emphasis should be to consolidate ACP markets, before fostering trade integration with the EC."[11] The EPA negotiations cannot thus be seen merely as an EU-ACP affair; they are also an intra-ACP matter. This gives rise to a host of complex legal and practical issues.

The most important issue relates to the status of these ACP sub-regional RTAs under international law: Are they mere facilitators of negotiations or autonomous institutions with power to conclude treaties on behalf of their respective members? The answer to this depends on a number of factors, including the nature of these ACP sub-regional RTAs, the terms of the treaties by which they are created, the mandate entrusted to them, and whether they will have independent legal personality of their own. Box 2.1 presents an overview of WTO Regional Trade Agreement rules that are elaborated more fully later in this chapter.

In WTO terms, for any ACP sub-regional RTAs to sign on behalf of their constituent members any future trade agreements with the EU, they themselves must be Customs Unions (CUs) in the sense of GATT Article XXIV with all its implications in terms of the internal and external trade regimes of such CUs. But being an Article XXIV CU alone will not be enough. As the Turkey Textiles Panel observed, "unless a customs union is provided with distinct rights and obligations (and therefore some WTO legal personality, such as the European Communities) each party to the customs union remains accountable for measures it adopts for application on its specific territory."[12]

This implies that in order for the EU to conclude EPAs with ACP sub-regional RTAs as such, those sub-regional RTAs will need to evolve into full-fledged CUs by the end of 2007 at the latest, in the sense of GATT Article XXIV, and that those CUs must be endowed with rights and obligations distinct from their constituent members and some form of WTO legal personality. Confirming this view, the draft negotiating guidelines prepared by the ESA region provides as follows: "Configurations of EPAs will be clear by the end of 2007 and if at this time an ESA country is party of a customs union it will sign an EPA as a customs union. Otherwise it will sign an EPA as a country. It cannot sign an EPA as part of a regional organization unless the regional organization is a customs union."[13] As the preceding argument suggests, this policy statement from the ESA negotiating guidelines is a result of need rather than choice. Indeed, it still needs to go further and state that that CU must also have legal personality independently of the constituent members.

[8] See Council of the European Union, *(Draft) Directives for the Negotiations of Economic Partnership Agreements with ACP Countries and Regions* (Annex I to Doc. 9930/02, 12 June 2002, hereafter *draft EU Commission negotiation mandate*), p.4.
[9] See full speech, Speech/04/355 at www.europa.eu.int.
[10] Art. 35:2 of the Cotonou Agreement on Principles.
[11] See *First Joint Report*, para. 4(b)(ii).
[12] *Turkey – Restrictions on Imports of Textile and Clothing Products* (WT/DS34/R, adopted on 19 November 1999), hereafter *Turkey Textiles Panel Report*, para. 9.40, footnote 272.
[13] See *Eastern and Southern African Negotiating Guidelines for Phase II Economic Partnership Agreement with the European Union* (Draft Revision 2.0, 1 Dec. 2003, hereafter *ESA draft EPA negotiating guidelines*), para 4.

BOX 2.1 RTAS, EPAS AND WTO COMPATIBILITY – ARTICLE XXIV AND THE ENABLING CLAUSE

In Article 36 of the Cotonou Agreement the parties to the agreement concurred to conclude new World Trade Organization (WTO) compatible trading arrangements, removing progressively barriers to trade between them. In Article 37, it is agreed that economic partnership arrangements (EPAs), including the new trading arrangements, shall enter into force by 1 January, 2008.

Two WTO rules are most relevant to ensuring the compatibility of the new trading arrangements. Firstly, that on regional trade agreements(RTAs), Article XXIV of GATT 1994 and secondly, that on special trading arrangements involving developing countries, the Enabling Clause. Given that the specific application of these rules is subject to interpretation there is legal uncertainty that clouds the conclusion of WTO compatible trading arrangements. Beyond compliance with the rules as they are currently, there is the possibility of revising them in the context of WTO negotiations to ensure compatibility, and further that the rules may also change after the EPAs are agreed, potentially raising new issues related to compatibility.

GATT Article XXIV contains the most important rules of the WTO system on Regional Trading Arrangements (RTAs). It recognizes voluntary agreements, such as customs unions (CUs) or free-trade areas (FTAs) that should "facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories". In both forms of RTAs the expectation is to eliminate restrictions on "substantially all the trade" between the constituent territories.

The main difference between a CU and an FTA is that in the case of the former the national tariffs and other trade regulations are generally replaced by a common external tariff and a common system of other external regulations of commerce. In the case of an FTA the distinct national trade regimes remain in tact. The rules of origin on products in the context of CU are less definitive than in FTAs. In an FTA, elimination of duties and other restrictive regulations of commerce is required is on substantially all the trade in products originating in the FTA. In a CU, elimination of duties and other restrictive regulations of commerce is required on "substantially all the trade in products ... or at least with respect to substantially all the trade in products originating in such territories". In the latter case determination of origin is relatively more optional.

If EPAs are concluded under Article XXIV the only option seems to be FTAs as it is unlikely that ACP countries would introduce roughly the same external trade regime as the EU, as would be required under a CU. However, as shown in this chapter meeting GATT rules remains elusive.

The Enabling Clause, officially known as the *Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries*,[14] is the other important source of law relating to RTAs, involving particularly developing countries. The Enabling Clause constitutes an exception from GATT Art. I in three senses since it authorizes: (a) developed country tariff preferences for goods of developing country origin on GSP terms (generalized, non-reciprocal and non-discriminatory); (b) special treatment for LDCs; and (c) South-South preferences as an exception from both Articles I and XXIV. Given that the Enabling Clause authorizes only South-South RTAs, there is no room for North-South RTAs, such as the future EPAs, to be justified under it. Developed countries have failed, on several occasions, to defend discriminatory preferences accorded to developing countries on the basis of paragraph 2(c) of the Enabling Clause.

Establishing compatibility of EPAs with WTO rules is a formidable task. Only for one of 270 RTAs notified to GATT have members agreed its compatibility with WTO rules.

One may then wonder whether or not the existing sub-regional RTAs could metamorphose into CUs with a legal personality independent of the constituent members within the period up to 2008. It is a possibility: Caribbean Community and Common Market (CARICOM) and the Economic and Monetary Community of Central Africa (CEMAC) already exist as CUs, while and the Economic Community of West Africa States (ECOWAS) is scheduled to become CU before 2008. However, whether many of these sub-regional RTAs will evolve into full-fledged CUs in terms of GATT Article XXIV by 2008 is far from certain. Nearly all ACP sub-regional RTAs, including COMESA, CEMAC, WAEMU, and EAC, were created taking advantage of the more lenient provisions of the Enabling Clause on South-South preferences rather than under GATT Article XXIV. Accordingly, many of these RTAs might find it difficult to satisfy even the relatively less onerous (compared to CUs) demands set by Article XXIV for FTAs.[15]

This means that the likelihood of seeing EPAs between the EU and sub-regional ACP RTAs is far from certain, thus perhaps leaving only one option for many of these sub-regions – the conclusion of EPAs between the EU and individual ACP countries. Given that no ACP country seems to have taken

[14] GATT doc. L/4903, 28 November 1979.

[15] See WTO Committee on Regional Trade Agreements. *Basic Information on Regional Trade Agreements: Agreements Notified to the GATT/WTO and in Force as of 31 January 2002 – Note by the Secretariat* (WT/REG/W/44, 7 February 2002).

a decision as yet to negotiate as an individual country, most ACP countries (except Somalia) are already taking part in EPA negotiations through their sub-regional RTAs, the preceding suggestion might sound rather unrealistic. It is also worth noting, however, that the fact that the ACP countries are negotiating as members of a sub-regional RTA does not necessarily imply a decision to conclude EPAs at such a level.

In sum, the Cotonou Agreement is vague at best on this issue. While it specifically mentions the possibility of sub-regional RTAs and individual countries becoming parties to the EPAs, it does not say anything about the ACP in its totality being a party to the EPAs. However, it declares a commitment to build EPAs on existing regional integration initiatives of the ACP countries. The official line, as well as the consensus approach in the literature seems to assume that EPAs will be concluded between the EU on the one hand, and ACP sub-regional RTAs on the other, and that EPAs between the EU and individual countries will be more of the exception. It appears, however, that this may not occur by 2008 and probably the opposite will be the case – i.e. we may generally see EPAs between the EU and individual ACP countries, while EPAs with sub-regional RTAs could be the exception. Moreover, regardless of whether EPAs are signed by individual ACP countries or sub-regional RTAs, it is clear that the EPAs will mark a departure from the tradition of treating all ACP countries as a bloc.

Object of the EPAs

One of the most fundamental objectives of the ongoing negotiations between the EU and ACP countries/subregions is to create EPAs that are compatible with WTO rules on RTAs, which generally requires reciprocal trade liberalization. This declared commitment to WTO compatibility appears to be the result of a combination of factors: (i) all members of the EU as well as nearly three-quarters of the ACP countries are already members of the WTO and bound by its system of rules; (ii) the experience of the past in terms of waivers for arrangements incompatible with those rules has been neither easy nor pleasant; and (iii) it appears that the trend in North-South trade relations is turning away from unilateral concessions legitimized through waivers into reciprocal arrangements concluded in accordance with WTO rules. If successful, this commitment to WTO compatibility will mean that any future trading arrangements between the EU and the ACP will exist without any need for a waiver from WTO obligations.

2.2 EPAs and WTO law on RTAs – FTA or CUs

Achieving the objective of satisfying the legal requirements of the WTO on RTAs through EPAs will be a major challenge for several reasons. These will be discussed after highlighting the WTO legal standards against which future EPAs will be judged. The relevant WTO legal standards are contained in GATT Articles I (on MFN treatment) and XXIV (on RTAs), the 1979 Enabling Clause, and to a more limited extent, Article V of the GATS. There are also some useful Panel and AB reports that could elucidate these often obscure provisions. The legal standards contained in these provisions are among the most complex and contentious, so much so that it becomes questionable whether a commitment to compliance means anything at all in practical terms.

From the perspective of WTO law, the issue of regional trading arrangements is primarily one of principle. Having laid its foundations on the principle of non-discrimination, the trading system treats all sorts of favouritism between countries with suspicion. The first paragraph of GATT’s very first provision declares that “any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.” This “give-the-best-to-everyone principle”, i.e. the most favoured nation (MFN) treatment clause, is the cornerstone of the trading system.

At the same time, however, it is now known that almost every WTO member today belongs to one or more RTAs, which by definition means that almost every country gives (and receives) preferential terms of access over what it gives and receives at the MFN level. The number of such preferential arrangements has grown rapidly over the past few years, but it is not a new phenomenon. It is interesting to note here that Kenneth Dam opened his 1963 article on RTAs with the following observation: “The last dozen years have seen a proliferation of customs unions and free trade areas of unforeseen proportions"(Dam 1963, p. 615). This is an observation that would be even truer today.16 The question will then be the following: If the principle of non-discrimination is such a core principle of the trading system, how can we explain the fact that we live in a world of ever-proliferating RTAs that are inherently discriminatory?

In legal terms, the answer is to be found principally in GATT Article XXIV, supplemented by the so-called Enabling Clause of 1979 for developing countries, and GATS Article V for RTAs in the area of services, this time called Economic Integration Agreements (EIAs). The legal landscape created by the interaction of all these principles and exceptions as applied over the years will be discussed in some detail here.

GATT Article XXIV

The most important rules of the WTO system on RTAs are contained in GATT Article XXIV. For a system that professes to be founded on the principle of non-discrimination, it is interesting to note that GATT Article XXIV:4, the provision which "sets forth the overriding and pervasive purpose for Article XXIV",[17] starts by recognizing "the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements." It then goes further and stipulates that "the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories." This purposive paragraph is followed by detailed operative provisions that set forth the substantive and procedural conditions that must be satisfied before a discriminatory RTA could be justified under the exceptions of Article XXIV. The meaning of Article XXIV has proved to be so contentious and its practical administration so difficult, however, that only in one of the over 270 RTAs notified so far to GATT/WTO were members able to reach a clear-cut decision on their compatibility with the rules. (The single exception relates to the 1994 CU between the Czech and Slovak Republics.) The following discussion only summarizes the legal issues that will have an impact on the negotiation and outcome of the EPAs.

Article XXIV distinguishes essentially between two forms of RTAs – FTAs and CUs, or interim agreements leading to the formation of either of these two. The main difference between these two forms of RTAs relates essentially to the depth of integration attained or contemplated among their respective members. Interim agreements in both cases are required to include "a plan and schedule" for the formation of the intended RTAs "within a reasonable length of time". The "reasonable length of time" for interim agreements leading to the formation of FTAs and CUs has been defined to mean a period not exceeding ten years unless justified by exceptional circumstances.[18]

As discussed later, the EPAs will first come in the form of interim agreements leading to the formation of FTAs, rather than CUs, and the length of the transition period permissible under Article XXIV will be important.

However, even if EPAs only aspire to be FTAs and not CUs, the law relating to CUs will play a role in the process because, as argued earlier, ACP subregions can conclude EPAs(as subregions) with the EU only if they constitute themselves as CUs in the first place. The substantive requirements of both FTAs as well as CUs are found in paragraphs 5 and 8 of Article XXIV.

Article XXIV, paragraph 8 is the definitional provision for both CUs and FTAs while paragraph 5 provides for the minimum substantive conditions that should be met by CUs and FTAs relating to internal trade among their constituent members and external trade with third parties.

[16] As of 5 December 2003, 273 RTAs have been notified to the GATT/WTO. Of these, 227 agreements were notified under GATT Article XXIV, of which 143 are still in force today; 19 agreements were notified under the Enabling Clause and 27 under GATS Article V. See WTO Committee on Regional Trade Agreements, *Report (2003) of the Committee on Regional Trade Agreements to the General Council* (WT/REG/13, 5 December 2003), para. 4. Of these, 107 were notified between 1948 and the end of 1994, while the remaining 166 were notified between 1995 and the end of 2003.
[17] See *Turkey Textiles, AB report*, para. 57.
[18] See Uruguay Round Understanding on GATT Article XXIV, para 3.

Customs Unions (CUs)

Definition

According to Article XXIV: 8(a), a customs union (CU) is defined as "the substitution of a single customs territory for two or more customs territories."[19] A CU is therefore a union of two or more customs territories with important implications for the flow of trade within that union (internal trade) as well as between the union and other countries (external trade) for each of which detailed requirements are listed. The requirements for CUs are found in paragraph 8(a)(i) on internal trade, and paragraphs 8(a)(ii) and 5(a) on external trade.

Requirements on internal trade

Regarding *internal* trade within CUs, sub-paragraph 8(a) (i) provides that "duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories." Four things are worth noting here: (1) the rule relates to "duties" as well as "other restrictive regulations of commerce" applying to trade between the members; (2) the requirement is to eliminate and not just reduce these duties and other restrictive regulations of commerce; (3) the requirement to eliminate applies to substantially but not all of the trade; and (4) this requirement to eliminate internal trade restrictions is subject to exceptions allowed under specified provisions. Although all of these elements are important, the concept of "substantially all the trade" is the most controversial and the most relevant, particularly to the identity of each of the intending parties to the EPAs. The same requirement also exists for FTAs, and the discussion below applies to both forms of RTAs.

In broad terms, the requirement to liberalize "substantially all the trade" between the constituent members of a CU is something that naturally flows from the object and purpose of RTAs as stated under paragraph 4 of Article XXIV: the desire to facilitate trade through voluntary closer economic integration between countries without adversely affecting the trade interests of others. However, the practical question of how much trade is "substantially all the trade" has proven to be a difficult one for trade diplomats and lawyers over the years. At least two major approaches have been suggested so far – quantitative (a certain percentage of actual or potential trade) and qualitative (for example, going beyond percentages to look at whether any major sector is excluded), or a combination of both. There is no consistent practice on the matter. The EC has played a major role in the development of the law in this area, as in many others. When the EEC Treaty was brought before a GATT committee for the consistency with Article XXIV of its provisions on the association of overseas territories, the Community argued that "a free trade area should be considered as having been achieved for substantially all the trade when the volume of liberalized trade reached 80 percent of total trade."[20]

However, many other members rejected this approach of fixing a percentage figure as inappropriate, preferring instead a case-by-case approach that considers every case on its own merits. Although the EC grew more and more sympathetic to this argument over time,[21] it still maintains its quantitative approach to the definition. Following its use of a 90 percent threshold in its TDCA with South Africa – made up of commitments to liberalize around 94 percent of EU imports from South Africa and around 86 percent of South African imports from the EU over a 12-year transition period – the EU is currently presenting this 90 percent threshold as "the WTO criterion" of the "substantially all trade" requirement.

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[19] Paragraph 2 of Article XXIV defines a customs territory to mean "any territory with respect to which separate tariffs or other regulations of commerce are maintained for a substantial part of the trade of such territory with other territories."

[20] See *GATT Analytical Index*, p. 824.

[21] For example, during GATT Working Party meetings that considered the accession of Portugal to the EEC, the Community was quoted as saying that:

> *no exact definition of the expression (substantially all the trade) existed and that the precise figures would vary from case to case according to several factors. At any rate, percentages were established as a general indicator of the trade covered by the Agreement and were not to be regarded as a conclusive factor* (idem).

Requirements on external trade

Regarding the *external* trade of members of CUs with non-members, sub-paragraph 8(a)(ii) provides that "substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union." A logical follow-up to the definition of a CU as "the substitution of a single customs territory for two or more customs territories" would normally be a requirement to adopt a single trade regime vis-à-vis all third countries. However, by requiring only "substantially the same" and not "the same" duties and other regulations of commerce to be applied by members of a CU to the trade of non-members, sub-paragraph 8(a)(ii) has made it clear that the formation of a CU does not necessarily mean the total "disappearance" of the constituent members as independent players in international trade regulation. Indeed, precisely because of this flexibility afforded by Article XXIV on the external trade regime of a CU, the *Turkey Textiles* panel went as far as concluding that "as a general rule, a situation where constituent members have "comparable" trade regulations having similar effects with respect to the trade with third countries, would generally meet the qualitative dimension of the requirements of sub-paragraph 8(a)(ii) (Turkey Textiles, Panel Report, para 9.151)." This was later found by the AB to have been too low a standard to satisfy the requirements of sub-paragraph 8(a)(ii), which it stated "requires the constituent members of a CU to adopt "substantially the same" trade regulations. It is generally agreed that "comparable trade regulations having similar effects" do not meet this standard.

The Turkey Textiles AB report has particular implications on the interpretation of the requirements on the external trade regime of CUs, together with the explicit authorization of quantitative restrictions on internal trade under sub-paragraph 8(a)(i). These are that (1) ACP countries can establish CUs among themselves at the sub-regional level while each of them still maintains otherwise legitimate quantitative or other trade restrictions on some of their internal as well as external trade; and (2) some ACP countries members of such CUs will still have the right to maintain such restrictions on selected third countries while the other members of the CU may not necessarily have such restrictions against any third countries.

The pre-1993 banana import regime applying in EEC member countries is instructive in this regard. It ranged from the tariff-free import system in Germany to the tariff-only import restrictions in the Benelux, to the various quantitative restrictions in France and the United Kingdom, to the complete ban on importation in Spain. A more recent and relevant example would be the new Italian labelling law (July 2003) "requiring that milk production facilities indicate on the label the location of the farm where the milk originated" (O'Connor 2003, p. 9). No such requirements exist under EU law or in other EU countries, and yet no one seriously claims that the EC does not satisfy the requirements of a CU merely because its members do not have a common external trade regime for bananas or lack common rules on the traceability of dairy products.[22]

Nevertheless, in all cases any such restrictions need to be permissible under WTO law. The notorious cases on *bananas*, although involving alleged FTAs rather than CUs, are a good example here. In *Bananas I* the EEC argued – unsuccessfully – that the many restrictive measures on the importation of bananas, including the total ban maintained by Spain, were permitted under GATT Article XXIV.

The EEC specifically argued that "Article XXIV:5 contained an exception not only to Article I but also to Article Xl (and, accordingly, to Article XIII)", and applied to its relationships with the ACP countries, which it said were "free trade area(s) between the EEC and each of the ACP countries" in the sense of Article XXIV:5 (Bananas I, paras. 222 and 246). According to this argument, therefore, Article XXIV would justify not only discrimination in violation of the MFN principle of Article I, but also a quantitative restriction in violation of Article XI. The Panel rejected this EC argument as follows:

> *The Panel noted that Article XXIV:5 to 8 permitted the contracting parties to deviate from their obligations under other provisions of the General Agreement for the purpose*

[22] See *EEC - Member States' Import Regimes for Bananas: Report of the Panel* (DS32/R, 3 June 1993, not adopted, hereafter *Bananas I*) and *EEC - Import Regime for Bananas: Report of the Panel*, (DS38/R, 11 February 1994, not adopted, hereafter *Bananas II*), cases challenging the EEC's successive banana import regimes of 1992 and 1993 respectively, also discussed *infra*.

of forming a customs union or free-trade area, or adopting an interim agreement leading to the formation of a customs union or free-trade area, but not for any other purpose. Article XXIV:5 to 8 therefore did not provide contracting parties with a justification for restrictive import measures as such; it merely provided them - within the limits set out in this provision - with a justification for not applying to imports originating in such a union or area the restrictive import measures that they were permitted to impose under other provisions of the General Agreement. The Panel therefore considered that the import restrictions on bananas could not be justified by Article XXIV (idem., para.358).

In summary, while the discussion in this section focused mainly on CUs, it is also possible to draw conclusions of a broader reach: the provisions of GATT Article XXIV should be interpreted to mean that member countries are allowed to violate other provisions to the extent necessary for them to be parties to RTAs that satisfy the requirements set by Article XXIV itself. GATT Article I is so far the only provision whose violation has been found to be necessary for the creation of RTAs. However, although it is difficult to imagine what other GATT provisions would pass this necessity test for the creation of RTAs, the AB has opted to leave the door open on this issue. This also means, for example, that the justifiability under Article XXIV of otherwise WTO-incompatible non-tariff barriers that may be introduced against third country imports by ACP countries on the occasion of the formation of EPAs will remain an open question.

Finally, while paragraph 8(a) provides the definitional elements of a CU, paragraph 5(a) goes a step further and sets important additional conditions on the external trade regime of the union:

The duties and other regulations of commerce imposed at the institution of any such union or interim agreement in respect of trade with contracting parties not parties to such union or agreement shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union or the adoption of such interim agreement, as the case may be.

Four points are worth noting here: (1) the creation of a CU may not be used as an opportunity to roll back prior liberalization measures of the constituent members vis-à-vis non-members; (2) the comparison is between the new single common external trade regime and the many individual external trade regimes of the constituent members vis-à-vis third countries; (3) this comparison is not item-by-item, but general; and (4) there is a distinction between duties and other regulations of commerce in that the new duties are not to be higher (quantitative), while other regulations are not to be more restrictive (qualitative). The implications of these requirements for EPAs will be discussed later on.

Free Trade Areas (FTAs)

Definition and requirements on internal trade

Article XXIV:8, sub-paragraph (b) defines a free trade area (FTA) as:

“...a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.”

An FTA is therefore an arrangement between countries that seek to create conditions for the free(r) flow of trade among themselves while preserving the independent customs territories of the constituent parties and with no need for harmonizing their respective foreign trade regimes vis-à-vis non-FTA countries. Most of the observations made earlier on the definitional elements of a CU could also apply to this definition of FTAs, and the comparison of FTAs and CUs in the next sub-section will develop this further. It is worth pointing out at this stage, nonetheless, that while CUs are defined in terms of their internal and external trade dimensions, the parallel provision defining FTAs does not say anything regarding the type of measures to be applied by members of FTAs vis-à-vis non-members.

There is also a small difference between these two definitions in respect of their product coverage for internal purposes. While sub-Article 8:(a)(i) on CUs requires elimination of duties and other restrictive regulations of commerce “with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories", sub-Article 8(b) on FTAs requires elimination of duties and other restrictive regulations of commerce "on substantially all the trade between the constituent territories in products originating in such territories." A minimum requirement for CUs is the elimination of duties and other restrictive regulations of commerce on products originating within members of RTAs – the preference being to extend such treatment to all products traded between those countries regardless of the origin of the goods – while this is all that is required for FTAs. The legal effect in both cases remains the same, but the wider reach of CUs has some symbolic value albeit hortatory. It also means that while determination of origin could be merely optional in the case of CUs, it is almost always mandatory for FTAs (unless of course an FTA also opts for elimination of barriers on all goods coming from or through other members regardless of their true origin – an unlikely scenario in practice).

Requirements on external trade

The absence of reference to the external trade dimension of FTAs in the definition does not mean there are no requirements for FTAs in this respect, however, only that they are found in paragraph 5 rather than the definition provision of paragraph 8. Paragraph 8(b) provides the definitional elements of an FTA in terms only of *internal* trade, but paragraph 5(b) goes a step further and sets important conditions relating to the *external* trade regime of the FTA:

> *With respect to a free-trade area, or an interim agreement leading to the formation of a free-trade area, the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area, or interim agreement as the case may be.*

The language of this paragraph is similar to that of paragraph 8(a) on the external trade regime of CUs; but there are also important differences. First, the objective in both cases is fairly clear: the principal purpose of sub-paragraphs 5(a) and (b) is to make sure that the pre-RTA level of openness to third country imports in each of the members of the new RTA would continue not to be adversely affected by the formation of the RTA. The impact of RTAs on third parties varies depending, at least in part, on the type of RTA created, i.e. whether it is a CU or an FTA. In the case of a CU, the national tariffs and other trade regulations are generally replaced by a common external tariff and a common system of "other external regulations of commerce", while in the case of an FTA, the distinct national trade regimes remain intact. Consequently, the assessment of whether the formation of an RTA has adversely affected the trade interests of non-members is more complicated in a CU than in an FTA. As FTAs are not required to harmonize their external trade regimes – and indeed no new customs territory is created by an FTA – the comparison here is between the external trade regime of each member of the FTA applying to third countries post-FTA and that same country's external trade regime pre-FTA. In other words, every third country can assess whether it has been adversely affected by merely comparing the duties and other regulations of commerce facing its goods in every FTA member country post-FTA vis-à-vis that which prevailed in each of those same countries pre-FTA. The comparison simply is between one country's external trade regimes at two different points in time. In the case of a CU, however, the comparison is not just between trade regimes at two different times, but also between two different entities – the pre-CU individual national trade regimes against the aggregate post-CU wide trade regimes.

Accordingly, while the requirement in the case of CUs is for the new trade regime not to be "on the whole" higher or more restrictive than "the general incidence" of such duties and regulations of commerce pre-CU, the requirement in the case of FTAs is for the new regimes not to be "higher or more restrictive" than the "corresponding" duties and other regulations of commerce pre-FTA. The greater precision in language in respect of FTAs compared to CUs is a result of the fact that in the latter case a completely new external trade regime effectively replaces the multiplicity of prior national external trade regimes, making direct comparison impossible.

There are also important differences under Article XXIV:5 with respect to tariffs and other trade regulations for CUs on the one hand, and for FTAs on the other.[23] In the case of a CU, the comparison is between "the duties and other regulations of commerce *imposed*" at its institution and "the general incidence of the duties and regulations of commerce *applicable* in the constituent territories prior to the formation of such union". In the case of an FTA, this comparison is between "the duties and other regulations of commerce *maintained* in each of the constituent territories and applicable" at its formation and "the corresponding duties and other regulations of commerce *existing* in the same constituent territories prior to the formation" (italics added). The significance of these differences in wording had been long debated. Due to the Uruguay Round Understanding on Article XXIV, it is now known that the duties and charges to be taken into consideration in the evaluation process for CUs "shall be the *applied rates of duty*."[24] This is preceded by the following: "The evaluation under paragraph 5(a) of Article XXIV of the general incidence of the duties and other regulations of commerce applicable before and after the formation of a customs union shall in respect of duties and charges be based upon an overall assessment of weighted average tariff rates and of customs duties collected." This therefore shows that the applied duty is used on both sides of the comparison.

Importantly for our purposes here, no such interpretation was adopted with respect to the parallel provision of Article XXIV: 5(b) on FTAs. The implication of this could be debated and one might still argue whether the comparison under Article XXIV:5(b) should be with the applied duty or the bound duty. However, the fact that these two provisions were couched in different wording from the outset and an explicit understanding has interpreted sub-Article 5(a) on CUs to mean applied duties while leaving it untouched in respect of sub-Article 5(b) on FTAs, should provide sufficient grounds to conclude that the duties for purposes of FTAs should be bound duties in cases where these are different from the applied rates.

One may wonder how or why this could be important for the EPA negotiations. It has been suggested earlier (and will be developed further *infra*) that EPAs between the EU and sub-regional ACP RTAs or individual ACP countries can only be FTAs and not CUs.

In speaking about EPAs therefore, one refers to the formation of FTAs, and indeed interim agreements leading to the formation of FTAs in the long run. We also know that most ACP countries maintain very high bound duties particularly on agricultural products while their applied duties are often much lower.[25] If the comparison of the external impact of the EPAs were to be assessed on the basis of the pre-EPA applied duties, as would be the case for a CU, the EPAs would necessarily have to result in very low MFN duties for these countries. If, on the other hand, the threshold is going to be the pre-EPA bound rates, then the ACP countries could still maintain high MFN duties on third countries regardless of how far they go in terms of the internal trade within the EPAs. Indeed, there have been cases where the formation of FTAs has resulted in applied tariff increases on goods coming from third countries. That EPAs are going to be FTAs and not CUs will thus mean that the degree of restrictiveness of the post-FTA external trade regime of the ACP countries will be compared against the pre-FTA external trade regime of those countries as contained in their schedules of bindings rather than their applied duties.

Nonetheless, this will be the case only if EPAs are concluded between the EU on the one hand and each ACP country on the other. As seen above, insofar as ACP countries conclude EPAs as sub-regional RTAs rather than as individual countries, they will have to constitute themselves as CUs in the first place. The question regarding the degree of restrictiveness of the external trade regime of these new CUs vis-à-vis goods coming from third countries will thus be assessed on the basis of the

[23] For more on this, see WTO Committee on Regional Trade Agreements, *Annotated Checklist of Systemic Issues: Note by the Secretariat,* (WTO/REG/W/16, 26 May 1997), p. 3.
[24] See para. 2 of the Understanding (italics added).
[25] A few examples showing the scale of bound duties: Schedule CXIX of Mozambique for agricultural market access which binds its customs duties at 100 percent, and under "other duties and charges" provides the following: maritime transportation tax at 100 percent, port tax at 100 percent, and other (sic) at 100 percent; Schedule XLIII of Nigeria provides for a ceiling binding for all agricultural products at 150 percent and "other charges" at 80 percent; Schedule LXVI of Jamaica binds duties for nearly all agricultural products at 80 percent and other charges at 80 percent; and Schedule CXXIV of Tanzania puts a ceiling binding of 150 percent for all agricultural products. However, we also know that the applied tariffs in these and other ACP countries are significantly lower than these bound rates. Information on national bindings for all WTO member countries is available at www.wto.org/english/tratop_e/schedules_e/goods_schedules_e.htm

pre-CU applied duties of the constituent members as required under GATT Article XXIV: 5(a). This will mean that (i) ACP countries signing an EPA as members of a sub-regional CU will have to set up a system of common external tariffs, which is no more restrictive than their applied tariffs that prevailed prior to the formation of the relevant CU; and (ii) when they sign the EPA – which is an FTA – with the EU, their external trade regime should not be more restrictive than their pre-EPA bound tariff levels as required under GATT Article XXIV: 5(b). The effect is clear – the pre-CU applied tariffs of the ACP countries will become the bound tariffs of the CUs both before and after the conclusion of the EPAs. ACP countries signing EPAs as sub-regional CUs will thus automatically lose the flexibility to move between high bound tariffs and low applied rates, while this same option will be available for ACP countries signing EPAs as individual countries. This has a potential to be another disincentive against ACP countries forming sub-regional CUs and signing EPAs, for example, through such CUs.

EPAs as FTAs not CUs

As noted earlier, the Cotonou Agreement does not delve into the nature of EPAs. Apart from the commitment to create EPAs that are fully compatible with the WTO, there is no mention as to whether they achieve that compatibility as FTAs or CUs or in any other form. Despite this, as suggested earlier, EPAs can only take the form of FTAs – and indeed interim agreements leading to the formation of FTAs – and not CUs or any third option.

The reasons could be summarized as follows:

- First, we have seen that the basic difference between FTAs and CUs is one of depth of integration – CUs being so-called “advanced FTAs”. Given the huge economic and developmental gulf between the EU and the ACP countries, and the condition of non-reciprocal market access that has prevailed between these two blocs so far, any EPAs between the EU and any ACP region/country can only start with an FTA. Considering GATT Article XXIV and the tradition of the EU in the creation of CUs with other countries, the formation of EPAs as CUs will automatically mean that the ACP countries will have to introduce roughly the same external trade regime as the EU – virtually adopting the EU external trade regime as did Turkey, for example when it concluded its CU with the EC in 1995. One can naturally expect at the most a higher degree of flexibility allowed to the ACP countries in such cases. Accordingly, a CU does not seem to be an option in this case.
- Secondly, and more authoritatively, the EU Commission negotiating mandate specifically provides that “EPAs shall be directed at establishing free trade areas between the parties.…”[26] This confirms that the vision is to create interim agreements leading to FTAs (note the words "*directed at*") and not CUs or any third option.

2.3 The Enabling Clause, RTAs and EPAs

Officially known as the *Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries*,[27] the Enabling Clause is the other important source of law relating to RTAs involving particularly developing countries. In general, the Enabling Clause constitutes an exception from GATT Art. I in three senses since it authorizes: (a) developed country tariff preferences for goods of developing country origin on GSP terms (generalized, non-reciprocal and non-discriminatory); (b) special treatment for LDCs; and (c) South-South preferences as an exception from both Articles I and XXIV. The relationship between the Enabling Clause and GATT Articles I and XXIV is of interest here.

RTAs and the Enabling Clause

Whether under Article XXIV or the Enabling Clause, preferences under regional trade arrangements are permitted as an exception from the cardinal MFN principle of non-discrimination on condition that they are used only to open trade among participating countries and not to raise barriers against trade from non-participants. To that end, Article XXIV:4 provides that “the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.” Similarly, paragraph 3(a) of the

[26] See draft *EU Commission negotiating mandate*, para 3.1 on *Objectives*.
[27] GATT doc. L/4903, 28 November 1979.

Enabling Clause provides that any preferential or more favourable treatment under the Enabling Clause "shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties." Although the wording in these two provisions is slightly different, the objective remains the same, that trade creation, as opposed to trade diversion, has to be the object of RTAs.

However, the commonalities end here. Significant differences exist between GATT Article XXIV and the Enabling Clause on regional integration. Indeed, if GATT Article XXIV is an exception from the MFN principle of Article I, paragraph 2(c) of the Enabling Clause on South-South preferential agreements is an exception from Article XXIV. According to paragraph 2(c), developing countries could enter into regional or global arrangements among themselves "for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the Contracting Parties, for the mutual reduction or elimination of non-tariff measures, on products imported from one another". Unlike under GATT Article XXIV, no specific name is given to such a South-South preferential trade arrangement – it is neither an FTA nor a CU. Given the limited scope and ambition implicit in its wording, however, it is closer to an FTA than to a CU. The corresponding provision of Article XXIV:8(b) on FTAs provides that:

> *"(a) free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.*

Three things are immediately apparent from this juxtaposition. First, while Article XXIV speaks about the formation of an FTA between any two or more customs territories, paragraph 2(c) of the Enabling Clause is limited to the formation of unnamed "regional or global arrangements" among only developing countries. The relevance of this distinction to the EPA negotiations is apparent since EPAs are to be concluded between a developed customs territory – the EU, on the one hand, and developing ACP countries and/or sub-regions, on the other. Because the Enabling Clause authorizes only South-South RTAs, there is no room for North-South RTAs, such as the future EPAs, to be justified under it. Indeed, developed countries, particularly the EC, have tried – and failed – on several occasions to defend discriminatory preferences accorded to developing countries on the basis of paragraph 2(c) of the Enabling Clause.[28]

Secondly, as regards tariffs, while Article XXIV speaks in terms of elimination of duties (with some exceptions) on "substantially all the trade" in goods originating from such territories, paragraph 2(c) of the Enabling Clause allows either reduction or elimination of tariffs and does not specify any quantitative or qualitative standard on the amount of trade to be covered.

Finally, in respect of non-tariff barriers, while GATT Article XXIV speaks in terms of the elimination of what it calls "other restrictive regulations of commerce" – a concept that is understood to mean non-tariff barriers – on substantially all the trade between the constituent territories in products originating in such territories, paragraph 2(c) of the Enabling Clause speaks once again about either reduction or elimination of non-tariff measures on any amount of trade between them and "in accordance with criteria or conditions which may be prescribed". No such criteria have yet been prescribed either by the GATT Contracting Parties or any WTO organ. The importance of these distinctions on the scope of liberalization to take place in respect of tariffs and non-tariff barriers between FTAs under GATT Article XXIV and those under the Enabling Clause is once again obvious – while developing countries could introduce preferential arrangements among themselves (e.g. COMESA and SADC) without necessarily eliminating duties or other restrictions on any significant portion of their trade, this would not be permissible in situations where some or all the members of the RTA are developed countries (as is the case with the future EPAs).

[28] See, *inter alia*, the following cases: *EC Bananas* I and II, and *European Community - Tariff Treatment on Imports of Citrus Products from Certain Countries in the Mediterranean Region, Report of the Panel,* (*GATT doc. L/5776,* 7 February 1985, not adopted, hereafter "EC *Mediterranean Citrus"*).

EPAs and the Enabling Clause

The Enabling Clause provides for the possibility of developing countries forming regional or global preferential arrangements among themselves without satisfying the requirements of Article XXIV on FTAs and CUs. Because several intra-ACP RTAs have been created under the Enabling Clause without satisfying the requirements of GATT Article XXIV, the EPA process in a way brings face-to-face two different categories of countries that have been pursuing the same goal of establishing closer regional integration for decades in accordance with two completely distinct parameters. To reiterate, Cotonou obliges the parties to the EPA negotiations to conclude only WTO-compatible FTAs. Given that the EPAs are being negotiated between the developed EU and the developing ACPs, by definition this means FTAs as envisaged under GATT Article XXIV. The option available for South-South cooperation in the form of RTAs under the Enabling Clause is simply not available for RTAs between developed and developing countries, such as the EPAs discussed here. They have to be concluded in compliance with GATT Article XXIV. As discussed below, however, the ACP Group of countries within the WTO are proposing changes to GATT Article XXIV as part of the Doha negotiations, so that options similar to those provided by the Enabling Clause would be extended to North-South FTAs. It is interesting to observe at the same time that the EU's proposal on the same issue only requests clarifications to Article XXIV and falls short of demanding the introduction of preferential treatment to developing country partners to North-South RTAs.

Until the desired changes are introduced to the relevant GATT provisions, however, the new EPAs will be judged only in accordance with the standards set by the current version of GATT Article XXIV. This has the potential to cause complicated legal issues in which an EPA has to comply with one legal standard (GATT Article XXIV), while its constituent elements are subject to two different and incompatible legal standards (GATT Article XXIV and the Enabling Clause). At its most extreme, this could result in a situation where trade between the EU and an ACP sub-regional partner would be freer than internal trade at the level of the ACP sub-region party to the EPA. In other words, ACP countries may have more obligations to open their markets for European goods than those coming from across their immediate borders. In apparent anticipation and fear of this possibility, the EU Commission mandate specifically provides that "the ACP countries shall undertake, at least, to extend automatically the treatment granted to the Community to all other parties to the EPA concerned, preferably ahead of trade liberalization vis-à-vis the Community."[29]

Two problems emerge from this. First, the ACP countries will have to give up their rights under the Enabling Clause to form sub-regional RTAs without being required to satisfy any minimum liberalization requirements. This will radically transform not just the relations of the ACP countries with the EU and among themselves, but also with all other countries of the world. Secondly, even assuming that ACP countries members of an EPA agree to automatically extend their commitments with the EU to their sub-regional neighbours, the depth of integration at the ACP level will still be the same as that to be reached for an EPA with the EU, which, as argued earlier, is akin to an FTA rather than a CU.

This will create difficulties for ACP sub-regional RTA at the WTO, as it is required to satisfy the requirements of a CU before its members could conclude an EPA as a group rather than as individual countries.

2.4 EPAs as WTO-compatible FTAs and the principle of SDT

The preceding analysis has shown that as long as both the EU and the ACP are committed to negotiating WTO-compatible EPAs, the current state of WTO law demands that EPAs satisfy the requirements of GATT Article XXIV on FTAs. This will initially take the form of interim agreements leading to the formation of FTAs as envisaged under GATT Article XXIV:5, in which case the parties are required to "include a plan and schedule for the formation of … such a free-trade area within a reasonable length of time"(Art. XXIV:5(c)). The Cotonou Agreement and subsequent negotiating documents promise that the EPAs will become WTO-compatible RTAs while still maintaining SDT for the benefit of the ACP countries. Box 2.2 provides an overview of the issues related to SDT and WTO compatible EPAs elaborated in more detail below.

[29] See draft EU Commission mandate, 12 June 2002, Annex I, p. 7.

Reciprocity versus the desire for asymmetry

The principle of asymmetry in this context implies giving ACP countries more rights than corresponding obligations undertaken by them. Article 37.7 of the Cotonou Agreement provides that negotiations will be "as flexible as possible in establishing the duration of a sufficient transitional period, the final product coverage, taking into account sensitive sectors, and the degree of asymmetry in terms of timetable for tariff dismantlement, while remaining in conformity with WTO rules then prevailing." The 2003 (First) Joint Report of the all-ACP-EU phase of the EPA negotiations further confirmed that "flexibility would be provided in the EPAs, and asymmetry in favour of the ACP would be granted both in terms of product coverage and transition periods (First Joint Report, para 6)." On that basis, ACP countries expect the principle of SDT to be reflected in the EPAs in terms of (1) the length of transition period and timetable for tariff dismantlement, and (2) product coverage.

