



## **EPAS: THINKING OUTSIDE THE EUROPEAN BOX**

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Note: Since the publication of this paper, in December 2007, negotiations have continued over EPAs (one agreement was signed with the Caribbean region, and several interim agreements were signed on a bilateral basis). However, we believe that the key points made in this paper are still relevant for the ongoing negotiations.<sup>2</sup>

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<sup>2</sup> For a recent assessment of the agreements already signed, see Stevens et al. (2008).

## Introduction

For the past five years, the European Union (EU) and the African, Caribbean and Pacific (ACP) countries have engaged the reform of the so-called “Cotonou Agreements.” These trade agreements, signed in Benin in 2000, continued the almost forty years of preferential market access offered by the EU to the exports of its former colonies

This reform was initiated to bring these preferential trade arrangements into compliance with World Trade Organization (WTO) rules.<sup>3</sup> Indeed, the multilateral organization allows for preferences only when they are part of *reciprocal* free-trade agreements or when they benefit developing countries (DCs) on a *non-discriminatory* basis. And, as Cotonou preferences are not reciprocal (EU exports do face tariffs when entering ACP markets) and are extended to only some DCs (and not many DCs in Asia and South America), they are not compliant with WTO legislation. Until now, this situation was maintained through the granting of a waiver at the WTO. However, this waiver is due to expire on December 31<sup>st</sup>, 2007. Moreover, the EU has been challenged several times by non-ACP DCs over the preferences it offered to ACP bananas.<sup>4</sup>

The EU is therefore trying to convince its ACP partners to conclude new WTO-compliant free trade agreements through the signature of the so-called “Economic Partnership Agreements” (EPAs). Such agreements would liberalize bilateral trade between the EU and six ACP regional groupings, among which free trade would also be established.<sup>5</sup>

The logic behind the European Commission’s (EC) promotion of the EPAs also relies on the belief that the virtues of regional trade integration could work in the ACPs: specialization, economies of scale, diminution of trading costs, and increased investment. According to the EC’s official line, the EPAs would thus retain the core objectives of previous EU-ACP trade arrangements: to reduce poverty and enhance development in ACP countries.<sup>6</sup> EU officials represent the resulting additional trade liberalization with the ACP countries as simply a means to achieve development goals, together with the deepening of regional integration, the enhancement of market access for ACP products on the EU market, and increased cooperation on services and on trade-related issues. However, this reintroduction of reciprocity into EU-ACP trade relations is a major political shift, which could have important economic consequences.<sup>7</sup> In 2003, the EU absorbed 31 percent of ACP exports and provided 29 percent of their imports (DG Trade, 2004).<sup>8</sup> Besides, reforming the trade regime framing these exchanges implies renegotiating principles and cooperation habits that have shaped EU-ACP relations for over thirty years. This is all the more a sensitive issue that the ACP region includes most least developed countries (LDCs) and the poorest rural populations of the world<sup>9</sup>.

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<sup>3</sup> “The Parties agree to conclude new World Trade Organization (WTO) compatible trading arrangements, removing progressively barriers to trade between them and enhancing cooperation in all areas relevant to trade.” (Article 36.1)

<sup>4</sup> The banana case was first initiated by Colombia, Costa Rica, Guatemala, Nicaragua and Venezuela against some EU members’ national banana trade regimes before the adoption of a single banana market in 1993. The case was then reiterated against the regime of the common market and is still unsolved. For more details, see Josling and Taylor (2003).

<sup>5</sup> These regional entities are: Austral Africa, Caribbean countries, Eastern Africa, Pacific countries and West Africa.

<sup>6</sup> “The partnership shall be centered on the objective of reducing and eventually eradicating poverty consistent with the objectives of sustainable development and the gradual integration of the ACP countries into the world economy.” (Article 1)

<sup>7</sup> The first trade agreements between the EU and the ACPs (the Yaoundé conventions) did imply reciprocity, which was suppressed as of 1975, when the Yaoundé conventions were replaced with the Lomé Convention. See annex 1 for a short overview of EU-ACP relations and Grilli (1993) for a detailed historical analysis of EU-ACP trade and co-operation.

<sup>8</sup> Trends of EU-ACP trade evolution are given in annex 3, table 8.

<sup>9</sup> Economic indicators of the ACP regions are given in annex 3, table 9.

Negotiations for EPAs were officially launched in September 2002, but since the mid-1990s, the necessity of reforming EU-ACP trade relations has been increasingly apparent. And, since then, academic researchers have highlighted the opportunities and risks associated with various reform options.<sup>10</sup> Yet, it is mostly since negotiators have got into discussing more detailed specifications and since the Doha Round of negotiations has been suspended and more attention concentrated on bilateral agreements, that EPAs have lousily emerged in the public debate. Researchers have thus recently been joined by NGOs, civil society representatives from ACP countries, and sometimes even representatives of EU member states. Criticisms expressed by opponents of the EPAs usually concentrate on the project of establishing a free trade zone between the EU and ACP regions. In short, opponents fear that trade diversion might be more important than trade creation, that a surge in imports of European products (especially subsidized agricultural goods) could harm local industries and ACP agricultural sectors; that regional integration could be hampered rather than encouraged; and that ACP government revenues from tariff collection could fall significantly. As these lost revenues are not easily substitutable, they might ultimately result in diminished investment in areas that are critical to development, such as education and health, or even production and trade infrastructures.<sup>11</sup> Moreover, as ACP countries already enjoy almost completely tariff-free access to EU markets, the EU can be perceived to be asking for a lot while offering very little in return. Indeed, preferences offered by the EU are gradually losing some of their value as the EU is signing more and more bilateral preferential agreements with other regions of the world. On the contrary, EPAs would probably remain the only bilateral trade agreements offered by ACP countries, thus conferring high value to their preferences.<sup>12</sup>

On the other hand, facts are that preferences have not allowed the expected development improvements over the past decades and that they are eroding anyway, as multilateral liberalization is being deepened. By the time EPAs enter into force, they might be significantly reduced. Moreover, non-ACP developing countries will most probably go on complaining about “unfair” trade preference and WTO rules-based agreements are thus somehow needed. Any viable option for a new EU-ACP cooperation framework must consider these two constraints.

The time available to find resolution of these quandaries is very limited: the Commission is pressing ACP countries to sign new agreements before the end of the year. Should these negotiations fail, the result would be very harmful to the economies of the ACP countries as the EC is offering only one alternative: a reversion to the substantially less generous General System of Preferences (GSP) offered to all DCs, with all the shocks that that would entail.<sup>13</sup> In all likelihood, this would also prove politically costly for the EU: a host of experts and NGOs stand ready to point out that the EU, with its self-image as a development champion, would thus have become the first of the developed countries to raise tariffs against some of the world’s most vulnerable economies.

Identifying less costly solutions has become urgent. This paper therefore questions the EC’s position, assesses the expected implications of the EPAs and proposes an alternative liberalization scheme.<sup>14</sup> It

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<sup>10</sup> Page, Stevens and Kennan among others, have contributed to launching the debate as early as 1998.

<sup>11</sup> EU development assistance funds are envisaged to overcome those losses. This, however, raises serious concerns over ACPs’ increasing political dependence on the EU.

<sup>12</sup> Preferences for EU exports will all the more significant that, on average, ACP countries have relatively high MFN tariffs.

<sup>13</sup> Least Developed Countries (LDCs) would enjoy more generous preferences under the “Everything But Arms” (EBA) initiative, a special GSP scheme dedicated to them. It has been operating since March 2001 and provides free market access to the EU for all products, with the exception of arms and ammunitions. However, this preference scheme is unilaterally granted by the EU (hence non-guaranteed) and it is less generous than the current Cotonou preferences – especially in terms of critical rules of origin provisions. EBA might yet be preferred as an alternative to EPAs by countries for which trade liberalization with the EU would be too costly. See Bouët et al. (2007), for an estimation of the impacts of turning back to the GSP/EBA schemes.

<sup>14</sup> The EPA proposal is examined focusing on their commercial aspects. Neither political and cultural cooperation, nor aid distribution are taken into consideration. Undoubtedly, these particular features of EU-ACP

is structured as follows. Section 1 summarizes the constraints facing current EU-ACP trade arrangements and the issues which any reform must tackle. The costs that would be imposed by the EU's current EPA proposals are then assessed both from a theoretical perspective (section 2) and from a more empirical and quantitative perspective (section 3). In doing so, the paper brings together the results of various studies to give a detailed view of what is at stake. Given the pessimistic conclusions of this assessment, section 4 puts forward an alternative path to liberalization, which would minimize the cost of complying with WTO legislation while addressing the concerns identified in section 1.

## **1. The need to reform**

### **1.1 The European Commission's Credo**

Since 1996 and the publication of a "Green Book on the Relations between the European Union and the ACP Countries on the Eve of the 21<sup>st</sup> century" (EC, 1996), the EC has acknowledged the failure of its preferential scheme in favor of its ex-colonies. Despite 99 percent tariff-free exports and commodity protocols<sup>15</sup>, ACP countries' share of the EU market had declined from 6.7 to 2.8 percent between 1976 and 1999 and from 14.8 to 4.1 percent of EU's trade with DCs (Ravenhill, 2002). Trade even fell in absolute terms between the 1980s and the 1990s. Besides, ACP countries' dependency on primary products has remained high, while the relative prices for these products have declined. While in the 1960s, the three main export products in Sub-Saharan Africa (SSA) represented a third of total exports, this share increased to two thirds at the beginning of the 1990s. Several countries still rely on one single product for over 40 percent of export revenues (Ribier, 2007). According to Moss and Ravenhill (1982), "the impact of the Convention on the trading relationship appears to be negligible".<sup>16</sup> One of the official motives of the Commission's proposal of EPAs is therefore that something else has to be imagined.

Furthermore, by the time EPAs enter into force, the preferential aspect of today's EU-ACP agreements might be significantly reduced. Thus, one of the EC's officially proclaimed motivations in proposing the EPAs is the critical need to address the preference erosion question.

The EC's argument in pursuing the EPAs further relies on the intent to foster liberalization gains in the ACPs via the interaction between enhanced regional integration among ACP countries and the establishment of free trade areas (FTAs) with the EU. According to the Commission, this would allow the creation of an enlarged market "governed by a stable, transparent and predictable framework for trade [that] will allow for economies of scale, will improve the level of specialization, will reduce production and transaction costs and will, altogether, help to increase the competitiveness of the ACP region" (EC, 2002). All of this, in turn, would positively affect both domestic and foreign investment. On a more political level, EPAs are seen as a "check valve" that would help efficiently address the fragmentation of ACP markets, their over-protection, and the lack of harmonization in the legislation

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cooperation will somehow mitigate the outcomes of the trade regime. However, this is very difficult to assess and the lack of precision over these aspects of the agreement makes it much more difficult to assess. Finally, only trade in goods will be closely considered as, negotiations running out of time, the Commission has decided to focus only on trade in goods before the December 2007 deadline.

<sup>15</sup> The commodity protocols allow ACP countries to export specified amounts of the concerned commodities (banana, beef, sugar and rum) at reduced levels of duty and at guaranteed domestic price on the EU market.

<sup>16</sup> This view should be nuanced however. ACP states benefited from highly above the market prices for the products exported under the commodity protocols. According to an overview of the studies examining the effects of the Lomé Conventions, it appears that in countries which did not have a very strong anti-export bias, non-traditional but preferential products "increased from very low levels in 1975 to (...) 13.5 percent of ACP non-oil exports in 1994", McQueen et al. (1997). Moreover, the somehow disappointing outcome of EU preference system is not only due to the system itself, but probably also to the lack of agricultural and economic policies in ACP countries.

governing them. EPAs would also foster the bargaining power of ACP countries on the multilateral scene by locking-in their reform processes and increasing their credibility. The EU would help facilitate this transition with financial aid and development assistance.

