

## **Trade Preferences and Africa – The State of Play and the Issues at Stake**

[DRAFT – NOT TO BE QUOTED]

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November 2004

### **Summary**

This paper deals with the contemporary situation regarding trade preferences and their implications for African development. It critically reviews the evidence on the effectiveness of the four most important schemes for African development – the Generalised System of Preferences, the Cotonou Accords, the European Union’s Everything but Arms (EBA) agreement and the United States’s African Growth and Opportunity Act (AGOA). Although concerns have been expressed regarding particular problems deriving from their conceptualization and implementation, certain African countries and sectors have undoubtedly benefited from these schemes. Moreover, recent research shows that utilization rates are far higher than is commonly supposed. Special and differential treatment has been considered as fundamental to give African countries the ‘breathing space’ required to be able to compete on international markets. Nonetheless, this paper makes a number of suggestions to improve preference schemes. Two serious problems are the complexity of existing agreements and their discretionary nature. African countries would do well to call for the homogenization of the existing preference schemes offered by the Quad countries, with the objective of achieving the gradual phasing out of the current ‘patchwork quilt’ of preferences. Firm commitments, over long time-horizons, by the Quad countries would minimize the uncertainty that has so far undermined the potential impact of these agreements. In this sense, QUAD countries should endeavour to ‘take politics out of preferences’. Finally, we recommend that the rules of origin should be simplified by granting automatic cummulation within Africa – something that would give an incentive to regional integration within Africa.

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## **1. Introduction**

Following the Ministerial Conference of the WTO in Singapore in 1996, many developed countries and developing countries have expanded or introduced market access preferences for marginalized developing countries, especially the least developed countries. In 2001 the WTO registered a total of 28 market access initiatives in favour of least developed countries, 19 of which were granted by developing countries or transition economies, and nine that were granted by developed countries, including the Quad countries — Canada, the European Union, Japan and the United States (UNCTAD, 2004: 245). Because 33 of the LDCs are African, these initiatives have a particular relevance for African development.

In a period when budgetary restrictions have become tighter, and the amount of foreign aid to developing countries has been stagnant or declining, preferential market access agreements have become increasingly popular among the Quad countries as a tool for helping poorest developing countries. Their popularity stems from two basic characteristics of market access agreements. The first is that, in budgetary terms, no explicit item has to be included *ex-ante*. Rather, the cost is assumed *ex-post*, in terms of the loss of tariff income on imports (Freres and Mold, 2004). In a period of budgetary restraint, this advantage is an important one.

Secondly, against a backdrop of “aid fatigue”, it is now widely believed that developing countries can benefit more from opportunities to increase their exports than aid “hand-outs.” It is commonly implied market access agreements like the European Union’s “Everything But Arms” initiative which provided free market access to the European market for the 49 LDCs, have a potentially greater on poverty reduction than traditional aid programmes.<sup>1</sup>

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<sup>1</sup> Again, not all economists agree with this – Harry Johnson (1968) shows that a unit of foreign exchange earned by trade can never be equivalent to a unit of foreign exchange from – trade does not provide resources directly for investment, but only through saving on the excess cost of import-substitution. In contrast, aid not only provides resources directly but also indirectly through saving on the excess cost of import-substitution. For a discussion of this, see Thirlwall (2004).

This paper deals with the contemporary situation regarding trade preferences and their implications for African development. The objective of the paper is not to provide any exhaustive analysis of the impact of particular preference schemes or their efficacy as tools for development – in the author’s opinion, that has been carried out admirably elsewhere.<sup>2</sup> Rather, the paper is intended to highlight the main issues which need to be considered in a negotiating setting for African countries.

The study not only examines the effectiveness of the existing agreements, but also proposes several ways in which preference schemes may be improved so that they have a greater impact on the African economies in terms of structural diversification, investment, growth and poverty-reduction. The paper begins with a review of the empirical evidence on the effectiveness of preference agreements as a development tool. In Section 3, we describe in more detail the main schemes which affect African development - the GSP, the European Union’s Lome Agreement, their Everything but Arms (EBAs) initiative for the 49- LDCs, and the United State’s African Growth and Opportunity Act (AGOA). We point to a number of pitfalls and weaknesses in these agreements which need to be addressed if their potential as tools for reducing poverty and helping economic diversification is to be fulfilled.