BOX 2.2: REVISION OF GATT/WTO RULES: SDT IN FTAS FOR EPA COMPATIBILITY

Two of the major concerns that ACP countries have with WTO rules as they negotiate ending non-reciprocal preferences and establishing WTO compatible FTAs (EPAs) are a) the extent to which trade needs to be reciprocal and b) the transition period for implementation of the agreement.

Under GATT Article XXIV, in an FTA, customs duties and other restrictive trade rules must be eliminated for "substantially all trade". While precedent exists suggesting that 90 percent of trade could be acceptable as "substantially all trade", it would still require ACP countries to open at least 80 percent of their market if the EU opened its market 100%. Several ACP countries seek to limit this degree of reciprocity in the EPA context through ensuring realization of commitments to SDT in the WTO rules.

Similarly, there is an interest in extending the time allowed to establish an FTA. Under current WTO rules the "reasonable length of time" generally permitted should not exceed ten years, although a longer period could be authorized "only in exceptional cases". While many FTAs have adopted longer implementation periods, and there have been no challenges, the fact remains that there has been no change in WTO rules.

In April 2004, the ACP Group of States, bearing in mind their ongoing negotiations towards WTO compatible economic partnership agreements with the EU under the Cotonou Partnership Agreement, submitted (TN/RL/W/155) a rationale and proposals to the WTO Negotiating Group on Rules, suggesting recognition of SDT principles, and therefore that GATT Article XXIV, the rules on RTAs, be modified to explicitly provide the necessary differential and more favourable treatment to developing countries that are party to RTAs with developed countries.

The ACP Group's submission called for developmental needs to be taken into consideration in reviewing GATT rules related to RTAs, for compatibility to be determined by the Committee on Regional Trade Agreements and for S&D treatment for developing countries to be formally and explicitly made available to developing countries in meeting criteria set out in paragraphs 5 to 8 of GATT Article XXIV in the context of regional agreements entered into between developing and developed countries.

Specifically on "substantially all the trade":

> *Appropriate flexibilities are proposed - on duties and measurement of trade and product coverage, allowing asymmetric lower levels for developing countries, and flexible interpretation on "other restrictive regulations of commerce", allowing contingency protection measures including safeguards and other non-tariff measures (e.g. rules of origin) on intra regional trade.*

Specifically on "reasonable period of time":

> *A longer time period that is consistent with the trade, development and financial situation of developing countries is proposed – it should not be less than 18 years and the circumstances under which a period can be extended should be clarified.*

In May 2005, the EC, in its own submission (TN/TL/W179) on Regional Trade Agreements to the WTO made explicit reference to the above ACP proposal and called for similar changes in GATT Article XXIV on RTAs to allow greater flexibility in North-South RTAs. It is anticipated that a change of rules to allow EPAs is more likely through modification of Article XXIV, which justifies RTAs, than through changes in the Enabling Clause as this would too greatly erode basic WTO MFN principles. There remains the issue related to the timing of conclusion of EPAs or the Doha Round and which WTO rules would apply to EPAs.

Asymmetry and the transition period: "reasonable length of time"

While it is certain that EPAs will be phased-in over an agreed period of time,[30] it is not possible at this stage to determine whether they will be presented to the WTO as FTAs or as interim agreements leading to the formation of FTAs. EU experience in this respect is also rather mixed. For example, the 1982 Mediterranean Citrus case under the GATT shows that the specific treaties at issue in that case were presented to the GATT by the EC and its partners "as interim agreements leading to the formation of a customs union under Article XXIV (Cyprus, Malta and Turkey), as interim agreements leading to the formation of a free-trade area under Article XXIV (Israel and Spain), or as agreements comprising a free-trade area obligation on the part of the EC under Article XXIV but no reciprocal commitments by the other parties consonant with Part IV (Algeria, Egypt, Jordan, Lebanon, Morocco and Tunisia)."[31] It is thus impossible to tell whether the EPAs will be presented as interim agreements or as full-fledged FTAs. It looks fairly certain, however, that there will be a transition period of some sort – not only is it promised by Cotonou and taken for granted by the negotiators, but this has also been the dominant practice in the negotiation of RTAs worldwide regardless of whether they are interim agreements. Indeed, GATT/WTO history shows that although most RTAs are implemented in stages, i.e. over a certain length of transition period, "very few have expressly been notified as "interim agreements".

In the event that EPAs are presented as interim agreements leading to the formation of FTAs, they will need to be accompanied with "a plan and schedule for the formation of … a free-trade area within a reasonable length of time." According to the 1994 Understanding on the interpretation of GATT Article XXIV, the term "reasonable length of time" should generally mean a maximum of ten years and any period longer than that will be allowed only in "exceptional cases" and upon full explanation. The requirement for a "plan and schedule" is then intended to provide detailed information on the different stages through which tariffs and other restrictions would be dismantled so as to establish a full-fledged FTA at the end of a given transition period.

Application of the asymmetry principle to the length of transition period would come in the form of EPA obligations taking longer phase-in periods for the ACP countries while giving effect to them either immediately or after a shorter phase-in period for the EU. The experience so far also confirms this approach. In the EU-South Africa TDCA, for example, the general transition period was ten years for the EU and 12 years for South Africa.[32] The ACP countries are already making an effort in the Doha negotiations at the WTO to inject further flexibility into the definition of "reasonable length of time" provided by the Uruguay Round Understanding. The April 2004 submission by the ACP Group of States within the WTO argues that the maximum length of the transition period "should be determined in such a manner that is consistent with the trade, development and financial situation of developing countries, but in any case not less than 18 years."[33] While suggesting a "not-less-than" methodology for a maximum permissible period might sound unusual, it probably indicates the high degree of importance the ACP Group attaches to the matter. However, there are at least two reasons to expect that the EU will press for a 12-year maximum.

First, there is already a recent "precedent" in the form of the TDCA, which, although often publicly rejected by both the EU and the ACP as an inappropriate model, will be invoked by the EU to press its case in that direction. The EU has also agreed a 12-year transition period in its 2000 agreement with Morocco. Secondly, a look at the final provisions of the Cotonou Agreement reveals that it is an agreement concluded for a 20-year period, starting from 2000.[34] The same Agreement requires that EPAs should be concluded by the end of 2007 so they would enter into force by 1 January 2008.[35] This

[30] Article 37:7 of the Cotonou Agreement provides that EPA negotiations "shall aim notably at establishing the timetable for the progressive removal of barriers to trade between the Parties, in accordance with the relevant WTO rules."

[31] See *EC Mediterranean Citrus,* para. 2.10.

[32] See WTO *Committee on Regional Trade Agreements, Coverage, Liberalization Process and Transitional Provisions in Regional Trade Agreements. Background Survey by the Secretariat,* (WT/REG/W/46, 5 April 2002) Annex 1, p. 22; and Annex 5, p. 36.

[33] See WTO Negotiating Group on Rules, *Submission on Regional Trade Agreements: Paper by the ACP Group of States* (TN/RL/W/155, 28 April 2004) para. 10(ii).

[34] See Article 95:1 of the Cotonou Agreement: "This Agreement is hereby concluded for a period of twenty years, commencing on 1 March 2000."

[35] See Article 37:1 of the Cotonou Agreement.

leaves only 12 years between the entry into force of the EPAs and the end date of the Cotonou Agreement. These dates could not have been fixed with so much detail without good reason. It is also notable that the TDCA with South Africa entered into force on 1 January 2000, while the Cotonou Agreement went into force a month later. It thus appears probable that the EU will resist any ACP proposal, whether at the WTO or in the EPA negotiations, for a transition period longer than 12 years.

Asymmetry and product coverage: "substantially all the trade"

More important than the length of transition period for the ACP countries in respect of EPAs is that of product coverage. On the face of it, Article XXIV:8(b) on the internal liberalization aspect of FTAs, requires that duties and other restrictive regulations of commerce be eliminated on "substantially all the trade" between the constituent territories in products originating in such territories. This concept limits the scope of applicability of the asymmetry principle, but is also one of the most contentious concepts in GATT/WTO law.

In practice, and particularly in cases of RTAs negotiated between developed and developing countries, asymmetries have traditionally been reflected in the form of shallower liberalization in terms of product coverage and level of reduction/elimination of trade barriers by developing than by developed countries. For example, the 1997 agreement between the EU and Tunisia resulted in: 100 percent of EU industrial imports from Tunisia duty-free, 5 percent of agricultural imports at MFN duty rates, 24 percent at reduced duty rates, and 71 percent duty-free. On the other hand, 99 percent of industrial imports from the EU would enter Tunisia duty-free, 1 percent at MFN duty level; 62 percent of agricultural imports from the EU at MFN rates, 38 percent at reduced duties while none is allowed duty-free.[36]

More recently, the EU–South Africa TDCA defines "substantially all the trade" to mean at least 90 percent of all the trade between the two entities. As noted earlier, this 90 percent threshold is made up of commitments to liberalize around 94 percent by value of EU imports from South Africa and around 86 percent by value of South African imports from the EU. Many argue that 90 percent is too high, while still others think it is too low. Nonetheless, the EU is currently presenting this 90 percent threshold as "the WTO criterion" for the "substantially all the trade" requirement. As discussed in the argument earlier on the length of transition period, this indicates that the EU is likely to stick to its own tradition and insist on a 90 percent standard. No agreement was reached during the all-ACP-EU phase of the negotiations on this issue and it still remains open, presumably due to an ACP objection. The likelihood is that this threshold will be negotiated at the regional level. While there is nothing wrong in this, the ACP fear, with good reason, that negotiations with the EU at the regional or country level only further diminish their bargaining power and that the EU might proceed with a "willing" region or country, rubberstamp its desired terms of arrangement and stick to them as a sort of blueprint to which everybody else must subscribe. Only time will tell whether this is a well-founded concern.

If assuming a 90 percent threshold for the purposes of discussion here, a commitment to this effect could be arrived at in several ways – such as equal 90 percent liberalization on each side or a lower level on one side compensated for by a higher commitment from the other side. In the present context, it is already a fact that well over 90 percent of ACP products enter the EU free of duties, and the negotiations in this respect will be largely on the percentage of EU trade that should get free access to the ACP partners in an EPA. Accordingly, while the EU and the ACP regions and/or countries will have the flexibility to incorporate asymmetry only in respect of the 10 percent overall margin, the ACP countries could still negotiate for application of the asymmetry principle to their benefit in two senses: (1) the 90 percent threshold could be achieved by a liberalization of just 80 percent on their part and 100 percent on the part of the EU, or any combination of figures between those two; and (2) the 20 percent or so margin that is left for them could be used to restrict the importation of EU goods of utmost sensitivity to ACP domestic economies.

It is submitted, however, that given EU sensitivity, particularly in the agricultural sector, this could turn out to be more of a wish list rather than a realistic expectation.

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[36] See WTO/REG/W/46, *supra* n. 45, Annex 1, p. 22.

EPAs and SDT: the way forward

As demonstrated above, neither GATT Article XXIV nor the Enabling Clause has any room for a meaningful application of the principle of SDT in the context of EPAs. Some of the possible approaches suggested above are drawn from state practice over the past decades rather than any clear legal authority. Now that the dispute settlement system has an unquestioned power to rule on the legality of any measures introduced in the context of RTAs, any of these practical arrangements are in principle vulnerable to challenge. The only way to achieve EPAs that are both WTO-compatible and asymmetrical in favour of the ACP countries or regions parties to those EPAs may thus be through a modification of the rules of GATT Article XXIV and the Enabling Clause. It will be argued that Article V of the GATS provides an existing model for any such amendment. Further, this is the line currently being pursued by the ACP Group within the WTO.

2.5 EPAs and other agriculture negotiation related issues

Just as under the multilateral trading system of the WTO, agriculture is also an exception under the RTAs. Most FTAs and CUs since the early days treated agriculture as an exception – either subjecting it to a special regime within the RTAs (e.g. the Treaty of Rome that set up the EEC) or even excluded the sector from intra-RTA liberalization completely (e.g. the Stockholm Treaty which set up the European Free Trade Association (EFTA) (Dam,1963, p. 654). As a WTO Secretariat survey observed, the strategy used for granting concessions on industrial and agricultural products is different for many agreements. For industrial products, most if not all RTA parties grant concessions on the basis of a negative list, i.e. they start out with the goal of full product coverage and remove or give extended transition periods to their most sensitive products. In contrast, many countries use a positive list approach to grant concessions in agriculture, i.e. concessions are granted only on certain traded products, excluding the rest.[37] The study concluded that the product coverage of agriculture is considerably less than that of industrial products, both in terms of import share and duty-free tariff lines. Indeed, traditionally, RTAs were primarily concerned with free trade in industrial products and it is only the modern RTAs that include agricultural concessions. Even then, only a small minority of RTAs offer duty-free treatment on both industrial and agricultural goods, while the majority offer duty-free (or near duty-free) treatment on industrial goods and duty reductions on selected agricultural goods.[38]

Whenever agriculture is excluded from the intra-FTA liberalization process completely – but also when it is subjected to a lower level of liberalization – the question has always been whether any such FTA satisfies the GATT Article XXIV:8(b) requirement that “duties and other restrictive regulations of commerce” be eliminated on “substantially all the trade between the constituent territories in products originating in such territories.” This was exactly the question that was presented to the EFTA countries when they submitted the Stockholm Convention to GATT in 1960. The EFTA members argued that “substantially all” trade did not mean “all” trade and “if one examined the statistics, it appeared that ninety per cent of all trade would be freed from restrictions” (Dam, p. 654).

Those on the opposite side replied that “whatever the statistics might reveal, the exclusion of an entire sector, particularly one as important as agriculture, indicated that the elimination of restrictions had not been extended to “substantially all” trade.”(idem) It is in response to such concerns that the qualitative approach to the question of “substantially all trade” was developed. According to this approach, no matter what the percentage level of trade liberalized between any two or more countries members of an RTA, they will not be considered to have liberalized “substantially all the trade” as long as an entire sector such as agriculture is excluded from liberalization.

The issue of agriculture becomes even more important in the current EPA negotiations for three main reasons: first, the Lomé agreements as well as Cotonou already provide duty-free access to the EU market for virtually all industrial products originating from the ACP countries and, from the perspective of ACP countries, the current negotiations could create additional market access only in the agricultural sector. Secondly, even if the EPA negotiations result in the reduction or elimination of all tariffs on ACP agricultural exports, the probability of many ACP countries successfully exploiting any such opportunity is rather minimal due largely to poor supply capacity on their part, and high SPS

[37] See WT/REGW/46, *supra* n. 45, para. 44, pp. 12-13.
[38] See idem, para. 46, p.14.

standards applying in the EU. Finally, given that the commodity protocols, particularly those on beef/veal and sugar, still play a crucial role in the economies of many of the beneficiary ACP countries, any moves towards reciprocal EPAs is likely to adversely affect the interests of those countries. These will be discussed in turn.

EPA negotiations and market access for ACP agricultural products

As noted earlier, the Lomé arrangements have always provided duty-free market access for ACP industrial products, while the arrangements for agriculture have been less generous and more complicated. In the case of agriculture, there has been a combination of duty-free access for some products, less-than-MFN duties for others, and access to EU guaranteed prices for fixed quantities of few other products (beef/veal and sugar under the protocols). The benefits of ACP agricultural exporters in many of these areas are being eroded for various reasons, including reduction and/or elimination of EU MFN tariffs at the multilateral level, and reform of EU domestic support schemes, particularly in products subject to commodity protocols in the Cotonou Agreement. Consequently, to the extent that EPA negotiations divert from their primary focus on dismantling ACP trade barriers to EU products, improved ACP agricultural market access will become the priority. Indeed, that is precisely what they mean when the ACP propose the extension of the EBA initiative to all ACP countries under the EPAs.

The experience so far, however, is not very encouraging. A WTO Secretariat study shows that of the seven EU trade agreements with developing countries included in its study (with Israel, Jordan, Syria, Algeria, Morocco, Tunisia and South Africa), the share of EU duty-free agricultural tariff lines ranges between 24 percent for Syria and 68 percent for Morocco, while the comparable figures for industrial products stand at 100 percent for all countries except South Africa.[39] While it is not possible to conclude from this that the EU will treat ACP countries the same way as it has treated the economically better-off countries included in this list, the notorious EU sensitivities in the area of agriculture will mean that ACP negotiators face a difficult challenge in this area. Moreover, even assuming that the EU will agree to duty-free access for ACP agricultural products under EPAs, the most difficult obstacle to ACP agricultural exports comes from the high EU health and safety standards in place particularly in the agricultural sector.

EPAs and health and technical standards

Much has been said about the chronic problem of agricultural protectionism, particularly in the developed world. The patently illegal quantitative restrictions on agricultural products that prevailed in the GATT era have come to an end due to the Uruguay Round Agriculture Agreement. But this does not mean agricultural trade is free today – it only means that those non-tariff barriers have been replaced by tariffs.

For agricultural products coming to the EU from ACP countries, tariffs are not the main problem, as the ACP countries benefit from duty-free market access for most of their products under the *Lomé acquis*. Rather, it is the EU's highly technical SPS that cause the real problem. The primary objective of these measures generally is the protection of human, animal and plant health and safety. As such, they are fully legitimate instruments under the WTO legal system.

The WTO recognizes that countries have an unquestionable right to adopt measures necessary for the protection of animal and plant health and life. However, there is also the equally legitimate fear that protection of health and life could serve as a smokescreen to cover otherwise illegal protectionist measures. To overcome this, the WTO requires that all SPS measures be based on a risk assessment and have a scientific justification; science is thus given the role of the final arbiter to decide the genuine health measures from the trade protectionist ones. As seen from experience and several WTO cases, such as the famous *Beef Hormones* dispute between the United States and Canada, on the one hand, and the EU, on the other,[40] this is a very complex area that requires enormous investment in scientific and technological infrastructure – often in rare supply in most ACP countries.

[39] See WT/REG/W/46, *supra* n. 45, Annex 2, p. 24.

[40] See *EC Measures Concerning Meat and Meat Products (Hormones)*, Complaint by the United States (WT/DS26/*/USA) and Canada (WT/DS48/*/CAN), 16 January 1998.

Developing countries campaigned for and won preferential treatment in terms of lower or zero tariffs and other non-tariff barriers for their products. Once the standards are in place, the only options are either to meet those standards and export accordingly, or drop the idea of exporting altogether. Ultimately, no consumer would buy anything agricultural that does not conform to prevailing standards. The most that has been achieved so far at the WTO level in this respect is a promise of technical assistance to those countries that do not have the necessary scientific and technical infrastructure to be able to comply with those standards.

The role of SPS issues in EPA negotiations is far from clear. What is clear is that the ACP countries can neither fear, nor expect to benefit from any SPS regime resulting from the EPA negotiations. The moment any EPA provision imposes a more stringent requirement than what the EU applies at an MFN level, there is technically a violation of Art. XXIV:4 – a provision which was given a prominent place by the AB in Turkey Textiles. This provision states:

> *The contracting parties recognize the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements. They also recognize that the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.*

The AB has stated in this regard that:

> *Paragraph 4 … sets forth the overriding and pervasive purpose for Article XXIV which is manifested in operative language in the specific obligations that are found elsewhere in Article XXIV. Thus, the purpose set forth in paragraph 4 informs the other relevant paragraphs of Article XXIV, including the chapeau of paragraph 5. For this reason, the chapeau of paragraph 5, and the conditions set forth therein for establishing the availability of a defence under Article XXIV, must be interpreted in the light of the purpose of customs unions set forth in paragraph 4 (Turkey Textiles, AB Report, para. 57).*

To the extent any EPA provision provides for a higher-than-MFN SPS standard between the parties, this “overriding and purposive purpose of Article XXIV” will be missed by a wide mark and the resulting RTA cannot be considered compatible with the WTO requirements. On the other hand, the ACP countries cannot expect the EPAs to introduce “preferential treatment” in the application of EU SPS. This is because, by definition, an SPS has to be necessary for the protection of human, animal or plant life or health. If the EU accepts lesser standards on goods from the ACP countries than from others in similar circumstances (e.g. geographically), then the need for such a measure will be in doubt, and possibly a case could be made for arbitrary discrimination since arbitrariness here would have to be interpreted in the context of the prevalence of risk in goods coming from any two countries.

Bearing this in mind, there is room to incorporate other forms of "preferences" in the EPAs, such as targeted assistance or organizing pre-shipment inspection facilities at the exit points in the ACP countries (e.g. at the airports or seaports). The ACP countries recognize that lack of scientific and technical know-how is the single most important obstacle standing against their agricultural exports to the EU. To the extent that they lack the capacity to produce exportable goods in acceptable standards and in commercial quantities, the value of any concessions in the EPA negotiations will be marginal. Developing pertinent scientific and technical capacity through the building of appropriate institutions will be an important step in that direction.

EPAs and commodity protocols

Commodity protocols are one of the unique features of EU-ACP cooperation in trade matters. Historically applying to four products – banana, rum, sugar, and beef/veal – the protocols have been annexed to the Lomé Conventions, and provided duty-free access to fixed quantities of the products under a TQ scheme (except on beef/veal), and in some cases provided further access to guaranteed minimum prices (beef and sugar) similar to those applying to similar EU products. The protocols have been an important source of export revenue for many ACP countries.

However, the value of these protocols has diminished over time for many, often extraneous, reasons. The WTO system has contributed its share in two forms – the successful challenge to both the banana and sugar regime, and the erosion of preferential margins with progressive reduction in MFN tariff levels. Internal CAP reform in the form of reduction of intervention prices (e.g. beef/veal) is also playing its part. Protocols 3, 4 and 5 on sugar, beef/veal and bananas respectively annexed to the Cotonou Agreement contain the remnants of these commodity-specific arrangements.

The potential impact of the EPA negotiations on these commodity protocols is as yet unclear. Nor does the Cotonou Agreement provide much guidance in this respect. Article 36:4 of the Cotonou Agreement simply reaffirms the importance of the commodity protocols and declares an agreement "on the need to review them in the context of the new trading arrangements, in particular as regards their compatibility with WTO rules, with a view to safeguarding the benefits derived there from, bearing in mind the special legal status of the Sugar Protocol." Compatibility of the protocols with WTO parameters thus appears to be the main objective of the EPA negotiations in this respect. This could mean significant changes to the way the protocols work.

Firstly, we know that both the banana and sugar regimes have been found to be in violation of WTO requirements, thereby setting a dangerous precedent for similar measures under the other protocols. Secondly, if the current negotiations succeed in establishing EPAs made up of two RTAs (the EU on the one hand, and ACP sub-regional RTAs, on the other), the current protocol beneficiary countries will find themselves effectively swallowed up by their respective sub-regional RTAs. Considering the argument above that those ACP sub-regional RTAs will have to be CUs before signing an EPA as RTAs, the dismantling of internal borders that this sub-regional process will entail might mean that the country-specific benefits from the commodity protocols will be automatically available to all members of those RTAs. This not only has the potential to kill the protocols as we know them, but also creates another disincentive against closer integration of ACP countries at the sub-regional level, thereby impeding progress on the road towards establishing the EPAs.

2.6 Reconciling EPAs with SDT under the WTO – The way forward

One route to achieve new "reciprocal" arrangements under the EPAs while still maintaining a degree of asymmetry in favour of the ACP countries would be by seeking a new waiver under Article IX of the WTO Agreement. Indeed, there are also possibilities under Article XXIV:10 for an RTA to be approved by the WTO, even if it does not fully satisfy the requirements of an FTA. This will, however, immediately breach the Cotonou commitment "to conclude new WTO-compatible trading arrangements" (see Cotonou Art. 36:1). This leaves only two other ways to achieve this – making any benefits available to non-ACP countries under the GSP scheme or amending GATT Article XXIV.

Extending the GSP

The effect on the ACP of extending preferential access to all other developing countries under the GSP system would not be the same as under the current system. An extension to all other developing countries will automatically erode preferences.

The potential extent of this erosion can be tempered, however, by the new Appellant Body (AB) ruling in the EU GSP case. This in effect allows the EU to differentiate among developing countries on objective and open-ended grounds. Paragraph 3(c) of the Enabling Clause provides that SDT of developing countries by developed countries "shall … be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries."

Interpreting this provision, the AB ruled:

> *we read paragraph 3(c) as authorizing preference-granting countries to "respond positively" to "needs" that are not necessarily common or shared by all developing countries. Responding to the "needs of developing countries" may thus entail treating different developing-country beneficiaries differently (*EU GSP, *AB Report,* April 2004, para. 162*).*

The AB then concluded:

> *(T)he term "non-discriminatory" in footnote 3 does not prohibit developed-country members from granting different tariffs to products originating in different GSP beneficiaries, provided that such differential tariff treatment meets the remaining conditions in the Enabling Clause. In granting such differential tariff treatment, however, preference-granting countries are required, by virtue of the term "non-discriminatory",*

> *to ensure that identical treatment is available to all similarly-situated GSP beneficiaries, that is, to all GSP beneficiaries that have the "development, financial and trade needs" to which the treatment in question is intended to respond (*ibid., para. 173*).*

At its most unusual extreme, one might wonder whether the special relationship between these two blocs over three decades, which is to end because of a WTO-compliance requirement, has created special "development, financial and trade needs". Such needs have to be responded to positively as required by paragraph 3(c) of the Enabling Clause – even though the demise of Cotonou arises from direct and indirect pressure through the WTO legal system, such as the banana and sugar disputes. Another, and perhaps a more feasible way to use the AB ruling to strike a balance between WTO conformity and preference erosion would be to use economic factors, such as gross domestic product (GDP) and vulnerability, as conditions on which beneficiary status depends and to define those conditions in such a way as to include as many of the ACPs as possible while also excluding as many of the non-ACPs. While this seems to be legally permissible, it will also certainly be a difficult one to sell at the political level. It would also risk re-igniting old divisions within the ACP itself based on each country's position on any such economic scale. As such, the GSP option does not seem to be very attractive in practice.

Revision of Article XXIV

In principle it would be possible to amend GATT Article XXIV to allow for non-reciprocal preferential arrangements over a given portion of the trade between members of RTAs. This could be done, for example, by inserting an SDT exception. One may wonder whether this would fall foul of the Cotonou commitment to conclude a WTO-compatible arrangement. However, the WTO-compatibility of any EPA will be judged according to the WTO law that exists at the time the EPAs enter into force. Accordingly, any successful move to modify existing WTO law so as to bring it closer to recognizing preferential terms of access and diminished level of reciprocity between partners to a North-South RTA, will have the same effect on the WTO-compatibility of an EPA as any successful move to bring an EPA closer to full reciprocity. The only question is whether this is achievable within the WTO.

The EU and the ACP seem to be pursuing this option with some degree of coordination in the context of the ongoing Doha Round. Article 37:8 of the Cotonou Agreement provides that:

- The Parties shall closely cooperate and collaborate in the WTO with a view to defending the arrangements reached, in particular with regard to the degree of flexibility available." Further, when the Doha Development Agenda was launched in the following year, paragraph 29 of the Doha Declaration provided for "negotiations aimed at clarifying and improving disciplines and procedures under the existing WTO provisions applying to RTAs.
- Most importantly, the Declaration stressed that the negotiations on RTAs "shall take into account the developmental aspects of regional trade agreements." (See WTO Ministerial Declaration adopted on 14 November 2001 (WT/MIN(01)/DEC/1, 20 November 2001, para. 29.)

The first Joint ACP/EU Report provided that:

> *EPAs must be compatible with WTO rules then prevailing and will need to take account of the evolutionary nature of relevant WTO rules, in particular in the context of the Doha Development Agenda. Both sides agreed to co-operate closely in the context of the WTO with a view to defending the arrangements reached, in particular with regard to the degree of flexibility then available (Joint Report, para. 4(a) (iv), p. 3).*

In their submission to the WTO Negotiating Group on Rules, the ACP Group of States within the WTO stressed the Doha commitment to "take into account the developmental aspects of regional trade agreements" and argued that "the negotiations on WTO rules on RTAs shall explicitly provide the necessary differential and more favourable (treatment) to developing countries' parties to RTAs with developed countries."[41] Acknowledging that the current version of GATT Article XXIV does not have room for SDT for North-South RTAs, the ACP Group has proposed to insert the following text in GATT Article XXIV: "members agree that SDT treatment for developing countries be formally and explicitly made available to developing countries in meeting criteria set out in paragraphs 5 to 8 of

[41] See ACP Group proposal, TN/RL/W/155, *supra* n. 46, para. 4.

GATT Article XXIV in the context of regional agreements entered into between developing and developed countries. (idem, para 10)." This in effect is a proposal to allow a certain degree of asymmetry in the trade relationship between developed and developing members of an RTA so that developing country members would become parties to RTAs and satisfy the requirements of GATT Article XXIV while opening their markets to a lesser degree than what would be expected of a developed country member of the same RTA. Recognition of asymmetry in the degree of intra-RTA liberalization is thus at the heart of this ACP proposal.

The EU has also made proposals on RTAs and their development dimension to the WTO Negotiating Group on Rules. While stressing the positive role of regional integration for economic development, the EU argues that "flexibilities (are) already provided for within the existing framework of WTO rules" and that the current negotiations should "involve further consideration of the relationship between GATT Article XXIV and the Enabling Clause, as well as an examination of the extent to which WTO rules already take into account discrepancies in development levels between RTA parties."[42] The EU further argued:

> *The economic logic of regional integration indicates that all parties to such agreements should pursue a high level of reciprocal market opening and regulatory harmonization or convergence while also pursuing an open approach to trade policy with third countries within the multilateral framework if they are to achieve the full potential benefits. This is as true for agreements among developing countries as it is for agreements between developing and developed countries or among developed countries alone. At the same time, it is important to recognise that the ability of many developing countries to adjust to greater competition on their domestic markets or take full advantage of additional market access opportunities can be constrained by their own individual level of development. This points to the need to examine, inter alia, the flexibilities available during the transitional or implementation period of RTAs, taking into account the needs of developing countries in a properly focused and appropriate manner so as to support their greater integration into the multilateral trading system. Aspects in respect of which such flexibilities might be appropriate include the length of the transitional period, the level of final trade coverage and the degree of asymmetry in terms of timetables for tariff reduction and elimination (*idem, p. 3*).*

In May 2005, the EC, in its second submission (TN/RL/W/179) refers specifically to the ACP Group proposal mentioned earlier and addresses key issues at the heart of their concerns regarding the establishment of WTO compatible EPAs, specifically coverage and transition periods, and possible SDT provisions essential to ensuring that GATT Article XXIV allows the needed flexibility.[43] Under section 5 on developmental aspects they call for fair and equitable treatment between different forms of RTAs to which developing countries are parties:

> *Existing rules fail to create fair and equitable treatment between different types of RTAs based on their developmental impacts and promotion of developing countries' participation in world trade. For example, while preferential tariff and partial liberalization agreements among developing countries fall under the Enabling Clause, ambitious and full-fledged RTAs, such as Free Trade Agreements between developed and developing countries are subject to the stricter requirements of GATT Article XXIV. Yet, North-South RTAs can have at least as high a developmental impact as any of those falling under the Enabling Clause, and it is difficult to see why the substantive requirements should be radically different.*

Further, they call on the Doha Round negotiations on RTAs to clarify the flexibilities already provided within the existing WTO rules on RTAs, in order to give greater security to developing country parties to RTAs to ensure that the rules facilitate the necessary adjustments. The submission indicates that:

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[42] See *Negotiating Group on Rules, Submission on Regional Trade Agreements by the European Communities and their member States* (TN/RL/W/14, 9 July 2002), p. 3.
[43] *See Negotiating Group on Rules, Submission on Regional Trade Agreements by the European Communities* (TN/RL/W/179, 12 May, 2005), p. 4 and 5.

> *The European Communities are prepared to explore various ways of achieving this aim, including the extent to which flexibilities might be appropriate with respect to, inter alia, the length of the transitional period, the level of final coverage and the degree of asymmetry for both under GATT Article XXIV. More specifically, the European Communities are open to consider separate and differentiated, i.e. lower, thresholds for developing countries and least developed countries, as proposed in the submission by the ACP-countries (TN/RL/W/155). Moreover, longer transition periods might be necessary to facilitate market building and consolidation through gradual openness to trade in weak and vulnerable developing countries, taking into account their specific needs and constraints. The European Communities would thus like to confirm in the negotiations these specific justifications for developing country parties to RTAs to depart, where necessary, from the general rule of ten years maximum.*

There is thus evidence of a good deal of public commitment by both the EU and the ACP Group to coordinate positions at the WTO. A joint ACP-EU bloc within the WTO has, in theory, the potential to be a formidable negotiating force representing well over one-half of the entire WTO membership. In practice, however, the positions being pursued by the EU and the ACP Group in respect of RTAs are at variance (see Chapter 3).

Lessons from GATT / WTO practice

Finally, it is worth reiterating the above point that both the EC and the ACP countries have argued on several occasions that the non-reciprocal Lomé agreements themselves were in full compliance with these same GATT/WTO rules. As the Turkey Textiles Panel observed:

> *In the history of GATT, except in the case of the 1994 customs union between the Czech Republic and the Slovak Republic, the contracting parties were never able to conclude whether or not a regional trade agreement was fully compatible with GATT. Today, under the WTO, members have yet to conclude that a regional trade agreement is in full compliance with the WTO Agreement. In short, virtually all working party reports on regional trade agreements have been inconclusive (*Turkey Textiles Panel Report, para. 9.107*).*

Nevertheless, to the extent that the WTO's dispute settlement system remains operational – and its competence over issues of compliance of national measures with relevant GATT rules on RTAs has been irrefutably established – the EU and the ACP countries could ignore the legal framework set by the WTO on RTAs only at their own peril.

Summary

This chapter has shown that the commitment to establish WTO-compatible EPAs is an extremely difficult and uncertain undertaking. There is a great risk that it can be achieved only at the cost of the ACP countries sacrificing several of their rights to SDT within the WTO. Of the apparent actions that might be taken to enable this commitment to be met only a modification of Article XXIV seems a possible option. Neither a waiver or under the GSP system could be considered a possibility. While it is not necessarily a negative thing for ACP countries to support the EU position in the Doha Round, this should nonetheless be informed by an accurate evaluation of their own domestic and regional priorities.

Furthermore, it is obviously difficult to ascertain the outcomes of these issues in the actual EPA negotiations except to state that much will depend on the skilfulness of the negotiators themselves and how attuned they are to their relevance. The bottom line should be that there ought to be consistency with positions taken regarding issues like IPRs in the Doha Round negotiations and that negotiators have a comprehensive focus of the international legal instruments of relevance and their provisions. In the area of GIs, the EU is likely to use the EPA negotiations to establish precedents and support for its positions at the WTO, and which it has employed previously, such as in its agreement with South Africa. It is well to remember that the agreement with South Africa goes beyond the existing TRIPs disciplines in recognizing the exclusive rights that EU producers have over certain GIs of immense economic benefit. Annex 2.1 below addresses these issues.

Annex 2.1
EPAs and the regime of Intellectual Property Rights over plant genetic resources

Intellectual Property Rights (IPRs) are a means of protecting and rewarding innovation. They include patents, trademarks, industrial designs and geographical indications (GIs). The core of the problem with IPRs lies in the balancing of private and public interests, for example, allowing an investor to recoup the costs of their research and the resulting product, but at the same time, safeguarding the interests of the public from exploitation motivated purely by profit. To a large extent, this is an issue that has divided developing from developed countries, a scenario that is repeatedly witnessed in debates at the WTO's Council on Trade Related Aspects of Intellectual Property Rights, the World Intellectual Property Organization (WIPO) and other competent fora. Without doubt, it continues to be an issue in the ongoing negotiations on EPAs between the EU and ACP countries. Although it is not explicitly on the agenda for negotiations by the EU, some regions, such as ESA, have included certain IPRs-related issues such as technology transfer in their negotiating mandate. Without question, the issue is bound to come up in the negotiations, whether in the form of enhanced IPRs protection (as it has in FTA negotiations by the EU with South Africa in the case of the protection of the names of certain wines and spirits), or in the form of new and improved regimes for the protection of plant varieties (as is required by Article 27.3(b) of the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (TRIPS), to whose implementation both the ACP and the EU have committed themselves in the *Cotonou Agreement*).

The aim of this section is twofold: (i) to present an overview of the existing framework of international legal instruments that regulate IPRs (particularly those relating to agriculture) and concepts of which EPA negotiators may wish to take note of or borrow from; and (ii) to explain the IPRs-related issues of relevance to the EPA negotiations by drawing lessons from previous agreements negotiated by the EU and the positions taken in the Doha Round. While inconclusive, this chapter will highlight the points of concern for EPA negotiators from the ACP region: (i) that IPRs are an issue of immense economic value and therefore of central interest to the EU; (ii) that despite their precise mention in the EU's negotiating mandate, they should nevertheless prepare themselves to respond to demands relating particularly to enhanced IPRs protection (the so-called "TRIPs-plus" demands); and (iii) that what they agree to in the negotiations regarding technology transfer, the protection of plant varieties and on other IPRs-related issues, will have an important impact on their quest for economic development, the improvement of agricultural productivity and food security.

The international framework for the protection of IPRs

The TRIPs Agreement

TRIPs is a product of the Uruguay Round. It entered into force in 1995, as part of the WTO single undertaking. Its main objective is to protect and enforce IPRs and to ensure that they contribute to the promotion of technological information and transfer. Of particular relevance in the context of plant genetic resources is Article 27.3(b) of the *TRIPs Agreement*, which makes it mandatory for WTO members to provide for the protection of plant varieties through patents, an effective *sui generis* system, or a combination thereof. This *sui generis* option provides valuable policy space for developing countries to draft national legislation that accords with their national agricultural development priorities and at the same time meets their WTO commitments.

This provision is problematic owing to difficulties in the interpretation of the precise meaning of "plant varieties". Developed countries have sought a broader meaning to widen the range of protection for biotechnological products, while developing countries generally relying on a traditional agricultural sector have sought a narrower interpretation of the term in order to allow for an unrestricted availability of plant species. The difficulty with the implementation of this provision lies in the absence of a mutually agreeable definition of "plant variety" among WTO members and the inconclusiveness of the ongoing discussions on the issue. Another issue of relevance in the *TRIPs Agreement* is Article 66.2 on technology transfer which requires developed countries to "provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer to least-developed country members in order to enable them to create a sound and viable technological base." Article 46 of the *Cotonou Agreement* binds the parties to adhere to the TRIPs Agreement (especially, in this case, Article 66.2) and to deepen their cooperation in IPRs in general.

The UPOV Convention

The International Union for the Protection of New Varieties of Plants (UPOV) is an intergovernmental organization established in 1961 to coordinate the implementation of plant breeders' rights. The *UPOV Convention* came into force in 1961. It was revised in 1972, 1978 and 1991. The 1991 *UPOV Convention* entered into force in April 1998. The 1978 version, to which a few developing countries are members, is closed to further signatories. It is generally held that the 1991 version is stricter in its recognition of breeders' rights as opposed to the so-called "farmers' privilege" that was implicitly allowed in the 1978 version, and has proven less attractive to developing countries.

With regard to UPOV, the main controversial issue relating to rural agriculture lies in arriving at an acceptable definition of the scope of the "private and non-commercial" exception under Article 15 of the 1991 UPOV Convention. This provides that a "breeder's right shall not extend to acts done privately and for non-commercial purposes." The question is whether the exchange of seeds or propagating material from a protected variety (i.e. a variety for which a breeder's right has been granted) and without the right holder's consent is lawful in view of certain uses of the exchanged material.

It is noteworthy that Article 14 of the *UPOV Convention* gives an overview of acts that are deemed to be within the rights of a breeder. It is also necessary at this point to remember that a "breeder's right" in this context is a form of a *sui generis* system of protection for plant varieties in terms of Article 27 (3) (b). Article 15 of the 1991 *UPOV Convention* provides several exceptions including acts done privately and for non-commercial purposes at subsection (1)(i), acts done for experimental purposes and acts done for the purpose of breeding other varieties. Given the limited scope of seed exchanges by small-scale farmers in a certain territorial ambit such as a rural community, one might consider that these acts are both of a private nature confined within that ambit, and for non-commercial purposes, especially given the economic conditions of the farmers.

Not all ACP countries have legislation in place to protect plant varieties. As stated above, TRIPs requires all WTO members to come up with a regime for plant variety protection. Article 27.3(b) gives three options: patents, a *sui generis* system, or some combination of the two. The UPOV system has been characterized as a *sui generis* system, in the meaning of Article 27.3(b), and is heavily portrayed as the ideal way of complying with this TRIPs commitment. It is probable that ACP countries that do not already have a plant variety protection regime in place could be compelled to draft domestic IPRs legislation that mirrors UPOV, especially bearing in mind that in Article 46(6), EU assistance could include the "preparation of laws and regulations for the protection and enforcement of intellectual property rights."

The International Treaty on Plant Genetic Resources for Food and Agriculture

The International Treaty on Plant Genetic Resources for Food and Agriculture (the "Treaty") is a relatively new feature in the international legal landscape, having come into force in June 2004, with unique provisions and thereby potential implementation challenges. The negotiations on the Treaty were arduous and lengthy. By Resolution 3/2001, the Treaty was finally adopted on November 3, 2001 by the FAO Conference at its 31st Session after a seven-year negotiating process.