At its core, however, the EC's argument for the EPAs rests largely on the need for WTO compliance. This argument serves both to justify the need to reform the Cotonou Agreement and, most importantly, to determine the type of agreement that might be adopted as a replacement for the current scheme.

## 1.2 WTO obligations

The need to become compliant with WTO rules implies two major constraints on EPA negotiations. First, that they must be concluded by December 31<sup>st</sup>, 2007. Second, that they should comply with the two exceptions to the most-favored nation (MFN) general rule of the General Agreement on Tariffs and Trade (GATT), which deals with regional trade.

On the one hand, regional trade agreements (RTAs) are permitted if they comply with a number of provisions, which are meant to make them inoffensive to non-party countries. Article XXIV of the GATT (1947) allows for the creation of FTAs and customs unions (CUs), but only on the condition that they “facilitate trade between the constituent territories” and do not “raise barriers to trade of other contracting parties with such territories.” These RTAs are thus considered WTO-compatible if trade barriers are eliminated by *all contracting parties* for “substantially all trade” within a “reasonable length of time.”

On the other hand, the “enabling clause,” officially named “Decision of Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries” (1979) allows developed countries to grant preferential access to all DCs, or to all LDCs, under what is known as the GSP.<sup>17</sup>

To conform to WTO legislation, future EU-ACP agreements would therefore need either to (i) imply reciprocity or (ii) extend the scope of the beneficiaries to all DCs (or to all LDCs) by deepening market access granted under GSP. The latter option would imply tremendous preference erosion for ACP countries, and has therefore not been envisaged in the EPA negotiations by the EC or the ACP countries – who clearly head towards the first solution.

In this context, WTO conformity would thus require ACPs to liberalize “substantially all trade” with the EU within a “reasonable length of time.” With reference to previous RTAs between the EU and DCs, the EU considers “substantially all trade” as 90 percent of its volume, without equality between parties. In this precise case, as ACP countries are being offered 100 percent tariff-free market access to the EU, they would have to liberalize about 80 percent of their imports. Thus, 20 percent of their imports could still be protected, so as to exempt “sensitive products” from liberalization. It should be underlined that the 90 percent threshold and its breakdown between the EU and the ACPs reflect the Commission's interpretation of Article XXIV.<sup>18</sup>

## 2. EPAs: theoretical considerations

Even though the EPAs are still in negotiation, we can safely assume that they will involve, roughly-speaking, a two-level integration process: a first level pertaining to the integration between ACP countries and the EU—a North-South integration—and a second one affecting trade relations among

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<sup>17</sup> Note to add on the possibility to apply GSP to all small and vulnerable economies only – cf. Bouët et al. (2007)

<sup>18</sup> In fact, article XXIV has been subject to many discussions within the WTO, but no conclusions have been reached so far.

the ACP countries—a South-South integration. In what follows, we will briefly review some aspects of the regional integration theoretical literature, in order to draw conclusions on the expected effects of the EPAs on ACP countries.<sup>19</sup> First, we tackle the North/South dimension of the integration process by presenting both short-term and long-term effects of the trade liberalization scheme. Afterwards, we review some arguments in favor of the South/South dimension of the EPAs. We conclude with a brief summary underlying the main benefits and challenges induced by the EPAs, from the ACP countries' perspective.

## 2.1 North/South integration

### i. North/South integration: short term trade effects

One of the key issues in the analysis of regional integration was made in Viner's pioneering work in which he set the basis for the analysis of static effects of RTAs<sup>20</sup>. His main finding is that a RTA is beneficial as long as it allows shifts towards more efficient producers. In this case, consumers will benefit from reduced prices and increased consumption. This is called trade creation. Whenever this is not the case, RTA members would suffer from costly trade diversion. Indeed, governments will lose previously collected tariffs on diverted trade. The net outcome then depends on the balance between trade creation and trade diversion.<sup>21</sup>

Upon the implementation of the EPAs, the loss of tariff revenue would be of particular importance for some ACP countries, notably the African LDCs. On average, tariff revenue accounted for nearly 34 percent of their total government revenue over the period 1999-2001 (UNECA, 2003). And, as long as tariffs will be kept on efficient non-partner countries, costs induced by trade diversion will still be in play. ACP countries would thus benefit from the EPAs in as much as the latter are used as a means of accelerating their integration into the world economy and not only with the EU. In this case, government losses would be more than compensated by consumers' gains.

Many parameters influence the final outcome of the RTA from a vinerian perspective. Among which, the efficiency of partner countries' producers<sup>22</sup>, the initial level of tariffs levied in the home country<sup>23</sup>, the latter's elasticity of demand for the product being liberalized<sup>24</sup>, and the level of tariffs levied against efficient non-party countries once the agreement is signed.<sup>25</sup> When assessing the eventual effects of the EPAs on ACP countries, one should thus mainly consider the efficiency of European producers as well as ACP countries' tariffs structure and the initial level and the geographical origins of their imports<sup>26</sup>. Empirical studies investigating the possible outcome of the EPAs on ACP countries' welfare are chiefly based on the aforementioned elements. Section 3 will present the main findings of these studies.

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<sup>19</sup> In what follows, we consider ACP countries to be "small" countries, as they don't affect world prices given their weight in world production. Conversely, the EU is addressed as a "big" country.

<sup>20</sup> The vinerian analysis tackled the short-term welfare effects of CUs.

<sup>21</sup> The framework of the analysis is a free competition market. Therefore, elements hindering free competition will reduce the scope of the price reduction induced by the trade creation.

<sup>22</sup> The more efficient are partner countries' producers, the more likely the RTA will be trade creating on a net basis.

<sup>23</sup> The higher the initial tariffs in the home country, the more likely the RTA will be trade creating on a net basis. Put differently, the lesser the initial imports of the home country, the more likely the RTA will be trade creating on a net basis.

<sup>24</sup> The more elastic the demand, the less trade diverted.

<sup>25</sup> The lower the tariffs levied against efficient non-party countries once the agreement is signed, the less trade diverted. One should note that ACP countries could alleviate eventual trade diverting effects caused by the EPAs by reducing unilaterally their MFN tariffs.

<sup>26</sup> As well as ACP countries' demand elasticities.

## ii. North/South integration: long term effects

In addition to trade creation/diversion effects, regional integration involves a long term dynamics. In what follows we will discuss some aspects of the latter.

### *Trade and productivity*

Coe and Helpman (1995) and Coe et al. (1997) conclude that trade is a vector transferring technological know-how and expertise between trading partners. Such a transfer positively affects the partners' global factor productivity. Furthermore, they highlight a positive relation between a country's openness degree and its global factor productivity.

What are the implications of these findings on regional integration? Schiff et al (2002) show that developing countries would gain more in terms of productivity when trading with developed countries rather than with developing ones, the former being more advanced in research and technology. Therefore, eliminating tariff barriers levied on European imports would benefit the ACP countries in the long run, through eventual technological spillovers. However, maximizing the benefits of such spillovers requires that the ACP countries target more specialized and higher value-added exports. For ACP countries, this can be achieved via the trade liberalization scheme envisaged by the EPAs and, perhaps more important, by minimizing the discrimination against non-partners. In order to do so, ACP countries should tackle some "trade facilitation" aspects: enhancing communication and transport infrastructures as well as streamlining administrative procedures. Such measures are essentially non-discriminatory, thus reducing the preferential – and eventually negative – aspect of the EPAs.

In the same vein, ACP countries should ameliorate their legal and institutional framework in order to attract much needed investments, notably foreign direct investments. These investments would help enhancing infrastructures and strengthening export-oriented enterprises, which in turn would accelerate the integration of the ACP countries into the world economy. Moreover, the same observations should help direct the European aid primarily towards sectors that will intensify the insertion of the ACP countries with the world economy.

### *Deep integration*

The EPAs could be broadened to engage trade liberalization beyond the mere fact of eliminating tariffs. Hoekman and Konan (2005) found that a "deep" integration between Egypt and the United States would be the most beneficial in terms of Egyptian welfare and Gross Domestic Product, compared to a normal/"shallow" integration.

More precisely and as suggested by the EC, the agreement could deal with non-tariff barriers hindering the competition between foreign and local producers. As competition between producers increases with the elimination of such barriers, the ACP countries would maximize their gain induced by the trade creating effects of the EPAs. These include technical and regulatory norms and border controls.

Adopting the EU technical norms of production as well as regulatory norms and standards would help increasing ACP countries' exports to the European market. This can be achieved through technical assistance provided by European experts, as well as financial aid. As for the border controls, ACP countries should streamline control procedures, notably by adopting efficient control techniques in focal exist points and by computerizing customs. The ACP countries should also eliminate eventual

para-tariff measures. These refer to surcharges and fees levied solely on imports, thus violating the national treatment principle<sup>27</sup>.

Given the sensibility of the issues at stake, the EU should not pressurize ACP countries to adopt deeper measures of integration – as the current negotiations seem to imply – but rather define a road-map with clearly-defined objectives coupled with the needed technical and financial assistance. In fact, such aid would amplify the ACP countries' propensity to undertake reforms, as will be discussed next.

### iii. North/South integration: the “lock-in” effect

One of the eventual benefits of signing a RTA with developed countries is the “lock-in” mechanism induced by the agreement. From a DC perspective, signing a RTA with a developed country would help it applying economical reforms<sup>28</sup>. In fact, and in terms of trade reforms, the developed country would “transfer” a part of its credibility to the developing country's authorities through the mere fact of signing the trade agreement. In addition, some agreements clearly stipulate the necessity of introducing/intensifying more general macro-economic reforms in the developing country.

To assess whether a particular PTA is a powerful engagement mechanism, one should carefully consider the provisions of the agreement and the intensity of trade between the signatories. Indeed, an agreement that clearly signals the need for undertaking reforms by the developing country is more likely to help engaging reforms in the latter. In addition, provisions for eventual sanction measures applied to recalcitrant countries are another factor enhancing the probability of engaging the needed reforms. As regard to trade flows between the signatories, the greater their trade relations relatively to their total trade, the more credible the agreement as a mechanism for engaging reforms. Indeed, the “cost” of not abiding by the rules will be higher than in the case where trade relations are not important between the signatories<sup>29</sup>. Given the importance of the EU in ACP countries' external trade as well as the need for controlling the African emigration problem from the EU perspective, provisions clearly stipulating the necessity to undertake reforms in the ACP countries would help increasing the credibility of the final agreements as engagement mechanisms.

## **2.2 South/South integration**

According to the Commission's rhetoric, a large part of the gains EPAs could foster would come from the enhancement of a currently very weak regional integration – chiefly, because it would foster economies of scale.

In fact, an enlarged market can allow some producers to reduce their average cost of production. But only if this reduction is translated into a decrease in price, will it benefit the consumers. However the latter's gains might not suffice to compensate the distortions induced on trade with non-partners. One should thus be careful when putting forward this point when justifying the South-South dimension of the EPAs. This said, economies of scale could take place in product categories in which the ACP countries are efficient producers and for which they face high European protection, such like agro-business products.

One can think of at least three more reasons why the ACP countries should push further for a South/South dimension of the EPAs.

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<sup>27</sup> The principle calls for eliminating discriminatory measures between local and foreign producers.

