

# Trade Negotiations Insights

## From Doha to Cotonou

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### CAP Reform and ACP Preferences: What is at Stake for ACP Countries?

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The European Union (EU) Common Agricultural Policy (CAP) is often blamed for distortions in the world markets for agricultural products. Consequently, the CAP also impacts on the ACP countries as a large share of their exports consists of agricultural products. The CAP imposes a high, subsidised internal EU price for agricultural products.<sup>1</sup> As farm support by the CAP leads to overproduction, export subsidies are used to make EU agricultural products competitive on world markets. This practice leads to a decrease in world market prices and an increase in price volatility. At the same time the enforcement of the CAP results in a highly regulated agricultural trade regime that then prevents cheaper world-market-priced products from getting into the EU market.

With the Mid-Term Review (MTR) of the CAP that was presented in July 2002 the European Commission (EC) proposes to move on with the reform process that commenced in 1992, making explicit reference to the objective of sustainable development and the outcome of the World Summit for Sustainable Development held recently in Johannesburg, South Africa.

#### Current preferences for agricultural products

For most ACP countries the EU is the most important export market. In principle market access is free for ACP products under the Cotonou Agreement. However, for agricultural products that are subject to the CAP these preferences are restricted. However, 80 percent of mainly tropical agricultural exports from ACP countries enter the EU market without restrictions.

For products that fall under the CAP different restrictions are in place. For sugar, beef and bananas access is regulated through special protocols that are included as Annexes to the Cotonou Agreement. However, the Banana Protocol had to be changed in 2002 because of a lengthy dispute in the WTO. For sugar and beef, those ACP producers that benefit from the import quotas receive the internal price in the EU, which is up to four times the world market price.<sup>2</sup> Therefore a financial transfer of approximately 500 million euros per year is associated with these protocols. Currently 1.6 million tons of ACP sugar is exported to the EU worth 844 million euro in 2001. This amounts to 86 % of all sugar imports to the EU. However, as the quotas have not been changed since 1983 exports could not increase.

Sugar producers in ACP countries that are not members of the sugar protocol and are not subject to the recent Everything But Arms (EBA) initiative's provisions cannot export sugar to the EU at all. Furthermore, exports of refined sugar to the EU are disallowed.

For cotton, tobacco, flowers and exotic fruits, preferential access to the EU market is also granted to ACP producers but only during off-season or within quantitative limits. These products have a market share in extra-EU trade of between 20 and 45 %. ACP countries were able to increase their exports particularly of flowers and fruits partly because of the preferential treatment. However, these are the sectors that have been liberalized under the Uruguay Agreement on Agriculture (AoA) and already trade preferences for ACP countries are thereby significantly eroded.

#### Contents

CAP Reform and ACP Preferences: What is at Stake for ACP Countries?	1
Negotiations on trade in Services under the Cotonou agreement	3
The Compatibility of EPAs with WTO Rules: A moving Target?	6
Calendar and Resources	8

#### The CAP Reform and Mid Term Review

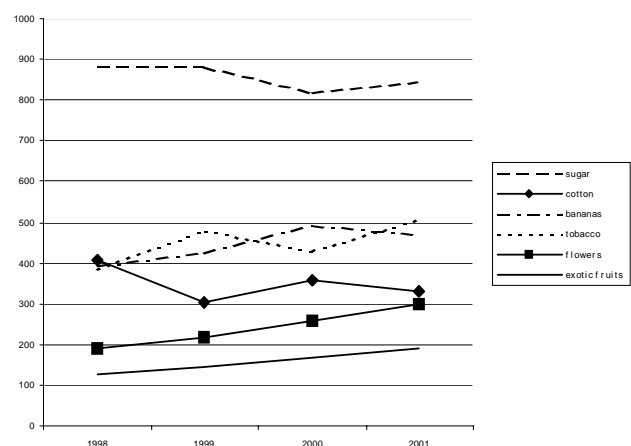
The reform of the CAP started in 1992 and was stepped up in 1999 with the Agenda 2000. In principle subsidies for European farmers should be decoupled from production and transformed into direct payments. One major reason for

this reform is for conformity with the disciplines in the WTO AoA. Therefore the EU had to transform its variable import levies into tariffs and reduce them by 36 % on average over a 6-year period.

*Continued on page 2*

#### Main ACP Exports of CAP Products to the EU

Million Euro (current)



Source: Eurostat, own calculations.

Internal support has to be reduced by 20 percent where it is regarded as trade distorting (amber box).

The reforms that are proposed in the MTR are intended to reduce the internal price of EU agricultural products, without undermining farm incomes. Through the reduction of the gap between internal EU prices and world market prices and increased flexibility of EU producers, agricultural production in the EU should become more competitive. Through a less intensive production and set-aside, environmental degradation in the EU should be reduced and production decreased. This should also reduce surpluses and therefore the need for export subsidies. However, even if farm subsidies are completely decoupled from production the fixed costs of farmers are reduced and therefore they can export their products below average production costs. Ultimately, all agricultural products should be treated equally and only a safety net with low intervention prices should be in operation with no incentives for production and no price distortions. However, the CAP does not only influence the competitiveness of EU products but also by other factors such as the exchange rate for the euro. For example in 2001/02 the unexpected weakness of the euro against the US dollar has reduced export refund payments significantly.