The Treaty has a broad sweep and covers "plant genetic resources for food and agriculture". It provides a framework through which plant genetic resources could be both conserved and used in a sustainable manner. One of its most innovative and novel provisions is on farmers' rights. It is the first binding international Treaty to recognize such rights and therefore constitutes a major step in their actual implementation. At Article 9.1, the Treaty recognizes:

> *"the enormous contribution that local and indigenous communities and farmers of all regions of the world, particularly those in centres of origin and crop diversity have made and will continue to make for the conservation and development of plant genetic resources which constitute the basis of food and agriculture production throughout the world." In effect therefore, the Treaty puts traditional farmers' rights on an equal footing*

with modern breeders' rights. Quite importantly however, the subsequent provision vests the responsibility for realizing farmers' rights in national governments and suggests that the framework for the protection and promotion of such rights could be in any appropriate form "subject to … (a country's) national legislation."

The Contracting Parties are therefore at liberty to design legislative and implementation mechanisms that accord farmers the protection of relevant traditional knowledge, their right to equitably participate in benefit-sharing of plant genetic resources, and their right to participate in national decision-making on the utilization and conservation of plant genetic resources. Subject to national law, the Treaty grants farmers extensive rights to "save, use, exchange and sell farm-saved seed/propagating material." The reference to "national governments" and "subject to national legislation" and "subject to national law" in Article 9 of the Treaty should underline the primacy of implementing the commitments of the Contracting Parties by formulating appropriate laws at the national level.

In Articles 10 through 13, the Treaty also provides for a Multilateral System of Facilitated Access and Benefit Sharing, commonly known as "the Multilateral System". It was designed to obviate the need for bilateral arrangements between countries on issues of access to plant genetic resources. The Multilateral System is a core feature of the Treaty and deserving of particular mention because it has important implementation challenges of its own. The Treaty does not deviate from the accepted principles of international law on the sovereign rights of states, and therefore recognizes, "the sovereign rights of states over their own plant genetic resources for food and agriculture, including the authority to determine their access to those resources rests with national governments and is subject to national legislation (Article 10)." The Multilateral System facilitates access of plant genetic resources for food and agriculture, and the fair and equitable sharing of the benefits of utilizing these resources in a manner that is complementary and mutually reinforcing.

The list of crops subject to the Multilateral System is spelled out at Annex I to the Treaty and includes 35 food crops and 29 forages. Access to the listed crops is subject to certain conditions as listed in Article 12.3 of the Treaty. During the negotiations, one of the most contentious of these conditions was that concerning IPRs over genetic resources. The provision in the Treaty now reads: "Recipients shall not claim any intellectual property or other rights that limit the facilitated access to the plant genetic resources for food and agriculture, or their genetic parts or components, in the form received from the multilateral system." As with many provisions in international treaty law, this phrase is subject to various, even conflicting interpretations. One may correctly say that the provision means that no intellectual property rights of any sort can be claimed since such rights per se will limit access. On focusing on the phrase "that limit the facilitated access", however, another interpretation may be that intellectual property rights could be obtained provided that such rights do not limit facilitated access as envisaged in the Treaty. There is also bound to be controversy over the precise meaning and scope of the "in the form received" phraseology in the same Article 12.3(d). Clearing up these and numerous other ambiguities in treaty interpretation is part of the mandate of the Governing Body, and it is likely to be a very involved task.

According to Article 12.4, facilitated access of plant genetic resources shall be provided on the basis of a standard Material Transfer Agreement (MTA) to be adopted by the Governing Body. The task of developing the standard MTA has commenced. In the first meeting of the Commission on Genetic Resources for Food and Agriculture (CGRFA), acting as Interim Committee for the Treaty, held on 9-11 October 2002, a regionally balanced Inter-governmental Expert Group was established to develop the standard draft MTA. At the same meeting, the terms of reference for this Expert Group were negotiated. The next meeting for of the Interim Committee is slated for late next year, and it is hoped that that meeting will follow up on the work of the Expert Group. Although the Treaty does not provide guidance on the exact content of an MTA or the formula for benefit sharing, it is expected that the main provisions of the MTAs will devote attention to IPRs and benefit sharing.

The provisions on benefit sharing at Article 13 also have a novel feature at subsection (d) concerning the sharing of monetary and other benefits of commercialization. According to this provision, a recipient that commercializes a product that is a plant genetic resource as envisaged by the Treaty and that is accessed from the Multilateral System is obligated to share these profits fairly and equitably on the basis of a MTA. Such an individual is also required to pay royalties that shall be used by the Treaty Governing Body as part of its funding strategy for benefit sharing. The provision also specifies that it is up to the Governing Body to determine the level, form and manner of payment, but that such payment shall be in line with commercial practice.

At Article 15, the Treaty provides a framework for ex situ collections of plant genetic resources held in trust by International Agricultural Research Centres (IARC), of the Consultative Group on International Agricultural Research (CGIAR), and other relevant international organizations. It invites CGIAR centres to sign agreements with the Treaty Governing Body to place their ex situ collections under the scope of the Multilateral System.

As explicitly required by Article 4 of the Treaty, “Each Contracting Party shall ensure the conformity of its laws, regulations and procedures with its obligations….” Article 6.1 also reiterates this by stating that “(t)he Contracting Parties shall develop and maintain appropriate policy and legal measures that promote the sustainable use of plant genetic resources for food and agriculture.” Necessarily, therefore, implementing the Treaty at the national levels will entail reformulating national policies and laws in order to conform to the Treaty’s requirements. Such legislation will need to put into effect the requirement in Article 9.2 on farmers’ rights. The FAO has been providing legal advice to countries that wish to draft such legislation.

It is well to remember that in general, international law requires full compliance with negotiated Treaty obligations, save for provisions to the contrary, in the Treaty itself. Since the Treaty does not have any such provisions, compliance is expected from Contracting Parties. The first meeting of the Interim Committee discussed the Treaty’s draft compliance procedures. Together with the more intractable issue of addressing situations of non-compliance, this will also be on the agenda of the first Governing Body meeting as required by the Treaty’s Article 21. The use of “shall” in Article 21 means that the adoption of compliance procedures at the first meeting of the Governing Body is a mandatory requirement. The challenge on Contracting Parties is therefore to prepare themselves for compliance with their Treaty commitments. This essentially translates into pressure on the need to develop the capacity to meet their obligations and utilize their rights under the Treaty. For developing countries, and countries with economies in transition, this is a particularly onerous task.

Article 21 provides some guidance on what the procedures and mechanisms of non-compliance should be. It states that such procedures and mechanisms “shall include monitoring, and offering advice or legal assistance, when needed, in particular to developing countries and countries with economies in transition.” Article 21 is not an entirely unique provision in recent international treaty law, as it has featured in various formulations in some recent international treaties. However, it is particularly important that it anticipate and provide assistance to developing countries and countries with economies in transition. Since the main objective of the procedures is to promote compliance and to address the difficulties of Contracting Parties, it also requires that such procedures be “cooperative and effective”, suggesting an emphasis on the need to resolve situations of non-compliance in an amicable way, and possibly, with preference being given to dialogue. The reference to “legal advice or legal assistance, when needed” is, however, novel in contemporary international treaty law. The Governing Body will be expected to formulate modalities on how and by whom such legal assistance and advice will be made available, but the objective of this assistance is clearly to be the resolution of compliance difficulties. The use of the phrase “shall include monitoring…” in this Article should mean that the list of compliance procedures given is not meant to be exhaustive.

The coming into force of the *International Treaty on Plant Genetic Resources for Food and Agriculture* has inspired countries to prepare laws to protect plant varieties and farmers rights. This inspiration comes from the fact that under patents, farmers would be prohibited from using seeds from patented varieties without the consent of the patent holder. As seeds saved by farmers and exchanged among them can account for up to 80-90 percent of the total seed requirements in developing countries, a patent system would severely constrain subsistence farming and food security, hence the need for workable *sui generis* systems.

The UN Convention on Biological Diversity (UNCBD)

The UN Convention on Biological Diversity (UNCBD) was adopted at the Rio Summit in 1992 and entered into force in 1993. The UNCBD aims at the conservation of biodiversity by sustainable utilization of genetic resources, especially by the biotechnology sector, and the recovery of economic benefits of such by its use into conservation activities, particularly in developing countries. Article 15.1 provides that: “Recognizing the sovereign rights of States over their natural resources, the authority to determine access to genetic resources rests with the national governments and is subject to national legislation.” The emphasis on national sovereignty is balanced by the recognition that the conservation of biological diversity is a common concern of humankind and by the obligation of each Contracting Party “to endeavour to create conditions to facilitate access to genetic resources ... and not to impose restrictions that run counter to the objectives of the Convention” in Article 15.2.

In addition to the UNCBD, Agenda 21, a non-binding programme of action for sustainable development, was adopted at the Rio Summit. It calls on governments to foster traditional methods and the knowledge of indigenous people and their communities, to share the benefits of biological resources, including biotechnology, and to develop national strategies for the conservation of biodiversity, the sustainable use of biological resources and the safe transfer of biotechnology, particularly to developing countries.

In Article 46(2) of the Cotonou Agreement, the parties “underline the importance of adherence to the Convention on Biological Diversity” a requirement that, in view of its recognition of sovereignty over natural resources, should serve to underline any discussions on IPRs in the context of the EPAs.

EPAs and IPRs

IPRs are re-affirmed in Article 46 of the *Cotonou Agreement* and are defined to cover “patents, including patents for bio-technological inventions and plant varieties or other effective *sui generis* systems.” This is in fact a more rigid conception of IPRs than that sought by WTO members in the context of the Doha Round of trade negotiations, although it was agreed to before the commencement of the Doha Round in 2001.

Despite no explicit mention of IPRs in the EU’s negotiating directives, it does not preclude the EU from raising the issue during EPA negotiations. Further, as provided in Article 46(4) of the *Cotonou Agreement*, the EU and the ACP countries “may consider the conclusion of agreements aimed at protecting trademarks and geographical indications for products of particular interest of either Party.” Indeed the EU will seek to “deepen” cooperation with ACP countries on IPRs and related issues through the EPAs. Article 46(6) of the *Cotonou Agreement* mandates this kind of broad cooperation in the following terms:-

> *The Parties further agree to strengthen their cooperation in this field (of IPRs). Upon request and on mutually agreed terms and conditions cooperation shall inter alia extend to the following areas: the preparation of laws and regulations for the protection and enforcement of intellectual property rights, the prevention of the abuse of such rights by right-holders and the infringement of such rights by competitors, the establishment and reinforcement of domestic and regional offices and other agencies including support for regional intellectual property organizations involved in enforcement and protection, including the training of personnel.*

Several reasons therefore justify why ACP countries should prepare themselves to offer responses to the EU on the question of IPRs, even though it has not explicitly arisen in the EU’s negotiating mandate. First, as stated above, the Cotonou Agreement clearly commits both parties to deepen their commitments and cooperation in IPRs. There is no better occasion for them to do so than in the ongoing negotiations on EPAs. In anticipation, some negotiating regions, such as ESA, have already included “trade-related issues” in their negotiating mandate. According to the ESA mandate:

> *Negotiations on trade-related rules should be based on the provisions of the Cotonou Agreement (in particular Articles 44 to 52) and the need to ensure increased co-operation in these areas, enhanced capacity building and technical assistance. ESA negotiators will stress the fact that there is a need to build adequate legal and institutional capacities in the ESA region before any disciplines in these areas can be envisaged for negotiations.*

Secondly, as evident from the aggressive position taken by the EU in relation to the post-Doha discussions on extending coverage of geographical indications (GI) protection to products other than wines or spirits, the EU has particular interests in GIs, especially over certain products of interest such as wines, spirits and cheeses. If ACP countries want a sampling view of what the EU may require of GIs, they should look at the EU-South Africa Agreement on Wines and Spirits.

The Agreement provides better protection for EU appellations of origin than the protection available in the TRIPs Agreement. In the Agreement, South Africa agreed to provide exclusive protection for EU wines such as “Champagne”, “Chianti”, “Mosel”, “Port” and “Sherry.” As concerns “Port” and “Sherry”, South Africa agreed also to refrain from using these terms for their own wines after transitional periods of 12 years in its domestic market, and after five years in export markets, with the commencement period for protection being 1 January 2000.

The Agreement also provides for the elimination of conflicting or misleading trademarks, especially those that may confuse buyers on the origin of wines. In the spirits sector, all European traditional names such as “Grappa” and “Ouzo” will be protected after a transitional period of five years.

Thirdly, in negotiations with the United States, developing countries have often been faced with “WTO-Plus” intellectual property demands through bilateral talks, such as in the Free Trade Area of the Americas (FTAA) and the North American Free Trade Agreement (NAFTA) negotiations. This is something ACP countries might expect from the EU, particularly in recalling the experience of South Africa in its negotiations with the EU. While Article 24(1) of the TRIPS Agreement requires WTO members to work to increase the general level of protection for GIs, it does not specify how this should be accomplished. There are significant possibilities that the EU may want to use the EPAs to accomplish this goal.

Fourthly, since most ACP countries are in the process of meeting their commitments under Article 27.3(b) of the TRIPs Agreement, it is possible that the issue may arise in the negotiations with the EU, especially since they have already committed themselves to adhere to this and other international IPR regimes (in Article 46(1), 46(2) and 46(3) of the Cotonou Agreement). This would have implications on the regime that they create for the protection of plant varieties as required by TRIPs, and whether this regime would be patent-oriented, a *sui generis* system, or some combination thereof. It may be expected, for example, that the EU will demand a proper plant breeders’ rights regime in the mould of UPOV 1991 for ACP countries without one in place already.

An issue on which ACP countries, particularly the LDCs, could be demandeurs in the EPA negotiations is technology transfer. According to Article 66.2 of the TRIPs Agreement, “Developed country members shall provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer to least-developed country members in order to enable them to create a sound and viable technological base.” This is an issue ACP countries could take up as a negotiated development supportive package in the context of the EPA negotiations, especially since both parties to the Cotonou Agreement recognize the linkages with the Doha Development Agenda. The ESA has already included it in its negotiating mandate, demanding that the parties to the EPA “negotiate a programme which will allow the transfer of science and technological information and knowledge required to enhance the trade and development capacities of ESA countries.”

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Chapter 3
Food security, EPAs and lessons from relevant EU trade agreements

Introduction

The specific focus of this chapter is to pose the question of the potential role of EPAs in supporting food security in ACP states. It assesses the current dynamic of ACP–EU trade, the effects that the preferences have had on the value chains associated with ACP exports and the extent to which this relationship may change in the coming years as a result of “preference erosion”. In this way it complements the parallel chapters on the effects of the CAP reform and EU enlargement on the ACP, the WTO dimension of the ACP–EU relationship and on the challenges facing the ACP in the effective management of their fisheries.

3.1 The centrality of food security

Trade is not a goal in its own right; its objective is to allow countries to enjoy a higher level of welfare than would be possible without it. Similarly, trade policy is not created in isolation. It needs to support the economic objectives of the countries concerned. In the case of the ACP–EU partnership, enhanced food security is central. This point needs to be emphasized frequently.

To reach the Millenium Development Goals (MDGs), most ACP countries will have to significantly step up efforts towards poverty and hunger reduction. A particular focus on food security in the context of poverty reduction strategies is indispensable due to the damaging consequences of hunger and malnutrition on human productivity. Indeed, recent evidence demonstrates that hunger has severe negative effects on the productivity of individuals and the growth rates of countries. FAO’s work on the links between hunger and economic growth suggests that for sub-Saharan Africa, the economic and social cost of hunger in terms of lost productivity, illness and death, is high. Rough estimates show that countries in this region could have attained an average per capita GDP level of US$2 200 in 1990 if undernourishment had been eliminated starting in 1960. This should be compared to the region’s average GDP per capita of only US$800 in the 1990s.

Long-term trends in food security and poverty indicators have generally been positive for the developing countries as a whole. However, improvements have been too slow and highly divergent across countries and regions. In particular, the ACP countries have not participated fully in the progress achieved. Table 3.1 presents FAO’s estimates of the number and percentage of undernourished people in developing countries and ACP countries, from 1969-1971 to 1999-2001. The data include 100 developing countries, as well as 48 ACP countries out of a total of 79. Estimates cover 40 out of 48 ACP countries in Africa, but only seven out of 16 ACP countries in the Caribbean and one out of 15 in the Pacific (Papua New Guinea). However, in terms of population, the estimates cover 93 percent of the population of the ACP countries in Africa, 96 percent in the Caribbean and 66 percent in the Pacific.

For the developing countries as a whole, the last three decades have seen a decline in the percentage of the undernourished people in the population from 37 percent in 1969-71 to 17 percent according to the most recent estimates, while the total number of undernourished people fell from 958 million to 798 million. Unfortunately, the 48 ACP countries covered by the estimates have not followed a similar trend: the prevalence of undernourishment declined slightly from 34 to 32 percent of the population, while the total number of undernourished actually increased from 98 million to 208 million.

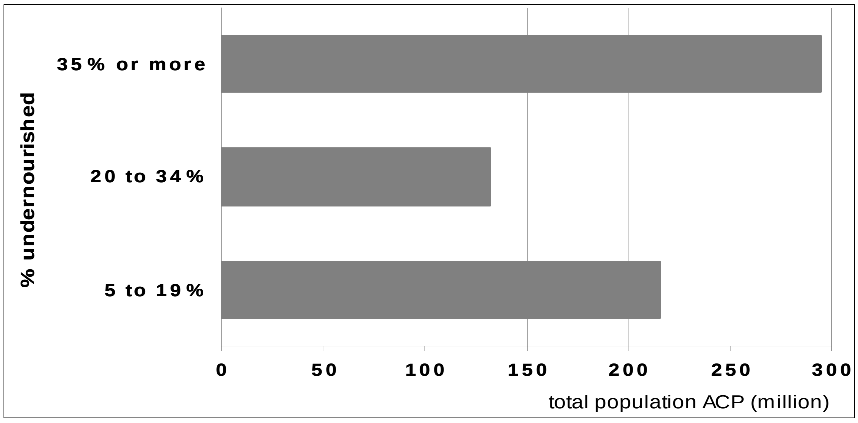
Three decades ago, the ACP countries accounted for 10 percent of the undernourished population in the developing countries; by 1999-2001 this share had increased to 26 percent. Only 13 of the ACP countries covered by the estimates saw the number of undernourished people decline from 1990-92 to 1999-2001; and only eight saw a decline in undernourishment during both the first and the second part of the decade.

TABLE 3.1: PREVALENCE OF UNDERNOURISHMENT

	Proportion of undernourished in total population (percent)				
	1969-71	1979-81	1990-92	1995-97	1999-2001
Developing countries	**37**	**28**	**20**	**18**	**17**
ACP countries	**34**	**35**	**34**	**35**	**32**
ACP countries in Africa	**35**	**36**	**35**	**35**	**33**
ACP countries in the Caribbean	**26**	**19**	**28**	**32**	**24**
ACP countries in the Pacific	**35**	**24**	**25**	**27**	**27**
	Number of people undernourished (millions)				
	1969-71	1979-81	1990-92	1995-97	1999-2001
Developing countries	**957.6**	**920.0**	**816.6**	**779.7**	**797.9**
ACP countries	**98.2**	**131.2**	**174.7**	**203.7**	**207.6**
ACP countries in Africa	**91.8**	**125.6**	**165.6**	**192.5**	**198.4**
ACP countries in the Caribbean	**5.5**	**4.9**	**8.2**	**10.0**	**7.9**
ACP countries in the Pacific	**0.9**	**0.7**	**0.9**	**1.2**	**1.3**

Note: The estimates include 100 developing countries and 48 ACP countries: 40 in Africa, 7 in the Caribbean and one in the Pacific.
Source: FAO and World Bank.

FIGURE 3.1: TOTAL POPULATION IN ACP COUNTRIES BY UNDERNOURISHMENT CATEGORY



Source: FAO

The magnitude of the undernourishment problem in the ACP countries is also illustrated in Figure 3.1, which shows how the population is distributed among countries with different prevalence of undernourishment: none of the countries has an incidence of undernourishment of less than 5 percent while the majority of the ACP country population lives in countries with at least 20 percent of the population undernourished. Close to 300 million people live in countries with an incidence of undernourishment above 35 percent.

A concern for food security should be central to any evaluation of alternative approaches to trade policy. ACP states in general depend relatively highly on trade for their food security. Their economies are relatively open. Many are reliant upon trade in agricultural products to earn export revenue and on food imports to satisfy domestic consumption. Some states rely on trade for both agricultural exports and imports.

The EU is the ACP's main trade partner for both agricultural and non-agricultural products. It took 31 percent of ACP export in 2003, compared with 27 percent of United States imports, and supplied 29 percent of ACP imports (DG Trade 2004). These figures, based on the total value of trade, are heavily influenced by the direction of a few high-value items (e.g. Nigeria's oil is exported mostly to the United States). If one looks at the range of products exported, the dominance of the EU as an ACP market is even more marked.

Moreover, food security is central to the livelihoods of the poor in ACP countries. It is important that the policy changes incorporated into EPAs support their livelihoods, for example, by facilitating trade from which poor people can benefit as producers or consumers. FAO has identified a range of ways in which regional integration schemes can foster pro-poor food security. These include trade facilitation, the harmonization of national agricultural policies and support to national Special Programmes for Food Security (FAO, 2003a, p. 61).

3.2 ACP–EU trade

The broad picture

If one looks at nominal figures for recent trade growth between the ACP and the EU the picture is quite bright (Figure 3.2). Exports increased by 67 percent and imports by 52 percent between 1995 and 2002, so that by the end of the period the ACP had a tidy merchandise trade surplus with Europe. By 2002, agriculture accounted for just under one-quarter of ACP exports to the EU but only one-eighth of its imports (see Figure 3.2)

In practice, however, when account is taken of the growth in EU trade with other regions, the ACP have been marginalized. Their share of EU imports between 1995 and 2002 fell from 3.4 to 3 percent.

An important distinction emerges between agriculture and non-agriculture when looking at the ACP's share of EU imports. The main reason that the ACP's share of total EU imports has slumped is that the non-agriculture share is tiny and has fallen badly. The share of agriculture, by contrast, is much greater and has fared better (Figure 3.4).

This re-emphasizes the point concerning food security and agriculture being central to the EPA negotiations. Whereas the ACP are marginal suppliers of the EU in manufactures, they account for a significant one-eighth of all EU imports of agricultural products.

Differential agricultural performance

One reason for the relative importance of agriculture is that the Cotonou Agreement provides preferences that are particularly commercially valuable on a number of CAP items for which trade policy is restrictive. One can divide the ACP's agricultural exports into three groups:

- traditional products, such as beverages, that are exported through a relatively undifferentiated, liberal world market;
- other traditional exports such as beef and sugar that are exported to markets heavily influenced by agricultural protectionism, notably but not exclusively in the EU;
- non-traditional products such as horticulture and flowers that are exported to markets, notably but not exclusively in the EU, that are characterized by some protectionism.

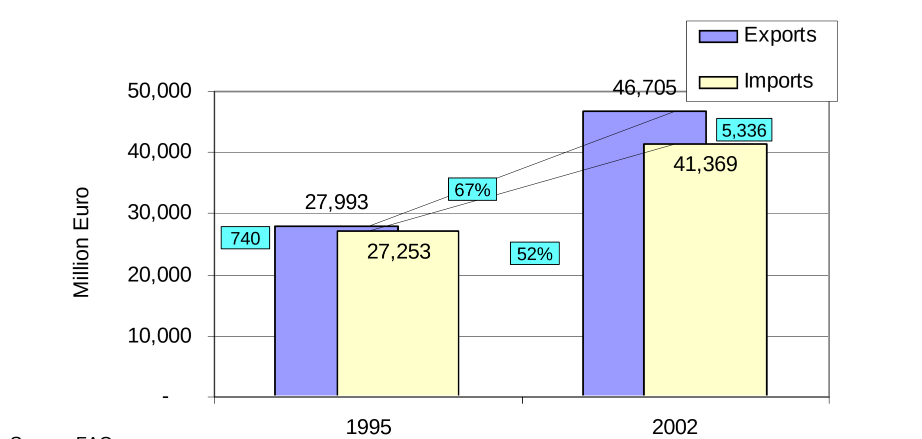
These three groups have had very different experiences on the world market. The difference is illustrated in Figures 3.4 and 5, which compare the net barter terms of trade (for sub-Saharan Africa only – not for the full ACP) for various agricultural export products and several imports. The picture painted in Figure 3.4 for the net barter terms of trade between traditional beverage exports and cereal imports is a familiar one.

Apart from a recent surge for tea, the trend over the period has been towards stability or decline. By the turn of the century a tonne of cocoa exports could fund only around two-thirds of the cereal imports that could have been purchased in 1980.

The picture for the other two categories of export is quite different (Figure 3.6). Only the pineapples and grapefruit trade have seen deterioration. Flowers and beans have both moved sharply in a favourable direction. By the turn of the century, a tonne of flower exports would buy around 25 percent more cereals than it would in 1990. For beans the improvement was one-tenth. Sugar has improved slightly, and beef has maintained its position after a mid-1990s trough.

Cotonou is crucial to this difference between the categories of product. As will be explained below, it has contributed to ACP exporters obtaining a part of the economic rent accruing as a result of CAP protectionism. The implications of this and of any change either to the CAP or to other influences on European agricultural supply and demand, such as enlargement or to the EU–ACP trading relationship; need to be taken into account in terms of their impact on food security.

FIGURE 3.2: RECENT TRADE: GROWTH



Source: FAO.

FIGURE 3.3: RECENT TRADE: SECTORAL COMPOSITION

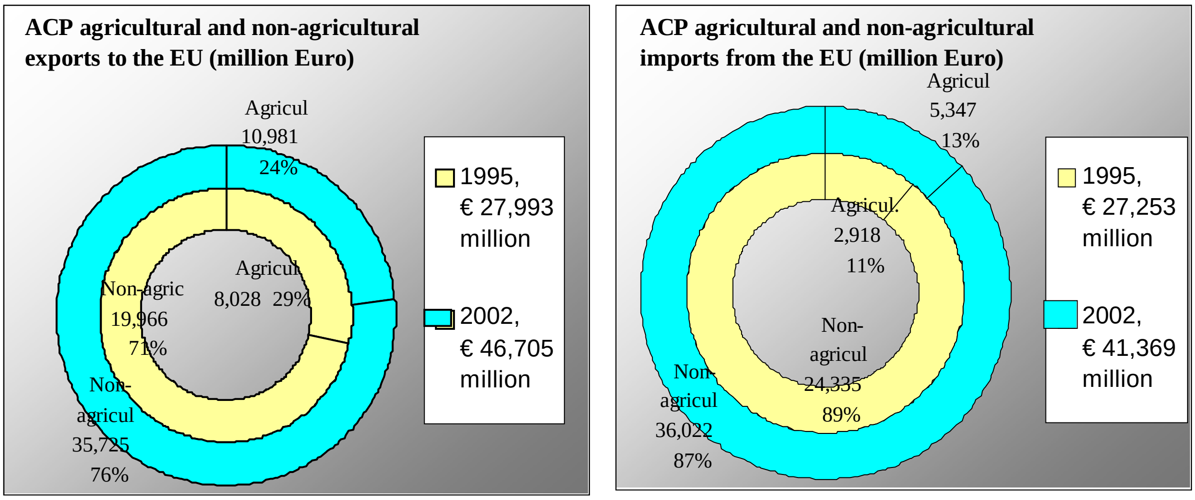
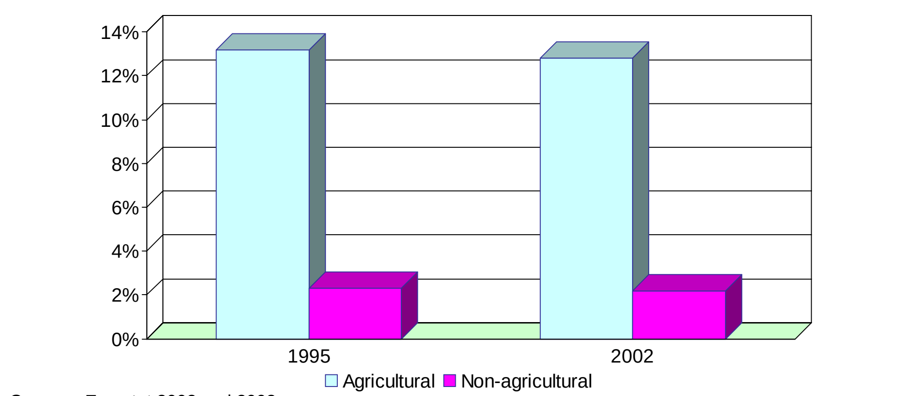
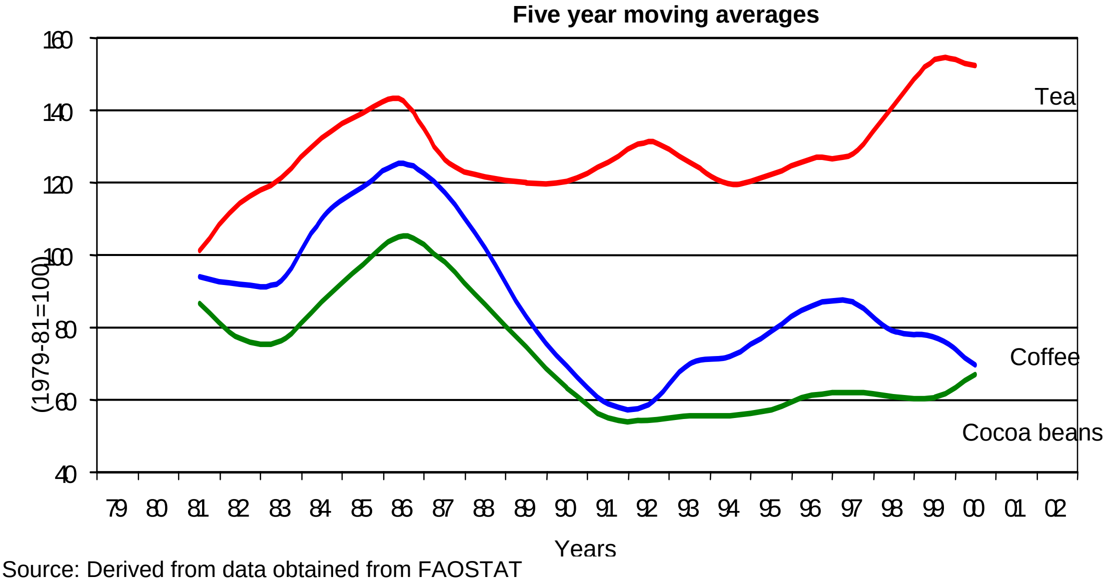


FIGURE 3.4: THE IMPORTANCE OF AGRICULTURE: SHARE OF EU IMPORTS



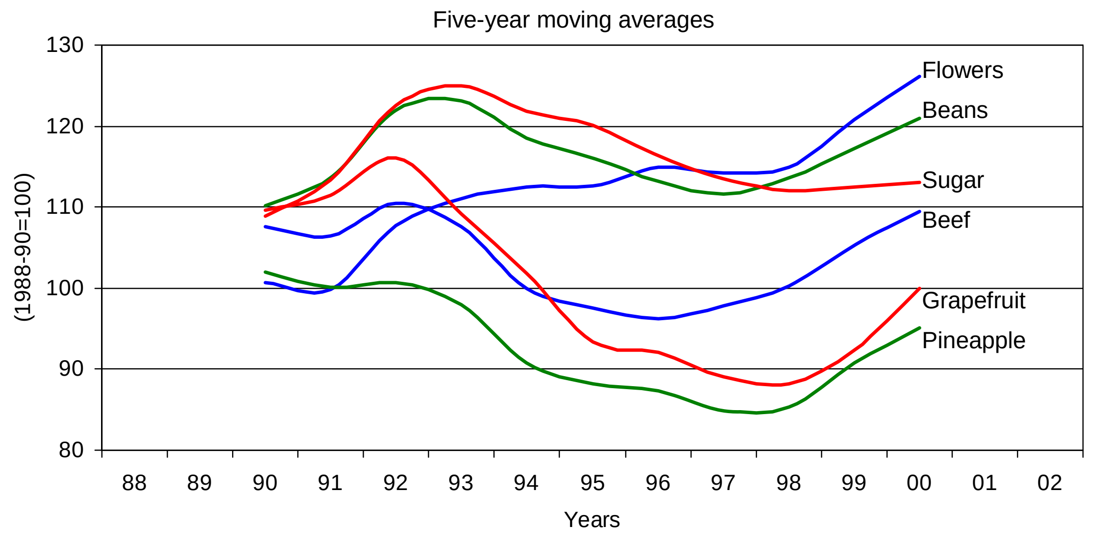
Sources: Eurostat 2002 and 2003.

FIGURE 3.5: NET BARTER TERMS OF TRADE: MOST IMPORTANT SSA EXPORTS AND CEREAL IMPORTS



Source: Derived from data obtained from FAOSTAT

FIGURE 3.6: NET BARTER TERMS OF TRADE: MOST IMPORTANT SSA EXPORTS AND CEREAL IMPORTS



Source: Derived from data obtained from FAOSTAT and Eurostat 2002 and 2003.

The link to Cotonou

To understand the economic effects of EPAs it is important to clearly understand how current trade preferences have had an economic impact on those ACP countries that have been able to take advantage of them. In most cases, the main constraint that has limited the ACP's uptake of the EU's agricultural preferences is supply capacity. This may seem surprising given the number of restrictions that apply to Cotonou's provisions for agricultural items covered by the CAP. This is not to suggest that there are no causes for ACP complaint that the letter of Cotonou fails to live up to its spirit.

Nonetheless, as explained in the next two sections, the commercial effects of a preference are not always easy to judge simply from looking at the text of the trade agreement. Trade preferences that may seem very generous on paper may turn out to be commercially worthless. Similarly, those that may seem to be hedged about with restrictions may be extremely valuable in the context of the product market concerned. The explanation for this paradox hinges upon the existence of what is termed in this chapter "trade policy rents".

How rents are created

Trade policy rents arise when a market is distorted but certain suppliers of imports receive preferential access. The purpose of the distortion is to enable domestic producers to sell goods that consumers would otherwise prefer to buy from foreign producers, whether because they are cheaper, of a preferred quality or some other reason. One way to do this is to subsidize the domestic producers, but this tends to be politically unpopular because it is visible and results either in higher taxes or lower government expenditure on other items. Another less visible and less politically costly way is to rig the domestic market so that consumers have to pay the higher prices at which domestic producers can compete. One of the fundamental mechanisms to achieve this is to impose protectionist trade barriers, which, by squeezing imports, restrict supply and maintain prices at higher levels than would otherwise apply. In some cases, these restrictions (and their price effects) are substantial. The principal intention of these distortions is normally to confer the rents on producers in the distorting state, but there is leakage – often through preferences. All of the OECD countries offer some form of preferential market access to certain developing countries.

In general terms, the protection–preference nexus makes sourcing imports from some suppliers more attractive than from others, but who gains what depends on the power distribution within a value chain. What is important is both the overall scale of the rent and the architecture of the rules that creates it.

Rents are most substantial in product markets that face such severe protectionism that it sharply restricts the possibility of importing from non-preferred sources.

This is the case, for example, with beef and sugar, for which the EU import tariffs are, respectively, 12.8 percent + €303.4/100 kg (beef) and €33.9/100 kg (sugar), equivalent to *ad valorem* tariffs of 94.5 and 116.2 percent, respectively.[1]

In the case of beef, all ACP countries are relieved entirely from the 12.8 percent *ad valorem* element, but this is of no relevance to most since they are unable to comply with regulations on foot and mouth disease (FMD). For the four southern African ACP countries that can comply (Botswana, Namibia, Swaziland and Zimbabwe), there is an extra preference, namely, that the specific duty is reduced to €24.2/100 kg.

For sugar, some ACP countries have country-specific quotas under the EU–ACP Sugar Protocol. They include the Republic of the Congo, Côte d'Ivoire, Madagascar, Malawi, Mauritius, Swaziland and Zimbabwe (as well as The United Republic of Tanzania and Uganda that do not have a surplus to export, and Kenya that has only recently resumed its exports). Under the Protocol the price received is related to the EU domestic price.

At the other end of the scale are items for which protection is so modest as to render any preferences of limited commercial value. For example, the tariff paid by non-preferred countries on exports to the EU of shelled almonds is only 3.5 percent, compared with preferential rates of 0-3.1 percent.

In the middle of the scale are commodity groups such as horticulture. EU tariffs are moderately high, for example, 12.8 percent for aubergines, so the duty-free access provided to a range of developing countries is significant. The advantage is available to many countries, and does not appear sufficiently large by itself to exclude totally non-preferred suppliers. The preference is insufficient to offset any substantial price uncompetitiveness on the part of producers or transporters, or obviously, any other failings in the fiercely rigorous supply chain required to move perishable items from a sub-Saharan African field to a European supermarket shelf within hours (Dolan *et al*., 1999).

How rents are distributed

Small rents almost certainly accrue to the importer/retailer/consumer end of the value chain. They do not influence purchasing decisions and are merely a windfall gain. Depending upon domestic market conditions, they are either retained by the importer, wholesaler or retailer or passed on to consumers. The distribution of large rents is influenced by the structure of the trade policy regime.

[1] The tariffs given are for raw cane sugar for refining (Combined Nomenclature (CN) code 17011110) and fresh or chilled boneless beef (CN 02013000). The *ad valorem* tariff equivalents were calculated using average world import unit values 1995–1997 for the Harmonized System 6-digit sub-heads into which the CN 8-digit codes fall.

In the most heavily protected sectors, preferences typically take the form of special quotas allowing some third parties to supply the high-priced market without paying the substantial import duties that either exclude other imports or drastically reduce their profitability. Sugar is the extreme example. One EU processor/distributor, Tate and Lyle, is substantially dependent on preferential sugar imports for its supplies, and in turn, is the monopsony buyer of exports to the EU under the Sugar Protocol. As a cane sugar refiner, the company needs access to imports since domestic European sugar production is beet. In addition, due to the high EU tariff, the financial viability of its operations depends on the continuation of supplies from preferred sources.

Since each beneficiary of the Sugar Protocol has a fixed quota, Tate and Lyle cannot play one off against another; if it cannot agree on a price with Mauritius, it cannot buy more from Zimbabwe, for example. Moreover, the Protocol requires the price paid to be related to the EU intervention price.

At the same time, as the owner of the main cane sugar refineries in Europe, Tate and Lyle is the only feasible purchaser of ACP exports to the EU. The alternative of exporting already refined sugar to the EU is not considered to be commercially viable on a substantial scale. The only but very partial alternative would be to sell outside the European harvesting season to EU beet refineries. But the beet and cane industries are in competition for market share.

Consequently, a range of market and institutional factors outside the formal trade agreement can influence the distribution of the benefit from preferences. It also follows that any change to these factors can alter the distribution and possibly has a greater effect on the interests of ACP socio-economic groups than any amendment to the formal trade agreement. A completely different power relationship, for example, will evolve from the EU’s “Everything but Arms” (EBA) initiative of 2001. Under this, all LDCs are able to sell unlimited quantities of any product including sugar but excluding arms to the EU. Implementation of the EBA has been partially deferred for bananas (until 2006), sugar and rice (until 2009), but in the interim the LDCs have duty-free access for an increasing quota of sugar and rice that is set at levels comfortably above past flows.

Unlike the Sugar Protocol, therefore, there are or will be no quantitative limits on the sugar that least developed African countries are able to export. But neither is there any built-in protection against the importers playing one supplier off against another and driving down the price received.

There are often measures that an ACP exporting state can use to favourably influence the distribution of rents. If market conditions allow, for example, this state can use the issuance of export licences to increase exporter bargaining power with importers. This tactic has been used to great effect by East Asian states for clothing exports under the Multi-fibre Arrangement (MFA), as well as for ACP banana exports.

3.3 The economics of EPAs

What will be in an EPA?

The basic arguments over the pros and cons of EPAs are over seven years old. They date back to the EU’s proposal at the outset of negotiations for a successor to Lomé IV that the trade regime be revised. The European Commission’s arguments for and against a change were set out in a Green Paper to which the ACP (and also civil society and research organizations) subsequently responded (EC, 1997). They included the points that a new regime should do more to foster the integration of ACP states into the world economy and should be more easily defensible in the WTO.

It was not possible to agree to such a new regime from the outset of the Cotonou Agreement. Instead, Cotonou extends the Lomé trade regime, but with the proviso that negotiations must commence for a successor regime that will come into effect in 2007. It is the scope of this post-2007 trade agreement that is the subject of the negotiations that began formally in September 2002.

The initial negotiating positions are set in very broad terms. The Commission obtained its draft negotiating mandate from the EU member states in June 2002 (EU Council 2002). The ACP agreed on their Guidelines for the Negotiations of Economic Partnership Agreements in July (ACP 2002). Neither document goes much beyond general principles.

EPAs will apply primarily but not only to merchandise trade. The EU also envisages a services dimension to the agreements. There will be modest, if any, improvements to ACP access to the EU market, not least because Cotonou already provides free access with only a limited number of exceptions. The most that the ACP could negotiate would be the removal of these exceptions. By definition, therefore, the agreements will be asymmetrical in the sense that many ACP countries will change their trade policy relatively more than the EU. This does not necessarily give any indication as to whether or not they are desirable economically for either partner.

In its negotiating mandate the European Commission has indicated that it wants ACP members of EPAs to:

- remove all quantitative restrictions (QRs) and reduce tariffs on goods imports over a transition period;
- remove “charges having equivalent effect” immediately;
- negotiate provisions in other areas, such as services.

Nonetheless, the ACP states would not have to remove all tariffs on all goods – they would need only to remove “substantially all” such import taxes. Nor would implementation occur immediately, except for charges having equivalent effect, but “within a reasonable period of time”.

In other words, “reciprocity” does not equal “liberalization”. The effect of liberalization is to alter the pattern of consumption and the location of production as a result of changes in price.

Reciprocity may reduce consumer prices, but it will not do so if:

- there is no tariff cut (because the product is one of those that are exempt from reduction);
- the exporter charges a higher price;
- the importer absorbs the tariff cut in higher profits;
- EPAs are overtaken by events elsewhere.