## **2. The Theoretical Framework and Its Limitations**

It is commonly argued that trade preferences have failed to act as the catalyst for economic development and structural diversification to the extent that many had hoped for (Cline, 2003). Yet ask any one in the European Commission, or the US Office of the United States Trade Representative, about the value of continuing such preferences, and they will reply that it is the African countries themselves who request the continuation of these schemes. Although there are many complaints regarding operational aspects of the preference schemes (e.g. excessively strict rules of origin, or a highly discretionary application of the

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<sup>2</sup> See, among others, UNCTAD (2004:Chapter 6), Cline (2003), Achterbosch, van Tongeren and de Bruin

preferences), it is true that African countries value these schemes positively, and are very much opposed to see their elimination or scaling-down.

Trade preferences are thought to be valuable on two basic counts. Firstly, there has been a consensus among most economists that trade is beneficial both for economic growth and poverty reduction.<sup>3</sup> Because it is directly linked to productive activities, some economists value trade more highly than aid. The "trade, not aid" slogan was born at the first UN Conference on Trade and Development (UNCTAD), at Geneva in 1964, but the need for specific market access advantages for developing countries was not officially acknowledged until UNCTAD II, held in 1968. The Generalised System of Preferences (GSP) was subsequently introduced in 1971 through a waiver in the GATT, being given permanent legal status in 1979.

A second reason for the popularity of market preferences is that they embody perfectly the idea of "*Special and Differential Treatment*" for developing countries. Because market preferences do not entail reciprocity – that is to say, a corresponding reduction in tariffs or trade barriers on the part of developing countries themselves- they are seen by many developing countries as superior policy instruments. *Special and differential treatment* is valued by developing countries because of an appreciation that productive capacities in most developing countries are not sufficiently strong to enable competition on a level-playing field with firms in the industrialized countries. Although developing countries are increasingly being offered free trade deals with the industrialized countries, most developing countries are extremely skeptical about being able to compete on such a basis.

Despite the apparent popularity of preference schemes, an intense controversy has recently taken place amongst development economists as to their benefits/costs (e.g. Rose, 2003;

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(2003), and Bora, Cernat and Turrini (2002)

<sup>3</sup> However, against the backdrop of a poor poverty reduction performance which coincided with a decade or more of trade liberalization, that view has recently become more nuanced than before. Recent experiences of rapid export growth in countries such as Mexico, Tanzania or Madagascar suggest that an impressive performance on trade alone is not enough to guarantee either accelerated economic growth or poverty reduction. See UNCTAD (2004) and Mold and Roza (2004).

Ozden and Reinhardt, 2003). Most liberal economists continue to oppose preferences granted to poorer developing countries, on the grounds that it undermines the system of multilateral liberalisation. The World Bank (2000), for instance, has argued that "*nonreciprocal preferences like the GSP are a "Faustian bargain"*". The basic criticism is that the GSP is anti-trade and that, on balance, the system actually delays a poor country's efforts to liberalise. Under traditional static analysis, it is argued that trade diversion effects may be larger than the benefits from trade creation between the two bilateral partners involved in the preferential agreement, especially if the rules of origin are excessively strict. It is also argued that preferences may engender a deterioration in the quality of the trade between two countries, artificially shifting economic activity towards sectors where trade preferences exist, but out of line with the country's long-term comparative advantage. In addition, once benefits are lifted, or eroded by tariff reduction with competing countries, the costs of adjustment are inevitably high.<sup>4</sup>

As we shall see in a moment, taken in isolation, some of these propositions have empirical validity. However, from the African perspective, preferential agreements are fundamentally better for Africa than free trade agreements or unilateral liberalisation if there is agreement on one simple principle – that African countries are generally not sufficiently capacitated to trade on a "level-playing" field with the industrialised countries, and that some form of residual protectionism is required to protect domestic industries and agriculture. At the same time, African countries have become increasingly skeptical regarding the willingness of the industrialized countries to dismantle, or even reduce, their elaborate systems of agricultural support. In such circumstance, greater emphasis can be expected to be placed by African trade negotiators on preferential access. Enhanced market access through preferential agreements is also valued highly because of the way in which it can potentially