The foreseen simplification will transform payments into one single direct income transfer to farmers, independent of the production of specific crops. One major advantage is that these transfers will then qualify as green box measures, which are allowed under the WTO without restrictions. Before, many of the EU transfers fell into the blue box category that might be abolished or reformed in the Doha round. Together with the cross-compliance that binds subsidies to non-trade-concerns such as environmental, animal health and food quality standards and the dynamic modulation that will reduce direct payments, this will allow the EU to continue with its support for farmers. It should be noted that the direct payments per farm will be limited according to the Commission proposal. So far the biggest farms have received most of the funds.

Reforms in the cereals sector are most advanced. In 2000/01 and 2001/02 intervention prices were cut by 15 percent in two equal steps. Compensation for producers will be approximately 50 percent in the form of direct payments. In the MTR the Commission proposes a final 5 % cut in the intervention price of cereals, the abolition of the monthly increments for the cereals sector and the adjustment of the Community border system in accordance with the international rights and obligations of the EU. So far the reforms in the cereals sector have led to an increase in production by 18 percent, although on average EU cereal prices declined by 45 percent between 1992 and 2000. Because of increases in productivity and development on world markets, no further increase in world market prices of cereals is expected. However, the increased production in the EU could lead to more exports towards ACP countries, thereby lowering demand for local production.

The Agenda 2000 reforms extended the trend towards direct aid for farmers to the beef and dairy sectors. It is difficult to assess the reforms because of the crisis in the beef sector after the BSE [I am not sure what this stands for] and foot and mouth disease. After the crises, prices and production in the EU increased, but it is expected that production will be less intensive in this sector therefore increasing import demand. However, the producers in Southern Africa that are benefiting from the beef protocol via special quotas might suffer some revenue losses because of lower EU prices.

On the other hand, the beef and dairy sector is one of those in which ACP producers have suffered most from subsidised exports of EU overproduction. For example, the Tanzanian "Tanga Dairy Development Program" supported by the Dutch Development Cooperation was seriously affected by competition from low-priced powdered milk products from the EU. Therefore, a reduction in overproduction in the EU through less intensive production will benefit most ACP countries. In the MTR it is proposed to include reforms in

the rice sector by decreasing the rice intervention price to world market levels and also compensate producers with direct aid. Although the EU produces less rice than it consumes, stocks have been increasing. This is due to the low quality of EU rice for which no demand exists within the EU. As a result of the reforms some ACP countries could be able to export rice to the EU.

The MTR increases the trend to make direct payments conditional upon cross-compliance to environmental, animal welfare and food quality criteria, which are dealt with in the WTO 'green box' under the heading of multi-functionality. After a number of scandals regarding food safety in Europe, consumers are more sensitive to these issues. For exporters from developing countries in general this could mean that they have to meet even higher sanitary and phytosanitary standards than before.

These standards prevent approximately 50 percent of potential exports of fish, meat, fruit and vegetables of low- and middle-income countries into the EU. The sugar, olive oil, cotton and fruits and vegetables sectors are so far not included in the reform process but are scheduled for reform possibly in connection with the Doha round. Overall, the trade preferences for ACP countries will be further eroded through the CAP Reform and MTR. More important, however, is the competition with subsidised EU producers in the ACP markets and in third markets. Only if subsidies are completely decoupled and ultimately reduced can ACP producers make use of their comparative advantage in the field of agriculture.

### **EBA increases speed of CAP reform**

Some ACP countries are not only granted preferential market access through the Cotonou Agreement but also through the 'Everything-but-Arms' (EBA) initiative, that grants free access for all products from least developed countries (LDCs). For ACP-LDCs access to the EU market for agricultural products has therefore been improved since March 2001. However, barriers will only be fully removed by 2006 for bananas and 2009 for sugar and rice. EBA has no time limitation. However, safeguard measures are introduced when massive increases in imports of products originating in the Least Developed Countries arise in relation to their usual levels of production and export capacity.<sup>3</sup> According to an UNCTAD/Commonwealth study, the main sectors where a significant increase in LDC exports is expected are sugar, rice, dairy products, fruits and vegetables and cereals. For the EU, however, the estimated welfare impact from granting additional preferences is negligible, except for the sugar sector where an extended transition period is applied. However, as the necessary support for the above-mentioned products is likely to increase as a result of EBA, it puts some pressure on the EU to speed up reforms of the CAP.

If the export of sugar will be duty free for all LDCs the main beneficiaries will be those ACP countries that have no or little quotas under the current sugar agreement. Therefore Malawi, Tanzania and Zambia will be the main beneficiaries of EBA. The increase in sugar imports to the EU will increase the need for storage and subsidies for re-exports, as sugar demand in the EU is not price elastic. This is likely to result in more pressure to include sugar into the CAP reform. Similar considerations are likely to apply for rice. Also, the recent appeals at the WTO made by Australia and Brazil against the EU trade regime on sugar increase that pressure.

### **Impact of CAP reform on EPA negotiations**

For the negotiations of Economic Partnership Agreements (EPAs) between the EU and the ACP states that started in September 2002, the CAP reform has important consequences. The reduction of the internal EU price reduces the value of the preferences for those countries that had preferential access, especially through the protocols. For these producers, it is essential to get timely and accurate information about intended changes of EU policies and their effect to

make the necessary adjustments. For processed agricultural products, access to the EU market should be improved further. So far, preferential access under the sugar and beef protocol is only granted for raw products. This has restricted the development of sugar refineries and other food processing activities in the ACP countries. These are the areas where the EU could prove that it is really “ready to open up its market further to ACP products” as Pascal Lamy promised at the opening of the EPA negotiations.