<sup>28</sup> Such PTAs could also help introducing political reforms in DCs.

<sup>29</sup> Schiff and Winters (2003) and World Bank (2000).

One rather practical reason is that regional blocs would facilitate cooperation between neighboring countries<sup>30</sup>. Indeed, such countries would benefit from the institutional framework of the regional bloc to undertake common projects that otherwise would be difficult to address. As far as the ACP countries are concerned, enhanced regional integration could help them speed up their integration with the rest of the world by, jointly, simplifying customs procedures and easing trans-border controls and transit. Also, ACP countries would enhance their regional integration by constructing/upgrading common infrastructures, such as regional road/railroad networks. A recent World Bank study highlighted the importance of upgraded road infrastructures for African countries' regional integration and for their integration with the rest of the world (Buys et al, 2006). In this respect, the technical and financial support of the EU would be of great help.

A second reason justifying the South/South dimension of the EPAs is that a regional bloc between ACP countries would support their negotiation position *vis-à-vis* the EU. Indeed, by pooling their common needs and working by sub-regions, ACP countries can pressure the EU for better conditions pertaining to the access of their agricultural exports, more flexible conditions regulating labor mobility and looser rules of origin.

Finally, intra-ACP countries integration would also help reducing the so-called hub and spoke phenomenon. If the EPAs were reduced to a North/South integration process, EU producers would benefit from a free access to all ACP markets while ACP producers would have a preferential access to the EU market only. Consequently, the EU would attract investment flows that would have otherwise been directed towards the ACP countries<sup>31</sup>. By establishing a RTA, ACP countries will mitigate this phenomenon and attract foreign investments, notably in export-oriented firms.

There is, however, one potential risk inherent to South/South integration. It is the eventual concentration of production in certain countries – generally the most developed ones – to the detriment of others. Such industrial agglomerations could imply a substantial divergence dynamics – in terms of growth – between member countries, which can lead to the break-up of the regional bloc<sup>32</sup>. In their 2006 paper, Shepherd and Kowalski show that though the global outcome of different liberalization schemes between Sub-Saharan countries is positive, the impact across countries would be very heterogeneous (see table 1, below).

Agglomeration effects should be lessened by the interaction with the North/South integration scheme. In fact, in all cases where European producers are the most efficient ones, ACP producers won't be able to supply regional markets, thus reducing the scope of any agglomeration effects. However, such effects could still be possible for the products solely provided by local producers and for some "sensible" products that will remain heavily protected. In this case, ACP countries should consider a compensation mechanism for the most affected countries.

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<sup>30</sup> Schiff and Winters (2003) and World Bank (2000).

<sup>31</sup> Indeed, by investing in Europe, investors would benefit from a free access to all ACP countries' markets in addition to the EU market.

<sup>32</sup> This was one of the main reasons of the break-up of the former East African Community in 1997, as Kenya attracted most of the industrial activity in the region, Schiff and Winters (2003).

**Table 1. Global welfare gains from different integration scenarios in Sub-Saharan Africa<sup>a</sup>**  
(Equivalent variation, US\$ million)

Integration policy	Regional Gain	Main losers <sup>b</sup>	Main winners
Removal of all tariffs <sup>c</sup>	489	Tanzania (-65), Uganda (-21), Madagascar (-6)	South Africa (+452), Zimbabwe (+272), Nigeria (+567)
Removal of agricultural tariffs only	120	Tanzania (-15), Madagascar (-9)	South Africa (+42), Zimbabwe (+42), Nigeria (+131)
Lowering trading costs	1285	Malawi (+9), Madagascar (+13), Mozambique (+17), Zambia (+17)	South Africa (+394), Nigeria (+187)

Source: Kowalski and Shepherd (2006), calculations using the GTAP model and version 6 of the GTAP database.

Notes: (a) The gains are not calculated on a completely disaggregated basis (individual results are available only for Botswana, Madagascar, Malawi, Mauritius, Mozambique, Nigeria, South Africa, Tanzania, Uganda and Zambia, Zimbabwe - other countries are aggregated into Rest of SADC, Rest of SACU and Rest of Sub Saharan Africa)

(b) In the case of lowering trading costs, all countries gain. Countries reported are those who benefit less from the policy change.

### 2.3 Summarizing

The ACP countries would benefit from the EPAs in as much as the latter are used as a means accelerating their integration into the world economy. For the ACP countries, this implies maximizing the potential gains of both North/South and South/South dimensions of the EPAs.

The elimination of tariffs applied on European exports would benefit the ACP countries, as long as the liberalization is trade creating. To maximize the trade creating effects of the EPAs, ACP countries should broaden their trade liberalization by reducing tariffs on efficient non-European countries. Thus, they will benefit from both short-term trade creation and long-term productivity gains. Moreover, the opening-up of the ACP markets would help restructuring ACP exports in line with their comparative advantages. Such restructuring would lessen eventual dynamics of growth divergence between the ACP countries induced by an exclusive South/South integration scheme. Deepening the integration would also enhance the expected gains from the liberalization scheme. For that matter, the European technical and financial aid is of a great importance. ACP countries should also engage macroeconomic reforms enabling them to attract investments. Such reforms would be highly dependent on whether the final provisions of the EPAs will signal their necessity.

Parallel to the liberalization of their trade with the EU, ACP countries would benefit from engaging South/South integration. Indeed, by opening their markets to each other, ACP countries would benefit from eventual economies of scale. In addition, this will lessen the investment-diverting “hub and spoke” phenomenon. ACP countries should also engage common projects, notably in infrastructures and trade facilitation, which will accelerate their integration with the rest of the world. Here again, the European aid and assistance would be the most welcome.

This said, many issues remain elusive as regard to the implementation of the EPAs – in particular, the question of the compensation for the revenue losses due to the liberalization and that of the “sensitive” products. The practical interaction between the North/South integration framework and the South/South one is also a key question. The next section deals with these issues.

### 3. EPAs: the expected impacts

Numerous impact studies have tried to capture the possible outcomes of EPAs. Reviewing this literature should help having a more detailed and realistic view of their economic relevance.<sup>33</sup> For a precise assessment of EPAs' possible outcomes, one first needs to examine the extent to which the dismantling of tariffs would effectively impact protection. Then, we address methodological issues and, finally, we review the results of impact studies, focusing on three points: the potential of EPAs to create trade; their impact on critical agricultural sectors; and their practical implications, in terms of intra-regional integration.

### 3.1 The real extent of liberalization: “much ado about nothing?”

Comparing the actual tariff structures of the ACP countries with the EC's tariff-dismantling proposal (that is, for ACPs, the suppression of tariffs on about 80 percent of their imports from the EU), Stevens and Kennan (2005) find that most ACP countries could sign EPAs and still avoid a rapid and substantial liberalization, if they chose to retain their highest tariffs. Indeed, high tariffs (which allow effective protection) are imposed on only a limited number of products, which do not represent much more than 20 percent of their imports from the EU.<sup>34</sup> Retaining tariffs on the 20 percent of trade which face the highest tariffs rates, would thus imply eliminating relatively low tariffs. The maximum tariffs that would have to be eliminated (marginal tariffs) are shown on a regional basis in the table below:

**Table 2. The real extent of EPA liberalization: marginal tariffs by region**

Region <sup>a</sup>	Marginal tariff (%) <sup>b</sup>	Range	Outliers
Caribbean	20	15-30	St Kitts, St Lucia, Surinam
Central Africa	30	20-30	None
East and Southern Africa	25	5-100	Burundi, Djibouti, Ethiopia, Seychelles
SADC	5	0-42.5	Angola, Botswana, Mozambique, Tanzania
West Africa	20	20-30	Nigeria

Notes: (a) the Pacific region is not taken into account, as data was unavailable.

(b) the marginal tariff reported is the most frequently encountered marginal tariff for all countries if they liberalize on 80 percent of imports.

Source: Stevens and Kennan (2005a)

Looking at the problem from an opposite point of view is even more telling. Products which currently face tariffs of 10 percent or less (that is, tariffs that are less protective), represent over 50 percent of total imports from the EU for 43 of the 55 countries considered by Stevens and Kennan (2005). Removing these tariffs would thus allow these ACPs to fulfill a significant share of the effort asked in EPAs without considerably undermining their current protection scheme.

This means that the EPAs would not, in practice, foster liberalization to a significant extent, as is often feared by opponents to liberalization. Yet, it also means that the theoretical gains associated with liberalization could be small. Notably, the allocation of resources would probably not shift significantly towards more efficiency. Still, a product-by-product analysis should be conducted to assess the precise extent of liberalizing. The studies reviewed in the following sub-sections should give an insight into this more detailed analysis.

<sup>33</sup> In this section, the paper concentrates on SSA countries. Indeed, negotiations with Caribbean and Pacific countries are already in an advanced stage and the very particular stakes associated with their insular economies are hardly comparable to that of SSA ACPs.

<sup>34</sup> Most ACP countries have already engaged in commercial policy reforms – though they still have higher protection patterns than OECD countries. Concerning agricultural products for example, European exports faced tariffs of 17 to 36 percent on ACP markets in 2004, respectively in SADC and in West Africa (Fontagnié et al., 2007). The detailed tariff structure of ACP countries is given in annex 3, table 11. Fontagnié et al. (2007) present a detailed analysis of how a post-EPA tariff structure would look like across the different ACP regions, for agricultural products.

### 3.2 Cautiousness requirements when considering quantified assessments

Assessing the impact of EPAs is a very difficult task and reviewing the literature on this topic does not allow coming to clear-cut conclusions. Indeed, adding to the traditional debate on the relevance of economic modelling and the difficulties of comparing studies that use different methodologies, assumptions or data sources, the assessment of EPAs raises particular difficulties.

The nature of the agreements implies that they will probably affect the economies of ACP countries on different levels and in all the sectors. Several studies have therefore tried to assess their outcomes using general equilibrium models, arguing that partial equilibriums would not give the full picture and would thus not really help negotiators when faced to signature. On the other hand, given the scarcity and the mediocre quality of data for African countries, general equilibrium models are not very reliable and, exports being concentrated in a very small number of sectors in most ACP countries, partial equilibriums might allow maximizing the available data. (Fontagnié et al., 2006). Finally, risk is not well taken into account in classical general equilibrium models and their results depart from reality when markets do not function as smoothly as supposed so. This might particularly be the case of agricultural markets, especially for low demand elasticity products.

Beyond this issue of model choice, the very use of models can be challenged. Indeed, the domestic characteristics of African economies are probably particularly badly reflected by the commonly used perfect competition assumptions. Moreover, since in most ACP countries a high proportion of consumers are also producers, notably for agricultural goods, commodities' price variation also mean revenues' variation, in which case assessing the net effect of these changes on welfare is complicated.

Adding to these difficulties, the disparity of ACP economies and the uncertainty over EPAs' final shape render the assessment of different options highly speculative. Finally, the models do not take into account exchange rate fluctuations, which are nonetheless a major factor of export competitiveness.<sup>35</sup>

Despite all these reserves, impact assessment studies are to be looked at. Most estimates take as their main scenario, the Commission's liberalization schedule position (that is 100 percent for the EU and 80 percent for ACP countries on average).

### 3.3 Literature review:

#### i. Can benefits outweigh losses?

A table with the results of selected impact assessment studies is presented below. It reports information on trade creation and diversion and on tariff revenue losses.