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<sup>4</sup> Bangladesh is commonly cited as an example of this. The EU provides preferential market access for Bangladesh's garment exports, exempting them from its 12.5 percent import tariff. At the beginning of the 1980s, garment exports were practically negligible. In the intervening twenty years, the industry has grown to contribute approximately \$4 billion a year to the balance of payments. However, with the imminent phasing out of the Multi-Fibre Arrangement (MFA) in 2005, Bangladesh's garment industry will face full-fledged competition from other low-cost producers like China, India or Turkey.

increase the rents from exporting to Quad country markets and encourage diversification into other sectors.<sup>5</sup>

In criticism of this view, it is sometimes argued that preferences might actually reduce the incentives to diversify. By increasing the potential income from traditional exports, in theory preferences could contribute to “locking in” developing countries into existing productive structures. The example of countries like Mauritius, which benefited enormously from both the sugar protocol and the MFA, shows that this is not at all inevitable, and suggests that countries can effectively use the additional income created by preferential schemes to help diversify the economic base of the economy. But it should be noted that this outcome is by no means inevitable.

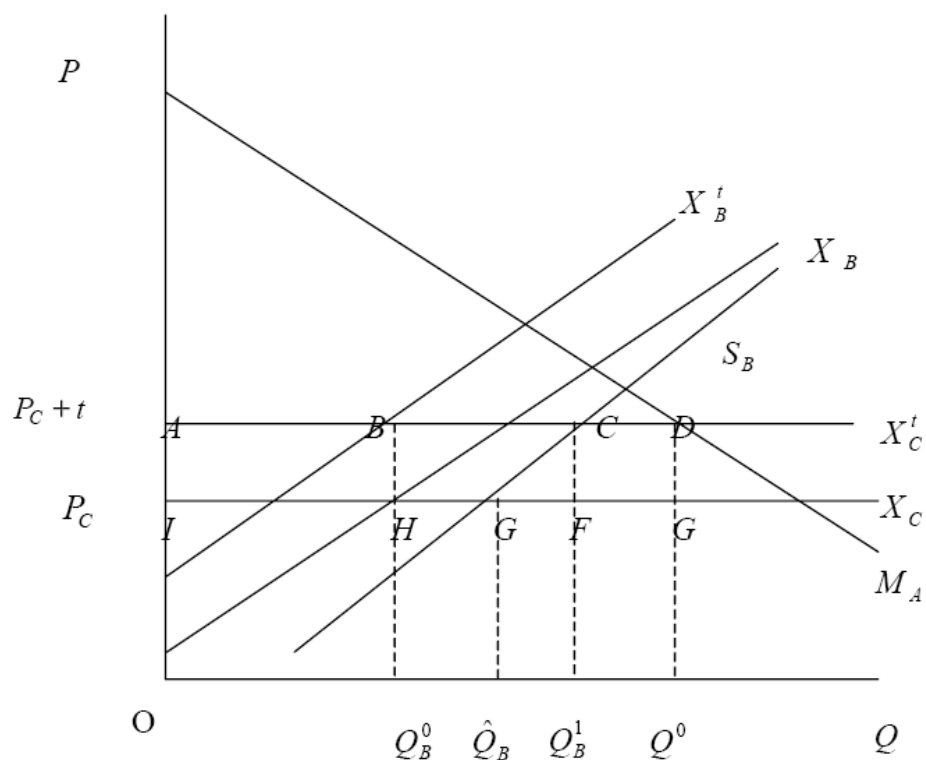
What does static partial equilibrium analysis tell us about the expected outcomes? Imagine a situation where we have a three regions – country A being the preference-granting country, country B being the preference-receiving country and country C being the rest of the world.<sup>6</sup> The good is assumed to be perfectly substitutable (a reasonable assumption for most commodities). Assume also that supply from the rest of the world is too large to be affected by changes in the import volumes in A (the case of a totally inelastic supply curve), again a realistic assumption for most commodities. Since the supply of the rest of the world is now perfectly horizontal, there would be no change in the import price in A after liberalization and no change in imported quantities. Necessarily, trade creation would be absent. The preferential agreement would instead cause a shift away from the rest of the world C and in favour of the partner country B. Supply from B will rise for two reasons: a direct terms of trade effect (due to better prices in the market of A) and a displacement effect (all production will be sold in A, with no sales in the domestic market of B). Hence the supply curve of B to A will not be anymore an export supply curve, but will correspond to the domestic supply curve of B -  $S_B$ .