The ACP countries should also insist on receiving support for capacity building to meet EU processing standards. The reduction of direct payments to EU producers minimises the level of unfair competition between EU and ACP producers. Nevertheless, the ACP countries have to look carefully at the definition of dumping within the EPA agreements as direct payments can also enable EU producers to export below average costs.

Therefore, dumping cannot refer only to the internal EU price. For products that are especially sensitive to ACP countries, because they provide income for the poorest groups within the countries, an exemption from free trade should be sought. This is possible under the current WTO rules on Free Trade Areas as Article XXIV only calls for the abolition of barriers for substantially all products, which is interpreted by the EU as 90 % of the existing trade flows among the parties. It would also be helpful to introduce a ‘development box’ in the WTO AoA, giving developing-country governments the possibility to protect their small farmers from dumping in general.

Again, it can be seen how the overlapping of different negotiations complicates matters for the ACP countries. This does not only refer to negotiations where they are directly involved, as in the case of EPAs and the WTO. It is also difficult to prepare precise offers for liberalization of ACP markets in the EPA negotiations without knowing the speed and effects of the CAP reform. The next phase of individual EPA negotiations between the EU and regional groupings is scheduled for September 2003, whereas the CAP reform was postponed to 2006 at the Brussels Summit in October 2002 after strong resistance by France. Overall the effects of a further CAP reform are ambiguous. Price fluctuations on international markets could even increase. As long as direct payments are still only made to producers and not to land owners, the reduction of EU production will be limited, as only regions with low productivity will react. Therefore, it is essential for the ACP countries and developing countries in general to assess the likely effects of further CAP reforms in detail to give them time to adjust their own trade and support policies.

## ENDNOTES

<sup>1</sup> Among others this price is applied to products such as cereals, rice, oilseeds, milk and milk products, beef and veal, poultry meat and eggs, pig meat, sugar, fruit and vegetables, flowers and life plants, cotton, and tobacco.

<sup>2</sup> The countries that are included in the sugar protocol are Barbados, Belize, Congo, Cote d’Ivoire, Fiji, Guyana, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Christopher, St. Kitts, Suriname, Swaziland, Tanzania, Trinidad and Tobago, Uganda, and Zimbabwe.

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## The Compatibility of EPAs with WTO Rules: A moving target?

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For African, Caribbean and Pacific (ACP) countries, two sets of demanding international trade negotiations are in progress; the Doha Round, since November 2001, within the framework of the World Trade Organization (WTO) and the negotiations on Economic Partnership Agreements (EPAs), since September 2002, between the ACP countries on one hand, and the European Union (EU) on the other.

The ACP-EU negotiations are supposed to yield EPAs that would be development oriented free trade areas (FTAs). The EPAs are set to enter into force by 2008. They would cover trade in goods, agricultural products, fisheries and services, and would address tariff, non-tariff and technical barriers to trade. Other trade-related areas should also be covered, including by increased cooperation between the EU and ACP countries within the framework of EPAs. Such areas include competition, protection of intellectual property rights, standardization and certification, sanitary and phytosanitary (SPS) measures, trade and investment, trade and environment, trade and labour standards, consumer policy regulation and consumer health protection, food security and public procurement.

The challenge of both the Doha Round and EPA negotiations is to realise expectations concerning the relationship between international trade and sustainable development. That is, the agenda of both trade negotiations must foremost address the development concerns of developing countries in general, and the ACP in particular.

In determining their trade strategy, ACP countries must be fully aware of the interconnection between the EPA negotiations and the Doha Round, if they want to effectively pursue their development interests.

In this context, ACP countries are faced with three major types of problems. First, the new trade agreements, or EPAs, with the EU must be compatible with the WTO rules. The extent to which the WTO rules can evolve within the framework of the Doha Round will determine the framework conditions for EPAs. Second, the content of EPAs will also depend on the Development Agenda and the conclusions of the Doha Round. ACP countries have to ensure the economic coherence between multilateral agreements concluded under the WTO and the EPAs negotiated with the EU. Finally, WTO and EPA negotiations are taking place, in part at least, concomitantly. These negotiations will therefore have to be conducted in parallel, ensuring complementarity of actions (for example in terms of defining trade policies and capacity building strategies), as well as coordination of the respective agenda of the Doha Round and of the EPAs.

## The international context

To complicate the matters further, ACP countries do not only participate in negotiations with the EU and within the framework of the WTO, but also among themselves and with non-ACP partners. The trade policies of the ACP countries is also conditioned by various other initiatives, such as the Generalised Systems of Preferences (GSP) of developed countries, including, for the United States, the African Growth and Opportunity Act (AGOA), and the EU ‘Everything-But Arms’ (EBA) initiative. Such institutional frameworks for preferential trade are important, to the extent that they both are conditioned by WTO rules and determine the trade policy strategies of ACP countries, including in the WTO and EPA negotiations.

It is against this complex and multifaceted background that the Development Agenda of the Doha Round and EPA negotiations must be considered. To this end, ACP countries should determine the compatibility and coherence of the Cotonou trade proposals with those of the WTO, within the framework of their general development objectives.