Impact studies remain problematic in projecting the net trade potential of the EPAs. Results are so varied, both on a regional and on a country basis, that it is very difficult to forecast EPAs' potential effects. For example, Karingi et al. (2005) find that EPAs would be especially trade creating in West Africa while Berisha-Krasniqi et al. (2007) find that they would be trade creating everywhere except in West Africa. One implicit conclusion might thus be that trade creation will not easily be fostered.

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<sup>35</sup> Most ACP countries' currency is the CFA franc, which is linked to the euro, a very strong currency. The competitiveness of their exports is therefore tightly linked to the value of the euro, which tends to be over-evaluated. According to Erik Orsenna (2007), it is a non-sense to negotiate commercial agreements that intend to help ACP countries to be more competitive when, at the same time, the European Central Bank favors a strong euro that has a much stronger effect on ACP competitiveness than difficult productivity enhancements. Bourdet (2005) also notes that "exchange rate policy plays a more important role than regional trade integration on private investment decision-making." For example, it seems that the creation of a CU in the WAEMU in 2000 has not much impacted the private investment. On the contrary, the devaluation of the CFA franc in 1994 boosted exports' competitiveness and thus private investments.

This is understandable, given the level of MFN tariffs ACPs currently impose. In fact, when EU producers will be the sole exporters on an ACP market, and if they price their products above their production cost, so that the equilibrium price will remain below world prices augmented by the MFN tariff, ACP countries will suffer from a higher cost of trade diversion and less trade creation.<sup>36</sup> This will be amplified whenever MFN tariffs are high. And, as shown by Messerlin and Delpeuch (2007), half of the ACPs have average applied tariffs higher than 15 percent in agriculture and one fourth have average tariffs higher than 15 percent in manufacturing. Moreover, their peak applied tariffs are high – almost 50 percent on average for all the ACPs in agriculture, and 40 percent in manufacturing.<sup>37</sup> Besides, and for a given product, whenever EU producers will not eliminate other foreign producers from the ACP market, they will benefit from an income transfer that will be greater, the higher the MFN tariff.<sup>38</sup>

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<sup>36</sup> All other things equal.

<sup>37</sup> Moreover, many ACP tariffs are still not bound and can, therefore, be increased without restraint. An increase of imports from the EU following the implementation of the EPAs might thus induce ACP governments to raise their unbound tariffs on non-EU imports. This would exacerbate trade diversion and would reduce total imports, whenever EU producers will not satisfy the entire ACP market.

<sup>38</sup> In such cases, ACP preferences will act as subsidies for inefficient EU firms.

**Table 3. Overview of findings on the effects of EPA implementation on trade creation and diversion and on government revenues**

Paper	Methodology	Scenario	Trade creation and diversion	Government Revenues
Wolf (2000)	CGE model Base year = 1994 Projection for 15 years	Full reciprocal liberalization of trade in goods between the EU and UEMOA	Trade diversion exceeds trade creation	Tariff revenues decline by: -50% in UEMOA LDCs -30% in other UEMOA
McKay et al. (2000)	Partial equilibrium model	EU-EAC EPA: 80% current trade flow liberalization in EAC with sensitive products identified on tariff basis	Trade diversion exceeds trade creation	Average 71.2% reduction in tariff revenues (1995 basis)
Nicholls et al. (2001)	Almost Ideal Demand System Projection over 1997-2000	FTA between the EU and CARICOM	n.r.	Tariff revenues decline by: - 3.45% in Jamaica - 3.71% in Trinidad and Tobago - 15.04% in OECS
Tekere and Ndlela (2002)	Partial equilibrium model (SMART) SADC Trade Project, Trains Comtrade, and Eurotrace databases	EU-SADC EPA: cumulative elimination of tariffs : 50% by 2012, 30% by 2016 and 20% by 2020.	Trade creation exceeds trade diversion – by large in some countries.	By 2020, tariff revenues have declined significantly in all countries, mostly in SADC non-SACU countries. Losses range from 7% to 39% of chapter imports from the EU.
Busse et al. (2004)	Partial equilibrium model (based on Verdoorn, 1960)	Full reciprocal liberalization of trade in goods between the EU and ECOWAS + Mauritania	Trade creation exceeds trade diversion	Across countries: - Tariff revenues decline by 28.3 to 89.5% - Total government's revenues decline by 3.5 to 20%
Karingi et al. (2005)	Partial equilibrium model (SMART)	Full reciprocity between the EU and SSA regions.	Trade creation largely overcomes diversion, especially in UEMOA	About \$ 1.5 billion lost for Africa
Milner et al. (2005)	Partial equilibrium model (based on Panagariya, 1998) Local trade and tariffs sources	EU-EAC EPA : total tariff removal.	n.r.	Tariff revenues decline very significantly in Tanzania and Uganda: - 65% and – 71% respectively.
Stevens and Kennan (2005a)	Calculation of revenue losses by applying the set tariff to the value of imports	EBA equivalent access for all ACP countries and liberalization of 80% of ACP imports from the EU	n.r.	Loss of tariff revenue from the EU: 75% of ACP countries would face losses of 40% or more and 33% of countries would face losses of 60% or more
Fontagné et al. (2007)	Partial equilibrium model with focus on substitution issues MACMaps database	EU-ACP EPAs: 80% current trade flow liberalization with sensitive products (identified according Jean et al., 2005) with infinite supply elasticity in ACPs	Trade creation largely overcomes trade diversion	The exclusion of 20% of bilateral trade with the EU allows to save 20 to 40% of the bilateral tariff revenues. Central Africa is the most affected region
Berisha-Krasniqi et al. (2007)	Computable general equilibrium model "MIRAGE" GTAP 6.2 and MacMap databases World Bank GDP projections.	EU-ACP EPAs: 80% current trade flow liberalization with sensitive products identified according to an index computing tariffs, trade and trade shares.	- Trade creation overcomes diversion in SADC, ESA, Caribbean and Pacific - Trade diversion overcomes creation in West Africa	Tariff revenues decline by: - Senegal: 44% - Nigeria: 31% - Rest of ECOWAS: 37%

Source: computed by the authors. Add Bouët et al. (2007)

Table 3 shows estimates of probable tariff revenue losses which are very significant. This is not surprising: it is on low tariffs, which allow imports, that governments raise tax monies. And, as seen in sub-section 3.1, it is most probable that governments will eliminate these low tariffs. According to impact studies, West Africa would be the region most affected. At the top-end of estimates, ECOWAS countries could lose up to 89.5 percent of tariff revenue, which is 20 percent of total government revenues (Busse et al., 2004). In fact, even the most optimistic studies suggest losses of at least 30 percent in West Africa.<sup>39</sup>

In theory, as tariffs on imports are eliminated, consumer prices should fall and consumption increase. The shift from import taxes to a more broadly-based consumption tax could then maintain government resources. However, political and economic factors in ACP countries might very well prevent such a smooth transition. This will depend, first, on the extent to which the elimination of import tariffs will be accurately reflected in consumer prices, thus allowing consumption increases. Secondly, it will depend on the extent to which part of the production structure is dedicated to self-subsistence or transits through the informal sector and, thus, is de facto excluded from the tax system (Azam, 2007). Finally, it will depend on the political and financial capability of governments to widen the tax basis and to overcome the difficulties in collecting the tax (since administering a consumption tax is much more costly than applying import duties), Gnanon (2007).<sup>40</sup> Moreover, such a transition will take time, meanwhile, only EU development assistance can fill the gap, which would undermine the sovereignty of the ACP governments (Messerlin, 2006).

The loss of tariff revenues thus represents a central issue to ACP governments, as their reliance on such revenues is extremely high and significantly depends on trade with the EU. In West Africa (ECOWAS), it has been estimated that almost a quarter of government revenues depended on import duties in 2001 (Adenikinju & Alaba, 2005).

## ii. Focus on agriculture and food security

Agriculture employs over 60 percent of the population of ACP countries, and more than two-thirds of their exports of manufactured goods are agricultural products. While these figures are higher than in DCs as a whole, indicators of agricultural performance, on the contrary, are much lower in ACP states than in the average DC.<sup>41</sup> Production is still very volatile in the ACP region, yields are low on an international level and dependency on a few primary commodities is very important. There is therefore a very profound gap between the agricultural sector in ACP states and in the rest-of-the-world. It requires particular attention to prevent ACP agricultures from being completely marginalized from a more integrated agricultural global market.

However, EU negotiators have not yet considered the agricultural sector in a privileged way, despite its vital relevance to ACP economies. This is all the more surprising that there is potential for development: there are about 198 million hectares of arable land in SSA, of which a significant share is still unused or partially used and of which only 4 percent is irrigated (compared with 11 percent on average in DCs). Moreover, “there seems to be a strong relationship between agricultural productivity

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<sup>39</sup> These figures are most probable overestimated as they rely on the estimation of losses of taxes that should be theoretically levied. Yet, to a large extent, tariffs are not effectively collected.

<sup>40</sup> A possible outcome of the replacement of tariffs with a value added tax (VAT) is that, in practice, the VAT would only be collected at borders. Unless it is acknowledged by third party countries and reported to the WTO Dispute Settlement Body as a discriminatory practice, this would enable a de facto status quo with the current situation despite an official reform of the Cotonou Agreement. This however, does not appear as a sustainable option for ACP countries as, undoubtedly, third party countries would pick on such a practice. Besides, in terms of governance and transparency, it would be most damageable.

<sup>41</sup> See annex 3, tables 9 and 10, for data on the importance of the agricultural sector in ACP economies.

on the one hand and success in hunger reduction on the other” and the need for enhancing food security is more absolute in ACP countries than anywhere else in the world (FAO, 2006).<sup>42</sup>

Little impact assessments have focused explicitly on the agricultural sector. Indeed, knowing the significance of the informal economy, modeling ACP agricultural markets is a particularly hard task. Assessing their liberalization is all the more difficult that the extent of the competition ACP producers will face from EU products is not known. The EU does not negotiate over its support policy in the framework of EPAs and has not finally decided over its future Common Agricultural Policy (CAP) reform. The Doha Round running late, ACP countries will most probably have to decide upon signing EPAs before any EU offer in terms of support reduction is adopted.

Yet indications that agriculture will be at the forefront of adjustment needs and potential development exist. Several studies – mainly by NGOs – underline the particular vulnerability of ACP agricultural sectors to the competition of highly subsidized European products.<sup>43</sup> Christian Aid (2005) and Action Aid (2005) have produced case studies on the impact of lowering agricultural tariffs in SSA, which point at important negative outcomes. In Senegal, for example, between 1994 and 2001, tariffs on tomatoes and processed tomato products were reduced of an average 36 percent and quotas completely eliminated, while the state-owned tomato-paste factories were privatized. As a result, the stable tomato industry, which provided the best-paid jobs to rural households in the 1990s, was largely undermined. Indeed, tomato-paste industries stopped buying fresh tomatoes to local producers and imported European triple-concentrate. Imports of EU tomato paste increased from 221 tones in 1993/94 to 4600 tones three years later and the local price for tomatoes was divided by two. In such cases, qualifying the endangered products as sensitive might prevent sectoral crises in the short run.

Even studies funded by the Commission acknowledge these risks.<sup>44</sup> The United Kingdom’s House of Commons explicitly rejected the idea that “ACP states should be asked to open their markets to EU [agricultural] products until all trade-distorting subsidies have been removed” and demanded that “the transition period for full reciprocity in the agricultural sector should be explicitly linked to CAP reform” (House of Commons, 2005). This has, however, not been offered by the EC.<sup>45</sup> This means that ACP countries have a deep interest in the reopening of Doha negotiations to pressurize the EU on these issues in the multilateral arena.