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<sup>5</sup> Preferential schemes have the added advantage of allowing developing countries access to the higher internal prices of the protected agricultural markets. This has been key to explaining the success of countries like Mauritius in the sugar sector. More will be said on this later.

<sup>6</sup> This discussion is drawn from Bora et. al. (2003:35-40)

**Figure 1: Partial Equilibrium Analysis of Welfare Effects of Preferential Trade Agreement**



Source: Bora et. al (2002:40)

As for the welfare effects, trade creation for country A is nil. Moreover, since B is less efficient at producing the required imports, trade diversion would result. The shift towards less efficient suppliers will entail a loss in tariff revenue from A, represented by area ACFI. So the preference-giving country loses. As for B, there is an improvement in the terms of trade, as a result of larger output volume and increased producer rents, as represented by ACGI. Finally the effects on the rest of the world are nil, since C has a flat export supply curve. In aggregate, there is a net loss for the world as a whole, as represented by the triangle CFG. This corresponds to the loss in tariff revenue in A less the increase in producer surplus in B, and derives from the fact that a more efficient producer C has been displaced by a less efficient one B.



Summarising then, from the point of view of static welfare analysis, some of the benefits of the preferential agreements are captured by consumers in the preference-granting countries (through lower prices for particular commodities). But these gains are offset by losses through lost tariff revenue and the trade diversion effect. Effects for third countries are negligible, while preference-gaining countries only gain in so far as they are able to respond to the opportunity provided by the preference margin, and increase total exports to the preference-granting countries.

What this simple model does not tell us of course is what happens to the extra income generated for country B from the increased exports. Profits are simply assumed away in a competitive model like this. But, as suggested earlier, cases like Mauritius show how a country can use the rents gained from preferential market access in one sector (sugar) and use them to help diversify into another (textiles). Since independence, Mauritius has been granted a certain volume of exports of sugar to the EU. Moreover, these quotas have been at a guaranteed price which has been as much as three times the world price. On average, between 1977 and 2000, the guaranteed price was above the market price by about 90 percent. The resulting rents to Mauritius have amounted to a hefty 5.4 percent of GDP on average each year, and up to 13 percent in some years. Most of these rents accrued to producers, which contributed to the sizable levels of domestic savings and financed investment in the EPZ sector. Sugar barons bought substantial interests in the EPZ sector (Surbramanian and Roy, 2003:223). In effect, therefore, the preferential agreement in the sugar sector acted like a subsidy to domestic production of sugar, but was in fact a transfer from consumers in the importing country to producers (and taxpayers) in Mauritius.

Models cannot, unfortunately, predict what would happen to the additional rents accumulated in sectors receiving preferential access. Indeed, one characteristic of the CGE Models is that, because of assumptions made about substitutability and margins, preferential market access simply leads to greater specialization in commodities – not precisely the impact that policy makers are looking for. But this is a limitation of the model, and not necessarily an outcome in reality, as the Mauritian experience testifies.