### EPAs/ WTO rules compatibility: a moving target

A major condition for concluding EPAs, or any alternative trading arrangement, is that these must be fully compatible with the WTO rules. The current challenge for the ACP and the EU is to negotiate EPAs while the WTO member countries are redefining the 'rules of the game'. That is, the form and content of the possible EPAs will be influenced by the content and outcome of the new WTO Round. Therefore, the WTO-compatibility of EPAs is, at present, an ill-defined objective.

WTO-compatibility implies first of all that, unlike the last Lomé Convention and the current transitional phase of the Cotonou Agreement, the ACP countries and the EU will not have to seek a new WTO waiver for their new trade agreements by 2008.<sup>1</sup>

EPAs, as FTAs between ACP regions and the EU, must conform to Article XXIV of the GATT 1994 on regional trade agreements, or a revised version of it. The application of Article XXIV, however, raises problems concerning its interpretation, which remains ambiguous. In particular, paragraph 8 (b) stipulates that in an FTA customs duties and equivalent measures must be eliminated for 'substantially all the trade' among the FTA members. But the article does not clarify how trade must be measured, nor which proportion of trade must be liberalised between the parties (in terms of volume, tariff lines, percentage of trade flows, etc.).

By way of illustration, within the framework of the Trade and Development Cooperation Agreement (TDCA) between South Africa and the EU, signed in 1999, the FTA will include 90 percent of the products traded between the two partners. Moreover, the coverage of this agreement is asymmetric. The EU, being more developed, will liberalise 95 percent of its imports from South Africa, while the latter will only import 86 percent of the EU products without customs restrictions.

This, and other experiences, provides a better idea of the possible interpretation of Article XXIV. Adopting the EU interpretation, and assuming that the EU would open its market to about 98 – 100 percent of ACP exports, the ACP would have to open up its market to only 80-82 percent of current EU imports. However, the WTO has not yet formally endorsed this interpretation by the EU, nor any other for that matter, which therefore remains questionable.

Equally, paragraph 5 (c) of Article XXIV provides for a possible period of transition to liberalise substantially all the trade among the parties. This 'reasonable length of time' in the establishment of an FTA should not exceed 10 years, but 'a longer period' may be authorised 'only in exceptional cases'. Once again, in the framework of the FTA between South Africa and the EU, the transitional period provided for is 12 years. This constitutes a precedent, but does not give any legal guarantees in respect of the compliance of these provisions with the WTO rules.

### Revising WTO rules

There is therefore a need to clarify these regulations within the framework of the Doha Round. The Doha Ministerial Declaration provides for 'negotiations aimed at clarifying and improving disciplines and procedures under the existing WTO provisions

applying to regional trade agreements [...], tak[ing] into account development aspects of regional trade agreements'.<sup>2</sup> This provision reflects the concern of certain developing countries, and in particular ACP countries, which are eager to introduce more flexibility into rules related to regional trade agreements between developed countries and developing countries.<sup>3</sup>

Unlike in Article XXIV of the GATT, such flexibility for developing countries is explicitly mentioned in Article V (paragraph 3.a) of the General Agreement on Trade in Services (GATS) on agreements on economic integration in the service sector. GATS, however, does not characterise the flexibility available. As a consequence, while the special and differential treatment (SDT) for developing countries is recognised for regional agreements on services, its practical scope is less than obvious.

Another option would be to revise the 'Enabling Clause' which permits preferential regional trade agreements between developing countries that only lead to a reduction, and not the elimination, of customs duties and non-tariff measures on products. By extending the scope of the Enabling Clause to regional agreements between developed countries and developing countries, including in an asymmetric manner to allow a preferential treatment for the exclusive benefit of developing countries, the ACP countries could obtain the desired flexibility and SDT to conclude EPAs, not available under the more rigorous discipline of Article XXIV. However, this option is not very realistic, as it is most likely to arouse the opposition of several WTO members, including among developing countries.<sup>4</sup>

### The pros and cons of a revision of Article XXIV

The objective of most ACP countries is to be able to limit the degree of reciprocity resulting from EPAs. This reflects a quite understandable temptation on the part of the ACP: to increase as much as possible their preferential trade access to the European market, while limiting the opening of their own market to the EU products. In this regard, ACP countries will have an important role to play in the WTO negotiations on Article XXIV.

Besides the degree of asymmetry, longer transitional periods for the establishment of EPAs (up to 15 years as in the case of Mexico in NAFTA) could also be negotiated, if need be, within the framework of a revised Article XXIV. Specific provisions on safeguards for developing countries could also be included (as in the case of the EU-South Africa Trade and Development Cooperation Agreement or the Mediterranean Agreements).<sup>5</sup>

The issue, however, is to determine to which extent the ACP economies would really benefit from a revised Article XXIV. The initial objective of this article was to allow some flexibility in the case of regional agreements with regard to the underlying GATT principle of non-discrimination enshrined in the 'Most Favoured Nation' treatment (Article I of the GATT), while introducing some discipline in derogating to this general principle. With the proliferation of regional trade agreements, the interpretation of Article XXIV has been extended. But the superiority of regionalism over multilateralism remains very controversial. Proponents of the regional approach generally advocate open regional agreements, as a first stepping-stone towards trade liberalisation in the multilateral framework.

This approach is advocated in the Cotonou Agreement in the context of the EPAs (Articles 34.1&2 and 39.1), which calls for the progressive liberalisation of the ACP economies. To significantly weaken the principle of reciprocity would no seem consistent with the intent to create an FTA. In this case, alternative-trading arrangements should be found to maintain the preferential access of the ACP to the EU market (possibly in the form of an enhanced GSP).