Moreover, since agricultural sectors are the most protected ones, and since the EU cannot satisfy the whole demand, they are the most likely to see important trade diversion effects, on a net basis. Bouët et al. (2007) find that for some of these products, the incurred diversion could be of a very significant extent. The table below illustrates this phenomenon in the case of meat:

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<sup>42</sup> While between 1969 and 2001 the prevalence of under nourishment has decreased from 37 to 17 percent in DCs as a whole, it has remained almost stable in the ACP countries, slightly shrinking from 34 to 32 percent (FAO, 2006). The situation is all the more challenging that West African population will have doubled within 20 years. This growth rate is two to three times superior to the highest population growth rate Europe ever knew and there is no precedent of such a rapid population growth in the planet’s history.

<sup>43</sup> Fontagné et al. (2007) find that EU exports to ACP countries would jump by 45 percent on average (with growth rates ranging from about 30 percent in the SADC to over 55 percent in Eastern Africa). The increase in competition for ACP producers will thus be very significant. If, in absolute terms, importing from a more efficient partner is welfare enhancing, given the importance of the agricultural sector in ACP economies, adjustment could prove to be very costly. However, despite these impressive increases in EU exports, Fontagné et al. find that the ACPs would increase their agricultural trade surplus against the EU by over 100 percent (in dollar terms). Yet, this situations is very contrasted across regions. What is more, this result is obtained without taking into account SPS norms, which could profoundly alter ACPs’ export potential.

<sup>44</sup> For example, Nuno Castel-Branco et al. (2004) acknowledge that the milling and bakery industries in Mozambique are “dynamic” but might be damaged if tariffs on EU imports are eliminated.

<sup>45</sup> It is worth noting, on this issue, that while the French National Assembly has been at the forefront of criticizing the Commission’s way to deal with EPAs (see Lefort, 2006) it is also at the forefront of the opposition to a renegotiation of the CAP.

**Table 4. Illustration of trade diversion caused by the EPAs, the case of meat**  
(rate of import variation in %)

<b>Exporters</b>	<b>Importers</b>	Nigeria	Rest of ACP	Rest of ESA and SADC	Rest of WECA	Senegal
Bolivia, Uruguay and Paraguay		-30.8	6.2	-13.7	-22.9	-24.7
Central America		-30.4	6.8	-13.2	-22.4	-24.3
China		-30.8	6.2	-13.7	-22.8	-24.7
EU (27)		67.1	180.2	85.1	109.5	92.8
Japan		-30.8	6.3	-13.6	-22.8	-24.6
Rest of South America		-30.6	6.5	-13.5	-22.6	-24.5
Thailand		-30.5	6.7	13.4	-22.5	-24.4
United States		-30.8	6.3	-13.7	-22.8	-24.7

Source: Bouët et al. (2007)

Note: The EPA scenario is defined as the implementation of FTAs between the EU and six ACP regions, which among themselves form FTAs. 20 percent of trade is excluded of the EU-ACP liberalization upon sensitivity criteria.

Variation par rapport à quelle année??

Finally, a key political issue concerning agriculture is the need to redirect funds to the sector. External assistance to ACP farmers has been continuously decreasing over past years. It is currently only about a quarter of its 1982 peak level (Petit, 2006). Moreover, aid is targeted at countries with the lowest prevalence of undernourished people (FAO, 2006). In the ninth European Development Fund, only 3 to 5 percent of the budget was dedicated to agriculture. Things have to change in this respect, not only concerning communitarian aid but also that of member states. In parallel, ACP governments mobilize significantly less resources for agriculture than DCs overall. Concerning the nature of assistance, it can only be recalled that massive investment in infrastructures is needed (According to the FAO, the state of current African infrastructures is comparable to that of India in the 1950s). This is, of course, not a new finding; however, despite abundant advocacy of structural investment needs in the agricultural sector, it is not actually taking place.<sup>46</sup>

### iii. Effects on regional integration

Investigating into the theoretical relevance of promoting regional integration, the second section of this paper concluded that south-south integration could be beneficial by reducing the hub-and-spoke risk, fostering economies of scale, helping address regional issues and by helping the integration of the region in world economy. The possibility for improvement is potentially important since regional integration is today extremely weak in most sub-Saharan sub-regions, as is illustrated in the table below.<sup>47</sup>

**Table 5. Significance of intra-regional trade in selected African regions, 2007**

<b>Region</b>	<b>Intra-regional exports (% of total exports)</b>	<b>Intra-regional imports (% of total imports)</b>
SADC	0.8	0.8
ESA	3.5	3.4
WECA	5.4	4.2
Caribbean and Pacific	3.6	3.1

Source: Berisha-Krasniqi et al. (2007)

<sup>46</sup> The recent release of the World Bank Development Report 2008, which is entirely dedicated to the agricultural sector, might signal a new impetus in this direction.

<sup>47</sup> Smuggling means that these figures are probably underestimated.

However, a last point of major concern relates to the EPAs' actual potential to foster intra-ACP regional integration. Indeed, EPAs pose a very serious challenge to regional integration: the harmonization of sensitive products' lists at the regional level. This harmonization could indeed be a difficult task. And, if sensitive products differ from one country to another, borders would again have to be settled within ACP regions. The problem is that "natural" national choices of sensitive products might not overlap on a regional basis. Stevens and Kennan (2005a) find that "in all cases, apart from East and Southern Africa, over half (and as much as 92 percent for West Africa) of the products included in any one country's basket of exclusions would be absent from the exclusion lists of all of its partners."<sup>48</sup> This is due to the high diversity of the sub-regions' production structures. (Ribier, 2007)

Moreover, countries might have different priorities and political objectives when choosing sensitive products. Indeed, three concerns can motivate the product choice: (i) protection against fiscal and budget losses; (ii) protection against EU competition; and (iii) protection against negative effects on labor, food security, or other social trends. In addition, lobbies will be at work within countries but also between countries. According to Faivre-Dupaigre (2007), powerful countries could try to game this situation for their own benefit, by influencing regional choices in their own interests (e.g. Ivory Coast in West Africa).

A second risk for regional integration is that the liberalization of some agricultural markets could enhance the tensions between coastal countries and inner Sahelian countries whose regional exports will face the competition of imported EU goods on the markets of the former, Faivre-Dupaigre (2007).

Furthermore, the fact that LDCs can benefit from tariff-free access to the EU through the Everything But Arms initiative (EBA) means that they have weaker incentives to enter EPAs than non-LDCs. If some of them chose to stick to EBA preferences and thus not open their markets to EU exports, they would have to implement new border controls with EPA-signing neighboring countries in order to prevent European products from transiting through them.

In an unpublished paper presented in the House of Commons (2005), the UK's Department for International Development (DFID) warned that "the EU is seeking to impose a European model of regional integration on DCs which is at least out of date and probably inappropriate." According to Stevens, "all in all, the outlook for EPAs to support regionalism is not good", Stevens (2005c). One might add that the EC's recent negotiation strategy consisting in negotiating directly with single countries in regions where the opposition to EPAs is strong can only reinforce these negative effects on regional integration.

#### **4. Rethinking EPAs**

The above review of the possible impacts of implementing EPAs as they are currently being offered to ACP countries calls for identifying policies which could help maximize their benefits and minimize their losses. Several of these policies have been evoked in the preceding sections and have also been investigated in more focal studies. The most important issues in this respect include the need to reform the rules of origin to make preferences effectively beneficial – by lessening the cost of compliance and making cumulation amongst regional partners easier. The preferential access to the EU market offered under the EBA has, for example, been little exploited by African exporters because rules-of-origin are too costly to comply with.<sup>49</sup> Very important also will be the internal reforms initiated by ACP

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<sup>48</sup> This analysis considers sensitive products as those which are currently the most protected.

<sup>49</sup> Rules-of-origin determine the extent to which products have to be produced or processed in a country or a region for that product to be said to originate from that country or region. Rules of origin most often entitle the right to cumulate products from different origins on different criteria: bilateral cumulation allows the partner country to use EU material, diagonal cumulation allows a limited use of third countries material, regional cumulation allows a limited use of products originating from a defined region and full cumulation allows unlimited use of products from a defined list of countries. The restrictiveness of rules-of-origin increasingly

countries to help compliance with EU rules, to enhance domestic competitiveness and to upgrade infrastructures and production capacities. In this last respect, financial and technical aid from the EU will be essential.<sup>50</sup>

However, these important issues are not likely to change dramatically the results of EPAs. Re-thinking the broad framework of the agreement might thus prove necessary. And, the assessment conducted in the two preceding sections indicates that some of the conditions needed to maximize the gains EPAs could foster and to limit their potential negative outcomes are linked to the nature of the liberalization scheme proposed, rather than to its extent. Reconsidering the nature of the efforts asked to ACP countries might therefore help making the best of the current broad EPA framework. This particular issue is more lengthily addressed below.

#### 4.1 Questioning WTO flexibility

First, it is worth noting that an ideal reform of EU-ACP trade deals would have taken place in conjunction with a reinterpretation of article XXIV in the Doha Round, as was initially planned.<sup>51</sup> It would have been an opportunity to reform rules that were established when the WTO was still a circle of relatively prosperous developed countries. However, given the current state of multilateral negotiations, there is little hope that any formal revision of article XXIV will be initiated.

The key question regarding WTO obligations therefore is whether all options have been considered and how far they can be circumvented when dealing with the special circumstances of the ACP countries, a group which includes most of the poorest populations of the world.

This is true at two levels: formal and informal. WTO conformity in trade agreements ensures certainty (by eliminating the risks of challenges). However, should conformity be too costly, some departure from the legislation could also be assumed. Indeed, the WTO can – informally – be flexible if all of its members is in agreement, or, if none of its members are in disagreement. For several years now, the US has thus granted non-reciprocal and discriminatory preferential access to African countries through the African Growth and Opportunity Act (AGOA), and to Caribbean countries through the Caribbean Basin Initiative (CBI). Besides, complaints before the WTO Dispute Settlement Body are rarely dealt with promptly, and more often take years to reach resolution.<sup>52</sup> Moreover, if the banana and sugar issues are excluded, chances of disputes might be small.<sup>53</sup> Indeed, a challenge to the EPAs, on general grounds, “would require a panel to decide on the definition of a legitimate regional trade agreement, including the meaning of ‘substantially all the trade’ in article XXIV:8.” (Bartels, 2007) And such a decision would affect most WTO members, who are party to dubious regional trade agreements.<sup>54</sup> WTO conformity is therefore probably not as binding and urgent as the EC has been proclaiming.

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determines the value of preferences entitled in preferential trade agreements and explains why many developing countries do not always export to partner countries under preferential agreements’ terms. For example, it is believed that the AGOA has more impact on African trade flows with the US than the EBA has on African trade flows with the EU – despite less generous tariff cuts – because of looser rules of origin, Collier and Venables (2007). For more details on the options to reform rules of origin, see Cadot and De Melo (2007).

<sup>50</sup> It should be noted that aid amounts should not be an issue in coming years. Funds are available but most often not used. However, much could be done to enhance aid effectiveness.

<sup>51</sup> The ACPs, as well as the EU, have submitted proposals for the introduction of differentiation in article XXIV.

<sup>52</sup> “According to the Dispute Settlement Understanding, the total period from commencement of consultations to the authorizing of retaliation, including an appeal, should be around three and a half years.” (Bartels, 2007)

<sup>53</sup> These two issues could be dealt with separately.