The effect of trade distortions

EPAs are intended, at least by the Commission, to promote regionalism and the integration of the ACP economies into the world economy. It is therefore helpful to recall the reasons for which countries and individuals trade. The fundamental reason is to gain access to goods and services that would be more expensive or impossible to produce domestically because they are subject to economies of scale (and the markets in some countries are below the optimum level) and/or a country’s resource endowments are not appropriate. In other words, the principal objective is to acquire imports – and exports are a means to this end.

In theory, countries should fund the importation of goods and services in which they have a comparative disadvantage and do so by exporting those in which they have a comparative advantage. These advantages and disadvantages arise from their relative endowments of resources, with the term “relative” meaning in comparison with other resources within the country and with the situation in all other trading countries.

This second aspect of “relative” is often overlooked. Labour, for example, may be relatively abundant in African countries compared with, for instance, infrastructure, but this relative abundance is nowhere near as marked as it is in, for instance, South Asia. Hence, African countries which might at first appear to have a comparative advantage in producing labour-intensive products may have a comparative disadvantage in comparison with South Asia.

In practice, however, some countries are not able to export some items in which they might seem to have a comparative advantage at a cost-covering price, while others are able to produce goods (for domestic consumption or export to certain markets) in which they appear to have a comparative disadvantage. This state of affairs arises because all countries distort their trade to some degree. If country X has a comparative advantage in widgets but country Y closes off its domestic market, X cannot export to Y. Indeed, if Y produces a surplus of widgets over domestic consumption and exports at a subsidized price, X may lose some of its other export markets, too. By contrast, if Z, with high costs of production, has favourable access to the market in X (with its artificially inflated prices), it may be able to export competitively even though it has a comparative disadvantage.

The reason for examining such basic points is that they have considerable relevance to the analysis of ACP–EU trade. Africa, for example, almost certainly has a comparative advantage in primary products, including agricultural goods, because it is relatively well endowed in natural resources. This underlying comparative advantage has been reinforced by policy distortions. The combination of the CAP and Cotonou preferences has created export opportunities in the EU for both competitive and less competitive ACP exporters for some goods, such as sugar, beef and horticulture. At the same time, of course, the CAP has also created increased competition from subsidized EU exports in other markets, including those in other ACP states. The net effect has been to make ACP exporters even more dependent on the EU market than they might otherwise have been.

The potential effects of a Free Trade Agreement (FTA)

If prices fall

Although EPAs will not be simply FTAs, and will have a development dimension, some of their features (such as reciprocal liberalization between members) overlap with those of FTAs. Hence, the effects can be assumed to be in the same direction as those of an FTA until the extent of the "development features" of the EPA are known.

The key question to ask is whether the tariff reductions actually result in a lower domestic price of imports. The assumptions behind FTA theory are that it will. This is expected to produce three types of effect:

- Trade creation occurs when consumers switch from domestic production to lower cost imports as a result of the removal of the tariff;
- Trade diversion occurs when goods that were previously imported from the most efficient global source are obtained instead from the higher cost FTA member because it enjoys a tariff preference;
- There is a revenue transfer from government (from the lowering of trade taxes) to citizens (from lower prices).

Traditionally, assessments of the economic impact of FTAs have involved a calculation of the relative sizes of these effects. But all assume that import prices actually do fall and consequently, this feeds through to the prices that consumers pay.

If prices do not fall

There can be circumstances, however, in which tariff cuts do not result in lower import prices. In such a case there would be no trade creation since there would be no reason for consumers to switch their purchases from domestic goods to imports. But there could still be trade diversion, with imports being switched from lower cost sources of supply to those located in the FTA members. Further, there would still be a loss of revenue to government, but the offsetting gain would accrue not to consumers, but to elements in the supply chain.

The net effects of a regime in which consumer prices did not fall would probably be trade diversion and an adverse movement in the terms of trade of the liberalizing country, with the two effects tending to be inversely related to each other. If exporters capture all of the tariff cut and increase their prices by the full amount, the adverse terms of trade impact will be maximized. If border prices do not rise by the full amount, but oligopolistic importers capture the tariff cut, this will encourage trade diversion by giving the importers a financial incentive to purchase from sources in the other FTA members.

The impact of an EPA will be determined therefore, partly by whether and how far it results in a change in the domestic price of imports, but also by a host of other factors as well. These include global events, and in particular what is happening in other trade policy areas, the characteristics of the ACP states involved and the characteristics of the EU as a source of imports.

The net effects of an EPA will be heavily influenced by trade policy changes introduced for other reasons, such as the WTO Doha Round or autonomous decisions by ACP states, during the period between now and the end of the EPA transition period, which could be as far away as 2020. The net impact of the EPA will be modest if between now and the date on which an ACP state has to reduce its tariff barriers on imports from the EU to non-constraining levels, the state has already engaged in substantial liberalization. There will undoubtedly be adjustment costs for the formerly protected sector and gains for consumers, but these will arise from the broader liberalization rather than the EPA. If, by contrast, there has been no such liberalization, and the EU is the only source that does not face constraining import barriers, then the impact will depend substantially on the state of the domestic market and the competitiveness of the EU. If markets are sufficiently competitive, there could be a fall in the price of imports, an increase in the quantity imported, and the full range of trade creation and diversion effects. If not, then the effects may be as described above in a situation in which import prices do not fall.

It is important to point out that until more is known about the time period over which EPA liberalization will occur, and each ACP country's commitments during this period in other fora, it is not feasible to produce a definitive assessment even of the direction of change under an EPA, let alone its scale. Still, some things are known about EPAs, and they can guide expectations on the range of possible effects.

Weighing up the costs and benefits

The strategic choice for each ACP state individually, for members of EPAs collectively, and for the entire ACP group as a whole is to determine whether or not the "costs" of an EPA exceed the "benefits" or vice versa. This cannot be done, of course, until more is known about the content of EPAs. Some scenario-building will help to identify critical features of EPAs that need to be included in order to better promote ACP interests.

It will also assist states in deciding whether they expect the EPA negotiations to turn out satisfactorily and hence, whether they need to take advantage of the Cotonou reference to "alternative arrangements" for states that do not enter EPAs.

Different players define both costs and benefits in conflicting ways. In the lexicon of trade negotiations, any reduction in import controls and taxes is seen as a "cost" and any cut in the barriers facing a country's exports is seen as a "gain". But for the liberal trade economist the picture is different. By increasing the volume of goods and services that a country's citizens can consume for a given level of exports, a reduction of import taxes is seen as economically beneficial, except in a limited number of cases where longer-term dynamic considerations make it sensible to accept variations. For the economist, trade diversion is a cost but trade creation is a gain.

One initial scenario-building task that each ACP state should perform is to focus on the implications of alternative tariff reduction formulae. As indicated above, the ACP are expected to reduce to zero only tariffs on "substantially all" trade, and to do so over a transition period that may be 12 or more years. Although the term "substantially all" has not been defined definitively, in the case of the EU–TDCA the EU stated that it considered the phrase to be fulfilled if, between them, the parties to the agreement reduce to zero tariffs on a group of products that in total accounted for 90 percent of the value of trade between them in the base year. In the TDCA, the EU went further and argued that this average 90 percent could be produced by asymmetrical reductions by the two parties: the EU is reducing to zero its tariffs on products that account for 94 percent by value of its imports from South Africa, and South Africa is doing the same on products that account for 86 percent of its imports from the EU.

If the same proportions were applied to the ACP, then countries would only need to reduce to zero their tariffs on a group of products that in the base year accounted for 86 percent of the value of their imports from the EU. If the spirit of the TDCA were applied, however, then the range of products that would need to be liberalized by the ACP would be even smaller. The EU import in excess of 98 percent of their goods from the ACP that are already duty-free. Hence, without any further liberalization by the EU, the "average of 90 percent" could be achieved by the ACP liberalizing only 82 percent of the value of their imports from Europe.

In addition, not all goods will need to be liberalized at the start. Some need not be liberalized until the end of the transition period. In the case of the TDCA, there is a 12-year transition period for South Africa. If this were applied to EPAs, then the most sensitive groups would not need to be liberalized by the ACP until 2020.

Armed with this information, tentative though it is, ACP states can calculate which products they would wish to exclude from liberalization altogether and which they would defer until the end of the transition period. This would indicate the extent to which there are likely to be either revenue or adjustment costs as a result of liberalization in the short to medium term. It would also help governments to ensure consistency with other trade negotiations, so that the same products are protected in each. For example, the list will probably overlap with that of products for special treatment by non-LDCs in the Doha negotiations.

In addition, there is a much wider range of information that needs to be gathered. In particular, in forming the ACP's strategy requires that empirical evidence be collected in three key areas:

- How valuable will ACP preferences be after 2007?
- How desirable is it that new preferences be created, and how feasible is this?
- How likely is it that EPAs will result in trade creation?

This chapter can deal with only the first of these three questions. The second question requires specific research for each EPA, and the third requires research in each ACP state. As regards question 1, the key is to understand how preference erosion may occur.

3.4 Preference erosion

As explained above, paradoxically, Cotonou agricultural preferences are most commercially valuable on the products that seem most restricted. In the case of sugar and beef, for example, ACP states (other than those least developed) are only allowed to export 1.3 million tonnes of sugar to the EU (and not unlimited quantities as would apply to all industrial products and most tropical agricultural products), while the southern African beef exporters have both a quota and pay an import duty on their sales, albeit at a reduced level). Yet, these restrictive preferences are particularly commercially valuable because they allow the favoured ACP countries to benefit from the artificially high prices created on the European market by CAP barriers.

Some ACP states, particularly those in ESA, have been substantially affected on the export front by the CAP – and almost all have been affected on the import side. Together with other protectionist OECD states, the EU has succeeded in artificially depressing world prices for some agricultural items, particularly cereals, and so reduced the cost of imports for net cereal-importing countries. The net effect of the gains for exports and imports has been to improve the agricultural terms of trade of ACP countries.

The source of erosion

How long will this continue? The answer depends partly on whether or not the trade preferences will continue to be commercially advantageous. They are advantageous in cases where EU taxes on imports from ACP states are set at a lower level than those on imports from competitors – and this difference is sufficiently substantial and sustained to induce importers either to pay higher prices for ACP exports and/or purchase larger quantities than would otherwise be the case. Anything that interrupts or interferes with this commercial link can erode the preference.

Such erosion could occur, therefore, for a whole host of reasons. Essentially, of course, a change to the text of a preference agreement could cause erosion. If EPAs are not in place by 2008 and the EU implements its stated objective of ending current access terms, there will obviously be a sharp erosion of preferences. ACP access will deteriorate to the terms of the successor regime, which could be as poor as the GSP for non-EBA states.

But change to preference agreements is not the only cause of erosion. Changes to other trade rules could have an impact. Considering the case of SPS, if EU SPS regulations on beef change in such a way that they cannot be met by Botswana or Namibia, then the commercial value of Cotonou for this product will disappear even without any change to the terms of the Beef Protocol. Less dramatically, if the SPS regulations change in such a way as to increase the costs of compliance, then the gains from trade will be reduced even though exports may continue to occur. As from 1 January 2005 the EU will have new pest inspection regulations in force on leafy agricultural product imports.

This will involve 100 percent inspection and payment of a "cost-covering" charge set at a graduated level but with a minimum fee. If these fees are more costly than for instance, those currently payable by Kenya or other eastern and southern African exporters on horticultural products, and if the increase cannot be passed on to the consumer, then the commercial value of the preference will be eroded.

Another principal avenue through which preferences can be eroded is the granting by the EU of equivalent or superior treatment to the ACP's competitors. The EU–Chile FTA and the upcoming EU–MERCOSUR agreement have the potential to significantly erode the commercial advantage that the ACP have over major competitor suppliers of agricultural goods to the European market. EBA has of course eroded the preferences of non-least developed ACP states, as will the EU–South Africa TDCA as it moves through its transition period and starts to cover a wider range of South African exports.

Finally, changes to the domestic EU market can cause erosion. Enlargement (covered in Chapter 5) has this potential, but so do a whole range of policy-induced and autonomous changes to the European market. Consumer tastes and concerns change. Unless ACP exporters are able to match these changes, then the market for their products may diminish regardless of whether there has been any formal change to their preferential treatment or any new trade-related policies such as SPS.

Changes on all of these fronts are currently occurring – and are assessed in these chapters. Evidently, the Cotonou Agreement is under renegotiation. There are also new EU SPS requirements for beef and horticulture/floriculture, behind a flurry of recent changes affecting fresh agricultural products. The preferences of ACP countries in agricultural products are being eroded by the new agreements described above. In addition, there is the major challenge presented by the phase-out of the Multi-Fibre Agreement (MFA) at the end of this year. Although this affects clothing and textiles, there could well be knock-on effects on the agricultural sectors of major ACP clothing exporters. This applies even if the countries do not export primarily to the EU. In Lesotho, for example, clothing is now the largest employer of labour, having overtaken the government sector earlier this century, and is largely based on exports to the United States. A substantial collapse of the clothing industry as a consequence of a relocation of the global division of production following the MFA expiry would tend to have major economic effects for all sectors.

The EBA scheme

Origins

The EU Council decided in February 2001 (EC, 2001b) that full duty-free access for 49 LDCs would come into effect from 5 March 2001 for all goods except armaments, bananas, rice and sugar. For bananas, rice and sugar there is an interim regime until full liberalization occurs on:

- 1 January 2006 for bananas;
- 1 July 2009 for sugar;
- 1 September 2009 for rice.

There are two elements to the interim regime: a progressive reduction in the tariff from its present level, and a duty-free TQ for the period until there exists completely free access.

The preferential tariff reductions on any out-of-quota exports are as follows:

- sugar under HS 1701 – 20 percent reduction on 1 July 2006; 50 percent reduction on 1 July 2007; 80 percent reduction on 1 July 2008;
- rice under HS 1006 – 20 percent reduction on 1 September 2006; 50 percent reduction on 1 September 2007; 80 percent reduction on 1 September 2008.[2]

The duty-free TQs have been set in relation to precisely defined product categories. In the case of rice, the whole of the relevant Harmonized System (HS) 4-digit heading (1006) is covered by the interim regime, but for sugar the TQ applies only to Combined Nomenclature (CN) code 17011110 (raw cane sugar, for refining, excluding added flavouring or colouring).

TABLE 3.2: TARIFF QUOTAS (TQS) FOR RICE AND SUGAR

	2001	2002	2003	2004	2005	2006	2007	2008
				Year starting July [a]				
Sugar (tonnes)	74 185	85 313	98 110	112 826	129 750	149 213	171 594	197 335
				Year starting September [a]				
Rice (tonnes)	2 517	2 895	3 329	3 828	4 402	5 063	5 822	6 696

[a] The Regulation states that both the TQs and the tariff reductions will be applied on the basis of the respective marketing years.

[2] For bananas the annual reductions will be 20 percent from January 2002.

The initial TQ levels are said to be derived from the best figures for total LDC exports "in the recent past". They will then be increased by 15 percent each year during the interim period.[3] The size of the TQs is set out in Table 3.2, which takes the initial level set out in the Official Journal and applies the agreed 15 percent growth rate to these base figures. According to the Regulation in the Official Journal, the initial TQs are set at the level of the best annual exports "in the recent past" increased by "a significant growth factor" which should "continue to be applied cumulatively every year until full liberalization" (EC, 2001b: 43, para. 10).

There is a safeguard mechanism incorporated into EBA. A Commission statement to the members of the GSP Working Party indicated how this is likely to work (EU Council, 2001). The Commission proposes automatically to examine whether safeguards (i.e. withdrawal of EBA preferences) need to be applied whenever imports from LDCs of sugar, rice or bananas exceed or are likely to exceed the level of imports in the previous marketing year by more than 25 percent.

The potential impact of EBA

The main limitations of EBA are that:

- it suffers from the institutional shortcomings of the GSP compared with the Cotonou Agreement (mainly that it is non-contractual, and therefore can be changed at the EU's whim);
- the initiative is subject to the special safeguard clause;
- the Rules of Origin are less favourable than those of Cotonou, especially with respect to cumulation.
- Its impact on LDCs (and competitors) will depend upon two factors:
- the extent to which the initiative represents an improvement on their current terms of access to the EU market;
- their capacity to increase their exports of the newly favoured products.

Changes to market access

The EBA initiative has had a direct effect on LDCs only in cases where previously there were restrictions on their access to the European market. Before EBA the LDCs already received highly preferential access to the EU market. The 40 that are part of the ACP group otherwise obtained access under the Cotonou Agreement, and the remaining nine benefited for some years from a special tranche of the GSP that provided them with additional preferences over those available to most developing countries. Since the LDCs already received relatively favourable access to the European market, many of their exports were already free of restrictions and so would not had been affected by EBA.

How great will the gain be resulting from the simple fact that the EU will no longer impose an import tax on LDC exports, and to whom will it accrue? The Commission has estimated that in 1998 these import taxes totalled €7 million (EC, 2001a). Henceforth, the loss to the European treasuries of this €7 million will be the gain of the suppliers.

But who in the supply chain will receive this €7 million? Unfortunately it is not possible to determine this across the board. It will depend upon relative negotiating power, which will vary between products, countries and firms. Hence, for example, the removal of customs duties could simply mean that importers or retailers make a larger profit or reduce retail prices. On the other hand, it could mean that the supplying countries or the producers therein receive higher prices. Alternatively, it could most likely be some combination of these two.

Nevertheless, in any event, it is likely to result in some improvement for LDCs. Obviously, if LDC suppliers gain the full benefit of the tax relief, they will earn more. But even if the entire windfall gain were to be absorbed by importers or retailers, this would increase their incentive to buy from LDCs, rather than from other suppliers on whom import taxes are still levied, and so would result in some (diminished) gain for LDCs in the form of an increase in their export volume.

[3] Excluded from the TQ are any imports from LDCs of, *inter alia*, raw cane sugar not for refining (CN 17011190), refined cane sugar containing added flavouring or colouring (CN 17019100), white sugar (CN 17019910), or cane sugar in solid form (CN 17019990).

Supply capacity

If LDC producers earn more, they may be able to afford to increase the volume of their exports, and then the ultimate impact of EBA could be much greater. If, for example, Bangladesh or Mozambique were able to divert some of their existing exports from lower-priced markets to the EU, or even to increase production so that they could export more *in toto*, the additional export revenue would be a dynamic gain from the EBA change.

While it is unrealistic to expect the EBA to have a major absolute impact on the volume of imports into the EU market – most LDCs do not have a large exportable surplus – there could be some export growth. The impact of EBA could be significant for competitors for one or both reasons. First, even an absolutely small increase in exports could be important in relative terms. The costs to competing developing countries could be relatively high if exports were concentrated in products of particular sensitivity or in intricately regulated EU markets. This may be the case with sugar.

Second, LDCs may increase their exports to the EU above current levels by:

- diverting sales from other markets;
- increasing imports for domestic consumption to allow a higher proportion of production to be exported; or
- in the longer term, by increasing total production.

All three ways, but especially the first two, are more likely to occur if EU prices are significantly higher than those elsewhere. This is even more likely to be the case for products in which EU protectionism from which LDCs will be relieved is high. The extreme case is provided by sugar, with EU prices over three times above the world market level.

Illegitimate effects

What follows provides a broad guide to the potential scale of legitimate exports, but what if non-least developed states attempted to pass off their production as if it were of LDC origin? EBA contains provisions outlawing fraud, such as the re-labelling of produce from non-LDCs in order to obtain EBA treatment, but there are legitimate reasons that other exporters might consider these to be inadequate. The first reason is that policing the system depends upon the EU's anti-fraud personnel and/or interested parties. The Commission needs to take steps to provide reassurances that the former will be as assiduous as competing exporters would wish. This is because if domestic public and private actors in the EU choose not to stamp out fraud, there is little that competing exporters can do; their interests are not under their own control. Moreover, fraud negates the objective of assisting LDCs. If fraud is identified and action taken, it must have a quick effect; otherwise, by the time the fraud is stamped out, much damage may have been done to legitimate trade.

The products likely to be affected

The EBA will affect LDC trade only for products on which:

- LDCs currently pay an import tax in the EU;
- LDCs have a supply capacity.

This section identifies the items on which the EU levied an import tax prior to EBA and in which LDCs are known to have a supply capacity because they already export them to the EU. Table 3.3 provides a detailed list of the very small number of items that are pre-2000 LDC exports to the EU and for which EBA will effect a change in the import regime. The broader product groups into which these fall, half of which face delayed implementation, are beef, cheese, maize, bananas, rice and sugar.

TABLE 3.3: THE LDCS' CURRENT EXPORTS TO THE EU THAT WILL BE AFFECTED BY EBA

CN_1997	Description	Current import restrictions (1999)	
		non-ACP LDCs	**ACP LDCs**
02023090	frozen bovine boned meat	9.8%+€332.6/100kg	0%+€332.6/100kg; Protocol K0%+€28.8/100kg
04069021	cheddar (excl. grated or powdered and for processing)	No preference	K€63.9/100kg
07099060	fresh or chilled sweetcorn	No preference	€10.1/100kg
08030019	bananas, fresh (excl. plantains)	No preference	€508/1 000kg (K0)
10059000	maize (excl. seed)	No preference	€75.19/tonne [b]
10062017	Long-grain husked brown rice, length/width ratio >=3, parboiled	Bangladesh K€109.82/1000kg; no preference	P€75.57/1 000kg b
10063098	wholly milled long-grain rice, length/width ratio >= 3, (excl. parboiled)	Bangladesh K€232.09/ 1000kg; no preference	P€160.51/1 000kg
17011110	Raw cane sugar, for refining (excl. added flavouring or colouring)	No preference	K0; Protocol 0
17011190	Raw cane sugar (excl. for refining and added flavouring or colouring)	No preference	K0; Protocol 0
17019910	white sugar, containing in dry state>= 99.5 % sucrose (excl. flavoured or coloured)	No preference	K0; Protocol 0 (for 1 item out of 2)
17031000	cane molasses resulting from the extraction or refining of sugar	No preference	K0

Note: "K" denotes rate within quota; "P" denotes ceiling.
Sources: Eurostat 1998; Taric 1999.

The small number of products affected directly is not surprising. Prior to EBA, all of the LDCs received duty-free access to the EU for all of their industrial exports and for most of their primary product exports other than those covered by the CAP or Common Fisheries Policies. Hence, the EBA has resulted in a change in access only for the limited number of temperate agricultural products that were restricted in 2000. On the other hand, the potential competitive advantage that EBA would confer on LDCs could be substantial. In all cases, the import regime facing LDCs and other suppliers is highly protectionist. Which LDCs will see the greatest improvement in market access? The answer is that the gains from the EBA are greatest for the non-ACP LDCs because the status quo is less favourable for them than it is for the ACP states. For eight out of the 11 items, non-ACP LDCs received no preference prior to EBA over the standard tariff payable by industrialized countries (the EU's MFN tariff), and for two items only one non-ACP LDC – Bangladesh – obtained a preference. Some or all of ACP LDCs already received preferences on all 11 items, but these were in most cases less favourable than under the EBA. The principal difference is the record of TQs and elimination of some preferential but positive tariffs. However, not all ACP LDCs currently receive a preference on all items under Cotonou. In the case of sugar and beef, only those countries that are parties to the Sugar and Beef Protocols benefit under Cotonou.[4]

The comparison between relative benefits for the ACP LDCs of the Cotonou regime for sugar and bananas with the EBA is complicated. ACP Sugar Protocol beneficiaries obtain duty-free access. This benefit is quota-limited, whereas the EBA is not. On the other hand, the Sugar Protocol provides that ACP beneficiaries will receive prices related to those applying within the EU. Under EBA the price received by LDCs could be subject to negotiation with importers, in which case it could be much lower since the world price is one-quarter to one-third of the EU level.

The case of bananas is nominally the same – the Cotonou regime provides duty-free entry, but only for a quota. In practice, however, for all of the ACP banana suppliers save Cameroon and Côte d'Ivoire, the quota matches or exceeds their supply capacity. Therefore, in practice they have duty-free access for all they can supply. EBA would represent an improvement only for ACP LDCs that might emerge in future as significant exporters.

[4] All the ACP least developed exporters of the sugar items identified (Madagascar, Malawi, Tanzania and Zambia) are Sugar Protocol beneficiaries. Of the beef item exporters, only Madagascar benefits from the Beef Protocol; the others do not, but in any case, probably cannot meet the EU's SPS requirements.

TABLE 3.4: EU SUGAR IMPORTS FROM LDCS, 1996–2002 (CN 17011110 ONLY)

Country	Imports							Increase		
	1996	1997	1998	1999	2000	2001	2002	2001/ 2000	2002/ 2001	2002/ 2000
					€ thousand					
Zambia	6 039	23 151	11 006	1 384	5 849	6 675	13 834	826	7 159	7 985
United Republic of Tanzania	6 298	7 002	11 792	6 405	8 458	6 635	11 175	-1 823	4 540	2 717
Malawi	7 533	6 103	6 232	6 552	8 815	6 053	10 997	-2 762	4 944	2 182
Sudan	–	–	–	–	–	–	8 430	–	8 430	8 430
Mozambique	–	–	–	–	–	–	8 237	–	8 237	8 237
Ethiopia	–	–	–	–	–	–	7 534	–	7 534	7 534
Burkina Faso	–	–	–	–	–	–	3 682	–	3 682	3 682
Total	**19 870**	**36 256**	**29 030**	**14 341**	**23 122**	**19 363**	**63 889**	**-3 759**	**44 526**	**40 767**
Subtotal Sudan–Burkina Faso	–	–	–	–	–	–	27 883	–	27 883	27 883
					Tonnes					
Zambia	13 513	43 352	24 788	3 000	12 427	14 513	27 044	2 086	12 531	14 617
United Republic of Tanzania	12 273	12 692	21 200	12 282	16 648	13 247	22 055	-3 401	8 808	5 407
Malawi	16 518	13 659	14 199	14 308	18 599	13 125	21 242	-5 474	8 117	2 643
Sudan	–	–	–	–	–	–	16 802	–	16 802	16 802
Mozambique	–	–	–	–	–	–	16 753	–	16 753	16 753
Ethiopia	–	–	–	–	–	–	14 555	–	14 555	14 555
Burkina Faso	–	–	–	–	–	–	7 113	–	7 113	7 113
Total	**42 304**	**69 703**	**60 187**	**29 590**	**47 674**	**40 885**	**125 564**	**-6 789**	**84 679**	**77 890**
Subtotal Sudan–Burkina Faso	–	–	–	–	–	–	55 222	–	55 222	55 222

Source: Eurostat 2002 and 2003.

Performance so far

EBA has not been in place for long and, given the lag in the EU's production of trade statistics there is not yet a great deal of independently verifiable evidence available on the take-up of the scheme.

However, a review produced by the European Commission (EC, 2004a) provides some guidance. It confirms that non-ACP states have made the most use of EBA. In 2002 some €2.5 billion of the €14.1 billion EU imports from LDCs received an "effective preference" under EBA. Of this total, only €66 million came from ACP LDCs; the great bulk came from Bangladesh, Cambodia, Laos, Nepal, Yemen and the Maldives, with Bangladesh on its own accounting for 78 percent of the total.

The term "effective preference" means that EBA treatment was requested and granted. There are three reasons that an item might not be accorded an EBA preference. One reason is that the EBA regime is no more preferential than the alternative, because MFN tariffs are set at 0 percent. In such circumstances there is no point in the importer claiming EBA treatment. The other two relate to cases where a preference exists, because without EBA treatment the importer would have to pay a positive tariff. It may not be claimed – either because of an oversight or deliberate choice by the importer. Alternatively, it may be claimed but not granted by the customs authorities, for example, because they deem the imports not to satisfy the EBA Rules of Origin.

The greater part of the EBA imports were in the area of knitted clothing, where the preference margin over standard GSP levels is 6.4–9.6 percent. These accounted for 57 percent by value of imports from LDCs that obtained EBA treatment. Seventy-three percent of EU knitted clothing imports from LDC actually received the EBA preference. The second most important category was woven clothing followed by fish (the highest ranking non-manufactured product), footwear, other textile items, hides and skins, carpets and sugar.

Neither the dominance of clothing in EBA imports nor the concentration of EBA preferences on non-ACP states is surprising. As the EC report itself notes, there is little reason for ACP LDCs to alter their administrative practice of seeking Cotonou preferences (on the EUR1 form) unless they are exporting an item that does not receive duty-free treatment under Cotonou. This is most likely to be the case for sugar.

Sugar is overwhelmingly the most important EBA import from ACP LDCs (EC, 2004a). It accounted for almost one-third of all the EBA imports (by value) from ACP states in 2002. According to the EU's figures, some €21.1 million out of the €63.68 million EU imports of sugar from ACP states (i.e. one-third) received EBA treatment.

One would expect all of the EU's imports from countries that did not receive a sugar preference prior to EBA, and all or most of the increase in exports from previously preferred LDCs to have flowed via the EBA regime. This is because the MFN tariff is sufficiently high to suffocate non-preferential imports. Yet, the value of imports in 2002 from Sudan, Mozambique, Ethiopia and Burkina Faso alone exceeds the Commission's figures for "effective preferences" on this sugar item. If one adds the increase in exports over 2000 for Zambia, The United Republic of Tanzania and Malawi, the excess of imports over the Commission's figure rises to almost €20 million. It would appear that the Commission's figures are missing up to half of the EU's EBA imports, or that the imports received a preference but have not been classified as EBA,[5] or that some LDC exports paid the MFN tariff.

3.5 The WTO Doha Round

The Doha Round is relevant to both sides of the equation in calculating the costs and benefits of an EPA and designing it to support food security for the poorest. The incremental effect of EPA reciprocity for ACP states will be determined partly by the changes to which they agree in Doha. The impact of CAP reform on them – both as exporters and importers will also be affected by whether or not it happens in isolation or forms a part of global trade liberalization. If the latter, then the adverse effects on exporters noted above could be mitigated by improved access to non-EU markets, although research suggests that SPS and security barriers are a more serious constraint for African agricultural exports to the non-EU Quad than are market access barriers (Stevens and Kennan, 2004).

As far as ACP imports are concerned, the conventional wisdom is that if and when significant liberalization occurs, the impact of OECD production cuts on world prices would be mitigated by increases in output from those states that are not able to afford such heavy subsidies, e.g. the members of the Cairns Group. Consequently, total world output would not fall by very much and prices will not rise very substantially. However, if this increased output does not occur during the period in which OECD subsidies and trade barriers remain significant, there could be a larger than expected surge in world prices. Hence, the progress or lack thereof on substantial multilateral liberalization will have a significant influence on the extent and direction of the impact that CAP reform has on ACP countries.

The extent of protectionism

The 1994 AoA began a process of reinforcing rules and liberalizing trade in temperate agricultural goods, but this still has a long way to go. In return for accepting rules that could become constraining after further rounds of negotiation, members were allowed to defer major pain by setting import restrictions and subsidies at high initial levels.

There has been much analysis of who would win or lose from a substantial liberalization of Northern agriculture. What would a more liberal agricultural regime look like?

Liberalization in the textbook sense means reducing government taxes and subsidies and amending protectionist rules that stop high-cost domestic producers from losing market share to lower-cost imports. It implies that the global location of production will change over time, with lower-cost producers increasing output and higher-cost producers declining.

An absolutely essential part of this process is the removal of OECD barriers to imports from developing countries. While tariff slashing would not in principle prevent OECD governments from subsidizing their farmers sufficiently for them to be able to compete with imports, the fiscal cost would be very high, making a continuation of current production levels improbable. Without the tariff cuts, it will remain feasible for governments to avoid production relocation through the payment of subsidies.

The Institute of Development Studies (IDS) has undertaken a comprehensive analysis of the agricultural tariff peaks[6] imposed by the Quad states[7] following the Uruguay Round. This has involved calculating AVEs for a large number of specific duties, and also removing from the list any items for

[5] This might have arisen, for example, if the reallocated quotas for special preferential sugar to LDCs were not treated as an EBA, even though the reallocation only occurred because of the EBA.

[6] The operational definition of a tariff peak is over 15 percent.

[7] Canada, the EU, Japan and the United States.

which trade preferences available to the generality of developing countries offer a much lower market access barrier. No fewer than 19 out of the 33 Harmonized System (HS) chapters covered in whole or in part by the AoA include tariff peaks in at least one Quad state. In most cases the peaks are applied by two or three of the states: six of the 19 include tariff peaks in three of the Quad states.

The chapters that include tariff peaks tend to be relatively more important for developing country exporters than for those from the OECD states. Further, these barriers are not systematically offset by preferences available to most developing countries: of the 6 643 agricultural tariff lines analysed by IDS, 16 percent faced tariff peaks, involved products that were important exports from developing countries, and were not subject to GSP schemes.

The products that most frequently encounter tariff peaks in the Quad under the current regimes are:

- beef: Canada and the EU;
- dairy products: the EU, Japan, the United States;
- vegetables, fresh or dried: the EU, Japan, the United States; fresh fruit: the EU, Japan, the United States;
- cereals and products: the EU and Japan;
- sugar: Canada, the EU, Japan, the United States;
- prepared fruit and vegetables: Canada, the EU, Japan, the United States;
- wine: Canada, the EU, Japan, the United States;
- spirits: the EU, Japan, the United States;
- tobacco: Japan, the United States.

Of course, due to the Cotonou Agreement the ACP face fewer tariff peaks in their most important agricultural export market, the EU. But they still face some peaks. Assessing precisely how many is a tricky task since it is difficult or impossible to establish accurate AVEs for specific duties and complex ones, such as so many € per degree of alcohol per hectolitre. Moreover, some tariff peaks are mitigated but only for a TQ of very small size, such as 400 tonnes for poultry meat.

TABLE 3.5: ITEMS NOT COVERED BY ACP PREFERENCES (2000)

HS/tariff line	# tariff lines	Description	Bound AV/AVE	
			max.	min.
ex 0210	2	Meat of sheep and goats: salted, dried or smoked	204.4	146
02109031	1	Edible pig livers: salted, dried or smoked	42.5	
ex 0709/0710	2	Olives: fresh or frozen	21.1	15.2
07119040	1	Mushrooms: provisionally preserved	217.6	
ex 0714	2	Manioc, sweet potatoes	83.8	15.9
ex 1006/1007	2	Broken rice and grain sorghum	72.4	51.5
ex 1509/1510/1522	6	Olive oils, soapstocks and residues	132.3	45
ex 1602	2	Prepared/preserved beef offal	163.4	130
ex 1701/1702	6	Cane and beet sugar, fructose	143.6	83.9
ex 1704/1806	3	White chocolate, chocolate flavour coating, preparations containing cocoa	18.9	18.7
19030000	1	Tapioca and substitutes	35.9	
19059045	1	Biscuits	20.7	
ex 2003	2	Prepared/preserved mushrooms	180.9	158.2
ex 2007	3	Jams and purees	40.5	27
ex 2008	6	Prepared/preserved fruit	31.0	25.6
ex 2009	5	Fruit juices	81.1	35.1
ex 2204	6	Wine and vermouth	?[a]	?[a]
ex 2207	2	Ethyl alcohol	?[a]	?[a]
ex 2208	6	Vodka, liqueurs and cordials	?[a]	?[a]
ex 2209	4	Wine vinegar, vinegar substitutes	?[a]	?[a]
23069019	1	Olive oilcake	39.0	
ex 2307/2308	2	Wine lees and grape marc	?[a]	?[a]
35021190	1	Dried egg albumin	24.1	

Notes:
Where this column is blank, the rate shown in the "max." column is applicable to all tariff lines in the aggregate.
[a] AVEs could not be calculated for any of the tariff lines within this product group.

What effect will Doha have on OECD market access?

The Harbinson proposal

The first significant attempt to forge a consensus in the agricultural negotiations was made in February and March 2003 by the Chairman of the special session, Stuart Harbinson. IDS research has shown that the application of the Harbinson proposal to the Quad's current tariffs would leave many of these product groups largely immune to imports. Tariffs would come down, but would remain at insurmountable levels. The principal product areas that would have retained tariff peaks of over 50 percent post-Harbinson were:

- the EU: beef, dairy products, bananas, prepared meat, sugar and grape juice;
- Japan: meat, dairy products, cereals, sugar, coffee/tea essences and silk;
- the United States: peanuts and tobacco.

In addition to these ultra-constrained products, those that would face 25–50 percent tariff post-Harbinson, which would reduce if not suffocate trade, include:

- the EU: meat (other than beef), fruit, vegetables, cereals, fruit juices, food industry residues, and tobacco;
- Japan: cereal preparations, miscellaneous food preparations;
- the United States: dairy products, sugar, butter substitutes.

The initiative failed to get much support even though its proposals were located in the middle of all the other major proposals (Matthews, 2003, footnote 4). Some further proposals during the months leading up to Cancún suggested that progress might be made at the Ministerial, but this turned out not to be the case.

The Derbez draft[8]

Although it was not adopted at Cancún, the Derbez draft was the most recent attempt at a consensus that was available until the Decision adopted by the General Council on 1 August 2004. From an ACP perspective, the key question is what the Derbez draft suggests in terms of how far Quad markets in general, and EU markets in particular, will be opened up as a result of the current round. The Derbez text suggested a blended approach, which would have subjected some tariff lines to the Swiss formula but others to the Uruguay Round (UR) formula (subject to there being a minimum simple average tariff reduction for all agricultural products), except for a limited number of items that could be dealt with separately on the basis of non-trade concerns. The Derbez draft also left the issue of special safeguards for further negotiations under which those countries that have reserved the right to do so, mainly the OECD states, can increase tariffs to deal with sudden import surges.

The August 2004 Decision

The Decision adopted by the WTO General Council on 1 August 2004 for the Doha Work Programme (WTO, 2004) notes that "special attention" is to "be given to the specific trade and development related needs and concerns of developing countries". Among these it refers specifically to "food security, rural development, livelihoods, preferences, commodities and net food imports…". Annex A to the 1 August 2004 Decision elaborates the framework for SDT and includes a number of innovations not present in the current AoA. These innovations include the designation of "Special Products" ("based on criteria of food security, livelihood security and rural development needs") and the establishment of a Special Safeguard Mechanism (SSM) to be used by developing country members.

These innovations are useful and could be developed within an EPA, but the assumption must be that whatever is undertaken will operate within a world agricultural market that remains distorted. The clear inference to be drawn from both the Derbez draft and the 1 August 2004 Decision is that many tariff peaks will remain after the closure of the current round of negotiations. If this is so, then there will not be the global re-distribution of genuine agricultural trade liberalization production assumed in the forecasts. On the one hand, this means that ACP importers of products that have been affected by the export and domestic subsidy negotiations will tend to have higher import bills. On the other hand, it will remain the case that some EU agricultural product markets will still be "managed" in the broad

[8] This sub-section draws heavily on Matthews (2003).

sense of the term, with limitations on the extent to which imports can be allowed to push down domestic prices. Under such circumstances there would be ample scope for providing trade preferences to ACP countries if the EU is willing to do so and if it can be squared with WTO obligations.

While few details are provided in the 1 August 2004 Decision on these innovations, there is some scope for believing that they could be useful to this process. The fact that it is specifically left to the negotiation phase to establish criteria and treatment is both an opportunity and a limitation. While certain possibilities are not definitively "ruled in", many are not "ruled out". The argument in this section is that the ACP must work backwards from their food security, livelihoods and rural development needs to identify the modulations in trade rules, both multilateral and within an EPA, that are required to facilitate the achievement of their goals in these areas.

Linking TRQs (sensitive products) and preferences

A literal interpretation of the wording in Annex A of 1 August 2004 Decision would appear to offer a potential way of linking measures in preference-giving countries that might be useful for preference-receiving states. An obvious area in which such flexibility might be useful is in the design of TRQs. Annex A para. 34 states that details of TRQs are to be negotiated. A link could be drawn between para. 41, especially the second sentence, and para. 34 on TRQs. This is because TRQs might help preserve some elements of preferences for some recipients.

At present, preference-recipients obtain two related advantages in different proportions depending upon the product concerned. One is that they are sold into an artificially high-priced market. Sugar under the EU–ACP Sugar Protocol is the extreme example of this, since not only is the EU sugar market price artificially inflated, but ACP beneficiaries are entitled to receive a price directly related to that prevailing on the European market. Horticultural preferences would be at the other end of the spectrum. The other advantage is that preference-recipients obtain a commercial advantage over other potential suppliers of the market. In the case of the Beef Protocol, for example, there is no possibility of substituting purchases from Namibia with, for instance, purchases from Argentina; if EU importers do not wish to buy the Namibian beef, they have to forgo that quantity of reduced-tariff import.

If the Doha Round fails to result in substantial cuts to EU market access restrictions on products covered by preferences, then EU prices will continue to be artificially high, although they may be lower than they are at present. Some preference-recipients might be able to continue to cover their production costs at these "artificially-high-but-lower-than-before" prices. However, if they face unbridled competition from other exporters who are able to sell at a lower price, they may not get the chance to do so. Such unbridled competition could occur if the EU opens TRQs for the products allocated globally (i.e. on a first come, first served basis) and that are sufficiently large relative to the Cotonou quotas, which importers would prefer to buy at a lower price under the TRQ than under the higher Cotonou.

If such circumstances occur, then some ACP preference-recipients would be squeezed out, although they would have been able to survive if the EU had opened country-specific TRQs. If the EU's TRQs were country-specific and allocated on the basis of past exports, an importer of beef, for example, would not be able to increase its purchases from Brazil above that country's sub-quota, even if a better price were offered than by Namibia or Botswana. Since one aspect that remains to be negotiated is whether they should be global or country- specific, there is scope for concerted EU–ACP action on this point. Other areas in which Special Products might be relevant may become apparent as the Doha negotiations progress.