### **3. Methodological Approaches to Evaluating Preference Schemes**

Before proceeding, it needs to be stressed that not all African exports to the Quad countries receive trade preferences – indeed, the majority do not. This is not because they are excluded from the preference agreement, but because the same items enter duty free from all potential suppliers across the board. Hence the preferences for Africa confer no commercial advantages (Stevens and Kennan, 2003:2). For instance, as Annex Table 3 shows, 74 percent of EU imports from Africa (by value) in 2002 were in items facing zero MFN duties. That means that preferences were applicable to only around 25 percent of African exports. This fact needs to be remembered in subsequent evaluations of the impact of preferences.<sup>7</sup>

In empirical research, there are several basic ways in which preferential schemes have been evaluated, each approach with its particular strengths and weaknesses:

- a. **Share in total imports of Preference receiving country(s).** A comparison is made between import share of preference-receiving country(s) in total preference-granting country(s) imports before and after the granting of preference. If the share has increased, it is inferred that preferences have had a positive impact on the export capacity of the preference-receiving country(s). Note that, logically, this conclusion does not necessarily follow – the increase in trade shares could simply be the result of trade diversion away from other export markets. Conversely, if the share has fallen, then it is assumed that the preferential agreement has been ineffective.
  
- b. **Analysis of Products Granted Large Preference Margins** The previous methodology presupposes that the preferential agreement has a global impact on export volumes. However, a more correct way to evaluate a preference agreement is

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<sup>7</sup> For instance, Cameroon and Cote d'Ivoire exported in 16.5 million and 5.5 million euros of bananas respectively under the MFN tariff in 2001. MFN tariff suspensions were used for sugar-cane molasses from Sudan and Senegal on exports worth 9.3 million and 2 million euros respectively (OECD, 2004:53).

to study the effectiveness of the scheme on a product-by-product basis: export products where the margin of preference is large would be expected to respond better to the incentive provided by the preference-giving country.

**c. Analysis of the utilization and utility rates of preference schemes.** The calculation of utilization and utility rates of different schemes has become standard practice in studies of the effectiveness of preferences. Utilization rates are defined as the value of imports receiving preferences divided by the value of the imports eligible for the preferences. Utility rates are the value of imports receiving preferences divided by total imports. Note that the two measures can vary substantially, depending upon the structure of the preferences on offer. The US GSP, for instance, scores very highly in terms of its utilization rate, whereas its utility rate is low, suggesting that the coverage of products is low (i.e. many exports are excluded from the scheme), but that the preferences that are on offer are fairly finely tuned to the existing export structure of preference-receiving countries (the converse is true of the EU system, where the coverage rate, as reflected by the utility rate is very high, but utilization is far lower – more will be said on this later). It should be stressed that this approach is limited to actual imports. The analysis would gain by being extended to the exports of developing countries eligible for preferential treatment that are not imported into the preference-granting country (on this point, see Stevens and Kennan, 2004).

**d. The Use of ‘Gravity’ Models** Econometric specifications using the gravity model approach have become popular in estimating the impact of preference agreements (e.g. Rose, 2002, Cline, 2004, Nielsson, 2002). Typically, gravity models of bilateral trade explain trade between countries as a function of the distance between them and their joint income. Although they have been generally successful in accounting for trade flows between countries, they have also been criticized for lacking a clear theoretical foundation. For analyzing the impact of preference market access, a dummy variable is added to account for membership of the

preferential scheme. If it is significant and positively signed, it is assumed that this reflects the positive impact of the scheme on trade volumes (i.e. bilateral trade volumes higher than would otherwise be expected).

- e. Analysis using CGE Simulation models.** Finally, the most popular way of all of evaluating the impact of preferential market access in recent years has been through general equilibrium simulation exercises (e.g. Ianchovichina, Mattoo and Olarreaga, 2003, Bora, Cernat and Turrini, 2002, Yu and Jensen, 2003). These models, the most popular of which is GTAP, permit simulations of policy changes to tariffs within a world setting. They are, however, limited by their basic assumptions regarding competition, substitution affects, returns to scale, and full employment (for critiques of these models, see Panagariya and Duttagupta, *no date*). The results are particularly sensitive to the extent to which products of alternative origin (produced in the importing country, the beneficiary country or a third country) can substitute for each other in trade. In CGE models such as those used by Bora et. al. (2002) and Iachovichina et. al. (2000), estimates of trade diversion pivot around Armington substitution elasticities and the sectoral composition of exports (Achterbosch et. al., 2003). More pointedly, the data sets are very poor for sub-Saharan Africa – only 7 SSA countries are currently included in the database. This means that the conclusions reached by these models must be treated very cautiously.