A revision of Article XXIV would provide for a greater transparency rule and legal certainty in the rule if it were about codifying the (current) interpretation of this article and preventing uncontrolled drifting, thereby reducing risks of dispute. But it could promote protectionist tendencies, including among developing countries, if it led to making superfluous substantive reciprocity in regional trade agreements between countries that are at different levels of development.

Besides, were a revision of Article XXIV introducing more flexibility desirable, it would most certainly be met with strong resistance from other WTO members which would prefer a more restrictive interpretation of the Article. Under these circumstances, ACP countries would be well advised to seek sufficiently strong alliances with the other WTO members to ensure that no revision would be made to the detriment of their interests.

More generally, the issue that is implicitly raised is the scope and relevance of special and differential treatment for developing countries in the WTO system, in for the ACP in EPAs. An examination of all SDT-related provisions is provided for within the framework of the Doha Round (paragraph 44 of the Ministerial Declaration), the objective being to determine to what extent they should or could be strengthened, be made more precise, more effective and more operational. The outcome of this examination will determine the specific regulatory measures that can be taken for the benefit of the ACP countries within the framework of EPAs.

### Coherence of subjects between the WTO and EPAs

Besides the legal aspects, which will have a significant bearing on the determination of the institutional framework and the format of EPAs, the WTO negotiations will also have a direct impact on the contents of EPA. The Cotonou Partnership Agreement provides for the negotiation of new trade agreements that should clearly benefit ACP countries, to strengthen their development, to integrate them into the world economy and to contribute to alleviate poverty.

The Doha Development Round pursues similar objectives for developing countries: promotion of sustainable economic development, poverty reduction and increased participation of developing countries in an open multilateral trade system.

Hence, in principle, EPAs negotiations and the Doha Round are but two different ways of pursuing the same objective: sustainable development. ACP countries should, therefore, adopt a coherent strategy in the development of their trade policies, by choosing the most appropriate forum for negotiating each issue or by making use of the complementarity between Doha and Cotonou.

On market access and other subjects such as trade-related issues, the scope of and potential benefits from EPAs will depend on the outcome of the Doha Round. Multilateral liberalisation reduces the margins of preferences in other trade agreements. Therefore, it also reduces the impact of opening up markets on a preferential basis. EPAs could hence offer the opportunity of pursuing issues not adequately addressed in the Doha Round (a WTO-plus agreement).

Examples could include greater access for ACP exports to the EU market or better provisions for SDT and support measures in the context of EPAs. To this end, the ACP should identify trade-related issues which could be covered by EPAs and which would be influenced by the WTO negotiations, and in which way. Other major issues include agriculture and services.<sup>6</sup> Synergies and potential conflicts between the Doha Round and the economic partnership agreement negotiations should be identified.

### Timing of the negotiations

As Doha and EPA negotiations take place in parallel and are intertwined for the ACP, an appropriate timing for the ACP-EU negotiations is crucial. The Doha Round, which began in November 2001, has a tight schedule, with the important milestone of the Fifth WTO Ministerial Conference in September 2003 in Cancun, Mexico. The Round is due to end on 1 January 2005 with the conclusion of a single undertaking. However, in view of the experience of the previous rounds of multilateral negotiations, the scope and variety of areas covered, the slow progress of the current phase of the negotiations and the slippage of deadlines already encountered, it is most likely that the 2005 deadline will not be respected.

As for the schedule of the EPA negotiations, it will partially depend on the Doha Round. Negotiations between ACP countries and the EU formally began on 27 September 2002. In the first phase, negotiations are aimed at establishing the guiding principles, the structure and the modalities for the negotiation of EPAs. Negotiations should also address crosscutting issues of common interest to all ACP countries. In practice, this first phase should mainly provide time for the ACP to further their preparation for the more substantial second phase of negotiation on specific regional EPAs, due to start in September 2003.

While the outcome of the WTO negotiations will ultimately influence the precise content of EPAs, the ACP and the EU cannot afford to wait for the conclusion of the Doha Round if they seriously intend to negotiate EPAs, expected to enter into force by 2008. Beyond general considerations for the timing of EPA negotiations, taking into account the Doha Agenda, a more thorough analysis is necessary on each of these issues. Given the current schedule, and taking into account possible delays, common in multilateral rounds, it is likely that ACP countries will have to take decisions within the framework of EPA negotiations before the WTO negotiations are concluded.

This obviously creates undesirable uncertainty. Under these conditions, it is all the more crucial for the ACP to adopt, at national, regional and ACP Group level, a coherent strategy and positions which encompass negotiations both within the framework of WTO and of EPAs.

### Support measures and capacity building

Clearly, the close relationship that exists between EPA negotiations and WTO negotiations, the complementarity and interdependence of the subjects dealt with, the necessary coherence required between these two fora for negotiations which take place concomitantly, and their impact on regional and bilateral policies of the ACP countries, all these factors play a part in exercising additional pressure on the limited resources of the ACP countries concerning trade-related capacities.

However, if the intricacy of the areas of negotiations in the WTO and between ACP countries and EU adds to the complexity of the EPA agenda, the Doha Development Agenda also provides new opportunities concerning support measures and technical cooperation to reinforce the limited capacity of the ACP countries. These initiatives, in the WTO context, aim to help developing countries formulate, negotiate and implement trade policies compatible with the WTO rules and coherent with the objectives of poverty reduction and sustainable development.