3.6 Sanitary and phytosanitary standards (SPS)

The nature of the problem

ACP countries can benefit from agricultural preferences in the EU market only if they are able to supply the items competitively. Although most have exported agricultural goods to Europe for many years, the rapid evolution of SPS requirements means that a continuation of past flows – still less diversification into new items by new countries – is by no means a foregone conclusion.

This section reviews recent changes to EU SPS regulations to determine whether or not they appear to pose an insuperable or merely a difficult challenge to continued trade.

SPS pose a substantial challenge to the ACP countries and have done so for some time, but they relate particularly to EPAs in two respects: EPAs may provide a vehicle to help the ACP meet SPS requirements and they might provide a framework within which to develop “development-friendly” SPS.

As a framework designed specifically to better integrate ACP countries into the world economy, EPAs offer an obvious vehicle for helping deal with the challenges that the ACP countries face. Many such challenges involve resources, both financial and human. There is a huge need for both financial and technical assistance to allow more ACP countries to participate more extensively and effectively in international trade on a wider range of agricultural goods. The EPAs should make specific provision to provide some of this support.

A World Bank study of the needs of five African countries for improved SPS infrastructure to allow them better to participate in international trade, for example, reveals a wide range of measures that need to be taken (Wilson and Abiola, 2003). The costs of complying with SPS requirements in the Kenyan horticulture industry, for example, are put at US$2 000 per month at the farm level and US$123 000 for quality controls from the farm to port of export (idem xlv). In Uganda, while there are 28 government gazette custom entry/exit points that should have inspection units, only 11 are served. Four domestic laboratories are still seeking international recognition as testing centres, and the overall estimated cost of their restructuring is US$12 million. Also, in Uganda, ISO certification is estimated to cost US$3 000, and training an average of US$7 000 – to be repeated every three years (ibid. l li)!

Nonetheless, it is clear that some, albeit far too few African producers are able to meet international SPS. The very fact that Botswana, Cameroon, Côte d’Ivoire, Ethiopia, Kenya, Ghana, Mauritius, Namibia, Senegal, Swaziland, Uganda, Zambia and Zimbabwe are all able to export fresh, chilled or frozen agricultural goods successfully to the EU is evidence that they have achieved the minimum level of competitiveness in terms of quality, timeliness and price. The preference simply provides an additional margin to the value chain that sources in Africa (compared with a non-preferred source), and thus facilitates diversification.

But will new SPS regulations bring this trade to a halt, and how might this be avoided? This introduces the second aspect that relates SPS to EPAs. The EU’s SPS are evolving rapidly – and this is creating additional challenges. Given that one explicit aim of EPAs is to foster the integration of ACP countries in the world economy, they offer an obvious framework for modulating these changes to reflect ACP conditions while not compromising on health standards.

Non-EU suppliers of fresh agricultural products must already comply with rigorous certification schemes that allow each carton to be traced back to a certified grower. Not only must phytosanitary and hygiene standards be acceptable in the EU, but also toxic residue levels, as well as the labour, social and environmental conditions of production (Lambert, 2002, p. 8).

There can be no question of the EU adopting lower SPS for ACP producers, and in principle such standards, if applied to all suppliers, should not necessarily be a particular problem in EPAs. Some of the health issues that arise from intensive and artificial production methods could be less difficult for ACP than for industrialized countries to avoid.

Further, even to the extent that SPS compliance imposes costs, these will apply in principle to all suppliers and hence not alter relative competitive conditions.

In practice, however, there are four sets of problems that could be associated with the ever-changing SPS requirements of major markets, some of which could be alleviated either through modulations to the regime in EPAs or through aid in support of trade. They are requirements that:

- are inappropriate to ACP circumstances;
- skew the distribution of gains from trade;
- are disproportionately onerous for small exporters;
- change too rapidly.

Evidence concerning the EU

The EU has a complex and overlapping series of Regulations and Directives on various aspects of SPS that have been introduced over a long period of time. Within this body, a core of 24 Regulations and Directives provide the principal source of impact on ACP agricultural exporters (Cerrex, 2003, p. 10).

This corpus is in the process of being revised and harmonized, partly to reduce barriers to trade within the single market. Much of the concern is associated with the changes introduced through this process.

Inappropriate standards

The argument is made that when SPS regulations in respect of, for example, pesticide residues are framed, they only consider the circumstances prevailing in the agricultural sector of the imposing country. There may not be any deliberate attempt to bias the detailed provisions against ACP circumstances and practice. Still, at the very least, there is an absence of the technical information required to modulate the detail of the regulation so that it takes full account of the husbandry practices and available agro-chemicals in the ACP.

This has been a particular problem with the EU's Harmonization Programme on minimum residue levels (MRLs) for pesticides. This Programme aims to establish common and obligatory MRLs for all active ingredients approved for use within the EU. Under its Pesticide Approval Review Programme, the EU is systematically reviewing the registration of 823 active ingredients approved within the EU prior to 25 July 1993. The continued registration of a pesticide depends on appropriate data being generated and submitted by interested parties (Cerrex, 2003, p. 12). If a pesticide fails to have its MRL renewed, the maximum acceptable residue will be set, by default, at the "limit of detection".

It has been estimated that approval will be withdrawn for at least 350 active ingredients:

> *Market opinion is that in the absence of agro-chemical companies investing in generating data to defend registration of MRLs of older, out-of-patent pesticides, many developing countries will be unable to complete the necessary dossiers to enable the continued use of many significant pesticides which are mainly relevant to use in tropical regions (Cerrex, 2003, p. 13).*

A report to the United Kingdom Tropical Agriculture Association considered that due to poor communications and a lack of understanding of the real consequences of the changes, insufficient work had been done to support the setting of MRLs for imported tropical and sub-tropical crops (Cerrex, 2003, p. 33).

The situation is considered particularly serious for post-harvest fungicide treatments, essential for sea-freight exports and where residues are most likely to remain on the surface of a product up to the point of retail.

EU has provided €25 million in funding to the Europe, Africa, Caribbean, Pacific Liaison Committee (COLEACP) Pesticide Initiative Programme (PIP). The PIP team in Brussels is processing applications from companies or groups of companies for PIP interventions (Lambert, 2002, p. 21).These include conducting trials in tropical regions to generate data to support the establishment of MRLs that are relevant to good agricultural practice in fruit and vegetable crops.

Distribution of gains

Two examples illustrate the issues over the influence of SPS on "who gains" from trade – and the extent to which changes to "trade policy" might affect the outcome. The first concerns the effect of United Kingdom "name and shame" provisions on pesticide residues on the buying strategies of British supermarkets. It is argued that this has accelerated a trend towards sourcing from large producers, who can provide the paper-based guarantees of standards compliance, and away from smallholders (Humphrey and Dolan, 2000; Dolan and Tewari, 2001). The problems that small producers face in demonstrating compliance with the paper- and process-based systems that underlie many ISO codes have been well documented and do not only apply to agriculture (Nadvi and Halder, 2002). The standards for horticulture and livestock set by EurepGAP, a group of 29 European retailers, increasingly represent the level to which exporters must aspire if they are to continue to find buyers. Not only does this create problems for small producers, but it discourages new entrants. EurepGAP is specifically aimed at the existing suppliers of its members (FAO, 2003b: 39).

TABLE 3.6: SUMMARY OF OIE GUIDELINES FOR MEAT EXPORT WITH RESPECT TO FMD STATUS

Status	Description of FMD control	Meat export requirements
1. Infected country or zone with no FMD control	No official control programme (private vaccination may be undertaken to protect herds)	Export of processed (canned) product only to any country from an approved abattoir Ante- and post-mortem inspection Avoidance of FMD contamination of product
2. Infected country or zone with official control programme	Compulsory systematic vaccination of cattle Cattle residency requirements Cattle sourced from areas with no FMD within 10 km for 30 days	Export of de-boned beef to FMD-clean or infected countries from an approved abattoir Ante- and post-mortem inspection Carcass maturation, removal of bone and lymph nodes
3. FMD-free country or zone where vaccination is practised	Cattle vaccinated Effective disease surveillance and reporting No outbreak of FMD for 1–2 years	Residency requirements Slaughter at approved abattoir Export of de-boned beef to all markets Unrestricted meat export to infected markets or those with similar FMD virus strains Export of fresh pork and other meats from animals that have not been vaccinated
4. FMD-free country or zone where vaccination is not practised	No vaccination permitted in free zone Free zone separated from others by surveillance zone or other barriers Measures to prevent FMD entry Effective disease surveillance and reporting No outbreak of FMD for 3 months	Residency requirements Slaughter at approved abattoir Unrestricted meat exports

Source: Perry *et al*. 2003: Table 2.1.

Since the requirements are commerce-led and the underlying trend appears to be in the same direction (towards a concentration of supply), it is not clear that there is a great deal that importing governments can do through their trade policy to influence the situation. To the extent that the trend is considered adverse for development, however, there may be steps that can be taken in the producer country (with donor support where appropriate) to assist small producers to make themselves attractive to the buyers and to increase the developmental gains from wage labour in the sector (McCulloch and Ota, 2002).

The other example comes from Botswana in relation to beef exports. This lies more centrally within the remit of importing-state governments. The conditions under which FMD-free countries may restrict imports are laid down by the Office International des Epizooties (OIE), which provides the technical advice in WTO disputes, and are summarized in Table 3.6. The EU's beef imports under Cotonou have generally come from regions of countries that satisfy Status 4, "FMD-free country or zone where vaccination is not practised." As an additional and unchallenged precaution, the EU further restricts the type of product that can be imported. Instead of allowing unrestricted imports, which would be permissible from a Status 4 region, it allows only imports of de-boned beef, the norm from Status 3 regions. This is to remove the risk of the disease being transmitted in bone marrow. Possibly, this could be challenged in the WTO, but the exporting states have not considered it to be in their interests to do so.

Southern African beef exporters have satisfied these requirements by applying the traditional method from which both small and large cattle producers can benefit. Essentially it involves the construction of physical barriers between the FMD-carrying buffalo and protected cattle, together with externally inspected abattoirs within the FMD-free zone. Anyone raising cattle of the appropriate quality standard within the FMD-free area is able to participate in the export trade – and the gains have been considerable (Perry *et al*., 2003).

The alternative system of shifting to Status 3 would involve vaccination and cattle passports. This would tend to limit participation to the more organized and larger farmers. So would new requirements, possibly, introduced under the heading of "Good Agricultural Practice" (GAP), requiring greater traceability within the controlled area. It is therefore a matter of concern that the

Government of Botswana has felt obliged to introduce the tagging of cattle (placing a bolus in each beast which can be "read" by an external monitor) to demonstrate the origin and movement of cattle in order to meet EU veterinary requirements. The concern is that it will limit small-farmer participation, especially if it becomes the norm in other countries with more limited scope to fund the costs from government resources.

Onerous administration and rapid change

There is evidence that the problem is institutional rather than technical; SPS rules as such do not create the problem. Firms involved in exporting agricultural products are reported not to attribute their greatest difficulties in dealing with SPS issues to be either the WTO SPS Agreement provisions or consumer concerns in the EU. Rather, they assert that the primary cause of their problems derives from "structural deficiencies that exist within their "single home" countries" (Cerrex, 2003, p. 44).

These problems include slow communication of new rules by the public to the private sector and confused lines of communication and responsibility within government. A case in point is the SPS problem Kenya experienced in exporting fish from Lake Victoria to the EU in 1997 and 1999 (Cerrex, 2003, p. 39). The EU indicated an intention to impose an import ban as a result of concern over hygiene standards, and later with respect to special food safety problems such as cholera and fishing with pesticides. Kenya was unable to react within the 60 days allowed for comment largely because of a diffusion of responsibility between different ministries. Responsibility is divided between the Ministries of Trade, Agriculture and Health.

New EU regulations on pest control designed primarily to promote trade within the Single Market are a particular concern for the horticulture and floriculture industries. A new Regulation will merge, harmonize and simplify 16 existing product-specific Directives and the General Directive 93/43.

> *The effect of this "tidying up" operation will be increased by its introduction as a Regulation which is directly implementable by EU member states as opposed to a Directive that allows variation by member states in the way it is translated into national legislation (Cerrex, 2003, p. 11).*

The substantial shift towards more uniform practice within the EU was heralded by a Council Directive of 8 May 2000 (CEC, 2000). This was subsequently amended by a Commission Directive of 19 March 2002 and a further Council Directive of 28 November 2002 (CEC, 2002a, 2002b).

Under the new regulations, which came into effect from 1 January 2005, all plants and plant produce imported into the EU are liable to inspection by plant health inspectors on arrival, whether or not they require a phytosanitary certificate. Among the changes has been the definition of plants to include "leaves", bringing cut flowers fully within the purview of the new system. The inspected plants will require a "plant passport" before further movement within the EU is permitted.

There are three causes of concern for the exporters. The first is the sheer speed with which events have taken place. The period for making representation to the Commission before the Directives were published was felt to be too short, as is the period before full implementation. It is inherently plausible that information flows from Brussels to producers in the ACP, especially the less well established, will tend to be partial. To the extent that this is the case, considerable scope would appear to exist for EPA institutions to assist the information and communication flow.

A second problem concerns the cost of meeting inspections. The EU regulation is quite clear: it states that "member States shall ensure the collection of fees … to cover the costs occasioned by the documentary checks …" (CEC, 2002b: Article 13d, 1) and that "No direct or indirect refund of the fees provided for in this Directive shall be permitted (ibid.: Article 13d, 4). This is presumably to avoid any hidden subsidies. The regulation allows member states to make their own calculations of costs, but it also sets out standard fees, which will always be taken to be "cost covering".

One important point to note is that these fees were published only on 28 November 2002, i.e. just two years before they come fully into effect. The second point is that they are generally composed of a base charge for consignments up to a certain volume, with supplementary charges for units above this minimum, and a maximum charge. This system, which reflects the reality that there are fixed costs in inspecting a consignment regardless of its size, nevertheless will bear disproportionately on small consignments, for example, the base "standard charge" for cut flowers, which is €17.5 for up to 20 000 stems.

What is the relative tax burden? For imports from Kenya in 2002 of chrysanthemums, for example, this charge would be equivalent to 4.3 percent of the value of 20 000 stems. If the consignment were fewer than 20 000 stems, the proportionate cost would rise. In May 2002 Kenya exported only 9 050 stems to Sweden, and in April, just 5 000 stems. Even if all the flowers had been concentrated in a single consignment in each of these months, the standard charge would have been nearer to 9 percent in May and as much as 16 percent in April. These are extreme cases, but in the two months of 2002 that Kenya exported to Germany, the total was around 30 000 stems per month, and in the other two months of supply to Sweden it was 22 500 and 36 690 stems (Eurostat, 2003). Given the probability that these monthly sales are divided into several consignments, it appears likely that the proportionate charge will often be greater than 4.3 percent. At the very least, it will discourage diversification to new national markets and the emergence of new ACP suppliers that do not sell the quantities that Kenya has achieved.

These problems are causing particular concern because they are being accompanied by a change in the frequency of inspection. In the past, the frequency has varied between national markets. Now, all plants specifically identified by the EU will be subject to “meticulous inspections” of “each consignment” (CEC, 2002b: Article 13a, 1(a)). In addition, plants that are not specifically listed will also be subject to “supervision” to ensure that they are not host to prohibited pests (ibid, Article 13, 3).

There is provision for inspection to occur at a lower rate of frequency in cases where an inspection was “already carried out in the consignor third country” (ibid., Article 13a, 2). This raises the question as to whether it would be appropriate to locate EU inspectors in ACP air and seaports.

3.7 Lessons from Relevant EU Trade Agreements

The EU–South Africa TDCA

In addition to the possibility of preference erosion emanating from multilateral liberalization, there is the probability that the EU’s sub-multilateral trade agreements will remove or reduce the commercial value of the ACP’s preferences. This section reviews the TDCA with South Africa, and the next section looks at the EU–Chile Agreement. On the horizon is the EU–Mercosur accord, which is expected to be finalized soon. If this moves ahead, it could have a substantial impact on ACP preferences, not least those on beef.

Although the TDCA came into effect in 2000, many of its more substantial improvements to South African access to the EU market have either only just come on stream or are not yet implemented. Table 3.7 sets out in broad terms the implementation schedule for agricultural products that are exported by ACP states. Most of the items that were fully liberalized by 2003 (top two rows) already faced low tariffs. For example, 14 of the 19 items exported by ACP states to the EU (to a value of €5 million or more in 2002) that were to be fully liberalized by 2003 are items for which the GSP tariff in 2002 was under 5 percent.[9] Further, none of the items (apart from cane and molasses – CN 17031000) had GSP rates exceeding 10 percent. Hence, the “preference erosion” that has already happened is very modest.

Among a second group of products in Table 3.7 – those for which liberalization began in 2000 but will not be completed until 2010 – there are a small number for which the ACP margin of preference over GSP levels (and those currently applicable under the TDCA) is substantial. Hence, by 2010 there will have been a significant erosion of ACP preferences, but this has yet to occur.

The fourth row of Table 3.7 lists the items for which liberalization did not begin until 2003 and for which it will be completed by 2010. Most of these are items on which the ACP states currently have a significant margin of preference over GSP tariffs, and for which, therefore, there will be a significant change in their relative competitiveness compared to South African exporters over the next six years. Finally, the table lists two items for which liberalization will not begin until 2005.

Missing from Table 3.7 are two groups of products, one of them fish. Unlike Cotonou, which provides for the possibility of ACP states negotiating FPAs with the EU but also provides preferential access to states that do not do so, the TDCA only provides for preferences if South Africa and the EU negotiate an FPA.

[9] These items are aggregated in Table 3.5 into broader commodity groups.

TABLE 3.7: IMPLEMENTATION OF THE TDCA: EU LIBERALIZATION SCHEDULE FOR ITEMS EXPORTED BY ACP [a]

Implementation period	Items	GSP tariff range % (2002)
2000	Vacilla	2.1
2000–2003	Capsicum and pimento	2.9
	Cloves	2.8
	Groundnut, coconut, palm kernel, babassu, vegetable oils	2.2–2.9
	Cane molasses	b
	Cocoa (paste, butter and powder)	2.8–6.1
	Tobacco and cigars	3.9–9.1
2000–2010	Peas	4.5–10.1
	Pineapples	2.3
	Avocados	0–1.6
	Table grapes (1 January to 31 May, excl. Emperor variety)	8
	Tobacco	7.7–14.9
2003–2010	Cut flowers (1 November to 31 May)	5
	Beans	6.9–10.1
	Vegetables nes	8.9
	Arrowroot, salep and similar roots and tubers	9.5€/100 kg/net[c]
	Prepared and preserved beans	15.7
	Prepared and preserved pineapples	14.1–15.7
2005–2010	Navels and sweet oranges (1 June to 15 October)	3.2c
	Table grapes (Emperor variety and excl. 21 July to 31 October)	4.5–MFN

[a] to a value of €5 million or more in 2002.
[b] This item is not covered by the GSP, and the MFN rate is not available.
[c] MFN rates, as the items are not covered by the GSP.
Sources: Eurostat 2003; UNCTAD TRAINS; EC 1999.

At present, negotiations on the FPA have been stalled and, hence, there is no immediate prospect of any improvement in South African access to the EU for these items that is more preferential than the GSP. Nonetheless, the GSP for many fishery items is relatively liberal with tariffs of less than 5 percent.

The second group of exemptions are agricultural products that are not scheduled for liberalization under the TDCA at present. These include sugar, beef, rum, some flowers and those citrus and vine fruits sub-categories not covered by the bottom pane of Table 3.7. While the TDCA leaves open the possibility of future negotiations, and often establishes that there will be a "periodic review" these have not yet resulted in any agreement to grant South Africa preferential access.

It must be emphasized that Table 3.7 only covers products that are both in the TDCA and exported at present by the ACP to significant values. It follows that there could be preference erosion on other agricultural items that are not yet exported (or only in trivial amounts) by the ACP. But it is in the nature of the issue that such level of detail on erosion can only really be identified through country-level analysis.

Similarly, it should not be assumed that South Africa has a supply capacity in all of these items (e.g. cocoa). Table 3.8 takes this into account by identifying from among the products summarized in Table 3.7, those that were actually exported to significant values by South Africa either to the EU or to elsewhere in 2002. Table 3.8 also identifies the principal ACP exporters to the EU for each of these products. The extreme right-hand column also shows the tariff payable by South Africa in 2004. In most but not all cases, this tariff will be reduced to zero by the end of the implementation period.

The list is quite short, only 20 eight-digit items in total. In 9 of these (cut flowers, miscellaneous vegetables, pineapples, groundnut oil, vegetable fats and oils, and various types of tobacco), South Africa is a relatively small supplier of the EU market despite having faced only moderate tariffs in the past. There is no reason to assume, therefore, that the TDCA will significantly alter the level of competition experienced by ACP states. The main items in which South Africa has a demonstrated supply capacity and where the TDCA will result in significant improvement in its access to the EU, at least by 2010, are grapes and preserved pineapples, with the principal ACP competitors being Namibia, Kenya and Swaziland.

TABLE 3.8: TDCA: THE "AT RISK" ACP COUNTRIES

CN8	Brief description	Exporter	Exports to EU (€'000) 2002	Share of EU total 2002 (%)	Change in share 2000–2002 (%)	EU tariff 2004
Liberalization by 2003						
15081090	Groundnut oil	South Africa	1 477	1	195	0
		Senegal	62 246	61	-5	0
		Gambia	10 588	10	485	0
		Sudan	6 010	6	8	0
59059	Vegetable fats and oils	South Africa	500	2	-15	0
		Ghana	3 178	16	178	0
		Togo	2 164	11	276	0
		Nigeria	514	3		0
17031000	Cane molasses	South Africa	8 180	4	-5	0
		Sudan	9 333	5	-14	0
		Guyana	2 021	1	151	0
		Senegal	1 988	1	-16	0
24011070	Dark air-cured tobacco not stemmed or stripped	South Africa	4 003	6	40	0
		Dominican R.	5 460	8	22	0
		Ghana	307	0	-16	0
		Caribbean	53	0		0
Liberalization 2000–2010						
07081000	Peas	South Africa	400	1	19	3.7–9
		Kenya	15 214	40	-9	0
		Zimbabwe	6 258	16	4	0
		Zambia	2 248	6	31	0
08043000	Pineapples	South Africa	5 510	2	1	2.9
		Côte d'Ivoire	103 990	31	-17	0
		Ghana	41 688	13	12	0
		Cameroon	1 539	0	-28	0
08044000	Avocados	South Africa	51 500	35	1	0-2.1
		Kenya	12 331	8	-8	0
		Swaziland	432	0	100	0
		Dominican R.	342	0	-22	0
08061010	Table grapes (1 January to 31 May excluding Emperor variety)	South Africa	260 013	44	7	5.3-5.8
		Namibia	12 630	2	69	0-11.5
		Kenya	2	0	-41	0-11.5
		Dominican R.	1	0		0-11.5
24011010	Flue-cured Virginia-type tobacco	South Africa	–	–		8.9
		Kenya	2 754	11	244	0
		United Rep. of Tanzania	1 692	7	79	0
		Zimbabwe	450	2	-62	0
24011041	Flue-cured Kentucky-type tobacco	South Africa	–	–		8.9
		Mozambique	2 654	13	39	0
		Uganda	1 325	6	6	0
		United Rep. of Tanzania	1 189	6	18	0
24012010	Flue-cured Virginia-type tobacco partly or wholly stemmed or stripped	South Africa	293	0	118	8.9
		Zimbabwe	173 134	21	13	0
		United Rep. of Tanzania	22 052	3	2	0
		Uganda	9 851	1	-2	0
24012020	Light air-cured Burley-type tobacco partly or wholly stemmed or stripped	South Africa	123	0	-25	8.9
		Malawi	62 752	17	19	0
		Uganda	5 817	2	-9	0
		Mozambique	5 477	1	163	0
Liberalization 2003-2010						
06031080	Cut flowers (1 November to 31 May) a	South Africa	7 437	3	3	5.4-6.3
		Kenya	45 433	21	17	0
		Zimbabwe	27 562	13	4	0
		Côte d'Ivoire	3 638	2	20	0
07099090	Vegetables nes	South Africa	1 785	1	5	6.9
		Kenya	57 127	37	12	0
		Ghana	8 586	6	-18	0
		Zambia	7 691	5	230	0
20082059	Preserved pineapples added sugar but no added spirit sugar content of =< 17 %	South Africa	1 383	3	22	11.6
		Kenya	5 586	13	91	0
		Swaziland	757	2	10	0
		Nigeria	12	0		0

CN8	Brief description	Exporter	Exports to EU (€'000) 2002	Share of EU total 2002 (%)	Change in share 2000–2002 (%)	EU tariff 2004
20082079	Preserved pineapples added sugar but no added spirit sugar content of =< 19 %	South Africa	5 731	5	88	12.7
		Kenya	25 887	25	7	0
		Swaziland	2 273	2	61	0
20082099	Preserved pineapples no added sugar or spirit	South Africa	1 841	4	-3	12.2
		Kenya	12 230	24	-6	0
		Swaziland	2 122	4	27	0
		Somalia	24	0	64	0
Liberalization 2005-2010						
08051030	Oranges –navel naveline navelate etc. (1 June to 15 October) a	South Africa	95 292	34	2	3.2
		Zimbabwe	9 285	3	3	0-0.6
		Belize	2 698	1	61	0-0.6
		Swaziland	2 607	1	-22	0-0.6
08051050	Sweet oranges (1 June to 15 October) [a]	South Africa	20 653	65	-3	3.2
		Zimbabwe	5 208	16	37	0-0.6
		Swaziland	3 170	10	40	0-0.6
		Dominican R.	96	0	-15	0-0.6
08061010	Table grapes (Emperor variety and 1 November to 20 July) [a]	South Africa	260 013	44	7	5.3% to (14.4%+€9.6)[b,c]
		Namibia	12 630	2	69	0% to
		Kenya	2	0	-41	(14.4%
		Dominican R.	1	0		+€9.6) [c]

Notes:
[a] The full specific duty is payable if the respective entry price is not reached.
[b] per 100 kg net
[c] The export values shown are for the whole year not for the specific period indicated in the implementation schedule.
Sources: Eurostat 2002 and 2003; EC 1999; UK Tariff.

The EU–Chile Agreement

Similar considerations apply to the EU's FTA with Chile. When fully implemented it may well erode significantly preference on agricultural goods that the ACP currently export to the EU. But implementation is back-loaded, so this effect has not yet been observed. With the exception of beef, which could be an important competitive product for the ACP, the tariff paid by Chile prior to the FTA on items for which liberalization has been fully completed was generally low (Table 3.9). For beef Chile has a small TQ starting at 1 000 tonnes and increasing by 10 percent on this base level per year. Moreover, Chile has duty-free access to the European market for its TQ, unlike the ACP states that pay a reduced, but not eliminated, specific duty on their quota.

Even by 2007 most of the areas of liberalization will be on products where Chile previously faced relatively low tariffs. The principal items where this is not the case are roses, carnations and other cut flowers, peas, other vegetables and winter table grapes. In all of these Chile was previously excluded from the GSP and therefore paid tariffs of between 8 and 14 percent.

The most substantial erosion will not occur until around 2010–2013 (as indicated in the bottom panes of Table 3.8). ACP preferences on grapes, chilled fish, citrus, prepared beans and pineapples will be particularly heavily eroded.

As in the case of South Africa, however, this list does not indicate whether or not Chile is a competitive supplier of the products for which ACP preferences will be eroded. The main difference is that the right-hand column is split into two: the column for 2002 shows the tariff payable by Chile before implementation of the agreement, while the 2004 column indicates not only the current tariff but also the "end tariff" for those items that were fully liberalized in 2003. While the list appears much longer, this is because it includes fishery products, which have been excluded from the TDCA.

While quota-limited, the preference to Chile on beef is particularly noteworthy. Alone among EU suppliers it has complete duty-free access. At the very least, this fact could be used in the EPA negotiations to support ACP arguments in favour of more liberal access to the EU market for their exports. At present Chile exports nothing to the EU, although it does have small frozen beef exports to the world.

TABLE 3.9: IMPLEMENTATION OF THE EU–CHILE AGREEMENT: EU LIBERALIZATION SCHEDULE FOR ITEMS EXPORTED BY ACP [a]

Implementation period	Items	MFN tariff range (2002) [b]	GSP tariff range (2002)
2003	Beef	12.8%+221.1–€304.1/100 kg/net	Not covered by GSP
	Saltwater fish, shark, cuttlefish, squid, octopus		2.5–15 [c]
	Capsicum and pimenta	6.4	2.9
	Pineapples	5.8	2.3
	Avocados	4 or 5.1	0 or 1.6
	Navels and sweet oranges (1 May to 15 Oct.)	3.2% to (4.8%+€7.1/100 kg/net)	Not covered by GSP
	Chocolate		4.8+EA
2003–2007	Freshwater fish, sole, swordfish, crawfish tails, shrimps, prawns		2.6–9 [c]
	Roses, carnations, other cut flowers	8.5 or 12	5 or 8.5
	Peas	8 or 13.6	4.5 or 10.1
	Vegetables nes.	12.8	8.9
	Table grapes (1 November to 14 July)	8% to (14.4%+€9.6/100 kg net)	4.5% to (14.4%+€9.6/100 kg net) [c]
	Vanilla		2.1
	Cloves		2.8
	Groundnut, coconut, palm kernel, babassu, vegetable oils		2.2–2.9
	Cocoa (paste, butter and powder)		2.8–6.1
	Coffee extracts		3.1
2003–2010	Frozen hake fillets/meat		4
	Navels and sweet oranges (April)	10.4% to (10.4%+€7.1/100 kg/net)	Not covered by GSP
	Table grapes (15 to 20 July)	14.1	10.6
	Cigars		9.1
2003–2013	Hake, flatfish, tuna, monkfish, saltwater fish	15–22	10.5–22 [c]
	Navels and sweet oranges (16 October to 31 March)	16% to (16%+€7.1/100 kg net)	Not covered by GSP
	Table grapes (21 July to 31 October)	14.1% to (17.6%+€9.6/100 kg/net)	Not covered by GSP
	Prepared and preserved beans		15.7
	Prepared and preserved pineapples and pineapple juice		11.7–15.7

Notes:
[a] to a value of €5 million or more in 2002.
[b] There are entries in this column only where an item is not covered by the GSP or where Chile is excluded from the GSP, or both.
[c] The upper rate is an MFN tariff, as not all items are covered by the GSP.
Sources: Eurostat 2003; UNCTAD TRAINS; EU–Chile Association Agreement.

The other items where Chile has significant exports, although not necessarily to the EU, and will benefit from a substantial improvement in market access are fresh-cut roses, carnations and other flowers, table grapes, oranges and fresh, chilled or frozen hake, monkfish and fish fillets. The main improvements to access for oranges have not yet been fully phased-in: the two varieties that were liberalized in 2003 still face significant specific duties if the entry price is below €35.4 per 100 kg (other than between 1 June and 15 October, when access is duty-free); the "liberalization" related only to the *ad valorem* element of the tariff which was quite low.

The ACP countries likely to be affected are Kenya, Zimbabwe, Namibia, Swaziland and Senegal. Botswana, Namibia and Swaziland would also be affected if the beef preference were to result in a change of market conditions in the EU – but with a TQ of only 1 000 tonnes any direct impact is likely to be very limited.

TABLE 3.10: CHILE: THE "AT RISK" ACP STATES

CN8	Brief description	Exporter	Exports to EU (€'000) 2002	Share of EU total 2002 (%)	Change in share 2000-02 (%)	EU tariff 2004	EU tariff 2002
Liberalization in 2003							
02023050	Frozen bovine boned crop chuck and blade and brisket cuts	Chile	-	0		0	12.8%+ €221.1[a]
		Namibia	6 397	32	-5	17.6€[a]	
		Botswana	4 157	21	2	17.6€[a]	
02023090	Frozen bovine boneless meat	Chile	-	0		0	12.8%+ €304.1[a]
		Botswana	4 559	2	-31	24.3€[a]	
		Namibia	1 482	1	26	24.3€[a]	
		PNG	28	0		304.1€[a]	
03026999	Fresh or chilled saltwater fish	Chile	632	15	-39	0	5.2 or 15
		Senegal	40 345	23	-11	0	
		Mauritania	16 305	9		0	
		Guinea	4 978	3	0	0	
03037998	Frozen saltwater fish	Chile	1 046	1	3	0	5.2
		Mauritania	7 400	7		0	
		Seychelles	7 314	7	200	0	
		Senegal	4 843	5	-11	0	
03075910	Frozen octopus (octopus spp.)	Chile	2 584	1	1	0	2.8
		Senegal	53 620	14	1	0	
		Mauritania	39 564	10		0	
		Ghana	4 340	1	341	0	
08044000	Avocados	Chile	3 448	2	475	0	4 or 5.1
		Kenya	12 331	8	-8	0	
		Swaziland	432	0	100	0	
		Dominican R.	342	0	-22	0	
08051030	Oranges-navel naveline navelate etc. (1 May to 15 October)[b]	Chile	321	0	68	0% to 7.1€[a,c]	3.2% to (4.8%+€7.1[a])
		Zimbabwe	9 285	3	3	0.9% to 0.9%+ 7.1€[a]	
		Belize	2 698	1	61		
		Swaziland	2 607	1	-22		
08051050	Sweet oranges (1 May to 15 October) [b]	Chile	-	0		0% to 7.1€ [a,c]	3.2% to (4.8%+€7.1[a])
		Zimbabwe	5 208	16	37	0.9% to 0.9%+ 7.1€[a]	
		Swaziland	3 170	10	40		
		Dominican R.	96	0	-15		
Liberalization 2003-2007							
03037987	Frozen swordfish (xiphias gladius)	Chile	1 031	2	-18	2.4	4
		Togo	3 621	7	236	0	
		Namibia	3 297	7	59	0	
		Seychelles	1 878	4		0	
06031010	Fresh-cut roses	Chile	-	0		5.1	8.5 or 12
		Kenya	139 060	46	12	0	
		Zimbabwe	37 015	12	-8	0	
		Zambia	21 671	7	10	0	
06031020	Fresh-cut carnations	Chile	3	0		5.1	8.5 or 12
		Kenya	8 974	8	-17	0	
		Dominican R.	3	0		0	
		United Rep. of Tanzania	1	0		0	
06031080	Fresh-cut flowers	Chile	79	0	227	5.1	8.5 or 12
		Kenya	45 433	21	17	0	
		Zimbabwe	27 562	13	4	0	
		Côte d'Ivoire	3 638	2	20	0	
08061010	Table grapes (1 November to 14 July) [b]	Chile	120 806	21	-9	4.5% to (8.6%+ 9.6€[a,c])	8% to (14.4%+€9.6[a])
		Namibia	12 630	2	69	0% to (14.4% +9.6€[a])	
		Kenya	2	0	-41		
		Dominican R.	1	0			

CN8	Brief description	Exporter	Exports to EU (€'000) 2002	Share of EU total 2002 (%)	Change in share 2000-02 (%)	EU tariff 2004	EU tariff 2002
Liberalization 2003-2010							
03049047	Frozen meat of hake (merluccius spp.)	Chile	6 505	16	6	3	4
		Namibia	16 531	41	-6	0	
08051030	Oranges – navel naveline navelate etc. (April) [b]	Chile	321	0	68	7.8% to 7.8%+ €7.1 [a,c]	10.4% to 10.4%+ €7.1[a]
		Zimbabwe	9 285	3	3	2% to 2%+€7.1[a]	
		Belize	2 698	1	61		
		Swaziland	2 607	1	-22		
08051050	Sweet oranges (April) [b]	Chile	-	0		7.8% to 7.8%+ €7.1 [a,c]	10.4% to 10.4%+ €7.1[a]
		Zimbabwe	5 208	16	37	2% to 2%+€7.1[a]	
		Swaziland	3 170	10	40		
		Dominican R.	96	0	-15		
08061010	Table grapes (15 to 20 July) [b]	Chile	120 806	21	-9	10.5	14.1
		Namibia	12 630	2	69	10.6	
		Kenya	2	0	-41	10.6	
		Dominican R.	1	0		10.6	
Liberalization 2003-2013							
03026966	Fresh or chilled hake	Chile	41	0	-76	12	15
		Namibia	23 568	27	-23	0	
		Mauritania	451	1		0	
03037811	Frozen hake	Chile	27	0	4	12.3	15
		Namibia	34 520	49	-10	0	
		Senegal	170	0	227	0	
03037981	Frozen monkfish	Chile	-	0		12.3	15
		Namibia	27 647	60	3	0	
		Senegal	229	0	70	0	
		Gabon	116	0	-11	0	
03041038	Fillets of saltwater fish fresh or chilled	Chile	653	1	-10	14.7	18
		Senegal	13 842	17	-3	0	
		United Rep. of Tanzania	2 064	3	30	0	
		Seychelles	2 040	3	-5	0	
03042095	Frozen fillets of saltwater fish	Chile	11 898	7	60	8.6 or 12.3	10.5 or 15
		Senegal	25 276	14	-1	0	
		Namibia	5 314	3	64	0	
		United Rep. of Tanzania	3 952	2	51	0	
08051030	Oranges – navel naveline navelate etc. (16 October to 31 March) [b]	Chile	321	0	68	13.1% to 13.1% + €7.1 [a,c]	16% to 16%+€7.1[a]
		Zimbabwe	9 285	3	3	3.2% to 3.2%+€7.1[a]	
		Belize	2 698	1	61		
		Swaziland	2 607	1	-22		
08051050	Sweet oranges (16 October to 31 March) [b]	Chile	-	0		13.1% to 13.1%+€7.1 [a,c]	16% to 16%+€7.1[a]
		Zimbabwe	5 208	16	37	3.2% to 3.2%+€7.1[a]	
		Swaziland	3 170	10	40		
		Dominican R.	96	0	-15		
08061010	Table grapes (21 July to 31 October) [b]	Chile	120 806	21	-9	11.5% to (14.4% +€9.6 [a,c])	14.1% to (17.6%+ €9.6[a])
		Namibia	12 630	2	69	14.1% to (17.6% +€9.6[a])	
		Kenya	2	0	-41		
		Dominican R.	1	0			

Notes:
[a]per 100 kg net
[b]The export values shown are for the whole year, not for the specific period indicated in the implementation schedule.
[c]Liberalization concerns *ad valorem* duty only; specific duty linked to the entry price is maintained.
Sources: Eurostat 2002 and 2003; EU–Chile Association Agreement; UK Tariff.

3.8 Conclusions

There is a great deal on agriculture and food security to negotiate on within the EPAs. Neither a satisfactory nor an unsatisfactory outcome is yet pre-ordained. The most critical task is for ACP countries to frame their current agricultural and livelihoods strategies in ways that make the link to EPAs, on both the export and import front, explicit and to establish the food security objectives that they need to achieve from any agreement.

Once established, the means to attain the objective can be developed. Much remains unclear on what would be in an EPA, but there is sufficient knowledge to allow quite extensive and detailed preparations to be made. It is known that the EU will require some liberalization by ACP members, wanting this to apply intra-regionally as well as in relation to trade with Europe). But only “substantially all” imports will be affected (which could be as low as 80 percent by value), and there will be a transition period that could be back-loaded.

The first step is for each country to identify its list of items to be excluded and back-loaded. Only then can the similarities or differences of potential EPA members be identified, and the implications noted of extending liberalization to intra-EPA trade. For example, an agreement by all EPA members to focus on agricultural products for which increased intra-regional trade could boost food security might be a very positive outcome from the negotiations.

On the export side, it is clear that ACP preferences will be eroded – but not all will disappear for all countries immediately. Moreover, there are possibilities (partly to be negotiated with the EU and partly in the WTO) that would extend the shelf-life of some preferences for some countries. As preferences are eroded, so the relative financial attractions of different agricultural activities will change. Food security plans need to take this into account. Even the process of retaining preferences for as long as possible may alter the impact of trade domestically, for example, by shifting it increasingly to the most competitive producers. The EPA negotiations provide both an institutional framework within which to develop these issues and an alarm bell to ACP food security strategists that policy may need to change in order to deal with the new emerging circumstances.

Preference erosion comes from many sources. EBA will be fully implemented by the time most EPAs get under way. The CAP is being reformed. The EU has enlarged. Doha continues to rumble away, and in the meantime, the EU is busy negotiating RTAs with the ACP’s competitors. In addition to all of these, however, the current patterns of trade are challenged by developments in the private sector. These involve the introduction of new SPS requirements that may be difficult for some countries to fulfil and that certainly bias production in favour of larger enterprises capable of supplying the paper-based compliance trail that is increasingly necessary in order to sell in the premium markets.

FAO is engaged proactively helping producers in developing countries not only to meet SPS requirements in major markets, but also to take advantage of them, for example in relation to organic food market niches (See FAO, 2001 and 2002). It is also heavily involved in the evolution of the GSP approach so that it can better support sustainable agriculture and rural development. It is providing an international and neutral platform for intergovernmental, private sector and civil society dialogue on the development of a GAP (FAO, 2003c). There may be considerable scope for using EPAs as both an institutional framework and a source of funds to continue both processes.

Once again, the EPAs both provide an institutional framework for addressing such concerns and need to take account of what is happening on the ground. FAO may have a substantial role to play helping individual ACP countries and producer groups within them to meet the public and private sector SPS and to foster global development of these standards in such a way as to make them development-friendly. All in all, there is a substantial amount of work to be done. The two years before the current Cotonou trade regime is due to end is not a long period within which to achieve all of this.

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Chapter 4
The impact of CAP reform on the EPAs

Introduction

The EU portrays its CAP reforms as an exercise in "liberalization". They have little in common with the concept of liberalization as understood by economists, however, which underpins the many analyses that aim to estimate the global effects of agricultural liberalization. Hence, there is no reason for which implementation of the CAP reforms should have the effects predicted in the economists' models.