<sup>54</sup> According to Bartels (2007), “it is worth noting that in *Brazil – Retreaded Tyres* (WT/DS332/R), a report currently on appeal, the EC claimed that Mercosur failed to meet the ‘substantially all the trade’ requirement in Article XXIV:8. One might question whether the members of Mercosur would risk a panel determining the meaning of ‘substantially all the trade’, with the implications that this would have for their own most important regional trade agreement.”

On a more formal basis, alternatives also exist. First, there are ways to buy more tolerance vis-à-vis a non-compliant trade agreement that have not been exploited. In fact, according to Bartels, any ACP country that is a WTO member can independently request a waiver at the WTO for a continuation of Cotonou preferences into the EU market.<sup>55</sup> Besides, article XXIV also states that a two thirds majority can approve trade agreements that do not fully comply with WTO obligations (article XXIV:10). Second, another possibility that would buy ACPs time to think through economically sounder agreements, is that the EU and ACP could notify only a very basic agreement plan as ‘interim agreements’.

All this means that there should be room for innovation, especially if the EU and ACP countries can bring in the perspective of an agreement with appeal to non-party countries.

## **4.2 Investigating into one path for alternative agreements<sup>56</sup>**

### **i. The acceptability of a different interpretation of trade liberalization**

Three interpretations of liberalization are possible: it can be understood as the diminution of all applied tariffs by a certain percentage (the U.S. vision); the elimination of a percentage of applied tariff lines (the EU vision); or the decrease of bound tariffs and the suppression of tariff peaks.<sup>57</sup> The only option envisaged in the EPA negotiations until now has been the second. Negotiations therefore concentrate on the percentage of trade volume that will have to be liberalized and on the choice of the sensitive products that will still enjoy tariff protection.

However, this definition of liberalization might not be the most efficient, and the third understanding of moving towards free trade might be more adapted. Moving towards a more or less uniform bound tariff structure (which might actually imply increasing some tariffs) is not often considered as a move in the direction of liberalization. Yet, as suggested by Messerlin (2001), such a “re-balancing” of bound tariffs at a level close to the applied tariff rates can be considered an effort towards freer trade as it significantly increases trade predictability and diminishes distortions. Indeed, in such a case, applied and bound tariff peaks would disappear and the eventuality of future tariff increases would be limited to a variation of applied tariffs that would already be below the bound limit, and only up to that limit. All applied tariffs would therefore be kept within a pipe, with certainty.<sup>58</sup> And, as shown by Messerlin and Delpeuch (2007), ACP countries have a lot to offer in terms of binding coverage: half of the African ACPs have bound less than a third of their tariff lines.

If considered from a multilateral perspective, such an approach could well receive support in the WTO framework, even if such an agreement would not be respecting WTO rules to the letter of the law. As proposed by Messerlin (2001), Hinkle and Schiff (2004) and Hoekman (2005), ACP countries could offer an effort towards free trade that would benefit the world as a whole, in exchange for being allowed to grant only minimal reciprocity to the EU. Indeed, non-EU WTO members would suffer if

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<sup>55</sup> "Waivers from WTO obligations are governed by Article IX:3 and 4 of the WTO Agreement, and the Understanding on Waivers (formally a part of the GATT 1994). [...]Formally speaking, Article IX:3(b) requires that a decision to grant a waiver be taken by vote of at least 3/4 majority of WTO Members. It was however decided shortly after the WTO was established that the ordinary practice of decision-making by consensus should also apply to waiver decisions under Article IX: WT/L/93, 24 November 1995." (Bartels, 2007)

<sup>56</sup> Several alternatives to the currently envisaged agreements have been put forward in the literature both in the form of alternative EPAs and alternative to EPAs. Bilal and Rampa (2006), in particular, exhaustively list and examine possible alternatives. However, there has yet not been any policy response to these proposals. This paper does not review these different options but rather tries to put the emphasis on one option – which is believed to be both politically feasible and economically desirable.

<sup>57</sup> Once declared to the WTO, bound tariffs cannot be increased (in contrast to applied tariffs, which can be increased if they are lower than bound tariffs).

<sup>58</sup> A short insight into the theoretical analysis of uniform tariffs is given in annex 2.

ACP markets were being opened to EU firms while remaining closed to their own firms (e.g. in the meat sector, several key WTO members would face significant trade diversion in favor of the EU as shown in sub-section 3.3). Moreover, the non-ACP developing countries negotiating preferential agreements with the EU have an interest in ‘better’ EPAs in order to avoid any negative precedent that could impact their own bilateral negotiations with the EU (Messerlin and Delpeuch, 2007).

For ACP countries themselves, a non-discriminatory re-balancing of tariffs would have several very significant advantages over a selective removal of tariffs only on EU imports.

ii. The advantages for ACP economies of multilateral liberalization as the price to be paid for limited reciprocity.

These advantages pertain to three elements: the non-discriminatory character of the proposed alternative, the harmonized character of liberalization as opposed to a selective removal of tariffs entitling the exclusion of sensitive products and the focus on bound rather than applied tariffs.

First, from an economic perspective, regional integration between the EU and ACP countries would be most beneficial if the integration process was opened to the rest of the world, so as to limit trade diversion.

Second, a more or less harmonized diminution of bound tariffs would have several advantages as compared to applied tariff elimination with exceptions (sensitive products). First, this would ease internal political governance by tremendously reducing the incentives for particular lobbies and limiting the loss of government revenues. Indeed, with the current EC’s proposal, political leaders in ACP countries will face a dilemma between saving government revenues (by retaining the lowest tariffs) or limiting the increase in EU competition for domestic products (by retaining tariff peaks). And, in resolving this dilemma, lobbying by special interest groups will likely play a role that might not favor the interest of the majority. In fact, lobby pressure would probably push governments to lower already low tariffs and maintain the high ones, thereby increasing distortion in the tariff structure and thus efficiency losses. Government revenues losses would be maximal, while gains for consumers would be minimal (as they will benefit only from small import price reductions). On the contrary, the choice of more or less uniform bound tariffs could be guided by the objective to maintain current government revenue levels.<sup>59</sup> Eliminating the sensitive product choice would also help regional integration. Indeed, the dilemma over this choice would also take place at the regional level, when harmonization is seek to avoid reintroducing trade barriers within ACP regions.<sup>60</sup> Finally, a more uniform tariff structure would facilitate border controls and reduce corruption risks.

Of course, higher or lower uniform tariffs deprive governments of using commercial policy as a strategic economic tool.<sup>61</sup> However, by guaranteeing tariff revenues, it gives them the ‘policy space’ to use other more efficient instruments, such as consumption or production subventions (especially for the agricultural sector) that are acceptable at the WTO for DCs (Messerlin, 2006 and Page, 2007).

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<sup>59</sup> Using as a reference the Chair text in the Doha NAMA negotiations, Messerlin and Delpeuch (2007) give an insight into how such a proposal could look like. They find that the ACPs would substantially cut their bound tariffs but only modestly cut their applied tariffs, meaning that they would avoid significant tariff revenue losses. Interestingly for other WTO members, the remaining tariff water (that is the difference between bound and applied tariffs) is often lower than 10 percent.

<sup>60</sup> For example, Kenya’s main objective in choosing sensitive products will probably be to protect its domestic production from European competition, whether Uganda, whose revenues already depend by half on foreign aid, might want to preserve its independency and limit revenue losses as much as possible.

<sup>61</sup> Concerning very specific development issues such as food security, exceptions to the bound tariff rule could be included in the agreement.

## Conclusion

As anticipated in the 2000 Cotonou Partnership Agreement, the EU and ACP countries have entered the final phase of negotiations. Just a few weeks before the deadline, imposed in order to avoid new sanctions in the WTO, the EU has not been able to convince the ACP countries that the declared objectives of enhancing development and reducing poverty will be met by the establishment of gradual, managed, and aid-accompanied trade liberalization. No ACP states have yet stated their official and definitive refusal to conclude EPAs, but civil societies are expressing their disagreements and it looks like the final decision over signature will be taken under very high pressure.

Reviewing impact assessment studies, this paper finds that the fears expressed by the opponents of current EU proposals are far from groundless. On the contrary, opponents of EPAs have a number of valid points, which the EC should be taking on board. While trade diversion might not be a risk for all countries, it will be for many. Government revenue losses will most certainly be significant. Regional integration will not be easily fostered. Agricultural producers will find it hard to resist the competition brought on by EU imports – especially in remote areas. And, the choice of sensitive products will be costly, both as a result of lobbying and of lost economic efficiency.

However, this paper does not call for maintaining non-reciprocal preferences *ad vitam aeternam*. Yet, brutally forcing changes in the system, at any cost, is not the solution either. Contrary to what had been promised to ACP countries in the Cotonou Agreement, the EC has proposed no other acceptable alternative. There is thus a pressing need to rethink the framework of the agreements, so as to maximize their potential positive outcomes.

It is senseless to attempt to conclude, under the gun and with so little time, agreements that are of such critical importance to poor countries' development. While WTO compliance is a commendable objective, the particular situation of ACP countries should be reason enough for the EU to seek a way of finding the necessary time to reach more mutually-acceptable solutions. A proposal to make future agreements valuable for non-party countries by a non-discriminatory liberalization in ACP countries should help the EU and the ACP countries to get the support for broad interim agreements preparing the ground for more economically, fiscally, hence politically sound final agreements.

In particular, the paper calls for an investigation into the effects of an alternative definition of liberalization—one that would lead to the adoption, by ACP countries, of non-discriminatory more or less uniform bound tariffs. Rather than pressing ahead with complex and wrongheaded negotiations over tariff elimination choices, the EC should take the opportunity, even at so late an hour, to consider such alternative solutions that could appeal to non-members despite not being fully WTO compatible.

The economic growth and development of ACP countries is, ultimately, in the EU's own best interest. Not only because the ACP zone is a potential market for EU products, but also because its development and well-being are closely linked with migration flows to Europe. Furthermore, according to a Eurobarometer survey of public opinion, 91 percent of EU citizens express their belief in the importance of policies that promote development (EC, 2005). Taking the time to conclude agreements that truly promote development is an opportunity to take a laudable and ambitious step in the right direction. Moreover, it would make EU's bilateral position much more coherent with its multilateral position.<sup>62</sup>

Political leaders in the EU should also be aware that, should the EPA negotiations fail, or continue

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<sup>62</sup> It was the EU who first introduced the idea of a round for free (i.e. a round during which LDCs would not be asked any liberalization effort) and who first accepted to drop "Singapore issues" from the Doha Round's agenda. It is therefore incoherent, that, in its negotiations with ACP countries, the EU takes the opposite positioning.

along their current path to an unsatisfactory and unsavory outcome, the ACP countries are not the only ones who will pay the price. If signed into effect, the current EPAs risk becoming a scapegoat—rightly or wrongly—for the continuing economic problems of Africa and the plight of some of the world’s most vulnerable populations. Meanwhile, China will not stay waiting in the wings, given the way the Chinese are already challenging the EU both economically and politically on the African continent.

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## **Annex 1. A short overview of EU-ACP cooperation**

The history of the EU-ACP cooperation framework goes back to the very creation of the EEC. The idea that the foreign policy priority of the EEC should be the promotion of development in Africa was already present in Schuman's founder declaration, in which he stated: "With increased resources Europe will be able to pursue the achievement of one of its essential tasks, namely, the development of the African continent."