These efforts can often be of direct benefit for the preparation, negotiation and implementation of trade policies within the framework of negotiated agreements with the EU. In addition, as EPAs are but one of the elements of the Cotonou Partnership Agreement, the EU is already committed to support capacity building and the sustainable development of the ACP economies.



To ensure maximal efficiency, this EU support must complement the support expected in the general framework of WTO. Increased coordination in this area is, therefore, essential, so as to ensure a greater coherence between the WTO and EU support programmes. Only in this way will new trade agreements, both between the ACP and the EU and at the WTO level, be effectively able to contribute to promoting the development of ACP countries, integrate them into the world economy and reduce poverty.

#### ENDNOTES

\* This article is adapted from a longer paper presented at the COMESA Workshop on EPA, 31 October-1 November 2002, Lusaka, Zambia.

<sup>1</sup> The main derogation is to Article I of GATT concerning the general treatment of the Most Favoured Nation. See the WTO Decision of 14 November, 2001 WT/MIN (01)/15. The second derogation valid up to 31 December 2005 is on the transitional regime of autonomous tariff quotas applied by the EU to banana imports. See WTO Decision of 14 November 2001 WTO/MIN(01)/16.

<sup>2</sup> WTO (2001), Ministerial Declaration of November 2001, WT/MIN(01)/DEC/1, paragraph 29.

<sup>3</sup> See Onguglo and Ito, 'Special and Differential Treatment in WTO Rules in the Context of the ACP/EU Economic Partnership Agreements', *Trade Negotiations Insights*, 1(2), June 2002.

<sup>4</sup> See for instance the proposal by Paraguay to WTO, TN/CTD/W/5.

<sup>5</sup> For some proposals, see Davenport, Michael, *Preliminary Analysis of Certain Issues for an ACP Position in the Post Cotonou Negotiations, in Particular WTO-Compatibility and the New EU GSP Scheme*, Commonwealth Secretariat Study, 2002.

## Negotiations on Trade in Services Under the Cotonou Agreement

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With the recent commencement of trade negotiations under the Cotonou Agreement between the African Caribbean and Pacific (ACP) states on the one hand, and the European Union (EU) on the other, the need for clear negotiating positions and objectives on the part of the ACP states could not be more acute. During the first phase covering the period September 2002- September 2003, the negotiations on economic partnership agreements (EPAs) are set to deal with objectives, principles and crosscutting issues of common interest for the ACP, as well as common mechanisms.

One of the most crucial preliminary activities of the negotiations is the impact assessment of trade liberalization with the European Commission. The impact assessments are supposed to be both economy-wide and industrial sector specific. If properly and conclusively handled, this exercise is crucial in determining the overall effects of liberalization on the ACP economies. And on this score, if well done and completed, the EPA negotiations would have begun on a better footing than the WTO negotiations on trade in services for instance. It should be borne in mind that both the ACP and the EU have their own processes with regard to the assessments. At the ACP level terms of reference for the conduct of assessments are being worked out presently. Such terms of reference will then be adopted, at the will of each ACP country, and depending on the specificities and circumstances of each individual country. The actual assessments are supposed to be conducted by each individual country, with either their own resources or with funding assistance from the e20 Million capacity building program fund.

In the WTO, the issue of assessment of services liberalization has been very divisive and has not been conducted to the satisfaction of developing countries. The assessments envisioned under the EPA negotiations will include the assessment of loss in government revenue arising from tariff reduction on import of EU products, and the financial and

other resources required to build capacity necessary to take advantage of new and additional market access opportunities in the EU under EPAs. Further, considering that EPAs will be negotiated in a regional context too, the exercise will do well to also take into account the results of regional impact assessments of EPAs. In addition there is a clear need for the regional impact assessment studies to be detailed and sector specific.

Trade in services has become increasingly important for developing countries in general and for many ACP countries in particular. Sectors like financial services, tourism, communication and transport are very central to the global economy, and any systemic changes or liberalization is bound to have far-reaching consequences. The services sector is the largest and fastest-growing sector of the world economy. It provides more than 60 per cent of global output and in many countries, an even larger share of employment. Whereas the ACP countries' participation in international trade in services is relatively low, the domestic services sector, particularly in Africa is large, contributing for instance, about 40 per cent to the gross domestic product (GDP) of Uganda and 50 per cent to that of Zambia.

In Kenya, South Africa and Zimbabwe, tourism is an important foreign exchange earner. Benin, Côte d'Ivoire and Tanzania get revenue from shipments from neighboring landlocked countries transiting through their ports, while Ghana and Mali receive remittances from their citizens working in service sectors abroad. Caribbean countries have expressed a deep interest in tourism services. Services liberalization is a complex and relatively new process. Its benefits to economies, especially weak economies such as the ACP countries, will need to be properly understood, and this can only be done by comprehensive and honest assessments of the consequences of such liberalization efforts. It should be remembered that for most developing countries, and ACP countries in particular, liberalization of the services sector, or invariably, privatization, by opening up to foreign companies, such as has been the case in the water and sanitation services sector across the African continent, is very much a 'natural' consequence of the opening up of trade in services.