As can be appreciated, then, none of the techniques described above are devoid of limitations. Annex Table 1 summarises some of the most important recent studies using the methodologies of econometric analysis and the CGE models. In the following survey of the evidence for Africa, we will focus on the four schemes which have had most impact on African development – the GSP, the ACP, the EBA and AGOA. Studies and evidence using each of the aforementioned methodologies will be cited.

#### **4. The Empirical Evidence on the Effectiveness of the Preference Schemes**

##### **a) *The ‘Mother’ of all Preference Schemes – the GSP***

The idea of ‘positive discrimination’ in favour of imports of manufactured goods had its origin in the first UNCTAD conference in 1964 as part of a programme for creating a ‘new international economic order’. The scheme known as the Generalised System of Preferences came into effect in the European Community and Japan in 1971, Canada in 1974 and the United States in 1976. The US scheme excluded certain developing countries and certain so-called ‘sensitive products’. The EC scheme was more comprehensive in its coverage but put stricter limits on the amount of an individual product that could be imported under the scheme. All schemes applied strict ‘rules of origin’ which required that products be substantially produced within the beneficiary country to qualify (Grimwade, 1998:256).

At the outset, it needs stressing that the relevance of the GSP system for Africa is limited – for SSA, only South Africa has been a principal beneficiary from the scheme, and then only since the end of apartheid. Indeed, only 3.2 percent of African exports enter under the European GSP (OECD, 2004:53). However, because of its nature as the longest-lasting and most comprehensive preference scheme, and providing as it does the basis for most other preferential schemes (the EBA, for instance, is a sub-set of the GSP), the GSP deserves special attention.

The implementation of the GSP in practice tended to be relatively restrictive (Cline 2003:66). Moreover, as Page (1994:21-22) points out, one of the weaknesses of the GSP is that it has always been a purely concessionary scheme on the part of the industrial countries and is in no way contractual. This has inevitably caused uncertainty about the permanence of the concessions, something which has hardly encouraged long-term investments in beneficiary countries. Another of the principal criticisms has always been the degree of effective coverage of exports. In general terms, the products which receive preference

under the GSP are not necessarily those most favoured by the exporter, but rather those which are least likely to be disruptive to the importer's producers. Moreover, modifications to the GSP have often been made in an arbitrary way, undermining any apparent commitment towards developmental objectives. For instance, when in 1991 the United States trade representative determined unilaterally that India's intellectual property protection was "unreasonable", President George Bush senior suspended duty-free privileges under the GSP for \$60 million in trade from India in April 1992. Such blatant *realpolitik* does little to dispel critics' perceptions of the GSP as a (heavy-handed) tool of foreign policy rather than development.<sup>8</sup>

Certainly, in line with the broad sentiment of these criticisms, empirical studies make it clear that a disproportionate share of benefits appears to have accrued to a relatively small group of developing countries. One early study, by Langhammer and Sapir (1987) estimated that three countries – Taiwan, South Korea and Hong Kong – accounted for about two thirds of the trade effect of the GSP, taking imports to all OECD countries into account. Some ten developing countries shared 90 percent of the gain. Langhammer and Sapir put the trade effect at \$4.6 billion for 1985, or roughly 3.2 percent of MFN dutiable imports.

Data provided to ECA by the European Commission confirm that this picture is still broadly true (Table 1): in 2002, *the top ten beneficiaries of the GSP accounted for approximately 78 percent of all imports to the EU receiving preferential access*. China alone accounted for a third of the total benefits, and the top three beneficiaries received in excess of 50 percent of total preferences. The concentration of benefits on just a few countries can be interpreted in a number of ways. On the one hand, it could be argued this implies that EU GSP fails on one of the most important criteria for any tool for development – equity, with many developing countries being effectively marginalized from participating in the benefits. On the other, bearing in mind the fact that China, India and

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<sup>8</sup> See also Freres and Mold (2004).

Indonesia alone account for the vast majority of the world’s poor, it could be argued that such an outcome is ‘pro-poor’, providing benefits for the countries which are in most need of help.