In this perspective, the 1957 Rome Treaty established a free-trade area between the EEC and its colonial territories as well as within these territories (with safeguards and exceptions for revenue and infant industry protection purposes).<sup>63</sup> In 1959, the European Development Fund (EDF) was created to provide technical and financial assistance to colonies and former colonies in Africa. This trade and cooperation framework was further institutionalized with the Yaoundé Agreements (Yaoundé I in 1963 and Yaoundé II in 1969), which replaced the single free-trade area with a set of 18 bilateral agreements of "reverse preferences" between the EEC and each of the former colonial territories thus abandoning the provision for free-trade among the territories.<sup>64</sup> At the time, the conformity with the legislation of the General Agreement on Tariffs and Trade (GATT) was already an objective as the agreements were referred to as "interim arrangements leading to the establishment of an FTA", Ravenhill (2002). In the second Yaoundé Agreement, the scope of the preferences and the number of beneficiary countries was enlarged, as new EEC member states increased the number of the Community's former colonies.

A first breakthrough in the commercial relationship appeared in 1975, when the first Lomé Convention replaced the Yaoundé Agreements. Indeed, in these new agreements, the reciprocal dimension of the trade preferences was abandoned. EEC partners were only asked not to discriminate between EEC members. Several factors led to this major evolution. First, the US, which had just pushed for the creation of the GSP, considered that asking for "reverse preferences" meant that the agreements did not aim at promoting development but served the EEC's interests and saw them as post-colonial agreements. Second, the UK used to offer very favorable conditions to its former colonies (e.g. the sugar protocol) and therefore asked for the upgrade of the ACP trade regime before accepting to join the Community.<sup>65</sup> Third, at the time, the EEC was dependant on ACP imports of raw materials and was therefore not in an absolute dominant negotiating position. Lastly, the newly created Directorate General of the Commission for Development favored such a change. It is therefore interesting to note that the changes proposed in the EPAs today are in fact a comeback to the very beginning of EU-ACP relationships.

While the two first Lomé conventions were based on the respect for sovereignty (as they were signed in the post-independence era, when the EU was afraid of being accused of post-colonialism and needed to secure its energy supplies), during the 1990s, conditionality became an increasingly important dimension of cooperation. The third and fourth Lomé Conventions included twenty articles of political nature. The emphasis was progressively put on the respect of human, economic and social and cultural rights, and, later, on the respect of civil and political rights, democratic principles, the rule of law, on good governance and on the inclusion of the private sector. This shift in the nature of cooperation was fostered by the increasingly dominant position of the EU in the negotiations as the ACP group became of less geo-political and economic importance to the EU (the dependence on ACP raw material declined<sup>66</sup>, the end of the Cold War and the successive enlargements of the Community put Eastern Europe high on Europe's diplomatic agenda and the Mediterranean area gained in economic and political importance because of immigration and terrorism issues). The progressive

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<sup>63</sup> Articles 131 and 136

<sup>64</sup> In the Yaoundé Agreements, the EEC offered free access to his market to ACP countries, but ACP countries also offered free access to European merchandises.

<sup>65</sup> The review of the Yaoundé Agreements was part of the terms of UK accession to the EEC (Ravenhill, 2002).

<sup>66</sup> The share of EU imports from ACP countries in total EU imports declined from 6.7 percent in 1976 to 3.11 percent in 2002 (Manchin, 2005).

enlargement of the ACP group of states participated to the weakening of their negotiation power as, the greater the number of member states, the more difficult the identification of common interests for which to fight united. Nonetheless, from 1975 on, non-reciprocity remained a funding principle.

Non-associated developing countries have complained about the preferences granted to ACP countries since they were created. In 1971, after pressurizing the EEC through the UNCTAD forum, they already obtained the creation of the GSP scheme (Grilli, 1993). However, Lomé was never challenged at the WTO before the Uruguay Round and a complaint of Central American countries over the banana regime in January 1994. In this case, the EEC was found guilty. The second GATT Banana Panel found that Lomé “contravened GATT’s most favored nation requirements” as it discriminated between countries of similar development level while it did not meet the requirements for an exemption under article XXIV. It has to be noted that only the banana quota system was being challenged. The EEC however asked for a WTO waiver for the whole Convention. The move towards Cotonou and the explicit adoption of the WTO conformity objective was thus primarily initiated by the EEC itself – maybe because the development of the ACP region was not a top priority anymore.<sup>67</sup>

A waiver was thus conceded in November 1994 to allow for a smooth transition. It was then extended up to 2007, during the Doha Ministerial, on condition that the new EU-ACP agreement would set a path for a future WTO-compatible agreement. When the last Lomé convention expired in 2000, it was therefore replaced by the Cotonou Agreement, which maintained the Lomé preferences up to 2007 only with the proviso that negotiations commence for a WTO compatible agreement that would take effect on January 1, 2008. A timetable of EPA negotiations is given in the following page.

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<sup>67</sup> Indicative of this evolution, in 1999, trade with the ACP region shifted from being a responsibility of DG Development to being a responsibility of DG Trade. (Ravenhill, 2002)

Table 6. EU-ACP co-operation over the past 50 years

Year	Event	Contracting parties		Evolution of the EU-ACP relationship
1957	Traité de Rome	EEC 6	31 OCTs <sup>(1)</sup>	The Rome treaty establishes a free-trade area between the EEC and all the colonial territories, as well as within these territories, with safeguards and exceptions for revenue and infant industry protection purposes for the OCTs.
1959	Creation of EDF	EEC 6	31 OCTs	Creation of the European Development Fund (EDF), under the Treaty of Rome which provides for technical and financial assistance to countries having strong links to EEC's member States.
1963	Yaoundé I	EEC 6	18 AASMs <sup>(2)</sup>	The Free Trade area envisaged in the Rome Treaty is replaced with 18 bilateral preferential trade agreements. Development support to former colonies, mainly in West Africa is granted.
1969	Yaoundé II	EEC 6 then 9	18 then 22 AASMs	
1971	Creation of EU's GSP scheme	EEC 6 then 9	All LDCs	Under pressure of developing countries which did not enjoy Yaoundé preferences and of the UNCTAD, the EEC introduces a GSP scheme that applies to all LDCs.
1975	Creation of the ACP group		46 ACPs	Following UK accession to the EEC, its development program extends to Pacific and Caribbean states. Creation of the ACP group of 46 States.
1975	Lomé I	EEC 9	46 ACPs	Co-operation agreement between the EEC and the ACP group and creation of related institutions: the Council of Ministers, the Committee of Ambassadors and the Joint Assembly. Preferential trade access becomes unilateral. ACP partners are only asked not to discriminate between EEC members.
1980	Lomé II	EEC 9 then 10	58 ACPs	Introduction of the concept of aid effectiveness.
1985	Lomé III	EEC 10 then 12	66 ACPs	Introduction of a human rights clause.
1990	Lomé IV (IV bis as from 1995)	EEC 12 then 15	68 ACPs	Reinforcement of political cooperation and introduction of conditionality, focus on the participation of private actors.
1996	Green Paper	EEC 15		Assessment and design of EU-ACP cooperation by the Commission
2000	Cotonou Partnership Agreement	EU 15 then 27	77 ACPs	Extension of Lomé preferences with the proviso to commence negotiations over a WTO compliant trade agreement by the end of 2007.

Notes: (1) OCT: Overseas countries and territories

(2) AASM: African Associated States and Madagascar

Sources: Grilli (1993) and ECDPM (2006)

Table 7. Timetable of EPA negotiations:

<u>Period</u>	<u>Negotiation</u>	<u>Trade Regime</u>
20/11/1996	The EU publishes a Green Paper “on the relations between the European Union and the ACP countries on the eve of the 21 <sup>st</sup> century”.	Lomé Regime (dating from 1975) <sup>68</sup>
07/2000	The Cotonou Agreement sets the Agenda for the negotiation of new WTO compatible EU-ACP agreements.	The Cotonou Agreement extends the Lomé preferences, on condition that new agreements are negotiated
01/2000 – 09/2002	EU-ACP negotiations on modalities for EPA negotiation. In June 2002, the EC mandate is adopted and, in July 2002, the ACPs adopt their <i>Guidelines for the negotiations of EPAs</i> . EU negotiation at the WTO for a new waiver allowing Lomé preferences.	Lomé preferences are maintained through a WTO Waiver, without reciprocity.
09/2002	Start of EPA negotiation on an all-ACP/EU basis	
10/2003	Start of negotiations on a sub-regional basis	
2004-2005	EU-ACP negotiation on alternatives for countries that are not able to sign an EPA.	
09/2006	EU-ACP review of the negotiations	
12/2007	Scheduled conclusion of EPA negotiations.	
From 01/2008	Application (with transition period) of EPAs	End of the Lomé regime and introduction of reciprocity. LDCs that do not sign an EPA enjoy EBA regime. Non-LDCs that do not sign an EPA enjoy the GSP.

<sup>68</sup> Before the Lomé region, the Yaoundé Conventions settled the bilateral trade regime between the ACP and the EU. At the time, reciprocity did exist and was later removed in the Lomé regime, as a development tool.

## **Annex 2. The theory of tariff harmonization**

Panagariya (1996) reviewed the literature on uniform tariffs both from a theoretical and empirical perspective. Uniform tariffs can be advocated in the context of small and open economies, when “exogenously specified non-economic objectives or political constraints” exist. The optimal tariff for a small open economy otherwise being complete free trade. Two of these non-purely economic objectives are protection and government revenue, two main concerns for ACP countries. Trade policy is rarely the first-best policy instrument to address these concerns. Yet, as mentioned earlier, in countries such the ACPs, alternative tax sources might not be easily collectable. Similarly, budgets might be too tight to offer subsidies as a more efficient protection instrument.

Panagariya finds that most of the debate on the subject comes from the opposition between “academic economists” who consider, theoretically, that uniform tariffs are rarely optimal<sup>69</sup> and “policy economists” who advocate a single tariff to minimize trade policy distortions in practice<sup>70</sup>. Papers by Corden illustrate well this contradiction between theoretical economics and practical policy concerns. Indeed, “in his academic writings, [he] has systematically shown why tariff uniformity is nonoptimal under most circumstances. Yet, in his policy writings and policy advice, he favours uniformity with strong conviction.” (Panagaryia, 1996)

Panagaryia identifies loopholes in both approaches: Theoretical economic arguments clearly fail to take into account administration costs and data unavailability while policy arguments at best illustrate the need for a limited number of tariffs. Yet, a case for uniformity can still be made, if true political concerns are taken into account. These include the possibility to escape from lobby influence, thus turning tariffs “from a private to a public good”. Setting uniform tariffs is also a means of tying the hands of future governments as departing from the rule will be much more visible.

This conclusion illustrates the interest of harmonizing ACPs’ tariff structure in at least one respect: dealing with internal governance. Several more advantages of such a policy pertain to the very specific case of EPA negotiations – as is explained in section 4.2.

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<sup>69</sup> Considering the revenue objective, Ramsey (1927) showed that, to minimize distortions, products should be taxed inversely proportionally to their demand elasticity. As products have very different demand elasticities, academic economists do not advocate uniform tariffs. Second, considering the protection objective, when subsidies cannot be used, the least distorting tariff policy would be “lowering tariffs on inputs used in exportables and nontradables and raising them on inputs used exclusively in import-competing sectors”. Again, uniformity is nonoptimal. (Panagaryia, 1996)

<sup>70</sup> The strongest argument of uniform tariff advocates is that the optimal tariff structure is practically very hard to determine as demand elasticities are very difficult to estimate. “Extra distortion caused by uniform tariffs is [then] likely to be less than other arbitrary tariffs that might be adopted.” (Panagaryia, 1996) Besides, a second justification for uniformity is transparency and administrative simplicity, considering that “costs of administration may rise with the complexity of the tariff code.”