Liberalization in the textbook sense means changing the government rules, taxes and subsidies that stop high-cost domestic producers from losing market share to lower-cost imports. It implies that the global location of production will change over time, with lower-cost producers increasing output and higher-cost producers declining. EU "liberalization", by contrast, aims to sustain European production but to reshuffle the subsidies and taxes to make them less costly to the European budget and more easily defensible in the WTO. They will have very limited effects on the EU's overall agricultural trade since they will neither decrease production nor increase market access. But they could erode ACP preferences.

The key structural change (see below) is a shift in the manner of supporting European farmers. There is a tendency to reduce the element of support that is provided through artificially high market prices, and to offset this decline, in whole or part, by income transfers. The problem for the ACP is that when their exporters benefit from the CAP, it is only from the artificially high prices; they have no access to direct producer subsidies. Hence, a change that maintained the level of subsidy at its current level but shifted its delivery from market prices to income transfer would tend to have an adverse effect on ACP exporters.

If there is no change to the terms of preference agreements, then the adverse effect would be felt particularly severely by exporters of products that are subject to TQs under Cotonou, e.g. sugar, beef, rice, other meats and some arable crops. In such cases, the architecture of the Cotonou Agreement would prevent even the most efficient ACP exporters from offsetting any decline in unit prices through an increase in the volume of exports.

The value of these trade preferences is also affected by complementary trade policy changes, such as the granting by the EU of preferences to other countries in the framework of RTAs, by the accession of new countries to the EU (see Chapter 5) and by internal EU policy changes. The most valuable preferences are for those commodities for which, paradoxically, the EU has the highest level of protection against third countries. These are generally agricultural products protected under the EU's CAP. In recognition of the value of these agricultural preferences to the ACP states, Article 1 (d) of Annex 5 dealing with the trade regime applicable during the preparatory period specifies:

The implications of these changes will depend partly on the level of costs in each ACP exporting state. Those producers with high costs may go out of business altogether even as a result of very small decline in EU domestic prices. There have long been fears, for example, for the long-term future of Caribbean sugar exports to Europe. More efficient suppliers may remain in business, but with lower profits for investing in the domestic economy. Mauritius is the best example of the productive use of trade policy rents. Profits from sugar have been invested in clothing since the 1970s and 1980s; profits from sugar plus clothing have been invested, first in tourism and now in other services.

Where CAP reforms affect the volume and price of EU exports, the tendency will be for world prices to rise. The absolute impact on world prices may not be great, but could be substantial for some ACP states. To the extent that ACP states have purchased cereals from the EU at "grey" prices, for example, they have benefited from a substantial additional subsidy although the goods do not qualify technically as food aid. If they are required in the future to obtain their imports from other sources, the price increase up to a "real" world market price level could be steep. On the other hand, there would be less competition for ACP exporters on their domestic and regional market.

The net effect, therefore, will be a complex set of losses and a number of potential gains. The balance of these effects will vary not only between countries, but often between socio-economic groups within countries. Many countries may be affected both positively and negatively at the same time. It is clearly important to try to start assessing the potential scale and incidence of these effects.

This chapter describes the background to the recent CAP reforms and the implications that these reforms will have for ACP states. These reforms are relevant to the EPA negotiations because they affect the value of the preferential access, which the ACP states are trying to safeguard through these agreements. Also, the Cotonou text clearly puts the commodity protocols "into play" in the negotiations, by agreeing to review them in the context of the new trading arrangements, while recognizing the special legal status of the Sugar Protocol. Finally, to the extent that the EPAs are seen as development instruments and not just trade instruments, their negotiation provides the ACP states with the opportunity to seek compensation for the loss of preferences arising from unilateral CAP reform, based on the commitment in Article 36 of the Cotonou Agreement where in the event of CAP reform, the EU ensures that ACP states continue to enjoy an advantage comparable to that previously enjoyed in relation to third countries.

4.1 The nature of reform

In the course of the past two to three years, the EU has undertaken considerable reform of the CAP, first in June 2003 with the MTR of the Agenda 2000 CAP reform and then in April 2004 when it adopted a package of reforms affecting Mediterranean-type products. In July 2004 the EU Commission proposed a major reform of the sugar regime. The legislative proposal setting out the reforms is now force starting from the 2005/2006 marketing year.

The significance of these reforms has not been lost on the ACP states. The Maputo Declaration, issued following the 4th Summit of ACP Heads of State and Government in June 2004, called for the following, inter alia:

> *We strongly urge the EU, in the process of its Common Agricultural Policy (CAP) reform, to examine thoroughly the effects on ACP economies with a view to mitigating any possible deleterious impacts. We are concerned by existing and potential damage to commodity export earnings through changes in the Common Market organization for key products. To this end, we also urge the EU to give due consideration to these adverse effects, in particular, with regard to bananas, sugar, rice and tuna, and responding appropriately to economic and trade interests of the ACP states (sic). Further, the EU should facilitate improved market access for ACP agricultural and value added food exports.*
>
> *We equally urge the EU to honour the provisions of Article 36(4) of the Cotonou Agreement, in particular the safeguarding of the benefits accruing to the ACP States from the Sugar Protocol. We therefore call on the European Union to ensure that under the future EC Sugar regime the ACP Protocol Sugar supplying states are guaranteed the same level of export earnings on a stable and predictable basis as provided to the EU sugar producers under the European Agricultural Guidance and Guarantee Fund (EAGGF).*

For many years, the EU's CAP was resistant to change. Apart from the introduction of milk quotas in 1984, its basic instruments remained largely untouched during the first 30 years of its existence (1961-1992). The CAP was introduced at a time when farming accounted for a much larger share of Europe's GDP and, in particular, greater employment than it does today, Europe was a net food importer and European agriculture was largely unmodernized. As the scientific revolution in farming took hold and partly facilitated by the high and stable prices guaranteed by the CAP, the face of European agriculture changed dramatically. Import deficits turned to commodity surpluses, there was a rapid outflow of labour to jobs in the growing manufacturing and services sectors, and the structure of farming became increasingly differentiated, distinguishing between a minority of large-scale, commercial producers and the larger number of smaller farms, often farmed on a part-time basis.

During the 1980s, the EU struggled with various mechanisms to try to curtail commodity surpluses and reduce the growing budgetary costs of its agricultural policy.

These mechanisms largely took the form of rules to bring about a reduction in the level of support prices whenever production or budget costs threatened to escalate out of control, and were often honoured more in the breach than in practice.

The first major change in the instrumentality of the CAP occurred as a result of the MacSharry reforms proposed in 1992 and eventually implemented in 1994. Ray MacSharry was the EU Commissioner for Agriculture at the time. The core of his reform was a nominal cut of 30 percent in the cereal price, phased-in over three years, complemented by smaller cuts in the institutional prices for beef and butter. The impact on farmers' incomes of these reductions in support prices were compensated by a per hectare payment in the case of cereals, and premium payments for beef cows and cattle. The 1992 reform introduced a set-aside scheme in the arable sector that allowed the Commission to curtail the arable area and gain control of surpluses. The reform also included three accompanying measures, including early retirement, agri-environment and afforestation schemes, designed to reduce production capacity and to improve the structure of farming.

The MacSharry reforms took place during the Uruguay Round of trade negotiations and facilitated its successful conclusion. The AoA led to all types of import protection, including the variable levy system used by the EU, being replaced by bound tariffs that were reduced by 36 percent on average; the binding and reduction of export subsidies by 36 percent in value and 21 percent in volume terms; and a 20 percent reduction in the aggregate level of trade-distorting domestic support over a six-year period. As a result of the Blair House deal with the United States right at the end of the negotiations, the EU's compensation payments were included in the blue box and were thus protected from reduction and challenge within the WTO.

The ink was not long dry on the MacSharry reforms before it was apparent that further reform would be needed. Forecasts of EU production and demand balances indicated that the EU would have difficulty in remaining within its WTO commitments after 2000, and there was a growing realization that the limits on export subsidies would prevent the EU from taking advantage of growth in export markets unless further reform was undertaken. The 1993 European Council meeting in Copenhagen offered EU membership to the countries of central and Eastern Europe, and there were fears that the cost of extending the CAP to the accession countries would be too great in the absence of further changes to the Policy. An Agricultural Strategy Paper produced by the Commission in 1995 put forward three options for continued reform: Status Quo (maintaining support levels and adjusting supply/demand imbalances through supply controls); Radical Free Market (abandoning price support); and Developing the 1992 Process (continuing the MacSharry process of gradual reductions in support compensated by direct payments) (Commission, 1995). The paper opted for the last of these options, which formed the basis for the next reform of the CAP proposed as part of the Agenda 2000 package and agreed on at the Berlin European Council in March 1999.

The Agenda 2000 reform included a reformulation of the aims of agricultural policy to give greater emphasis to environmental policy objectives and the multifunctional role of the European model of farming. It reduced cereals support prices by 15 percent, reduced the beef intervention price by 20 percent while replacing permanent intervention in the beef market by a much lower "safety net" intervention, and reduced dairy support prices by 15 percent, although this was postponed to the 2005/2006 marketing year because of the high budgetary costs of compensation. In each sector farmers were compensated for the revenue losses by an increase in the existing compensation payments and by the introduction of compensation in the milk sector in the form of a dairy premium per tonne of quota.

The Agenda 2000 package also introduced the idea of an integrated rural development policy as a second pillar of the CAP. This brought together the accompanying measures of the MacSharry reform plus compensatory allowances under the less favoured areas measure, as well as rural development measures previously financed by the FEOGA, into a single Rural Development Regulation. The Agreement also established tight budgetary limits on EU agricultural spending in the context of the EU's medium-term financial framework.

TABLE 4.1. THE CHANGING COMPOSITION OF EU FARM SUPPORT (PERCENT)

		European Union	United States
Market price support	1986–1988	57.7	6.3
	1995–1997	32.5	7.5
	2000–2002	30.3	9.3
Direct subsidies	1986–1988	10.3	7.7
	1995–1997	28.6	7.4
	2000–2002	30.1	17.0
Total producer support	1986–1988	68.0	13.9
	1995–1997	61.1	14.9
	2000–2002	60.4	26.3

Source: OECD PSE database, reworked with world prices as the denominator.

The impact of these two sets of reforms on producer support within the EU is shown in Table 4.1. What emerges clearly from the table is that there has been little change in the overall level of support, but a significant change in its composition. While the overall level of support (expressed as a percentage of the value of EU production at world prices) fell slightly from 68.0 percent in 1986-1988 to 60.4 percent in 2000-2002, the significance of market price support fell from 57.7 percent to 30.3 percent. This reinstrumentation of support (in WTO terms, moving support from the trade-distorting amber box to the less trade-distorting blue box) undoubtedly limits the trade-distorting impact of EU agricultural policy compared to the mechanism of open-ended price support that it replaced. But it still left the CAP vulnerable to a further round of trade reform. There was also growing internal dissatisfaction within Europe with the impact of agricultural policy, driven in part by an increasingly powerful environmental movement highlighting the negative impact of intensive agriculture on the natural environment, as well as by a succession of food and animal health scares which undermined consumer confidence in the food supply.

The latest CAP reforms

The Agenda 2000 Agreement was intended to cover the 2000-2006 period but had mandated a mid-term review in 2003. In the event, the Commission proposals went further than a mere fine-tuning of the previous reforms. The MTR agreed on by the Luxembourg Council of Agricultural Ministers in June 2003 has three main elements:

- *the bundling of all existing production-linked payments into a single farm payment that will be paid to farmers on the basis of their historic entitlements and that will be linked to land rather than production, which is the biggest change*. While the final negotiations gave member States more flexibility to retain production-linked payments than the Commission intended, it nonetheless remains a major step in the decoupling of direct aids from production. Eligibility for payments remains subject to cross-compliance with a variety of EU environmental, animal welfare and food safety standards;
- the continuation of the sectoral reform process with changes to the market regimes for problem *commodities such as durum wheat, rice and rye*;
- *the transfer of money between CAP objectives.* Up to 5 percent of the value of the single farm payment to larger farmers will be “modulated” and transferred to rural development measures. There is also a financial discipline mechanism whereby payments can be further reduced to ensure that overall expenditure remains within budgetary objectives.

While the Luxembourg Agreement is the core of the MTR, further reforms have also taken place in April 2004 with respect to a number of Mediterranean products, and the Commission’s proposal for reform of the sugar regime was made in July 2004. These reforms also need to be evaluated in the light of the decision of the European Council in October 2002 on the resources to be made available for CAP market expenditure and income support over the period 2007-2013. This chapter explains the content of these reforms and assesses their implications for the ACP group of countries.

Decoupling

The decoupling of production-linked payments to farmers is the centrepiece of the MTR. Its proponents see a number of advantages:

- It will greatly simplify the administrative burden on both farmers and state administrations in making payments to farmers. Instead of receiving money through up to a dozen different schemes, each with its own eligibility requirements and regulations, farmers will now receive a single payment without needing to demonstrate compliance with individual scheme regulations.

However, eligibility for the single farm payment will continue to require demonstration of "good agricultural practice" and farmland cannot be abandoned.

- The introduction of a single farm payment will encourage farmers to pursue a greater market orientation. Instead of production decisions being driven by "envelope farming", or the attempt to maximize the drawdown of subsidies, the only way farmers can increase their income in the future will be from the marketplace, which should give a greater incentive to take into account consumer needs and concerns.
- Because EU subsidies will no longer be linked to animal numbers, there will be a reduced incentive for farmers to intensify production, which should help to reduce the pressure on the environment. This impact will not be felt in cereal-growing areas where arable aid payments were already made on a per hectare basis unrelated to yield.
- There will be an improvement in the efficiency of income transfer to farmers. On some farms, farm income as reported in farm accounts surveys is less than the value of direct payments that the farmer received. Farmers are engaging in production at a loss in order to gain eligibility for the associated production-linked payment. Decoupling the direct payment will ensure that its entire value goes to increase farm incomes.
- Decoupling farm subsidies will make it easier to extend CAP payments to farmers in the accession countries after enlargement. Direct payments to farmers in these countries are being phased-in on an area basis under a simplified scheme intended to last for a transition period until 2006. It will be relatively easy to convert this to the single farm payment after that date.
- Finally, the single farm payment is designed with the criteria for green box supports in the WTO in mind, and it is thus hoped that the reform will make it easier to defend CAP payments in the WTO in the future.

Various flexibilities were allowed to member states as part of the compromises necessary to reach a final agreement. These include:

- The possibility to delay the start date to introduce decoupling from 2005 to 2007.
- The possibility to make the payments on a historic basis to individual farmers, or to pool the payments received, on either a national or regional basis, and to pay farmers on the basis of the national or regional average.
- The option to retain a proportion of the current production-linked payments based on a series of menu choices. Member states can:
- pay 25 percent of the arable aid payment or 40 percent of the durum wheat payment;
- pay 50 percent of the ewe premium;
- pay 100 percent of the suckler beef cow premium and 40 percent of the slaughter premium or 100 percent of the slaughter premium or 75 percent of the special male beef premium.

While France, for example, has opted to take maximum advantage of this last set of flexibilities, other countries such as the United Kingdom and Ireland have opted for full decoupling. In general, it is felt that the advantages of simplification will encourage all countries to move towards full decoupling over time.

The *greening* of the CAP

One of the motives behind the retention of partial coupling of direct payments has been the desire to prevent the abandonment of farmland in marginal farming regions. This is also linked to the growing importance of integrating environmental considerations into agricultural policy formulation. Formal recognition that the protection of the environment should be one of the functions of EU agriculture only dates back to 1985 with the publication of the Commission's Perspectives paper (Commission, 1985). We have seen that the MacSharry reform reforms introduced an agri-environment scheme that was the first attempt to pay farmers for the provision of environmental services. It also strengthened the environmental dimension of the various common market organizations. For example, set-aside in the arable crops regime was partly justified on environmental grounds. In the beef sector, the premia were made conditional on respecting maximum stocking rates, and additional payments were made to encourage further extensification. The Common Market Organization (CMO) for fruit and vegetables was changed to require producers to adopt integrated pest control.

The reformed CAP puts greater emphasis on cross-compliance. Hitherto cross-compliance was voluntary for member states and applied to environmental standards only. Cross-compliance is now compulsory for all farmers receiving direct payments. A “priority list” of 18 statutory European standards in the fields of environment, food safety, and animal health and welfare have been established and farmers will be sanctioned for non-respect of these standards through cuts in direct payments. Beneficiaries of direct payments will also be obliged to maintain all agricultural land in good agricultural and environmental condition in order to avoid land abandonment and subsequent environmental problems. Where a farmer fails to comply with such requirements, reductions in his payments will be applied as a sanction.

Modulation

The modulation rate of 5 percent will result in additional rural development funds of €1.2 billion a year being made available. The reform also extends the scope of currently available instruments for rural development, starting from 2005, to promote food quality, meet higher standards and foster animal welfare. The changes are targeted primarily to help farmers respond to new challenges. It will be for member states and regions to decide if they wish to take up these measures within their rural development programmes.

The new measures will comprise:

- *Food quality measures*: Incentive payments will be available for farmers who participate in recognized schemes designed to improve the quality of agricultural products and the production processes used and to give assurances to consumers on these issues and support for producer groups for activities intended to inform consumers on and promote the products produced under quality schemes will be eligible for public funds.
- *Meeting standards:* Member states may offer temporary and degressive support to help their farmers adapt to the introduction of demanding standards based on EU legislation concerning the environment, public, animal and plant health, and animal welfare. Aid will not be payable where an individual farmer is not respecting standards already included in national legislation.
- *Farm Advisory Service:* Support will be available for farmers to help them with the costs of using farm advisory services.
- *Animal welfare:* There is now provision to support farmers who enter into commitments for at least five years to improve the welfare of their farm animals and that go beyond usual good animal husbandry practice. Support will be payable annually on the basis of the additional costs and income foregone arising from such commitments.

Financial discipline

The need to control agricultural spending has always been one of the main driving forces of CAP reform. It is important, therefore, to examine the financial implications of the current MTR reforms and the extent to which they can be financed. The EU budget is organized on the basis of a medium-term financial perspective (FP). The current FP was agreed on as part of the Agenda 2000 package in 1999 and covers the period 2000-2006. It is agreed on as part of the Inter-Institutional Agreement between the two arms of the EU budgetary authority, the European Council and the European Parliament.

Each FP is characterized by:

- On the revenue side, an overall ceiling on the EU’s own resources, currently set at 1.24 percent of EU GNI in the Agenda 2000 FP. The EU’s own resources are a combination of “traditional” own resources (customs duties and agricultural levies, and a percentage VAT levy on a harmonized base of consumer expenditure) and the GNP resource (a percentage contribution from each member state based on its GNP).
- On the expenditure side, separate ceilings on commitment appropriations (i.e. commitments or promises to pay which are entered into in a particular year with a view to payment in that year or a subsequent year) and payments appropriations (i.e. actual payments in a particular year arising from commitments entered into in that year or in previous years). Because the EU budget is legally required to balance each year, payment appropriations cannot exceed the agreed ceiling on its own resources revenue.

- A classification of expenditure under a series of headings, each of which has its own expenditure ceiling. In the Agenda 2000 FP, agricultural expenditure is classified under two headings. Heading 1a refers to CAP market measures, including market support and direct payments expenditure, funded by FEOGA. Heading 1b refers to rural development expenditure funded by the FEOGA. The other main expenditure heading refers to the EU Structural Funds, designed to assist in achieving economic and social cohesion within the EU.

The Agenda 2000 FP was the first to make provision for EU enlargement. It also placed a ceiling on CAP Heading 1a market expenditure of €48 billion, increased by 2 percent per annum to allow for inflation. Actual CAP market expenditure has been below this ceiling in each of the years of the FP to date.

In February 2004 the Commission submitted its proposal for a financial perspective to cover the seven-year period 2007-2013. This is now being debated among the member states with a view to the new FP being approved by the European Council in June 2005. The Commission proposal aims to cover the needs of a 27-member state Union, consistent with the objective of allowing Bulgaria and Romania to join in January 2007 if they are ready. Key elements of the Commission's proposal are:

- The Commission proposes an FP with commitment appropriations averaging 1.26 percent of EU-27 GNI over the period. The payment appropriations arising from these commitments (and from the commitments outstanding from the period before 2007) are projected to average 1.14 percent of EU-27 GNI. This level of payment appropriations is consistent with the current own resources ceiling of 1.24 percent of GNI, assuming average GNI growth of 2.3 percent over the period; the Commission is not proposing a further increase.
- The Commission also proposes a reorganization of the expenditure headings to highlight their consistency with the EU's political priorities over the period. Agricultural expenditure would be included in a new Heading, "Preservation and Management of Natural Resources". CAP payments would be separately identified and subject to the October 2002 European Council decision on the ceilings for market expenditure and direct payments for EU-25. This decision was to hold the overall expenditure in nominal terms for market-related expenditure and direct payments for each year in the period 2007-2013 below the 2006 figure for the EU-25 allowed in the Agenda 2000 FP increased by 1 percent per year. Estimated expenditure for Bulgaria and Romania has been added to that figure.
- Rural development measures would be concentrated in a single instrument based on three objectives: increasing the competitiveness of the agricultural sector through support for restructuring; enhancing the environment through support for land management; and improving the quality of life in rural areas through promoting the diversification of economic activities.

The adequacy of these proposals to cover the demands for CAP expenditure over the 2007-2013 period are assessed as follows:

- There are significant differences among the member states in the appropriate level of EU expenditure in the next FP period and the methodology to be followed in agreeing on the FP by June 2005. The Commission proposal, supported by a number of member states, starts from an assessment of the needs of the enlarged EU over the coming period, taking into account the political and policy commitments already assumed by the Council. On this basis, it estimates that required expenditure will average 1.14 percent of EU GNI per annum. A number of other member states propose, instead, a top-down approach in which an overall budgetary ceiling is first agreed on and then policy objectives are prioritized within that ceiling. These member states have called for a 1 percent expenditure ceiling, which would require a paring back of EU expenditure commitments and would call into question the October 2002 agreement on the resources to be made available for CAP market measures.
- The EU has been able to accommodate the cost of extending the CAP to the new member states by introducing direct payments on a phased basis in accordance with the following schedule of increments expressed as a percentage of the level of such payments in the Union: 2004 – 25 percent; 2005 – 30 percent; 2006 – 35 percent; 2007 – 40 percent and thereafter in 10 percent increments so as to ensure that in 2013 the new member states reach the support level then applicable in the current EU. However, the margin between committed expenditure and the CAP market expenditure ceiling is now such that there is very little room to pay more compensation to

EU farmers for further cuts in support prices, for example, the sugar reform proposed in July 2004 or new dairy or beef reform if required by a new WTO trade agreement.

In its original MTR proposal, the Commission had proposed modulating the single farm payment to larger farmers by 20 percent in order to create additional resources for possible compensation in further CAP reform. As discussed above, this proposal was not accepted in the final package. However, the MTR regulation provides for direct payments to be cut if expenditure threatens to overshoot the CAP market expenditure ceiling.

4.2 Implications of CAP reform on selected products and for ACP states

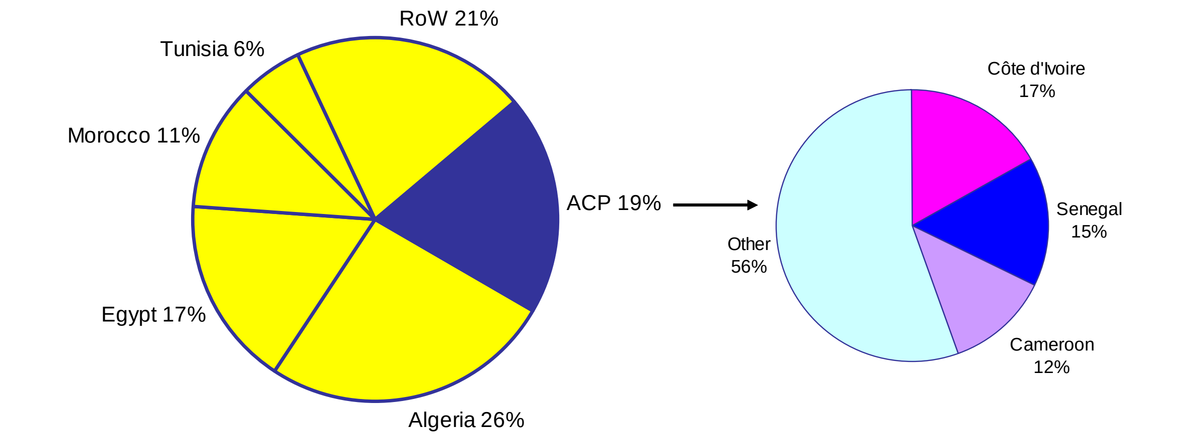
Budget resources currently appear to be adequate for the commitments that the EU has already entered into with respect to CAP market measures (compensation payments to EU farmers and the gradual extension of these payments to farmers in the new member states). The two main uncertainties are whether the agreed ceiling on CAP expenditure will be maintained in the new FP, and if so, whether even that ceiling could accommodate further increases in the single farm payment to compensate for any additional reductions in support prices. It might be argued that the absence of compensation would mean that it would be politically more difficult for the Council to agree to such reductions, thus putting a brake on further CAP reform. As further reform over the 2007-2013 period is likely to be driven largely by new WTO commitments, however, agricultural ministers may not be in a position to reject or soften reform proposals that the Commission might make. If the CAP budget is significantly reduced as a result of the pressures of the net contributor member states, the EU strategy is clearly to make the required adjustment to the single farm payment rather than to market support measures. Any impact on ACP trade flows would then depend on the extent to which the single farm payment is decoupled from production or not.

Cereals

The MTR has limited implications for the EU cereals market. Cereals support prices had been reduced in both the MacSharry and Agenda 2000 reforms, and farmers were compensated by means of arable aid payments, paid per hectare of cereals planted on eligible land. On larger farms, annual set-aside is required to retain eligibility for direct aids. Arable aid payments are thus currently coupled to the area planted, but decoupled with respect to yield.

Including arable aids in the decoupled single farm payment will have the following effects. On the one hand, some cereal farmers may now find it more profitable to switch out of cereals production given that they are no longer required to continue in cereals production to receive their annual payment. This might see a small fall in production. On the other hand, the concept of eligible land is eliminated and, in principle, other farmers can take up or expand cereals production on land not previously used to grow cereals while retaining any single farm payment they may be entitled to on that land. However, the MTR regulation states that member states should ensure that there is no significant decrease in permanent pasture land. While there is some margin of discretion as to how this is interpreted, the regulation will avoid any significant shift of land use from grassland to tillage. In addition, the compulsory set-aside provision on larger farms has been continued. The intervention prices for soft wheat, maize and barley remain unchanged although a 50 percent cut in monthly increments slightly reduces the effective support price. There are more significant changes for the minor crops of rye and durum wheat. In the case of rye, intervention is abolished in 2005 and, for durum wheat, supplemental payments to farmers in “traditional areas” are reduced and a special premium per tonne has been introduced.

FIGURE 4.1: EU EXPORTS OF WHEAT AND MESLIN



Source: Eurostat 2003.

Implications for ACP states

These changes do not have major implications for ACP states, as their consequences for the market balance in cereals within the EU will be minimal. Moving to decoupled payments is thought likely to reduce production by less than 1 percent, which is mostly accounted for by durum wheat and rye, where the accompanying policy changes have a greater impact on marginal production incentives (FAPRI, 2003). The slight fall in the effective support price offsets any small upward pressure on prices arising from reduced production, leaving EU internal prices unchanged. EU net grain exports will be slightly reduced, but the impact on world market prices will be an increase of less than 1 percent. Figure 4.1 shows the main importers of wheat and meslin from the EU. The ACP account for almost one-fifth of total EU wheat exports – a very substantial share given the countries' role in world trade. The three largest importers are the West African countries of Côte d'Ivoire, Senegal and Cameroon. North African countries account for a very large proportion of the rest. Indeed, the four North African countries identified in Figure 4.1 accounts for 60 percent of the total, between them. Africa accounts for almost four-fifths of Europe's wheat and meslin exports.

Rice

EU rice production is supported by an intervention price (currently €298.35/tonne), which increases with small monthly increments as well as significant tariff protection. In addition, compensatory payments differentiated by member state are paid per hectare of rice sown. Rice imports are, as in the case of other cereals, subject to import duty ceilings linked to the prevailing intervention price. In the case of husked indica, this is set at 180 percent of the EU rice intervention price. A ceiling is also imposed on the duty-paid import price of processed (milled) rice at a level of 263 percent of the intervention price in the case of indica rice. Intervention rice stocks have been growing, and there is the potential for the high EU price to attract significant imports from EBA countries once access to the EU rice market is fully liberalized for LDCs. As one of the three sensitive commodities, full liberalization of rice access will be phased-in between 1 September 2006 and 1 September 2009 by gradually reducing the full EU tariff to zero.

In the meantime, LDC rice can enter duty-free within the limits of a TQ. The quota will grow by 15 percent every year, from 2 517 tonnes (husked-rice equivalent) in 2001/2002 to 6 696 tonnes in 2008/2009 (September to August marketing year). Once the quota restrictions are removed, it is feared that rice imports from LDCs would put downward pressure on milled rice prices within the EU, while paddy rice prices would remain supported at intervention levels, leading to an unacceptable build-up in intervention stocks.[1]

Rice was therefore one of the few sectors where changes in the market regime were proposed in the MTR, following the failure to agree to a reform of the rice market in 2001. The changes agreed on

[1] For a review of the EU rice sector and the implication of reforms for ACP states, see http://www.agritrade.cta.int/rice/executive_brief.htm.

include a 50 percent reduction in the intervention price to €150/tonne to be applied from 2004/2005, the abolition of monthly increments and a limit on intervention purchases of rice to 75 000 tonnes per year. Compensation will be paid for this price reduction, more than half of which is to be included in the single farm payment. Because the reduction in the intervention price has the effect, given the tariff rules outlined above, of also reducing the applied tariff rate that can be applied to imported rice, the EU has sought to open negotiations in the framework of the WTO for the modification of the bound duties for rice with the EU's trading partners.

Implications for ACP states

The Commission's market forecasts for the period 2003-2010 project a 14 percent decline in rice production compared to the level that would have prevailed in the absence of reform. However, this implies an increase of some 2 percent compared to current levels of EU rice production attained in 2001 and 2003, but a reduction by 3 percent compared to production levels attained in 2002) (CTA, 2004a). EU rice imports are projected to increase significantly as EU rice consumption responds to the lower prices.

The main immediate effect will be felt by those ACP states that benefit from the preferential access arrangements for rice established under the Cotonou Agreement, which provide for a reduction in tariffs of 65 percent on amounts imported within specified TRQ. Guyana and Suriname are the two principal beneficiaries. These countries will clearly lose from the erosion of the value of their trade preferences in rice. It is of little comfort to learn that much of this fall would likely occur in any case once the rice market would be fully liberalized to LDC exporters after 2009. Compensatory trade measures, such as eliminating the remaining 35 percent share of the duty that ACP exporters must pay on in-quota exports, or increasing the size of these quotas would be a way of offering compensation to those ACP exporters adversely affected by the reform.

Beef

Coupled payments are more important in the beef sector than in the crops sector, and thus the decoupling of these payments in the MTR will have a corresponding larger effect on production. In many countries, payments make up almost the entire gross margin in the beef enterprise, suggesting that there could be a significant fall in production once the payments are decoupled. Considerable flexibility was left to member states on the degree of decoupling they could pursue. Member States can retain 100 percent of the suckler cow premium and 40 percent of the slaughter premium or 75 percent of the special male beef premium as coupled payments.

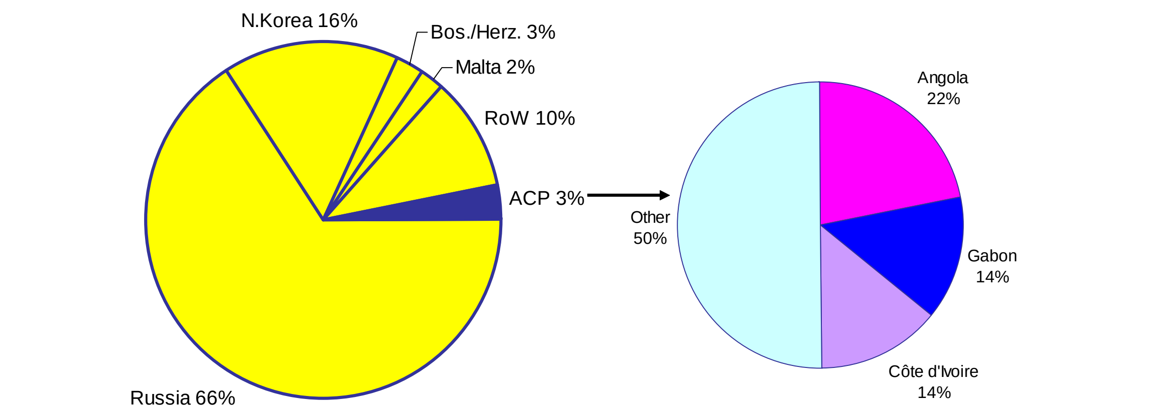
Estimates of the impact on beef output must take into account herd dynamics, which imply that the longer-term effects are likely to be considerably greater than in the short-term. Indeed, there could even be increased output and a dip in beef prices in the immediate term as farmers adjust their cattle inventories to the new incentive structure.

The Commission forecasts that internal beef prices could rise (on the assumption that imports remain limited by TRQs) by around 6 percent, while FAPRI project a smaller price increase of around 1 percent rising to 4 percent by 2012 (Commission, 2004a; FAPRI, 2003). Part of the difference might be accounted for by different assumptions on Commission behaviour in setting export refunds. The Commission could decide to react to rising internal beef prices by reducing the size of export refunds in compensation.

Implications for ACP states

The implications of the MTR should be separated from the longer-term implications of the Agenda 2000 reforms in the beef sector. The latter saw a reduction in beef support prices and the removal of the previous system of intervention support and its replacement by a “safety net” intervention system, which was expected to put downward pressure on producer prices of between 12 percent and 20 percent (see Commission, 2000). The expected slight fall in production and greater stimulus to consumption was expected to lead to a fall in net exports. Therefore, to the extent that the MTR might put some upward pressure on internal beef prices, this must be seen against the backdrop of the much larger reduction arising from the Agenda 2000 package. This is of importance to those ACP states that

FIGURE 4.2: EU EXPORTS OF FROZEN BEEF



Source: Eurostat 2003.

benefit from the Beef Protocol under the Cotonou Agreement. The ACP is a very modest market for Europe (two-thirds of its frozen beef exports going to Russia). Angola and Gabon, however, are the two largest ACP markets and their geographical proximity to the major beef-producing regions of the ACP makes it legitimate to question whether ACP export interests have been adversely affected by European supplies that are often sold at an extraordinarily low price.

In the case of EU exports of products that are mainly imported by ACP states, there is no such tension between the impact of CAP reform on exporter and importer interests. Here the immediate effect of any change is likely to be an adverse movement in the terms of trade of ACP importing states. While the Agenda 2000 reform led to erosion in the preferential margin enjoyed by ACP exporters, the MTR reform will, if anything, slightly increase it. The further fall in net exports of beef that will follow from decoupling will also be welcomed as removing a competitive source of beef supplies on international markets.

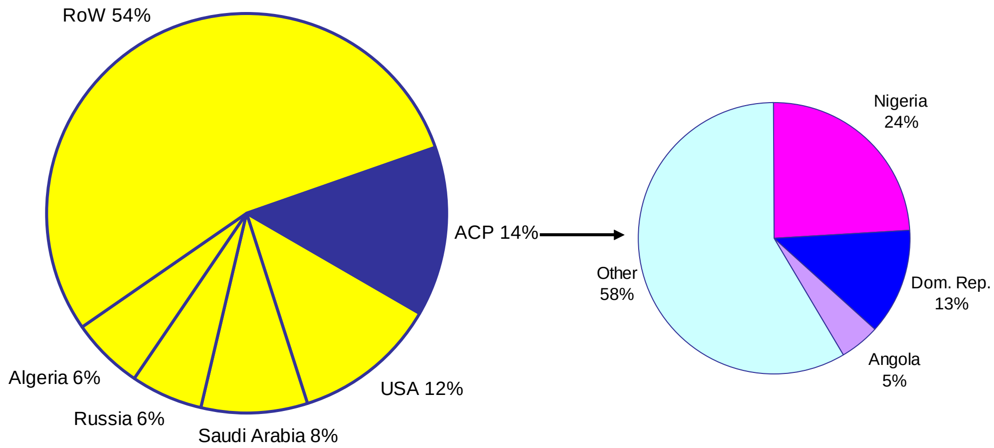
Dairy

The MTR confirmed that milk quotas will be kept until 2014/2015, and that there will be an increase of 0.5 percent per year in 2006, 2007 and 2008. The main thrust of the dairy reform is to reduce internal EU prices for dairy products towards world price levels. Dairy sector reform had already been agreed on in the Agenda 2000 package, which foresaw a reduction in the intervention prices for butter and SMP by 15 percent in three equal steps over the period 2005–2007. In the MTR the reduction in the butter intervention price was increased to 25 percent, to be phased-in over four years (7 percent in each of 2004, 2005 and 2006, and 4 percent in 2007), and the reductions were brought forward one year to start in 2004. In addition, the amount of butter that will be allowed to go into intervention automatically will be subject to a ceiling, which will fall from 70,000t in 2004 to a level of 30 000t from 2008 onwards. After the fixed amount of butter has been purchased into stores, the EU can operate a tender system and take in more butter, but this will probably operate at a lower intervention price, if it operates at all. This will effectively reduce the amount of support available in the market place. The target farm-gate price for milk has also been removed, which implies that export refunds will now be set on the basis of a tender system, which will further weaken support for the dairy market. Farmers will be compensated for this fall in market returns by means of a dairy premium that will be paid to them on the basis of quota held on March 2004. This payment must be decoupled and included in the single farm payment by 2007 at the latest.

Implications for ACP states

The changes made in the dairy sector are small, and it is likely that the milk quota will continue to determine production over the next decade in the absence of further policy change. Therefore, there will be no change in total milk production, but internal demand will be stimulated a little by the reduction in butter prices, which will lead to some small reduction in EU net exports. But while the aggregate effects will be small, the reduction in the butterfat price to farmers and the incorporation of the dairy premium into the single farm payment will lead to widespread restructuring of production in

FIGURE 4.3: EU EXPORTS OF DAIRY PRODUCTS



Source: Eurostat 2003.

many countries. The impact will be small on ACP states, which tend to be net importers of butteroil and milk powder. The ACP share of EU dairy product exports (Figure 4.3) is only slightly smaller – at 14 percent. For the first time in any of these charts, a non-African ACP country appears as a significant market – with the Dominican Republic taking one-eighth of the ACP share. But Nigeria is the main importer, and together with Angola, accounts for almost 30 percent of the ACP total. Only Algeria among the North African countries is a sufficiently large importer to be identified separately in the figure.

The "Mediterranean crops" reform of April 2004

At the Luxembourg Council in June 2003, the Council invited the Commission to submit a communication in autumn 2003 on the reform of the common market organizations for olive oil, tobacco and cotton based on the principles of the June CAP reform. The Commission submitted its Communication in September 2003 (Commission, 2003). It proposed transferring a significant part but not all of the current production-linked direct payments in these sectors to the single farm payment scheme, as from 1 January 2005. This would imply that these payments would have to respect the statutory EU environmental and food safety standards through cross-compliance and rules of good agricultural practice, and would be subject to the modulation and financial discipline mechanisms. The proposal for cotton is examined below as a case study of this approach.

The cotton sector proposals had become very politically sensitive given the high profile of the case made at the WTO Ministerial meeting in Cancún by four West African cotton exporters for direct and immediate action to eliminate the distortions caused in world cotton markets by the direct subsidies paid to cotton growers in developed countries. The EU currently contributes around 2.5 percent to total world production. The EU cotton regime does not use export subsidies and provides for duty-free access, so the only support to EU production has taken the form of direct payments. These take the form of a direct aid per tonne of unginned cotton, subject to a National Guaranteed Quantity for each member state. The level of the aid, which is granted to processors who agree to pay a minimum price to producers, is fixed periodically on the basis of the difference between a "guide price" and the world price.

In its Communication, the Commission proposed to transfer the expenditure on cotton during the reference period (2000-2002) into the funding of two producer-support measures. Sixty percent would be transferred to the single farm payment and the remaining 40 percent to a new production aid, granted as an area payment. The proposal would thus replace a deficiency payment-type mechanism by a mix of non-trade-distorting (green box) and less trade-distorting (blue box) forms of support which, according to the Commission, would minimize the already marginal impact of EU cotton on world markets. In the final agreement reached in April 2004, the proportion going to the decoupled single farm payment was actually increased (to 65 percent) and the proportion destined for the area aid was reduced (to 35 percent), with the introduction of the change delayed until 2006.

Similar mixed reforms were undertaken in the tobacco and olive oil sectors. In the case of tobacco, at least 40 percent of the current tobacco premia must be transferred into the single farm payment immediately, but member states can decide to retain up to 60 percent as a coupled payment for a maximum period of four years. After 2010, tobacco aid will be completely de-linked from production. Fifty percent will be transferred to the single farm payment, and the remaining 50 percent will be used for restructuring programmes under the rural development policy.

In the case of olive oil, a minimum of 60 percent of the average current production-linked payments during the reference period 2000-2002 will be converted into entitlements under the single farm payment scheme from 2006. For holdings smaller than 0.3 ha, 100 percent of payments must be decoupled. The remaining aid (40 percent) can be paid to producers as an olive grove payment.