Within the context of the EPA negotiations, the end object is to come up with a framework agreement on trade in services. This may be envisaged in particular for the Pacific ACP member countries. Whereas there has not been any debate amongst member countries, it is not clear whether this potential services agreement will be freestanding or it will be an annex to the Cotonou Agreement. The implications of a freestanding agreement will depend on its specific provisions. Presently, the negotiations are at ambassadorial level, and focus on broad general issues. It is not anticipated that any real substantive discussion, on services or any other specific topic, will take place in the first phase of the negotiations. At best, in the most optimistic scenario, negotiations could be on the principles and approach to be adopted for the service negotiations 'bottom up' approach, and perhaps a better coherence and coordination between the ACP-EU in the GATS negotiations.

### Provisions in the Cotonou Agreement

The overarching objective of the ACP-EU partnership is to negotiate an economically viable, socially acceptable and politically sustainable economic and trade cooperation agreement within the framework of the Cotonou Agreement. The objectives of this undertaking are well spelt out in Article 1 of the Cotonou Agreement. They include the reduction and eventual elimination of poverty "with the objectives of sustainable development and the gradual integration of the ACP countries into the world economy." Under Article 2, the fundamental principles spelt out include that of flexibility to take account of the level of development, needs and long-term development strategy of each individual country. Least developed countries are accorded special and differential treatment, and the vulnerabilities of land-locked and island-

states are taken account of. These elements are instructive as guiding lights in the opening up of the services sector. In particular, the proposals by some countries in opening up essential services such as water and sanitation, in the WTO GATS negotiations, has attracted a lot of debate within civil society groups and amongst negotiators. It is likely that any proposals along the same lines in the EPA negotiations will attract the same attention and the same concerns.

In the Cotonou Agreement, Articles 41 and 42 specifically target the trade in services sector, with Article 42 singling out Maritime transport for special mention and Article 24 covering tourism services. In Article 41.2 the parties "reaffirm their respective commitments under the General Agreement on Trade in Services (GATS), and underline the need for special and differential treatment to ACP suppliers of services".

This re-affirmation extends to the commitment for "progressively higher levels of liberalization of trade in services through successive rounds of" negotiations as spelt out in the preambular provisions to the GATS, a far-reaching and controversial understanding in its own right. ACP countries do not seem to have much of a choice in this regard, and most likely, will be faced with demands for liberalization under EPAs and under GATS periodically, and probably repeatedly, in the foreseeable future. ACP countries should bear in mind that in accordance with Article 41.1 of the Cotonou Agreement, the further liberalization foreseen should only take place if the negotiated provisions of an EPA are an unequivocal affirmation in that regard. Admittedly, there are flexibilities in Article XIX of GATS, and many developing countries agree that the GATS is probably one of the most friendly of the WTO agreements. However the realities, especially taking account of global power asymmetries would make an assumption that the flexibilities in Article XIX are all-accommodating, a rather naïve standpoint.

The Cotonou Agreement goes further to require the EU to accord sympathetic consideration to the ACP states' priorities for improvement in the EC schedule, as stated in Article XIX of GATS, with the view to meeting the specific interests of ACP states. This provision in effect, imports GATS Article XIX into the Cotonou Agreement. Of particular significance to ACP countries is the GATS provision that "The Process of Liberalization shall take place with due respect for national policy objectives and the level of development of individual country Members, both overall and individual sectors."

This is where the importance of the assessments comes in. ACP countries should be careful to utilize this provision to make sure their weak economic/developing economy status is taken account of, and more particularly, that the poor state of their services sector is recognized. The GATS Art.XIX section above goes further to demand that "There shall be appropriate flexibility for individual developing country Members for opening up fewer sectors, liberalizing fewer types of transactions, progressively extending market access in line with their development situation and, when making market access commitments to foreign service suppliers, attaching to such access conditions aimed at achieving the objectives referred to Article IV." This section offers considerable discretion to ACP countries in the negotiations under the GATS with obvious implications under the EPA negotiations. Under the GATS negotiations, some delegations have described it as the most developing-country friendly provision in the GATS.

In Article 41.4 of the Cotonou Agreement, the Parties further agree on the objective of extending under the economic partnership agreements, and after they have acquired some experience in applying the Most Favored Nation (MFN) treatment under GATS, their partnership to encompass the liberalization of services in accordance with the provisions of GATS and particularly those relating to the participation of developing countries in liberalization agreements.

Quite importantly, Article 41.5 provides that the European Union shall support the ACP States' efforts to strengthen their capacity in the supply of services, with particular attention being paid to services related to labor, business, distribution, finance, tourism, culture and construction and related engineering services with a view to enhancing their competitiveness and thereby increasing the value and the volume of their trade in goods and services.

### The Position of the European Union

According to the EC mandate, the scope of negotiations will cover "a progressive and reciprocal liberalization of trade in services aiming at assuring a comparable level of market access opportunities, consistent with the relevant WTO rules, in particular Article V of the GATS, taking into account the level of development of the ACP countries concerned." The parties will also endeavor to provide for a commitment not to take any new discriminatory measures from the day before the start of negotiations. The liberalization process will take place on an asymmetrical basis. The EC mandate states that ACP countries will be allowed a certain measure of flexibility depending on their level of development in overall terms as well as in terms of sector and sub-sector in accordance with GATS provisions, in particular those relating to developing countries' participation in the liberalization agreements. For the Community, the transition period will not exceed ten years.

For the ACP side, a transitional period compatible with the objectives of the Cotonou Agreement and WTO rules will be applied in a flexible way, to take into account specific constraints of the ACP countries concerned. ACP countries belonging to an EPA will undertake to apply at least the same arrangements between them as they apply to the Community. "The EPAs will reconfirm the commitments made under the terms of Article 42 of the Cotonou Agreement".