### Annex 3. Descriptive statistics

Table 9. Imports and exports (total and agricultural products) between the EU and ACP regions: 1999-2005

Regional Entity	Imports (million euros)			% Agriculture in total Imports		Exports (million euros)			% Agriculture in total Exports	
	1999	2005	1999 = 100	1999	2005	1999	2005	1999 = 100	1999	2005
Total ACP Zone	22292	36077	162	38	24	22151	30619	138	14	12
West Africa	8326	13764	165	36	23	9895	13782	136	17	14
Central Africa	3212	4666	145	13	11	2494	2939	118	13	14
Eastern Africa	9011	12959	144	35	26	13444	16106	120	11	10
Austral Africa	2200	7450	339	32	11	1718	3121	182	17	15
Caribbean	2353	3823	163	46	24	3550	4681	132	11	9
Pacific	591	1246	211	85	34	108	568	527	15	2

Sources: Eurostat, FARM (2006)

Table 10. Basic indicators for ACP regions and the EU

(all data is for 2004, when not mentioned explicitly)

Regional entity <sup>71</sup>	GDP in million €	% of total ACP GDP	Population (millions)	% of total ACP population	Rural Population (%)	% of Active population in agriculture	Degree of under nourishment	Number of LDCs	% LDC GDP in regional GDP
West Africa	106424	35,3	258	35,9	57	50	24,7	13	26,6
Central Africa	34636	11,5	91	12,7	54	58	37,7	5	36
Eastern Africa	66286	22	245	34,2	73	72	30,1	10	66,4
Austral Africa	44840	14,9	79	11,1	64	75	32,3	4	68,9
Caribbean	42416	14,1	35	4,9	48	30	12,3	1	7,3
Pacific	7114	2,4	9	1,2	80	65	16,2	5	11,4
Total ACP Zone	301717	100	717	100	n.a.	n.a.	n.a.	39	39,6
European Union	9755400*	3233%**	455	63,5%**	24	6		0	0

Notes: n.a. not available ; \* data for 2003 ; \*\* total EU/ total ACP x 100

Sources: Boussard et al. (2005a), FARM (2006), Fontagnié et al. (2006)

<sup>71</sup> Regional Entities (LDCs are marked with a \*)

- West Africa encompasses ECOWAS countries (Benin\*, Burkina Faso\*, Cape Verde\*, Ivory Coast, Gambia\*, Ghana, Guinea\*, Guinea Bissau\*, Liberia\*, Mali\*, Niger\*, Nigeria, Senegal\* Sierra Leone\* and Togo\*) plus Mauritania\*

- Central Africa encompasses CEMAC countries (Cameroon, Chad\*, Central African Republic\*, Congo, Equatorial Guinea\* and Gabon) plus the Democratic Republic of Congo\*, Sao Tome and Principe\*

- Eastern Africa corresponds to the COMESA region, except for Libya and Swaziland (Burundi\*, Comoros\*, Djibouti\*, Eritrea\*, Ethiopia\*, Kenya, Malawi\*, Mauritius, Madagascar\*, Rwanda\*, Seychelles, Sudan, Uganda\*, Zambia\*, and Zimbabwe)

- Austral Africa corresponds to the SADC region (Angola\*, Botswana, Lesotho,\* Mozambique\*, Namibia and Tanzania\*) plus Swaziland

- Caribbean countries (Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Dominican Republic, Grenada, Guyana, Haiti\*, Jamaica, St. Kitt and the Grenadines, Suriname and Trinidad and Tobago)

- Pacific countries (Cook Islands, Fiji, Kiribati\*, Marshall Islands, Federated States of Micronesia, Nauru, Niue, Palau, Papua New Guinea, Samoa\*, Solomon Islands\*, Tonga, Tuvalu\*, Vanuatu\*)

Table 11. Trade diversification in agriculture (2000-2004)

Country	4 top agric. Export products (% of agric. Exports)	4 top agric. Export products (% of total exports)	Export diversification (Herfindahl-Hirschman Index)	Country	4 top agric. Export products (% of agric. Exports)	4 top agric. Export products (% of total exports)	Export diversification (Herfindahl-Hirschman Index)
<b>West Africa:</b>				Swaziland	71	23	0,416
Cape Verde	100	0	0,853	Mozambique	67	12	0,332
Benin	92	78	0,698	Tanzania	53	22	0,254
Mali	91	20	0,799	Namibia	52	10	0,256
Burkina Faso	90	77	0,760	South Africa	39	4	0,174
Gambia	88	58	0,578	<b>Central Africa:</b>			
Nigeria	81	0	0,530	Central African Republic	100	10	0,755
Niger	78	28	0,394	Sao Tomé & Príncipe	100	97	1
Guinea	77	2	0,469	Gabon	93	1	0,635
Ghana	68	25	0,452	<b>Caribbean:</b>			
Togo	67	23	0,361	St. Lucia	97	56	0,680
Senegal	65	11	0,397	St. Kitts & Nevis	95	18	0,742
<b>Eastern Africa:</b>				Belize	94	68	0,560
Rwanda	99	60	0,626	Grenada	94	42	0,624
Burundi	96	43	0,820	Guyana	94	33	0,649
Seychelles	96	1	0,713	Antigua & Barbuda	92	4	0,583
Malawi	93	81	0,641	Bahamas	92	10	0,762
Mauritius	92	18	0,829	St. Vincent & the Grenadines	85	68	0,498
Ethiopia	80	68	0,461	Dominica	79	31	0,558
Madagascar	80	37	0,559	Barbados	75	25	0,399
Zimbabwe	77	41	0,502	Jamaica	57	14	0,274
Sudan	76	14	0,416	Trinidad & Tobago	49	3	0,235
Uganda	70	44	0,397	Dominican Republic	44	20	0,205
Kenya	67	38	0,386	<b>Pacific:</b>			
Zambia	62	10	0,321	Cooks Islands	100	18	0,838
Eritrea	55	24	0,294	Papua New Guinea	88	11	0,503
<b>Austral Africa:</b>				Fiji	79	29	0,597
Botswana	80	3	0,447	Samoa	78	6	0,393

Table 12. African ACP countries' 2006 MFN tariff structure for goods

Country	Average Applied Tariff (trade weighted)		Maximum tariff	% of tariffs under 25%	Exemptions (> 5% of a product group)	Tariff peaks	Member WAEMU (CET)	Member ECOWAS 2008	Member COMESA -2009	Member SACU (CET)	Member EAC (CET)	Member CEMAC (CET)
	Ag	Non Ag										
Angola	9,6	6,8	30	95	No	No			x			
Benin	14,3 (14,4)	11,6 (11,4)	20	100	No	No	x	x				
Botswana	9,3 (n.d.)	7,8 (n.d.)	96	91,4	Yes	Yes				x		
Burkina Faso	14,3 (14,9)	11,6 (11,3)	20	100	No	No	x	x				
Burundi	10,5 (n.d.)	13,1 (n.d.)	30	79,3	No	No			x			
Cameroon	22,1 (18,2)	17,4 (13,7)	30	43,5	No	No						x
Cape-Verde	11,7 (17)	10,2 (10,2)	50	85,3	Yes	Yes		x				
Central African Republic	22,1 (24,7)	17,4 (20,5)	30	43,5	No	No						x
Chad	22,1 (n.d.)	17,4 (n.d.)	30	43,5	No	No						x
Comoros	26,2	29,3	150	27	No	Yes			x			
Congo	22,6	17,7	30	41,4	No	No						x
Côte d'Ivoire	14,3 (n.d.)	11,6 (n.d.)	20	100	No	No	x					
Democratic Republic of the Congo	12,8 (n.d.)	11,9 (n.d.)	20	100	No	No			x			
Djibouti	21,7	29,1	33	64	No	No			x			
Equatorial Guinea	22,1		30	43,5	No	No						x
Eritrea	10	7,6	25	100	No	No			x			
Ethiopia	17,3	16,7	35	76,2	No	No			x			
Gabon	22,1 (20,4)	17,4 (15,8)	30	43,5								x
Ghana	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.		x				
Guinea Bissau	14,3		20	100	No	No	x	x				

Guinea	14,6 (n.d.)	11,5 (n.d.)	20	100	No	No		x				
Kenya	19 (20,3)	11,7 (5)	100	97,7	Yes	Yes			x			x
Lesotho	9 (n.d.)	7,8 (n.d.)	96	92.4	Yes	Yes				x		
Liberia	n.d.	n.d.						x				
Madagascar	14,7 (8,8)	13,1 (9,4)	20	100	Yes	No			x			
Malawi	14,7 (n.d.)	13,3 (n.d.)	25	100	Yes	No			x			
Mali	14,3 (n.d.)	11,6 (n.d.)	20	100	No	No	x	x				
Mauritania	12,4 (n.d.)	10,5 (n.d.)	20	100	Yes	No						
Mauritius	7,1 (4,6)	3 (1,7)	42	85,6	Yes	Yes			x			
Mozambique	16,4 (9,5)	11,4 (9)	25	100	No	No						
Namibia	9,2 (n.d.)	7,8 (n.d.)	87	91,7	Yes	Yes				x		
Niger	14,3 (n.d.)	11,6 (n.d.)	20	100	No	No	x	x				
Nigeria	15,6 (n.d.)	11,4 (n.d.)	50	96,2	No	Yes		x				
Rwanda	14,6 (n.d.)	19,4 (n.d.)	30	72.8	No	No			x			
Sao Tome and Principe	n.d.	n.d.										
Senegal	14,3 (11,6)	11,6 (8,2)	20	100	No	No	x	x				
Seychelles	n.d.	n.d.							x			
Sierra Leone	16,4 (n.d.)	13,1 (n.d.)	30	90,7	No	Yes?		x				
Somalia	n.d.	n.d.										
South Africa	9 (9,4)	7,9 (5,9)	77	92,4	Yes	Yes				x		
Sudan	30,6 (n.d.)	18,5 (n.d.)	40	43,1	Yes	No			x			
Swaziland	9,3 (n.d.)	7,8 (n.d.)	96	91.4	Yes	Yes			x	x		
Tanzania	19 (23,6)	11,7 (8,3)	100	97,7	Yes	Yes						x
The Gambia <sup>[1]</sup>	14,3 (n.d.)	n.d.	20	100	No	No	x	x				
Togo	14,3 (13,2)	11,6 (10)	20	100	No	No	x	x				
Uganda	19 (19,6)	11,7 (10,3)	100	89	Yes	Yes			x			x
Zambia	18,8 (16,3)	13,2 (10,2)	25	100	Yes	No			x			
Zimbabwe	n.d.	n.d.	n.d.	n.d.	n.d.	n.d.			x			
ECOWAS	n.r.	n.r.	20	100	No	No						
COMESA	n.r.	n.r.	25	100	Yes	No						
WAEMU			20	100	No	No						

Source:

OMC, CNUCED and ITC. 2007. "World Tariff Profiles"

Notes:

n.r.: not relevant

n.d.: no data

[1] Not in the Report

Data for Zambia are for 2005

Data description:

Products concerned are categories 1 to 97 from the Harmonized System (SH), only when available in national statistics at the 6-digits level in the SH 1996 or SH 2002.

Products are aggregated into groups according to the Multilateral Commercial Negotiations (MCN) system created during the Tokyo round and adapted to the HS during the Uruguay Round. These categories are listed in pages 25-26 of the World Tariff Profiles. Aggregation methods are described in pages 179-182, the estimation method for determining the ad valorem equivalents of non ad valorem tariffs are described in pages 186-192 and data sources are described in pages 199-206.