Implications for ACP states

World cotton prices have been depressed by government support to cotton producers, especially in the United States, China and the EU. Prior to the meeting in Cancún, four West African cotton exporters proposed a Cotton Sectoral Initiative. This called for the establishment of a mechanism for phasing-out support for cotton production with a view to its total elimination and for financial compensation to LDCs as long as cotton subsidies continued. In the July 2004 Framework Agreement Establishing Modalities in Agriculture in the WTO negotiations, the vital importance of cotton for a number of developing countries was recognized. Members agreed to address the problems “ambitiously, expeditiously and specifically”, but within the context of the agriculture negotiations. A subcommittee on cotton was established in late 2004 to ensure that cotton is given due priority in the ongoing negotiations on the three pillars of support.

The impact of United States subsidies attracted most of the attention, partly because of their absolute size. In 2000/2001, United States assistance to its domestic cotton producers amounted to $2.3 billion, Chinese assistance amounted to $1.2 billion and EU assistance amounted to $700 million (ODI, 2004). This is also because United States subsidies were successfully formally complained about by Brazil to a WTO dispute panel. A recent ODI study argues that EU subsidies may be more damaging to developing countries and to West and Central Africa in particular, than its share in total subsidies would suggest because EU cotton production in Greece and Spain actively competes with cotton production from developing countries in third country markets (ODI, 2004).

If this is the case, then the EU cotton reform should considerably reduce the adverse effect of its policy on world markets and developing country exporters. The conversion of two-thirds of the current subsidy into a decoupled payment, which does not require farmers to grow cotton to receive this payment, and the conversion of the remainder into an area payment, should reduce the direct incentives for cotton production in southern Europe. However, the extent to which production will in fact fall will depend on the profitability of alternative crops, and even one-third of the current subsidy paid as an area payment may be sufficient to retain much of the existing area in cotton production. The key question is whether the EU has done enough in this reform to meet any specific disciplines that emerge from the remainder of the Doha Round negotiations designed to provide a satisfactory outcome to the cotton issue as mandated in the July 2004 Framework Agreement.

Sugar

Sugar briefly became part of the “Mediterranean crops” reform package when it was included in the Commission Communication on further CAP reform in September 2003. The EU had extended the sugar regime in 2001 for five years while asking the Commission to prepare a report on the sector with appropriate proposals in 2003. This Communication fulfilled the Commission’s obligation. While reforms for the other three crops included in the Communication (cotton, tobacco and olive oil) were agreed on in April 2004; however, the formal consultation on Commission proposals on sugar with various stakeholders that followed, were not published until July 2004. As well as setting out various options for reform, the Communication was accompanied by a summary of the Extended Impact Assessment of the various options considered.

The Commission Communication drew attention to a number of criticisms and drivers of change with respect to EU sugar policy:

- By encouraging non-competitive EU sugar production which must be disposed of on the world market, it distorts international trade and damages the development prospects of poor countries.
- The high internal EU price favours producers at the expense of consumers and processors.

- The allocation of quotas to member states leads to low market integration and inherently favours non-competitive production.
- High prices have encouraged producers to seek higher yields with negative environmental impacts.
- The unilateral import concessions awarded to the LDCs through the EBA initiative and to the Balkan countries have the potential of disrupting the balance of the EU sugar market.2 Further preferential imports may arise in the context of international negotiations with MERCOSUR or in establishing EPAs with the ACP states.
- The successful legal challenge to the EU sugar regime within the WTO by Brazil, Australia and Thailand will undermine the current export subsidy arrangements in the sector.

The Commission Impact Assessment examined four sets of options:

- *Status quo option.* This option would imply extending the current regime beyond 2006, but it would nonetheless embody some necessary changes, in particular, to accommodate the various preferential agreements that the EU has entered into, as well as respecting, current and future WTO disciplines. The continuing high EU internal market price relative to the world price would stimulate production expansion, especially in the favoured preference-receiving EBA countries. Production supported by EU intervention would depend on the actual volume of preferential imports and the allowed volume of subsidized exports. Some reduction in domestic “A” and “B” quotas would be necessary even under this option. As the WTO panel requested by Brazil, Australia and Thailand has already ruled against the EU sugar regime, the required reduction in sugar production in Europe is likely to be quite drastic. However, the essential features of the current regime, including the partition of the EU market into national quotas and the high cost imposed on EU consumers, would continue. There would be scope for reducing the EU beet price without affecting beet farmers’ incomes because there would be effective compensation in the form of abolished levies due to the reduction in “C” quota sugar exports.
- Fixed quota option. This option is similar to the first one except that it envisages reintroducing quotas on EBA and western Balkan preferential imports. It therefore has the drawback of requiring the EU to renege on an international commitment, which has been an important part of its negotiating position in the Doha Round. On the other hand, LDCs are themselves calling for negotiations to continue the orderly marketing arrangement now in force for EBA imports. The ACP states that are signatories to the Sugar Protocol have also come out in favour of returning to fixed quotas. If this option were introduced, the Commission foresees the possibility of encouraging greater mobility of quotas between member states, while maintaining a delicate balance between the principle of cohesion and an allocation of quotas according to comparative advantage.
- Fall in prices option. The principle behind this option is that EU market prices (supported by tariffs) would be allowed to fall to the point where internal EU consumption would be met by EU and preferential supplies. The tariff on non-preferential sugar, including safeguard duties, would be reduced to ensure parity between the entry price of non-preferential sugar and the EU market price. Implicit in this option is that high-cost producers both within member states and among ACP states would exit the market. EU beet farmers would be compensated by an increase in the single farm payment.

TABLE 4.2: MAIN CONSEQUENCES OF ALTERNATIVE SUGAR OPTIONS

	Present situation	**“Status quo” option**	**“Fixed quota” option**	**“Fall in prices” option**	**“Liberalization” option**
EU price [a] (€ per tonne)	725	600	600	450	350
EU production (million tonnes)	20.0	16.0	16.0	14.0	6.0
EU imports (million tonnes)	1.9	4.0	3.5	2.5	10.0
EU exports [b] (million tonnes)	5.3	4.0	3.5	0.5	0.0
Fall in ACP revenues (€ million)		150	150	300	350

Notes:
[a] price of white sugar
[b] including “C” quota sugar
Source: Commission Staff Working Paper SEC 2003.

2 Imports from Serbia and Montenegro were suspended for a period, but this suspension is now lifted.

- *Liberalization option.* This option would mean abolishing domestic price support for sugar and beet, as well as ending production quotas and quantitative and tariff restrictions on trade. In the absence of any protection, domestic sugar prices would fall into line with world market prices. The EU would become a major net sugar importer, but imports would come from competitive exporters, such as Brazil, rather than preferential exporters, as in the other options. The EU impact assessment highlights the potential dangers from a reduction in source of supply, with much greater exposure to the weather and economic and political risks of a single large supplier.

Implications for ACP states

Any option leading to a reduction in the internal market price will have a significant impact on the countries benefiting from the Sugar Protocol under the Cotonou Agreement. Furthermore, it would greatly reduce the potential benefits that LDCs might expect once quotas on preferential EBA imports are removed after 2008/2009.

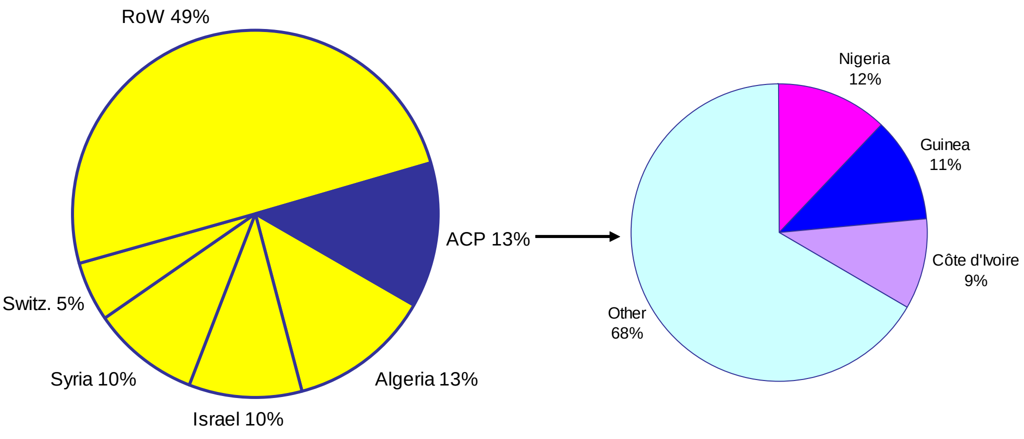
The expected fall in ACP export earnings under each of the options is shown in Table 2. (What is not clear from the text is whether these are net losses that include the offsetting impact of gains due to higher prices for non-EU exports.)

The implications for ACP states have been discussed in the CTA Executive Brief on the EU sugar regime (CTA, 2004b). The impact on individual countries will vary, depending on:

- the extent of their preferred access to the EU market;
- the extent of their access to other preferred markets;
- the extent of their exposure to world markets;
- their underlying costs of production;
- the scope for the expansion of low-cost sugar production to serve non-distorted world sugar markets.

The Commission Communication proposes an indicative two-stage scenario for the “fall in prices” option, which would result in a fall in the price offered for ACP sugar to €435 per tonne under phase I and to €290 per tonne under phase 2. In the first phase, it suggests that the Democratic Republic of the Congo, Jamaica and Madagascar would cease exports to the EU. Following the second phase, the Commission believes that only Zimbabwe, Zambia, Sudan, Ethiopia and Mozambique would continue exporting to the EU, and that the amounts supplied would be relatively small (around 0.2 million tonnes). CTA (2004b) argues that the Commission estimate of the revenue loss to ACP states of €300 million may well be an underestimate, and could be as high as €356 million. (In any case, the exact figure would depend on the level of world market prices assumed at the time of the calculation.) In addition, it points to the further losses to LDC sugar exporters. While these would be relatively modest on the basis of current export flows, which are limited by quota, if LDC sugar exports under the current EBA preferences would reach as high as 2.4 to 2.9 million tonnes as suggested by some agencies, then the losses in terms of benefits foregone to LDCs could be as high as €600 million.

FIGURE 4.4: EU EXPORTS OF SUGAR



Source: Eurostat 2003.

CTA (2004b) also points out that the ACP states could be adversely affected even if the "status quo" option were implemented. It was pointed out above that some reduction in domestic "A" and "B" quotas would be necessary even under this option. If the EU continued to adopt the policy of a pro-rata reduction in the "maximum supply needs" for cane sugar imports, in line with the reduction of EU "A" and "B" quotas, then ACP preferential sugar importers would not only be affected by any EU decision to reduce the internal price of sugar, but also by decisions to reduce the size of domestic quotas.

A final point highlighted by CTA (2004b) is that the process of reform could progressively relax the constraints on EU exports of sugar-based value-added foodstuffs imposed as a result of WTO disciplines on export refunds for these products (known as "non-Annex 1" products). Despite the fact that these refunds are intended to compensate food manufacturers for the higher cost of domestic sugar rather than confer a direct economic advantage to the processing sector, that a product is subsidized immediately brings it within the ambit of the WTO disciplines. If domestic EU sugar prices fall, this could result in an expansion in exports of non-subsidized simple value-added foods to African ACP states.

A number of United Kingdom development NGOs have pointed out that the value of the export refunds paid on the re-export of ACP sugar to the world market is around €800 million per annum, which is paid for from the CAP budget. If this is compared to the estimated €356 million loss to ACP producers from the "fall in prices" option,[3] it highlights the relatively inefficient way in which this mechanism transfers development finance to the recipients (Oxfam, 2004). The development NGOs also point out that the distribution of current ACP preferences has no poverty focus, in the sense that those few ACP states that benefit from the current Sugar Protocol are arguably not those with the greatest development needs. Nonetheless, a significant sugar policy reform is likely to lead to the collapse of the sugar industry in the relatively high-cost and small-island ACP states, which currently benefit from the Sugar Protocol.

In the light of these impact assessments, both the ACP group and LDCs have called for support for the status quo or fixed quota options in the Commission's September 2003 Communication. In March 2004, the LDCs submitted a proposal that the EU would defer the liberalization of sugar market access under the EBA proposal until the period 2016 to 2019[4] and would substitute instead gradually increasing quotas, both for raw and refined sugar. On the EU side, it would agree to maintain the value of access for preferential sugar at a remunerative level during this period. Following that period, the EU would be free to opt for any of the options included in the Commission's September 2003 Communication, including presumably full liberalization. The LDCs' proposal is based on the belief that LDCs have the potential to be low-cost exporters of sugar in the medium-term, but that their industries need a period of sustained investment to be able to compete with the well-established industries in Brazil, Australia and Thailand.[5]

The Commission's July 2004 proposal, however, recommended the "fall in prices" option, with an even larger price cut than envisaged in the September 2003 document (Commission, 2004b). The main features of the Commission proposal are:

- reduction of the institutional support price from €632/tonne to €421/tonne in two steps over three years;
- reduction of the minimum price for sugar beet from €43.6/tonne to €27.4/tonne in two steps over three years;
- abolition of public intervention, to be replaced by a private storage scheme;
- reduction of the EU-25 production quota by 2.8 million tones, from 17.4 tonnes to 14.6 tonnes over four years;
- new decoupled payment for sugar beet farmers to partially compensate (60 percent) for their income losses;

[3] Oxfam put the premium received by ACP states by exporting to the EU rather than to the world market slightly higher, at around €433 million.

[4] The EU proposes to reduce the CCT on sugar products from 100 percent to 0 percent for imports from EBA countries between 1 July 2006 and 1 July 2009.

[5] See www.sugartraders.co.uk/proposal0304.pdf.

- compensation to be funded by the substantially reducing in export refund expenditure and from abolishing the production refund for the chemical and pharmaceutical industries and of the refining aid;
- quotas transferable between factories in different member states;
- conversion scheme of €250/tonne for factories leaving the sector whose quota is not purchased by operators elsewhere, with the resulting quota extinguished;
- provision for review of the sugar regime in 2008, owing to the uncertainty of the outcome of the WTO Doha Round and the real effects of the EBA Agreement when the sugar market is fully opened to LDCs.

The Commission projects that the 33 percent cumulative reduction in the white sugar intervention price plus the reduction in production under quota will lead to a reduction in EU-25 subsidized exports of 2 million tonnes. The Commission also foresees that imports from preferential partners will increase by the relatively small amount of 0.5 million tonnes over the four years 2005/06 to 2008/09 (from 1.9 to 2.4 million tonnes), mainly because of the impact of the zero tariff arrangements under the EBA for LDCs. It is important to recall that EBA imports are still restricted to TQ amounts throughout this period. The Commission further expects a reduction in production under quota as a result of the quota cuts of 2.8 million tonnes.

Thus, the net reduction in internal supply is of the order of 2.3 million tonnes, but as domestic sugar consumption is expected to continue to fall by 0.2 - 0.3 million tonnes, the expected reduction in subsidized exports is just 2 million tonnes. The Commission proposal fails to discuss the likely impact on “C” sugar or unsubsidized exports, which amount to around 2.7 million tonnes. The WTO panel on the complaint brought by Brazil, Australia and Thailand in its interim report has apparently ruled that these exports are effectively cross-subsidized by quota sugar production. It has also apparently ruled that the EU is contravening its WTO commitments by subsidizing the re-export of an amount equivalent to imports of sugar from the ACP states and India of 1.6 million tonnes (Oxfam, 2004). If these findings are upheld in the final Panel Report and on appeal, and then if the EU wishes to maintain the lower price level of €421/tonne, even more drastic cuts in quota would be required.

Even a 33 percent reduction in the internal support price would have a significant adverse effect on ACP preferential exporters. The Commission estimates that the lower intervention price would translate into a raw sugar price of €329/tonne, compared to the current price of €523.7/tonne. On 1.3 million tonnes of Sugar Protocol imports, this amounts to a revenue loss of €253 million. In addition, there would be further losses to preferential exporters who benefit from the special preferential sugar arrangements. The Commission has suggested that, in time, after unlimited access is provided to EBA countries after 2009/2010, the Maximum Supply Needs instrument would no longer be needed, which will effectively lead to the demise of the SPS scheme. Non-LDC exporters in southern Africa who currently benefit from this scheme will lose out as a result.

In its July 2004 proposal the Commission recognizes that its implementation would imply adjustments in the sugar sector of ACP states and India. It has put forward some guidelines of an action plan which defines (although vaguely) appropriate accompanying measures, which will include both trade and development measures. On the trade side, the Commission points out that the Cotonou Agreement foresees the review of the Sugar Protocol in the context of the EPA negotiations, and that the Sugar Protocol should be integrated into the EPAs in such a way “that does not prejudge the EU’s commitment to LDCs for full market access for sugar from 2009 and that ensures full compatibility with WTO rules.” As regards development measures, the Commission intends to propose the introduction of specific measures to help Sugar Protocol countries/India to adapt to new market conditions.

Such programmes “would focus on improving the competitiveness of the sugar sector where it is viable, and on supporting diversification where improvements in competitiveness in the sugar sector are not sustainable.”

4.3 Implications of CAP reform for the EU's WTO commitments

A potentially important indirect effect of CAP reform from the viewpoint of the ACP states is its implications for the EU's negotiating stance in the Doha Round. To what extent does the reform make it easier for the EU to propose and agree to significant reductions in domestic support, market access barriers and export subsidies? This issue is explored in a recent FAPRI analysis of the MTR, and its conclusions are summarized here (FAPRI, 2003).

The principal element of the MTR is the introduction of the single farm payment, which is constructed to fit within the current definition of green box support. Therefore, the main effect of the reforms will be to transfer a sizeable portion of EU agricultural payments from the blue box (payments which are currently exempt from disciplines on the grounds that they are production-limiting) to the green box. The small changes to the dairy, rye and rice market regimes will result in only a small reduction in amber box (trade-distorting) support. The FAPRI classification of projected payments is shown in Table 4.3. (Recall that the assumption underlying this analysis, which was undertaken in September 2003 before countries had clarified what use they would make of the flexibilities available in the regulation, was that the single farm payment would be introduced from 2005 on.) Two scenarios are modelled, one where it is assumed countries would choose the minimum permissible level of decoupling (LEAST) and one where countries fully decouple (MOST). In the LEAST scenario, blue box spending falls to €7 billion annually by 2007, and in the MOST scenario, to €0.4 billion annually. In both scenarios, annual amber box spending falls slightly, to around €32 billion. In the baseline scenario based on pre-2003 CAP reform policies, FAPRI estimates that amber box spending would amount to around €34 billion, while blue box spending would rise to around €27 billion.

These figures suggest that the EU could afford to make a generous offer on domestic support without needing to go beyond the policy structure just approved in the MTR. Projected amber box levels are approximately 52 percent below the Aggregate Measurement of Support (AMS) limit, and this is very close to the EU offer to cut trade-distorting (amber box) support by 55 percent in the Doha Round. Also, the projected level of blue box support, even under the LEAST scenario, is below the limit of 5 percent of the value of production suggested in the joint United States-EU framework proposal in August 2003.

CAP reform will have a significant effect on EU domestic support measures, but has much less impact on reducing EU export subsidies or import barriers. Both the Commission market forecasts and the FAPRI analysis suggest only small net changes in EU net trade, domestic prices or world prices for most commodities. FAPRI points out, for example, that EU net trade in wheat and coarse grains is only around one million tonnes lower in the CAP reform scenarios than in the baseline, and both EU and world prices change by less than 1 percent.

There are three specific exceptions to this generalization: in beef, EU market prices rise but exports, and therefore the need for export subsidies, fall; further, the fall in EU butter prices reduces the tariff level necessary to protect the EU market, while EU rice prices also fall sharply and net imports are lower than in the baseline.

TABLE 4.3: EU-15 DOMESTIC SUPPORT LEVELS, MILLION EURO

	2001/2	2002/3	2003/4	2005/6	2008/9
Permitted AMS	**67 170**	**67 170**	**67 170**		
Current AMS					
Baseline	40 081	34 814	34 687	34 332	33 520
MOST			34 687	32 972	32 121
LEAST			34 687	33 059	32 208
Blue box					
Baseline	23 064	24 018	23 989	25 020	27 033
MOST			23 989	367	379
LEAST			23 989	26 976	7 089

Source: FAPRI 2003.

4.4 Conclusions

The latest steps in CAP reform confirm the direction that the EU has been taking since the MacSharry reforms in 1993. Market support prices have been reduced, with at least partial compensation provided to EU producers by means of direct payments. In the latest reform step, these direct payments have now been largely but not totally decoupled from production.

The consequences of these changes for ACP states will occur through four channels:

- Insofar as these changes affect the net export position of the EU compared to what it would have been in their absence, the latest CAP reforms will impact on the ACP through their position as net exporters or importers of the relevant commodities.
- Insofar as some ACP states benefit from preferential access to the EU market, the reforms will diminish the value of this access.
- While EU farmers have been compensated for the loss of revenue arising from the reforms, ACP states with preferential access have not. The Cotonou Agreement makes it clear that the EU undertakes to ensure that ACP states continue to enjoy an advantage comparable to that previously enjoyed in relation to third countries. The EPA negotiations provide the opportunity to press the EU to fulfil this commitment.

While not a direct result of CAP reform, the EPA negotiations must also address the future of the commodity protocols. The CAP reform influences both the future value of these protocols and the EU’s room for manoeuvre to improve them.

In examining the impact of the latest CAP reforms on the net export position of the EU, a key issue is the extent to which the decoupling of direct payments will in fact lower production incentives to EU farmers. The fact that EU farmers will no longer have to produce particular crops or animal products in order to be eligible for these payments could also lead to a restructuring of the overall level of production. Although the new single farm payment is not directly linked to either production levels or market conditions such as prices, farmers must continue to hold land and to keep it in good agricultural condition in order to retain eligibility for these payments. It is not realistic to assume that farmers’ production decisions are wholly uninfluenced by the level of these payments (even leaving aside that, for some years, a number of member states have opted to retain partial coupling to output levels in any case). On the other hand, it would be wrong to draw the conclusion that because the overall level of payments to EU farmers is unchanged, they will continue to produce exactly the same amount as they would have done in the absence of decoupling. Over time, production levels in the EU will be driven increasingly by the level of market prices and not by the effective price including the compensation payments.

Based on an assessment of the market effects for individual products, this chapter concludes that the largest impacts of reform will be felt in the sugar and rice sectors, followed by the beef and cotton sectors, and with only limited effects for milk and cereal products excluding rice. The largest effect will be felt in the sugar market because here the proposed reform includes both a significant price reduction (33 percent) and a sharp fall in production induced by a quota reduction. The large impact in the rice sector is because of the 50 percent cut in the support price for rice, and the fact that half of the compensation payment will be decoupled.

The impact on the cotton market is due to the fact that two-thirds of the current output subsidy will be decoupled, and the remainder paid as an area subsidy. The impact on the beef market also arises entirely because of the decoupling of the compensatory payments in the beef sector, which will raise the domestic EU beef price above the level that it would otherwise achieve. The limited impact on the dairy market is due to the fact that production will remain limited by quota, and the limited impact on the other cereal markets is because the existing arable aid payments are area-based and thus largely decoupled in any case.

The implications of these changes will affect ACP states, in the first instance, depending on whether they are net importers or net exporters of the relevant products. Further, those countries which benefit from preferential access will be worse off because of the changes in the sugar and rice regimes, although those countries benefiting from the Beef Protocol could be slightly better off as a result of the CAP reform. In the same way that compensation for EU farmers can be calculated, it is easy to assess the loss of revenue that ACP beneficiaries will experience as a result of the loss in the value of their preferences. These figures should provide the starting point for negotiations with the EU on appropriate forms of compensation.

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Chapter 5
Implications of EU enlargement for ACP agricultural trade

Introduction

In Copenhagen, in December 2002, the EU completed negotiations with ten potential new members – eight Central and Eastern European (CEE) countries – Poland, Hungary, Czech Republic, Slovakia, Slovenia, Estonia, Latvia and Lithuania – and Cyprus and Malta. All of these countries became EU members on 1 May 2004. EU enlargement will have an impact on agricultural commodity markets in both current and new member states. The consequent changes in production and consumption will influence trade flows both within the enlarged EU and between the EU and the rest of the world. This chapter discusses the context for these changes, their likely magnitude and the possible opportunities and threats for ACP countries.

The chapter has three objectives:

- to describe the agricultural trade policy and other changes that resulted from the accession of the ten new member states to the EU;
- to discuss the channels and mechanisms by which third countries, including ACP countries, might be affected by these changes;
- to identify specific ACP commodity trade flows that may be influenced by these changes, either positively or negatively.

The agricultural dimensions of enlargement to include the ten CEECs are well known. The EU population will increase by 28 percent, arable land area by 38 percent and livestock output by around 20 percent. Economic reform during the 1990s transformed the volume and mix of these countries' production, consumption and trade. Agricultural production fell by up to 30 percent in many countries, as the heavy state supports to farm production under the centrally planned regimes were removed, markets in the Newly Independent States (NIS) of the former Soviet Union disappeared, the terms of trade moved unfavourably against farmers. Further, it has taken time to replace the input supply and marketing chains disrupted by the restructuring of farms (Pouliquen, 2001; Leifert and Swinnen, 2002).

TABLE 5.1: BASIC INDICATORS OF THE ACCESSION COUNTRIES, 2001

Country	Population ('000)	Per capita GDP as percent of EU average (%)	Agricultural land ('000 ha)	Arable land ('000 ha)	Agricultural share of GDP (%)	Agricultural share of employment (%)
Cyprus	790	83	117	72	4.0	4.8
Czech Republic	10 2260	61	4 278	3 076	4.2	4.6
Estonia	1 337	37	1 433	1 120	5.7	7.1
Hungary	9 917	52	5 865	4 614	4.3	6.1
Latvia	2 406	30	2 480	1 841	4.8	15.1
Lithuania	3 689	28	3 487	2 930	7.2	16.5
Malta	392	n.a.	10	9	2.6	2.3
Poland	38 577	38	18 392	13 974	3.8	19.2
Slovakia	5 403	50	2 450	1 450	4.5	6.3
All 2004 candidates	74 796	n.a.	38 479	28 496	n.a.	n.a.
EU-15	375 346	n.a.	142 614	74 470	1.5	4.7

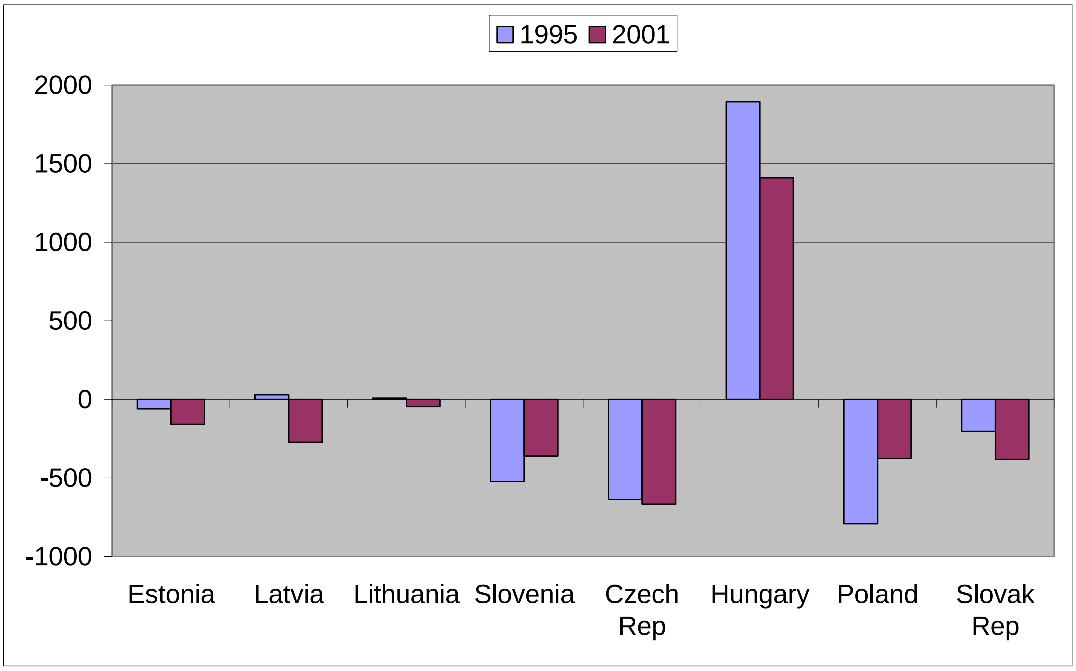
Source: Cochrane 2004b.

5.1 EU Policy framework in an EU-25 Context

Pre-accession trade relations

In all accession countries, the share of agriculture and food exports in total exports has declined since the early 1990s. The shares are highest for the Baltic countries, such as 12.3 percent for Lithuania in 2001, followed by Poland and Hungary around 7-8 percent. The share of agro-food imports in total imports showed some increase in the mid-1990s, but has since begun to decline. Shares are again highest in the Baltic countries; Latvia has the highest proportion at 12.8 percent. Among the new member states, only Hungary shows a net exporter position in agri-food products (Figure 5.1). For the eight larger accession countries, excluding Cyprus and Malta, the region was self-sufficient in food in 1994. A large deficit of €1.9 billion opened up in 1996, and the deficit fluctuated around €1.5 billion during the remainder of the 1990s.

FIGURE 5.1: AGRICULTURAL AND FOOD TRADE BALANCES IN THE CEECs IN 1995 AND 2001



Source: OECD 2002. The figure for Slovak Republic is for 2000 rather than 2001.

The accession countries already have significant agri-food trade links with the EU. For example, the EU accounted for around 50 percent of the exports of Poland and Hungary in 2001. Although the EU market is becoming more important for the Baltic countries, its share of the agri-food exports of the other accession states has been falling. There is a clear trend for the importance of the NIS as an export market to decline, while inter-CEEC trade, already important for most countries, has been growing over time.

The EU signed a succession of agreements during the 1990s designed to promote integration with the new member states. Trade protocols attached to Association Agreements provided a means for steadily increasing mutual market access. Reciprocal tariff concessions were offered on agricultural goods, although sensitive CAP products were not included in the early stages. In 2000, the EU signed "double zero" agreements with all the candidate countries. The idea was to provide duty-free access, within TQs set at a level covering traditional trade volumes, in return for the abolition of export subsidies.

As a result, almost two-thirds of traditional trade in agricultural producers was exempt from import duties (Commission, 2002). TRQs opened for some agricultural products under these agreements were increased from July 2001. Further tariff concessions for processed products were extended at various times between August 2001 and February 2002. These were followed by the "double profit" agreements signed in 2002, which opened duty-free quotas for the most sensitive CAP products, such as wheat, corn, beef and dairy products excluded from the first round of agreements, and which allowed nearly free trade in fruits and vegetables. At the same time, progress was made in reducing and removing TBT and SPS barriers to trade, which, for example, restricted the ability of milk and meat processors in some of the accession countries to export to the EU during this period. As a result of these agreements, much of CEEC-EU agricultural trade has already been liberalized.

Simultaneously, trade barriers on agri-food trade between the CEECs themselves were reducing. The three Baltic States were members of the Baltic Agricultural Free Trade Agreement (BAFTA), while the Central European Free Trade Agreement (CEFTA) provided the framework for regional trade between the rest of the CEEC-10. The trend towards more liberal trade under these agreements was occasionally interrupted as governments re-introduced import tariffs and other trade barriers as a result of import surges from neighbouring countries.

Accession arrangements

The EU first set out its accession strategy in the Agenda 2000 plan adopted by the Berlin European Council in 1999. This was based on a two-stage strategy, with an initial six CEECs expected to join in 2002. Under the EU's medium-term financial framework for the period 2000-2006, sums were allocated for regional development and agriculture in the new member states during this period. Importantly, no provision was made for the extension of direct payments to farmers in the accession countries. The candidate countries began the process of adopting the Community acquis, a complex process of planning, screening and reporting on their progress in implementing the legislative changes and introducing the institutional structures to implement EU agricultural policy. This has been a massive effort, including the establishment of financial controls and databases, and the management of border controls, animal identification and land parcel registration essential for the operation of the CAP (Jensen and Frandsen, 2003).

In October 2002, EU leaders reached an agreement on a financial ceiling for CAP market expenditure for the medium-term. In the Agenda 2000 package, it had been agreed to stabilize CAP market expenditures (excluding rural development) at €40.5 billion (at 1999 prices) over the period 2000-2006, plus a 2 percent annual allowance to adjust for inflation. This agreement was extended in October 2002 to cover the period 2007 to 2013, but with a lower inflation adjustment figure of 1 percent. This then set the framework within which the EU had to finance the extension of the CAP to the new member states.

In March 2002, the European Commission proposed a comprehensive financial plan for the agricultural aspects of enlargement. The CEECs never agreed to their exclusion from direct payments. The Commission plan accepted their position but met the financial constraint by proposing a long phasing-in period. Direct payments would be set initially at 25 percent of the EU level in 2004, gradually increasing over a ten-year period to parity. The plan also set out the Commission's views on the appropriate levels of reference quantities, quotas and reference yields, etc.

These were generally related to recent production levels in the CEECs, in contrast to the proposals of the CEECs themselves, which tended to be based on the higher levels of output realized before transition began and the presumed potential for the existing higher output.

In November 2002, the EU introduced the idea that CEECs would be permitted to "top up" their direct payments from their national budgets, as well as use funds being made available under EU rural development programmes. This would permit payments up to 40 percent of the level of payments to farmers in the existing member states in the first year, with gradual increases thereafter. This proposal was prompted in part by the realization that some new members states could otherwise become net contributors to the EU budget immediately after enlargement. Further concessions were made at the Copenhagen Summit in December 2002 where the final accession agreement was reached. The maximum allowable proportion of existing EU payment levels was raised to 55 percent in the first year. CEECs were offered a simplified implementation scheme for direct payments that was not tied to actual production at the farm level; they were not required to introduce a set-aside scheme for arable crops, at least for a limited period after accession. Quota and reference quantity levels were also bargained upwards in the final negotiations, but remained well below what the accession countries had originally sought.

5.2 Implications of EU enlargement for agri-food trade policy

As noted previously, trade integration between the EU and the new member states had already advanced quite far under the Europe Agreements. Nonetheless, some important changes took place on 1 May 2003. All remaining tariffs and export subsidies were eliminated in addition to non-tariff barriers on internal trade within the EU-25. These included remaining tariffs on trade between the CEECs themselves. Actions now that were sometimes taken by CEEC governments would no longer be possible, such as imposing increased import duties and minimum import prices, enhancing export subsidy programmes and tightening veterinary checks as a way of relieving import pressure on domestic markets. Because of food safety concerns, a special “safeguard clause” in the Treaty of Accession (Article 38) provides the EU with powers to seal off a country if a food safety problem occurs. Such measures can be taken up to three years after accession and may remain in force after this period. Transitional periods are in place for some food processing plants in the new member states to give them time to meet the quality and hygiene standards demanded by EU legislation. During this period only sales on the domestic market will be permitted.

Enlargement also brought important changes in the external trade policy of the CEECs. The accession states aligned their external border protection on the EU’s Common External Tariff (CET). They also took on the obligations of the EU’s preferential trade regimes, including duty-free access for the LDCs under the EBA scheme and the trade provisions of the Cotonou Agreement. Like all WTO members, the CEECs had negotiated schedules of commitments in the Uruguay Round AoA. Since these countries were still emerging from central planning at the time of these negotiations, they were given a status similar to that of developing countries. They could set their bound tariffs using ceiling bindings and not necessarily reflecting the difference between the national and the international price. In general, bound duties were set at relatively high levels, although the rates applied in practice were much lower. A particular instance is Romania (not part of the current accession wave), which negotiated average bound tariffs for agri-food products of 143 percent, compared to the Czech Republic average of 18 percent (Chevassus-Lozza and Unguru, 2001).

In general, while adoption of the CET will imply a lowering of the weighted average of the tariffs applied to third countries by the CEECs, this is not necessarily true for all countries and commodities. In their analysis of four countries Chevassus-Lozza and Unguru found that for Poland and Hungary the adoption of the EU tariff would lower tariff protection while the opposite would be the case for the Czech Republic and Slovakia.

Article XXIV.5 of GATT requires that the duties applied by countries forming a CU “shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union”. A 1994 Understanding makes it clear that it is the weighted applied tariff average that should be used in assessing conformity with this provision. Article XXIV.6 obliges the EU to enter into negotiations with third countries that have negotiating rights in any of the accession countries to agree on compensation if the adoption of the EU’s CET results in an increase in the bound tariff of that country, taking due account of reductions of duties on the same tariff line made by other countries joining the CU at the same time. Compensation can only be claimed by principal suppliers whose share of imports by the accession countries must therefore, by definition, be greater than the EU, or “suppliers with a substantial interest”, generally interpreted as exporters with more than 10 percent of the market. The EU has notified the relevant trade statistics to the WTO and is waiting for third countries to lodge claims for negotiating compensation. On the basis of previous experience, the most likely form of compensation for potential losers is the creation of tariff rate quotas within a quota based on past trade flows. Chevassus-Lozza and Ungaru (2001) believe that there will only be a limited basis for compensation claims, mainly affecting bananas (some Latin American suppliers), rice (Asian countries) and mushrooms and fruits (China).

EU enlargement means the harmonization of accession country health, safety, and related standards to EU norms. This process will be on balance favourable to third country exporters that sell to the EU and thus already meet EU standards. For example, a United Kingdom importer of an ACP agricultural export that is approved in the EU may want to sell it in the Czech Republic, but find that the Czech authorities claim that it does not meet the Czech standard. Not having to design, test, and certify products for small national markets in central and eastern Europe will lower costs and open markets that otherwise might be too small for some third country exporters to tackle. Accession also means acceptance by the candidate countries of EU non-tariff barriers to trade, such as EU directives regarding genetically modified organisms (GMOs) and the ban on imports of hormone-treated beef. Another example is due to a ban on treating carcasses with chlorine, the EU currently bans all poultry meat imports from the United States, which could cost the United States its market for cheap poultry cuts in Poland and the Baltic States (Cochrane, 2004a). There are swings and roundabouts here, because the accession countries gave up previous national regulations that may have been more restrictive on some issues than EU law.

Potential impact

Trade effects of EU enlargement

There are two kinds of trade effects of EU enlargement:

- those resulting from the changes in trade policy described above affecting the level of the trade barriers on intra-EU and extra-EU trade;
- those resulting from the extension of the CAP price and income support policies to agricultural markets and producers in the new member states.

The admission of ten new countries to the EU CU will have classic trade creation and trade diversion effects. *Trade creation* is the replacement of high-cost domestic production in one of the countries of the enlarged EU by lower cost production, either from one of the other member states or from third countries. An example would be if German pork exports increase following enlargement at the expense of pigmeat production in Hungary because the latter is not competitive due to lower feed efficiency. Economists generally see trade creation as welfare-enhancing, although this assumes that the resources created unemployment in Hungary can quickly find alternative employment opportunities. From the point of view of ACP countries, the lowering of tariff barriers in the EU-10, as well as the opening of preferential market access opportunities should also encourage trade creation for export products where ACP countries can become competitive suppliers.

Trade diversion is the second channel through which ACP exports might be affected, this time negatively. Trade diversion is where imports from competitive third countries before enlargement are displaced by higher cost production from another member state of the enlarged EU, simply because of the more favourable access the latter country now enjoys as a member state. For example, during the 1990s the United States built up a market in Poland and the Baltic states for low-cost poultry products. An example of trade diversion would be if as a result of enlargement, this market were now supplied by poultry producers in Germany or the Netherlands. For ACP countries, any danger of trade diversion would arise with respect to current exports to the EU-15, which might potentially face more intensive competition from producers in the new member states. Even where it is shown that ACP countries and the EU-10 both export similar products to the EU-15 (thus raising at least the possibility of trade diversion), the fact that EU-10 producers are likely already to be benefiting from duty-free access to the EU-15 market should be borne in mind.

The next trade effect likely to follow from EU enlargement is also a positive one from the point of view of ACP exporters. This is the *trade expansion* effect that will follow from the expected boost to economic growth rates in the new member states following accession. If their economic growth accelerates, then all existing exporters to their markets will benefit in proportion to their existing market shares. Statistics of trade flows between ACP countries and the EU-10 will be examined later in order to identify which products might benefit from this effect.

Price changes and supply response following enlargement

The second way in which EU enlargement may affect ACP agri-food trade is through the extension of CAP price and income support mechanisms to farmers in the new member states. The conventional wisdom has been that the extension of the CAP to cover agricultural production in the EU-10 would provide a significant stimulus to increased production while tending to dampen consumption. The increased export surplus was expected to lead to increased competition on the markets of the EU-15, as well as increasing the overall net export surplus of the enlarged EU. Fears were expressed that this would put additional pressure on the EU budget and make it more difficult for the EU to remain inside its WTO commitments without further CAP reform.

The reality is likely to be a little different. According to the conventional view, support prices in the CEECs were considerably lower than those in the EU-15, with the implication that enlargement would bring a significant boost in the profitability of farm production.

However, price levels in the accession countries had been converging steadily on the EU price level for many years, for a number of reasons:

- Changes in exchange rates meant that the currencies of the candidate countries gradually strengthened against the euro.
- CAP reform under Agenda 2000 meant reduced EU intervention prices for arable crops, beef and sheepmeat.
- CEE governments during the 1990s deliberately began to align their prices with those in the EU as part of their preparations for EU membership.

For many products, price gaps in the 1990s reflected quality differences rather than policy differences. For example, prices for pork and beef in the EU are reported for the three top grades in terms of lean meat content, whereas CEE statistical offices have historically reported average prices for all grades. As meat quality improved and more beef and pork entered the higher grades in the CEECs, so have their average prices converged on EU levels (Cochrane, 2004a).

Of course, important variations existed at the individual country and commodity level. For example, in Poland, wheat farmers received higher support prices than in the EU, while Slovenian farmers also had high levels of protection for both crop and animal products.