The negotiations will open early enough to be concluded by the end of the preparatory period (end of 2007), as laid down in Article 37(1) of the Cotonou Agreement. Where justified by particular economic, social and environmental constraints encountered by the ACP countries, the negotiations may be postponed. In such an event the parties will regularly assess the situation in the course of the EPA negotiations and will set the date for the start of the negotiations in this sector in 2006 at the latest. They will ensure that the preparatory phase to these

*Continued on page 8*

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## Calendar & Resources

negotiations is actively used to prepare for the negotiations, in particular by mobilizing appropriate support for the development of services in line with the provisions of the Cotonou Agreement.

### The Position of the ACP States

The objectives of ACP states with regard to trade in services is addressed in Section III of the *Draft ACP Guidelines for the Negotiations of Economic Partnership Agreements*. ACP countries aim to strengthen their capacity, efficiency and competitiveness in the supply of services of export interest to them, "in particular labor, business, distribution, financial, tourism, cultural and construction and related engineering services, air transport and communications, among others, with a view to increasing the value and the volume of their trade in goods and services." In addition, they aim to improve access to the EU of services originating in ACP countries, particularly in mode 4 relating to the movement of natural persons and to develop effective measures for implementation of GATS Article IV with a view to increasing ACP participation in world trade in services through, *inter alia*, access to technology; access to distribution channels and information networks; and the liberalization of market access in sectors and modes of supply of export interest to the ACP.

### Negative List or Positive List

In the WTO, negotiations on trade in services follow a special pattern so as to fully take into account the development needs of members. The EU's approach to service negotiations under EPAs should reflect this and be based on the "bottom up" or "positive list" approach that involves the respective parties indicating which sectors will be up for liberalization and to what extent liberalization will be pursued. If one read Article 42 of the Cotonou Agreement in *pari passu* with Article XIX.2 of GATS, the inevitable conclusion with regard to this issue would be that the positive list approach is both desirable and allowed. It is unlikely that any questions can be raised about this issue, not least by the European Commission, which has accepted the positive list in the WTO GATS negotiations. Further, in view of the sensitive public interest questions that a liberalization of certain services sectors is likely to raise in poor countries, the EU might be well advised to allow as much leeway to ACP countries as they wish. Unwelcome bilateral pressure is however foreseeable, particularly when the negotiations get to the second phase as substantive negotiations are unlikely to take place in the first phase.

### The Movement of Natural Persons

This mode of delivery of services is of particular importance to ACP states. There has been no exchange of views between the parties on how this could be done. And according to the ACP Secretariat, there is no negotiating position on the issue yet. Both parties should be careful not to let the EU's over-sensitiveness to the issue of immigration color the negotiations. ACP states should stress that the negotiations have nothing to do with persons seeking citizenship, permanent employment or permanent residence in Europe. "Movement of natural persons", as properly understood, refers to the entry and temporary stay of persons for the purpose of providing a service. It consists of persons of one Member temporarily entering the territory of another Member to supply a service for example accountants, doctors or teachers.

In conclusion, the Cotonou Agreement has established the overall framework for economic and trade cooperation between the ACP and the EU. The negotiated EPAs, and the outcome in each of the specific negotiated issues will have to be coherent with the overall objectives and principles of the Cotonou Agreement.

### WTO Events

2-3 Dec	Negotiating Group on Market Access
4-6 Dec	Trade Negotiations Committee
5-6 & 9 Dec	Council for Trade in Services
10 & 11 Dec	General Council
12 & 13 Dec	Textiles Monitoring Body
16, 17&18 Dec	Special Session of the Dispute Settlement Body
18 Dec	Working Group on Trade Debt and Finance
19 Dec	Dispute Settlement Body

All WTO meeting take place in Geneva. Please contact the Secretariat for confirmation of dates (also available at <http://www.ictsd.org/cal/>).

### ACP-EU Events

December: 1st Meeting of the ACP Ministers of Culture - Dakar, Senegal. Date to be announced.

9 December: Meeting of the Civil Society Follow-up Group - Brussels, Belgium.

9-11 December: 76th Session of the ACP Council of Ministers - Brussels, Belgium

November/December: Seminars of the National and Regional Authorising Officers at regional levels – Venues and dates to be determined

Contact ACP Secretariat, tel: (32 2) 743 06 00, fax: 735 55 73, e-mail: [info@acpsec.org](mailto:info@acpsec.org), Internet: <http://www.acpsec.org/>

### Other Events

14-19 December: US-AGOA Session, Mauritius

14-15 January 2003: A New Dawn for Africa - New Partnership for Africa's Development (NEPAD) with the German Federal Ministry for Economic Cooperation and Development, United Nations Economic Commission for Africa and the African Development Bank. (This event is mainly for Members of parliament from the NEPAD countries and the G8. Other participants will have to receive an invitation from the organizers), Bonn, Germany.

## Resources

**Commerce international et développement durable: voix africaines et plurielles.** Published by the International Centre for Trade and Sustainable Development, August 2002. To order a copy, please contact Alice Chardonnes, [achardonnes@ictsd.ch](mailto:achardonnes@ictsd.ch).

**Preliminary Analysis of Issues for an ACP Position in Post-Cotonou Negotiations, In Particular WTO Compatibility and the New EU GSP Scheme.** By Michael Davenport for the Commonwealth Secretariat, September 2002.

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