Production incentives are also affected by direct payments. Direct payments to farmers in the CEECs were much less important than in the EU-15, largely because of budget constraints in the former. Because of the lower reference yields and also the phasing-in of the payments over ten years, the per hectare payments received in the CEECs will initially be around one-quarter of those received by the average EU farmer. Payments, of course, will vary by country and by farm size (Cochrane, 2004a). The agreement to extend the Agenda 2000 levels of direct payment to farmers in the CEECs, particularly when the simplified area system came to an end in 2009 and payments were eventually coupled to production, could have provided a powerful incentive to increase production. However, the CAP reforms approved in June 2003 will convert these payments to a single whole-farm payment between 2005 and 2007, so that they will remain decoupled from production decisions. The new payment will not differ very much from the simplified area system currently in place in the CEECs. There is still debate on the extent to which these payments can be considered decoupled, given that they remain linked to the use of land. Some boost to production should therefore likely occur once farmers in the CEECs start to receive these payments.

Another factor likely to limit supply response in the new member states is the additional burden of meeting food safety and production process standards and the high cost of compliance. Grain producers will have to meet minimum quality standards to receive the EU price. Livestock farmers will have to observe animal welfare regulations and follow the record-keeping requirements of the EU. These measures will increase production costs and erode the net returns of producers (Cochrane, 2004a).

5.3 Implications for commodity market balances

In the light of these uncertainties, the likely impact of enlargement on market balances for the main agricultural products in the EU-25 will be examined. For this section, information has been drawn from the most recent set of market forecasts prepared by the Commission for the period 2003-2010 (DG Agri, 2003).

These show that the market surpluses likely to be available in the CEEC-10 following enlargement will remain very small, with the important exception of cereals and particularly coarse grains.

At first sight, therefore, the implications of enlargement for commodity market balances in the EU-25 look fairly minor.[1] The perspective adopted in examining these forecasts is important. One can

[1] At the individual country and commodity level, considerably more "action" can be expected. The most comprehensive study to date to explore this has been prepared by the Danish Food Economics Research Institute (Jensen and Frandsen, 2003). However, the Danish study was undertaken before the CAP MTR, and thus factors in an important stimulus effect from the extension of (coupled) direct payments.

adopt a *before and after* approach, in which the overall level of net exports for the enlarged Union in 2010 is compared to the existing levels for the EU-15 and the CEEC-10 separately in 2003. This indicates the overall change in the level of competition, which ACP exporters of particular commodities might face, or the overall change in the level of market opportunities, which might be available. The development in the market balance for each commodity over the decade is the outcome of all influences affecting consumption and production trends in the old and new member states, including the policy changes due to enlargement. Alternatively, one can adopt a *with and without* approach. Here, the focus is purely on whether enlargement per se makes a difference to the overall EU market balance in 2010 as compared to what it would be for the countries involved without enlargement.

The Commission's market projections are based on a number of assumptions. These include that the EU's WTO commitments will be respected but are not expected to change over the 2003-2010 period. An exchange rate for the euro of around 1.1 to the United States dollar is also assumed as the Commission expects the short-run factors that have contributed to the recent weakness of the United States dollar to reverse over the medium-term. Specifically, in the case of cereals, the projections assume that the reduction in the set-aside rate from 10 percent to 5 percent in the arable crop sector for the 2004/2005 marketing year will be reversed to 10 percent again from 2005 onwards. On this basis, the Commission expects EU-25 **cereals** production to rebound from 230 million tonnes in 2003 to 272 million tonnes in 2004, and to stabilize at this level reaching 277 million tonnes in 2010. It believes that this additional supply will be absorbed by a sustained domestic market, resulting in the stabilization of the marketable surplus in the EU-15, at around 20 million tonnes. Imports of around 11 million tonnes should also remain stable following the implementation of the new import regime for medium and low quality wheat and barley. Thus, the Commission is forecasting EU-15 exports of around 31 million tonnes by the end of the decade. This will be slightly above the annual limit for subsidized EU-15 exports set by the URAA due to some unsubsidized exports of durum wheat, common wheat and malt barley. The projections indicate a further 6-7 million tonnes marketable surplus in the CEE-10. The Commission forecasts that the enlarged EU will increase its internal trade of cereals, with increased markets for barley in the new member states offset by increased imports of maize by the EU-15, particularly from Hungary.

The Commission expects the EU-15 **beef** market to be in slight deficit in the medium term, with imports exceeding exports. The new member states will increase the projected EU-15 levels of production and consumption by approximately 10 percent, adding around 100 000t to the EU marketable surplus. As a result, the Commission expects a decline in average EU beef prices of around €50 to 70€/tonne, compared to the situation without enlargement.

The Commission's projections for **pork and poultry** envisage a steady expansion in production, largely driven by increases in internal and external demand over the period. Pork and poultry consumption will be favoured by the expected increase in beef prices arising from the decoupling of direct payments in the beef sector and by positive demand trends in the new member states.

However, diverging trends are expected in the relative competitiveness of member states in these two sectors. Poultry production is increasingly competitive in the new member states, where there has been significant foreign investment in production and processing. Following enlargement, a growing share of this production will be exported to the current members states. In the case of pork production, the new member states are foreseen to exhibit a comparative disadvantage with respect to quality (lean meat content) and feed efficiency, resulting in a net import flow from the current member states.

The outlook for milk products in the enlarged EU-25 will be affected by CAP reform. Production of bulk products – butter and SMP – is expected to increase in the short term in the new member states because of a significant increase in their prices. In the longer term, however, production of butter and SMP is expected to decline in the current member states. This will help to balance the EU-25 milk market over the medium term despite the structural surplus of bulk dairy products in the new member states. The movement from butter/SMP production in the current member states will be encouraged by the expected strong growth in demand for cheese and fresh dairy products in the new member states. The impact on milk prices will depend on the speed with which the dairy industry in the current and new member states can restructure production towards marketable products.

The focus so far on the impact on the market balances for bulk agricultural commodities overlooks the fact that the most dynamic sector within agri-food trade is likely to be in processed foods. This will be driven by rising consumer incomes in the CEECs and the demand for greater variety. More disaggregated analysis of the trade experience during the 1990s shows that the sudden increase in the variety of goods available to consumers in the accession countries, compared to what was available under central planning, translated into an initial large deficit in differentiated goods, balanced in part by exports of homogeneous commodity products (Pouliquen, 2001). In time, however, we would expect to see an increase in intra-industry trade within food groups as firms in the accession countries compete increasingly on quality and less on price.

One area where producers in the new member states may be able to convert an apparent disadvantage, such as low intensity of production, into a comparative advantage, and achieve premium prices, is by selling some agricultural produce as organic produce. National bodies have been set up in most countries to set organic standards and to take responsibility for the control and certification of organically produced goods under the EU 2091/91 regulation, the law on organic standards within the EU. Since there is very little domestic demand as yet for organic produce in the new member states, organic production will only develop on the basis of export demand in the near future.

5.4 Implications for the ACP countries

The changes described as a result of the recent EU enlargement could have three possible effects on ACP states, which might be combined. Indeed, any one country could experience all three of the effects, with differential impacts on socio-economic groups.

These are:

- increased competition on the EU market and other markets for products that the ACP currently export or might export in the future;
- increased demand on the EU-25 market for goods that the ACP export;
- an increased supply to the world market from EU-25 of goods that the ACP import.

While the incremental trade policy changes that occurred in May 2004 are not major (since, as noted above, many were presaged by earlier transition measures), their impact on Europe’s demand and supply for goods is likely to become evident only over time. On the contrary, some of the effects may already have been experienced (resulting from the earlier reforms in the transition period), and others will become apparent (amid a flurry of other changes) over the next five or ten years.

It is premature, therefore, to try to identify precisely which ACP country or socio-economic group has been affected and in which way. Nonetheless, a broad-brush sensitization analysis can show the products where some sort of effect appears to be most likely and the ACP countries for which this might be important, as described in the remainder of the chapter.

Potential export competition

What products are exported by both the EU-10 and the ACP? The answer, in broad terms, is shown in Table 5.2. There are just four: frozen beef, fish (which may of course be of very different varieties), sugar and molasses, and coffee or tea extracts and essences. Of these, beef and sugar would seem to be the most likely areas for direct competition, given the nature of the products and the EU regimes.

The EU regime for enlargement on sugar claims to be “neutral” in the sense that EU-10 will not have a net effect on either EU imports or exports. But net figures can conceal a considerable degree of underlying trade – and it remains to be seen whether or not the terms of accession in relation to sugar produce a desired result. Effectively, the impact of enlargement needs to be fed into the scenario-building around CAP reform.

Potential export demand

Table 5.3 lists the principal areas in which enlargement might result in an increase in demand for ACP exports. These are products that are imported already by the EU-10. The adoption by them of the acquis means that ACP countries will now have improved access to the markets of some new members. The range of products in Table 5.3 provides no surprises, since they are standard ACP exports.

TABLE 5.2: AREAS OF POTENTIAL EXPORT COMPETITION

Product	HS heads	New entrants' exports 2002 ('000€)	ACP exports to EU 2002 ('000€)
Frozen beef	0202	23 885	16 649
Fish	0304, 1604	290 797	380 280
Sugar and molasses	1701, 1703	78 997	15 107
Coffee or tea extracts, essences, etc.	2101	29 847	27 688

Source: Eurostat 2003.

TABLE 5.3: INCREASED DEMAND FOR ACP EXPORTS

Product	HS heads	New entrants' exports 2002 ('000€)	ACP exports to EU 2002 ('000€)
Frozen beef	0202	13 027	16 649
Fish	0304	212 260	197 329
Cut flowers	0603	27 313	313 672
Bananas	0803	249 105	448 660
Citrus fruit	0805	87 100	24 590
Coffee, tea and extracts/ essences	0901, 0902, 2101	294 988	859 787
Sugar	1701	37 579	12 627
Cocoa	1801, 1803, 1804	247 141	2 214 884
Tobacco and products	2401, 2402	242 456	468 879

Source: Eurostat 2003.

TABLE 5.4: INCREASED SUPPLY OF GOODS THAT ACP IMPORT

Product	HS heads	New entrants' exports 2002 ('000€)	ACP exports to EU 2002 ('000€)
Frozen beef	0202	23 885	10 098
Pork	0203	141 234	12 728
Poultry offal	0207	46 307	134 080
Dairy products	0401, 0402, 0405, 0406	564 011	39 987
Potatoes	0701	19 301	25 077
Wheat and meslin	1001	281 291	221 869
Soya bean oil	1507	12 147	114 495
Sugar	1701	52 294	137 474

Source: Eurostat 2003.

The principal question mark will be over the ACP supply capacity. In few, if any, cases do the ACP supply more than a handful of national markets in the EU-15. These markets can absorb all the products that the ACP can supply, except, of course, items that are quota-constrained, and even for beef it is clear that the ACP do not fill the existing TQ. Nonetheless, if increased supply capacity is considered to be part of a revitalization of ACP economies, then the increase in demand is to be welcomed. Even if ACP states do not export directly to the EU-10, some of their competitors may do so, thus relieving pressure on them in the more traditional markets.

Import effects

Table 5.4 shows the products produced in the EU-10 that are imported to a significant extent by ACP countries. An interesting feature of 7 is that some products, such as beef and sugar, appear in all three! This underlines the varied nature of the ACP economies and the fact that even individual countries sometimes import and export the same product. Nevertheless, the presence of wheat and dairy products in Table 5.4, which are significant ACP imports that might be subject to higher prices following CAP reform, should be a slight reassurance that supplies will not necessarily dry up.

5.5 Conclusions

Finally, EU enlargement integrates the agri-food markets of the old and new member states of the EU-25. It sets in train a process whereby production growth in each country will depend on its underlying comparative advantage within the enlarged EU, rather than being influenced by trade barriers of one sort or another. The immediate impacts of enlargement on agri-food trade will be relatively limited. This is partially due to the gradual integration of agri-food markets under the earlier Europe Agreements. It also reflects the gradual convergence of price levels within the new member states to those prevailing in the EU in the years prior to accession. The relatively restrictive allocations of quota and reference quantities to the new member states, based on recent production levels rather than historic or hypothetical levels, will also help to limit the production impact of membership. Finally, by removing the production incentive of coupled payments that had been due to kick in under the pre-reform regime after 2009, the 2003 CAP reform will limit the market effects of enlargement in the medium term.

TABLE 5.5: AGRI-FOOD EXPORTS AND IMPORTS BY DESTINATION, 1993 AND 2001

	EU	OECD	CEECs	NIS	Other	Total
Agriculture and food exports by destination, 1993						
Estonia	18	0	21	45	17	100
Latvia	10	5	20	66	1	100
Lithuania	16	4	12	66	2	100
Slovenia	36	12	2	5	45	100
Czech Rep.	33	9	32	13	13	100
Hungary	54	n.a.	n.a.	20	n.a.	100
Poland	58	13	6	18	5	100
Slovak Rep.	16	7	57	13	7	100
Agriculture and food exports by destination, 2001						
Estonia	18	7	24	36	14	100
Latvia	23	13	29	33	2	100
Lithuania	32	12	24	29	3	100
Slovenia	30	4	3	2	61	100
Czech Rep.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Hungary	48	8	31	10	3	100
Poland	48	5	12	20	15	100
Slovak Rep.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Agriculture and food imports by destination, 1993						
Estonia	50	0	5	9	36	100
Latvia	36	11	17	25	10	100
Lithuania	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Slovenia	32	19	11	2	36	100
Czech Rep.	44	11	20	1	24	100
Hungary	54	n.a.	n.a.	2	n.a.	100
Poland	52	20	7	2	18	100
Slovak Rep.	24	10	51	1	14	100
Agriculture and food exports by destination, 2001						
Estonia	52	6	15	7	19	100
Latvia	44	17	30	4	5	100
Lithuania	51	9	27	11	3	100
Slovenia	49	6	16	2	27	100
Czech Rep.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Hungary	47	7	17	2	27	100
Poland	53	7	10	3	27	100
Slovak Rep.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Source: OECD 2002

With the exception of Hungary, the agri-food trade of all of the new member states moved into deficit during the 1990s. EU membership will help to reverse this trend, but the effects for the main commodity markets will not be major. The Commission expects maize exports to EU-15 markets to increase, while barley exports will increase in the other direction. The CEE-10 will export a little more beef to EU-15 markets, and also poultry, but it is expected that pork exports will increase in the other direction. CEE-10 exports of bulk dairy products will increase, but will be offset by increased imports of cheese and fresh dairy products. With greater investment in the food processing sector in the CEECs, including foreign investment, greater two-way trade, particularly of processed food products, will take place. The speed at which this occurs will be influenced by whether the new member states can make effective use of EU structural fund assistance over the next few years.

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Chapter 6
Fish trade issues in WTO and ACP–EU negotiations

Introduction

Total world exports of fish and fishery products grew by 8.5 percent in 2003 to US$63.2 billion with the share of developing countries in fish exports slightly above 50 percent. Net exports earned by developing countries from fish trade in 2003 were US$18 billion, an amount larger than for any other traded food commodity such as rice, cocoa, tea, sugar or coffee.

For many developing nations, fish trade represents a significant source of foreign currency earnings, in addition to the sector's important role in income generation, employment and food security. For LIFDCs alone, net export revenues in 2002 were US$8.2 billion. The LIFDCs account for 20 percent of total exports in value terms.

World imports are more concentrated, with developed countries accounting for over 80 percent in value terms. Japan is the biggest single importer of fishery products, accounting for some 18 percent of the total, but its share is declining. The EU has further increased its dependency on imports for its fish supply and is the largest world market for fish imports (39 percent), when seen together as a group. The United States, in addition to being the world's fourth major exporting country, is the second biggest single country importer (17 percent). Overall, 38 percent of world fishery production is now traded internationally (live weight equivalent). In 2002, for the first time China became the world's largest exporter, overtaking Thailand. China is by far the largest producer of fish in the world, but is also an important fish importer, the eighth largest in 2003.

Among the major issues concerning international trade in fishery products are the following:

changes in quality and safety control measures in the main importing countries;

- introduction of new labelling requirements and the concept of traceability in major markets;
- residues in products from aquaculture;
- the concern of the general public about over-exploitation of fish stocks;
- the sustainability of aquaculture, including its future feed requirements;
- illegal, unreported and unregulated fishing (IUU);
- value-addition and third-country processing in developing countries;
- international trade negotiations in the WTO;
- expansion of regional trade areas and the increasing number of new bilateral trade agreements including those being negotiated by ACP-EU.

6.1 WTO and fisheries

With 148 countries now members of the WTO, virtually all international fish trade is regulated by the WTO trade agreements. The only two important suppliers of fish to world markets that are not yet members, the Russian Federation and Viet Nam, have commenced negotiations to join and could become full members starting from 2005 or 2006. As a result of the Uruguay Round, the previous round of multilateral trade negotiations which took place in 1986-1994, international trade in fish and fishery products was further liberalized with import duties on fish and fishery products in developed countries now reduced to an average 4.5 percent. However, most developing countries maintain considerably higher import tariffs.

The current Doha Round includes a number of issues of particular importance to international trade in fish and fishery products, including improved market access, fisheries subsidies, environmental labelling, the relationship between WTO trade rules and environmental agreements, as well as technical assistance and capacity- building.

Market access

Improved market access for fish and fishery products is linked to reductions in tariffs and in non-tariff barriers. It is important to note that fish and fishery products are not covered by the WTO's AoA. Improved market access for fishery products is therefore linked to progress in the negotiations on "Market Access for Non-Agricultural Products".

After the completion of the Uruguay Round, average weighted import tariffs on fish products in developed countries were reduced to around 4.5 percent. However, this average hides a number of tariff peaks and cases of tariff escalation for processed or value added fish products in the most important import markets. Import duties in developed country markets continue, therefore, to present a barrier to processing and economic development in the fishery industries in many developing countries.

In the present Round, a proposal has been tabled for sectoral elimination of import duties in a number of sectors of particular importance to developing countries. One of these sectors is fish trade. Although there is no consensus regarding this proposal, one can anticipate that import duties on fish and fishery products in the future will be further reduced. As a consequence, those countries that today benefit from duty concessions and preferences, will see their preferences eroded in the future.

In addition to tariffs in importing countries, non-tariff barriers continue in many markets to present obstacles to imports. Such non-tariff barriers are frequently linked to technical standards or procedures. Although WTO rules include agreements on both “Technical Barriers to Trade and on Sanitary and Phytosanitary” issues (relevant for food quality and safety), capacity-building measures to assist countries and exporters in effectively implementing these agreements are needed.

Subsidies

The role of fishery subsidies has been receiving increasing attention both from governments and civil society due to likely negative impacts of some subsidies on trade of fish and fish products and on the sustainability of living aquatic resources. Before and after the adoption of United Nations Convention on the Law of the Sea (UNCLOS) in 1982, many coastal countries implemented economic support programmes to take full advantage of their recently acquired Exclusive Economic Zones (EEZs). FAO brought the world’s attention to fisheries subsidies in 1992 when it published Marine Fisheries and the Law of the Sea: A Decade of Change. From the study it appeared that at the end of the 1980s the value of subsidies was equivalent to a significant proportion of the landed value of the world’s fish catch, which were a stimulus to overcapacity and overfishing. Afterwards, a number of mandatory and voluntary international fishery instruments were adopted (e.g. Cancun Declaration (1992); UN Conference on Environment and Development (UNCED), Agenda 21, Chapter 17 (1993); FAO Code of Conduct for Responsible Fisheries (1995); New York Agreement (1995)).

They emphasized the need for the sustainable development of living marine resources. Fisheries subsidies started to be considered not only in relation to their potential distorting effects on fish trade, but also in relation to likely negative effects on the sustainability of fishery resources.

This trend was substantially confirmed in 1996 when the WTO Committee on Trade and Environment (CTE) decided to include fisheries as one of the economic sectors that would be discussed by the Committee in the context of the environmental benefits of subsidy removal. Discussions in the CTE showed important differences of views among groups of countries. At the start of the debate, the differences focused on whether there was consistent evidence to support the view that fisheries subsidies had a negative impact on the status of fish stocks and whether such subsidies should be singled out for special treatment.

In addition to the CTE, the issue is also being discussed in other fora involving IGOs, including FAO, OECD, United Nations Environment Programme (UNEP), Asia-Pacific Economic Cooperation (APEC), etc. and NGOs, in particular World Wildlife Fund (WWF). The FAO voluntary international instruments – The International Plan of Action for the Management of Fishing Capacity (IPOA-CAPACITY) and International Plan of Action to Prevent, Deter and Eliminate Illegal, Unreported and Unregulated Fishing (IPOA-IUU) adopted in 2000 and 2001 respectively, called for, inter alia, the elimination of all factors including subsidies, causing overcapacity and IUU fishing, respectively.

Negotiations on subsidies in fisheries have been propelled recently by the Doha Declaration (2001), where Ministers committed to “clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries” (WTO, 2001). Also, the World Summit on Sustainable Development (WSSD) Declaration (UN, 2002) made a call to “eliminate subsidies that contribute to illegal, unreported and unregulated fishing and to over-capacity, while completing the efforts undertaken at the WTO to clarify and improve its disciplines on fisheries subsidies…”.

Technical work on fisheries subsides and negotiations in the WTO

The present discussions are taking place at the technical and policy levels mutually influencing each other's outcomes. On the technical side much progress has been achieved from a theoretical and analytical point of view from work in FAO, OECD, UNEP and APEC, etc.[1] There are still some important technical issues where agreement is pending: an operational definition of fisheries subsidies,[2] the identification of categories of subsidies, and how to take due account of the importance of this sector to developing countries. There is also a need to improve the empirical knowledge of the effects of subsidies on fish trade, on overcapacity, on overfishing and on livelihoods of fishing communities.

Some of these technical issues have been addressed in the FAO Technical Consultation on the Use of Subsidies in the Fisheries Sector, which took place in Rome from 30 June to 2 July 2004.[3]

The Technical Consultation worked under the terms agreed on by the Twenty-fifth Session of The Committee on Fisheries (COFI), which established that attention should be given to a practical mandate to consider the effects of subsidies on fisheries resources. These subsidy effects include IUU fishing and overcapacity, and take into account the impact of subsidies on sustainable development, trade in fish and fishery products, food security, social security and poverty alleviation, especially in the context of recognizing the special needs of developing countries and small island developing states as recognized in international instruments. The Technical Consultation agreed that FAO should give priority to its programme of work by carrying out short- and long-term activities. In the short term, FAO should broadly examine the relationship between subsidies, overcapacity and IUU fishing. As part of the short-term work programme, the examination should also consider the situation in developed and developing countries, high seas and EEZs, and the artisanal and industrial sectors.

In addition, FAO should examine the role and impact of subsidies in fisheries development, particularly in the artisanal sector and with respect to food security and livelihoods, and should consider the effects and role of other economic instruments. The long-term task was identified as evaluating the impact of fisheries subsidies on the various fisheries management regimes. In this regard, the Technical Consultation agreed that as a continuing part of its mandate FAO should work on developing related indicators, operational guidelines and capacity-building activities in developing countries. A detailed outline of the short- and long-term work programmes should be presented at the 26th session of COFI for discussion and decision.

At present, the main centre of interest for fisheries is the negotiations on fisheries subsidies in the WTO Negotiating Group on Rules based on the Doha Mandate. Negotiations resumed in March 2004. Several negotiating proposals have been presented. A common element is that they recognize that subsidies that enhance fishing capacity should be prohibited. This recognition is placed in a common "traffic light approach" in the context of different architectures. The EU proposes red and green lights while the United States proposes red and amber lights. As its primary discipline, New Zealand would prohibit all subsidies causing overcapacity and overfishing, as well as other trade distortions with envisaged general exceptions (red light) and transitional provisions (green light). "Small vulnerable coastal developing states" request SDT and the exclusion from the definition of fisheries subsidies of access fees, development assistance and fiscal incentives to the development of domestic and artisanal fisheries. In front of these proposals, Japan sustains the view that trade distortions are not unique in the fisheries sector. It does not agree with the claim that special disciplines are required for fisheries subsidies.

Recently, however, there has been a shift in the debate from the issue of whether there is a need for specific disciplines in the sector to the question of the nature and extent of any such disciplines. The shift has its roots in the change in the position of Japan, which now proposes that the Negotiating Group on Rules should also discuss which subsidies are really problematic in terms of overcapacity

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[1] An updated review of this work is presented in the document, "A summary of recent work on subsidies in the fishing sector" FAO 2004. www//ftp.fao.org/fi/DOCUMENT/tc-sub/2004/inf3e.pdf.

[2] The SCM Agreement is WTO's basic subsidy agreement and the definition included therein is the one considered on trade disputes regarding the fisheries sector.

[3] Information on these pending issues can be found in *A Global technical initiative on fisheries Subsidies.* Available at www. ftp.fao.org/fi/DOCUMENT/tc-sub/2004/2e.pdf.

and IUU fishing, and what sort of subsidies should be permitted to ensure the sustainable development of the fishery sector.

The negotiations currently seem to be sustained between two main positions. One is a proposed broad ban on all subsidies, with exceptions defined through the negotiating process and using reduction of fixed or variable costs or enhancement of revenues or incomes as basic tests to be applied within new rules (as proposed by New Zealand and supported by others). Another bottom-up negotiation approach, taking into account various roles of subsidies and their subsequent categorization as implied in Japan’s proposal. A possible third area of debate is being opened by a number of developing countries in relation to the SDT to be accorded to such group of countries.

ACP countries in the context of current negotiations

With the exemption of a few fish-exporting countries, developing countries have not participated very much up to now in the current debates and negotiations on subsidies in fisheries. This seems to be changing now, even though the negotiations appear to be in an advanced state. However, it is still difficult to predict how the WTO negotiations on fishery subsidies could affect the ACP-EU fisheries relationship and FPAs in particular. This will certainly depend on how some of the technical issues will be defined and agreed on. The issue of whether or not foreign access payments are considered as subsidies under the current WTO definition of subsidies has been highly controversial. However, it is a fact that those payments have not so far been challenged as subsidies by any party under the WTO procedures. Several of the submissions put forward during the current negotiations propose that government-to-government financial compensation paid for access to surplus resources by Distant-Water Fishing Nations (DWFN) be prohibited and/or heavily conditioned. Also, some types of development aid to the fisheries sector could end up being considered a harmful subsidy.

If agreements on such proposals make progress, government-to-government payments for access to fisheries and the utilization of incentives for domestication and development of fisheries in developing countries may be conditioned and eventually constrained by the new disciplines. The EU proposal for a "new generation" of fisheries agreements, termed "Fisheries Partnership Agreements,” has been designed to take into account the critical views concerning the potential harmful impact on trade and sustainability attributed to the traditional format of fishing agreements. Through the partnership itself, they contain provisions aimed at contributing to the conservation of resources and the sustainable development of the coastal country fisheries.

In the face of these potential developments, a key starting point for ACP countries should be to provide technical and policy support to the formulation of their negotiating positions within a national strategic vision for their fisheries development. Regional and subregional exchange of information and cooperation among ACP countries could also be strengthened in this regard. Finally, close attention should be paid to the current WTO discussions to define the reach of the SDT clause.

6.2 Fish quality and safety in the WTO

The SPS and TBT Agreements

Significant implications for food safety and quality arise from the Final Act of the Uruguay Round, and especially from two binding agreements: the Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures, and the Agreement on Technical Barriers to Trade (TBT Agreement). The SPS Agreement confirms the right of WTO member countries to apply the necessary measures to protect human, animal and plant life and health. But these measures must be consistent with obligations prohibiting arbitrary or unjustifiable discrimination on trade between countries where the same conditions prevail and are not disguised restrictions on international trade.

The Agreement requires that with regard to food safety measures, WTO members base their national measures on international standards, guidelines and other recommendations adopted by the Codex Alimentarius Commission (CAC) where they exist.

This does not prevent a member country from adopting stricter measures if there is a scientific justification for doing so, or if the level of protection afforded by the Codex standard is inconsistent with the level of protection generally applied and deemed appropriate by the country concerned.

The SPS Agreement requires that SPS measures should be based on an assessment of the risks to humans, animal and plant life and health using internationally accepted risk assessment techniques.

Risk assessment should take into account available scientific evidence, the relevant processes and production methods, the inspection/sampling/testing methods and the prevalence of specific illnesses.

The TBT Agreement is a revision of the agreement of the same name first developed under the Tokyo Round of negotiations (1973-1979). Its objective is to prevent the use of national or regional technical requirements, or standards in general, as unjustified technical barriers to trade. The Agreement covers standards relating to all types of products including industrial products and quality requirements for foods, except requirements related to SPS measures. It includes numerous measures designed to protect the consumer against deception and economic fraud.

The TBT Agreement basically provides that all technical standards and regulations must have a legitimate purpose and that the impact or cost of implementing them must be proportional to their purpose. It also states that if there are two or more ways of achieving the same objective, the least trade-restrictive alternative should be followed. The Agreement also places emphasis on international standards since WTO members are obliged to use all or part of them except those that would be ineffective or inappropriate in the national situation.

Both the SPS and TBT Agreements call on WTO member countries to:

- promote international harmonization and equivalency agreements;
- facilitate the provision of technical assistance, especially to developing countries, either bilaterally or through the appropriate international organizations;
- take into consideration the needs of developing countries, especially the LDCs, when preparing and implementing SPS and quality measures.

The Codex Alimentarius Commission (CAC)

Since 1962, the CAC has been responsible for implementing the Joint FAO/WHO Food Standards Programme. CAC's primary objectives are the protection of the health of consumers, the assurance of fair practices in food trade and the coordination of the work on food standards. It is an intergovernmental body with a membership of 165 member governments. In addition, observers from international scientific organizations, food industry, food trade and consumer associations may attend sessions of the CAC and of its subsidiary bodies. An Executive Committee, six Regional Coordinating Committees and a Secretariat assist the CAC in administering its work programme and other activities.

The work of the Codex Alimentarius is divided between two basic types of committees:

- nine general subject matter(s) committees that deal with general principles, hygiene, veterinary drugs, pesticides, food additives, labelling, methods of analysis, nutrition and import/export inspection and certification systems;
- 12 Commodity Committees which deal with a specific type of food class or group, such as dairy and dairy products, fats and oils, or fish and fish products. The work of the Committees on hygiene, fish and fishery products, veterinary drugs and import/export inspection and certification systems are of paramount importance to the safety and quality of internationally traded fish and fishery products.

In the environment of the SPS/TBT Agreements, the work of the CAC has taken on unprecedented importance with respect to consumer protection and international food trade. The Codex standards are meant to be voluntary and adopted by consensus. Yet, under the new SPS/TBT Agreements, the Codex standards cannot be called voluntary, nor are they fully mandatory, falling in an area in between, which resembles "voluntarism under duress". This is why the Codex has been undergoing significant reforms to improve its standards setting and management procedures, and the participation of developing countries to its deliberations.

Eco-labelling

The Doha Mandate also addresses labelling requirements for environmental purposes, or "eco-labels". Its aim is to clarify the impact of eco-labelling on trade and examine whether WTO rules stand in the way of eco-labelling policies. In the fisheries sector, a number of eco-labels exist already. The goal of these eco-labelling programmes is to create market-based incentives for better management of fisheries by creating consumer demand for seafood products from well-managed stocks or from sustainable aquaculture. Although eco-labelled products are not yet prominent in any market, they raise questions concerning the lack of internationally agreed guidelines for labelling and certification of products, the choice of information and transparency of the process, the role of governments in voluntary labelling and certification, and the special requirements of developing countries in adopting eco-labelling of fishery products. Finally, the relationship between WTO rules and voluntary labelling schemes needs to be clarified.

The FAO Committee of Fisheries (COFI) adopted a set of voluntary guidelines for the ecolabelling of fish products during its 26th session, held 7-11 March 2005. The new guidelines are aimed at providing guidance to governments and organizations that already maintain, or are considering establishing, labelling schemes for certifying and promoting labels for fish and fishery products from well-managed marine capture fisheries. The guidelines outline general principles that should govern ecolabelling schemes, including the need for reliable, independent auditing, transparency of standard-setting and accountability, and the need for standards to be based on good science. They also lay down minimum requirements and criteria for assessing whether a fishery should be certified and an ecolabel awarded, drawing on FAO's Code of Conduct for Responsible Fisheries to do so.

With trade in fishery products at an all-time high and concern over the status of wild marine stocks growing, ecolabelling offers a way to promote responsible fish trade - crucial for many developing countries - while preserving natural resources for future generations.

6.3 The EU-ACP Fisheries Partnership Agreements

The member states of the European Community, following the evolution of the Law of the Sea in the 1970s, agreed to transfer to the Community their competence to concluded fisheries agreements in a Council Resolution of 3 November 1976. Southern Bilateral Fisheries Agreements between the European Union and ACP Coastal Countries have been signed in the last 25 years with 17 countries. These establish the general framework for the access of Community fleets to the waters of these countries. Such agreements have been concluded for the acquisition of tuna, demersal and pelagic fish licences; specifying details such as the number and types of vessels allowed to operate, conditions of fishing operation, and the amount and type of financial support to be provided to the developing states concerned.

The major Agreements have been signed with countries that have significant fisheries resources due, inter alia, to favourable up-welling conditions: Mauritania, Senegal, and Guinea-Bissau on the Atlantic centre-west coast and Angola on the southwest coast.

The ACP has a significant trade surplus in its fish trade with the EU. In 2002, ACP exports were US$ 2.1 billion, of which canned and processed tuna worth US$531 million was the major product (25 percent). Other major items were fish fillets (US$409 million), shrimp (US$355 million) and chilled fish (US$159 million).

Total ACP fish imports from the EU in 2002 were worth US$315 million. They consist mainly of yellowfin (US$57 million) and skipjack tuna (US$53 million) from the EU fleet, which is used as raw material by the tuna canning industry located in ACP countries. In addition, some ACP countries, in particular in West Africa, are major importers from the EU of small pelagic species such as herring and mackerel for domestic consumption (US$97 million). In volume, this import is considerable, with annual amounts reaching several hundred thousand tonnes. For example, in 2002 alone, Nigeria had total imports of small pelagic species of 288 000 tonnes; Cote d'Ivoire, 60 000 tonnes, and Ghana, 94 000 tonnes. For these countries, imports of low-cost protein-rich fish play an essential role in guaranteeing adequate fish supplies for domestic consumption.

Table 6.1 shows the 20 largest ACP fish exporters to the EU in 2002 and Table 6.2 shows the 20 largest ACP fish importers from EU in 2002.

TABLE 6.1: 20 LARGEST ACP FISH EXPORTERS TO THE EU IN 2002 (US$)

Country	Export value
Namibia	222 158 844
Seychelles	218 992 291
Senegal	192 088 183
Madagascar	159 614 294
Cote d'Ivoire	155 642 557
Mauritania	125 739 953
United Republic of Tanzania	114 546 683
Ghana	98 995 850
Cuba	75 323 427
Mauritius	72 321 918
Mozambique	65 714 551
Uganda	60 791 121
Nigeria	55 330 192
Kenya	38 027 565
Angola	37 268 054
Bahamas	31 216 922
Guinea	20 895 819
Suriname	18 229 055
Gabon	14 523 398

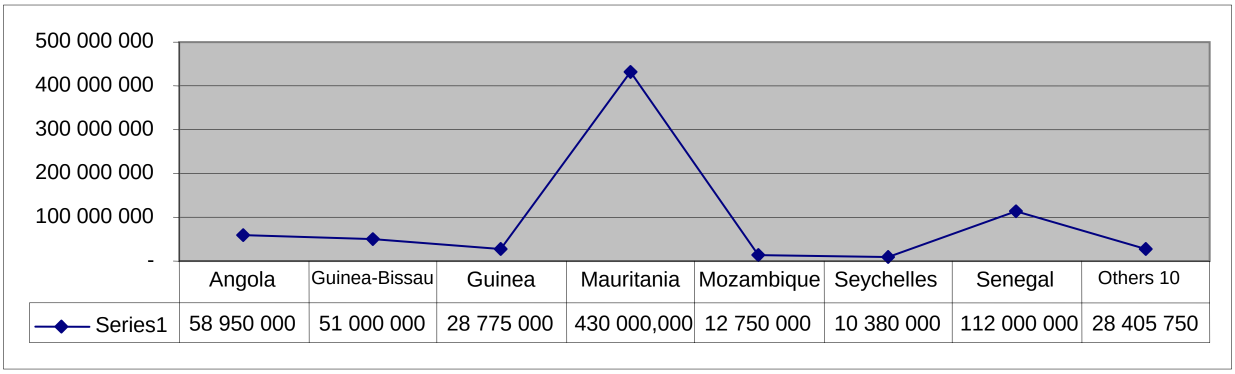
TABLE 6.2: 20 LARGEST ACP FISH IMPORTERS FROM EU IN 2002 (US$)

Country	Import value
Nigeria	119 030 154
Cote d'Ivoire	72 656 082
Seychelles	46 320 858
Mauritius	14 017 535
Madagascar	12 951 547
Saint Kitts and Nevis	9 996 162
Angola	4 893 495
Ghana	3 945 728
Jamaica	3 349 017
Cuba	3 260 705
Kenya	3 196 096
Senegal	2 950 202
Dominican Republic	2 122 677
Haiti	2 068 329
Gabon	1 571 633
Congo	1 566 515
Sierra Leone	1 046 606
Benin	991 115
Equatorial Guinea	442 744
Mozambique	418 652

EU fishery activities and the Fisheries Partnership Agreements

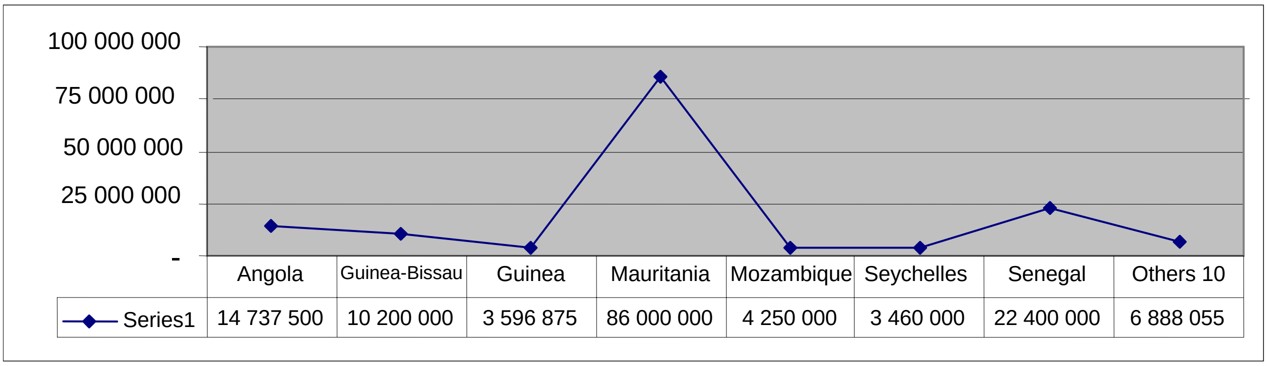
The total amount that will be spent by EU during the period 2000-2007 is presently estimated at €732 26 750. Before the end of this period, the fisheries agreement will be renewed so the final amount will be greater. The yearly average is around €150 million. The main beneficiaries during this period are shown in Figure 6.3. With €430 million, Mauritania is by far the most important for a five-year period. It represents 59 percent value of all agreements.

FIGURE 6.3: TOTAL VALUE (EURO) OF THREE TO FIVE-YEAR AGREEMENTS (2000-2007)



Source: FAO

FIGURE 6.4: AVERAGE VALUE PER YEAR



Source: FAO

The ten other beneficiaries are: Cape Verde, Comoros, Equatorial Guinea, Gabon, Gambia, Côte d'Ivoire, Kiribati, Madagascar, Mozambique, Sao Tome and Principe, and Solomon Islands. These agreements concern mainly fishing tuna in their EEZ.

The countries that can provide access not only to tuna, but also to significant demersal stock (such as: Angola, Guinea-Bissau, the Republic of Guinea, Mauritania, Mozambique and Senegal) can derive significant financial benefits. Among the other countries that offer access to tuna resources, Seychelles is somewhat of an exception. The country has a very large EEZ, important tuna resources and its main port, Victoria, is used as the main base of operation by the Spanish and French tuna seiner fleets fishing in the Indian Ocean.

Targeted actions

The total amount provided under the agreements for actions to promote resource conservation and sustainable development (targeted actions) represents around €122 million. This represents about 17 percent of the total amount disbursed under the agreements. These targeted actions are generally provided in order to sustain the main functions of the local fishery administration and of fishery research institutes (where these have been established). Sometimes targeted actions are also aimed at developing the national fisheries industry.

Activity of the EU fleet

The Spanish fleet has about 200 vessels fishing in the EEZ of five countries: Mauritania, Senegal, Guinea-Bissau

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The agricultural dimension of the ACP-EU Economic Partnership Agreements

The African, Caribbean and Pacific (ACP) countries are facing several major sets of closely interlinked forces that are likely to have significant impacts on the development of their agriculture (including fisheries) sectors and their food security situations. The possible conclusion and outcome of both the negotiations for Economic Partnership Agreements (EPAs) under the Cotonou Agreement (with the European Union [EU]) and the World Trade Organization negotiations pose serious concerns on the future of their agricultural trade and development. Furthermore, the ongoing Common Agricultural Policy (CAP) reform, which will determine the nature of EU agriculture over the next few years, and the process of EU enlargement have also created additional challenges for ACP states as to how to address these multifaceted forces so as to reap the maximum benefits for their mostly agrarian economies.

This study is one of the outputs of a programme of assistance provided by FAO to the ACP Secretariat and member states in preparing for the detailed phase of negotiations on EPAs with the EU. It provides an introduction to some of the most critical aspects of the agriculture and fisheries negotiations including feasible approaches and options for the ACP to ensure that their agricultural and fisheries sectors reap maximum and sustained benefits with a view towards enhancing their food security situation.

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