**Table 1: Utilization of EU GSP, 2002**

	<b>Dutible imports</b> <b>(millions euros)</b>	<b>% Share of total</b>	<b>Elegible under GSP</b> <b>(millions euros)</b>	<b>% Share of total</b>	<b>Receiving preferential</b> <b>(millions euros)</b>	<b>% Share of total</b>	<b>Utility Rate</b>
China	56,740	34.4%	24,536	24.6%	17,646	33.4%	71.9%
India	9,564	5.8%	7,480	7.5%	6,129	11.6%	81.9%
Indonesia	6,538	4.0%	4,767	4.8%	3,009	5.7%	63.1%
Viet Nam	3,696	2.2%	3,673	3.7%	2,540	4.8%	69.2%
Brazil	5,284	3.2%	3,392	3.4%	2,530	4.8%	74.6%
Thailand	6,669	4.0%	3,607	3.6%	2,375	4.5%	65.8%
South Africa	5,107	3.1%	4,822	4.8%	2,249	4.3%	46.6%
Bangladesh	3,130	1.9%	3,117	3.1%	1,908	3.6%	61.2%
Pakistan	2,615	1.6%	1,729	1.7%	1,532	2.9%	88.6%
Argentina	1,871	1.1%	1,698	1.7%	1,333	2.5%	78.5%
<i>Total</i>	<i>165,055</i>	<i>61.3%</i>	<i>99,834</i>	<i>58.9%</i>	<i>52,867</i>	<i>78.0%</i>	<i>53.0%</i>

*Source: Calculated from data provided by the European Commission*

From an African perspective, however, neither argument is totally valid. Firstly, with the exception of South Africa, sub-Saharan countries benefit from other preferential access agreements – principally the Cotonou schemes – and so the standard GSP is not an issue for them. Secondly, it might still be contested whether countries like India and, especially, China need to receive benefits on such a large scale from preferential access: both countries have large, diversified economies, and have industries which are capable of competing on international markets, regardless of preferential treatment. Moreover, because of their immense size, both countries have the capacity to borrow on international markets in a way which is not open to small developing countries in Africa. In other words, both countries have at their disposition alternative methods of financing their pro-poor policies, something which is not true of poor African countries still dependent upon the export of one or two primary commodities. What about the other GSP schemes in operation? How do they compare to the EU scheme? Table 2 provides some extensive data on the usefulness of GSP

from each of the Quad countries (Canada, EU, Japan and USA) for the 49 LDCs, 33 of which are African countries.

**Table 2: Effectiveness of Preference Schemes for LDCs as Measured by the Import Coverage, the Utilization Rate and the Utility Rate, 1994-2001**

Country/ country group	Year	Total imports  (a)	Dutiable imports  (b)	Imports eligible for GSP preferences (c)	Imports receiving GSP preferences (d)	Imports covered by GSP scheme (c)/(b)	Utilization rate of GSP scheme (d)/(c) (%)	Utility rate of GSP scheme (d)/(a)
		(\$ million)						
Quad	1994	5 347.0	3 917.3	2 071.0	999.0	52.9	48.2	18.7
	1995	6 087.8	4 706.1	2 564.3	1 361.2	54.5	53.1	22.4
	1996	9 956.3	7 451.1	2 985.0	1 517.9	40.1	50.9	15.2
	1997	10 634.1	8 163.4	5 923.1	1 788.2	72.6	30.2	16.8
	1998	9 795.7	7 915.1	5 564.2	2 704.5	70.3	48.6	27.6
	1999	10 486.5	8 950.4	5 869.3	3 487.5	65.6	59.4	33.3
	2000	13 359.2	11 715.5	7 836.0	4 990.2	66.9	63.7	37.4
	2001	12 838.2	11 167.1	7 185.5	4 919.9	64.3	68.5	38.3
Canada	1994	..	..	..	..	..	...	..
	1995	175.9	41.3	6.4	4.1	15.5	64.1	2.3
	1996	336.9	34.5	6.3	2.9	18.3	46.0	0.9
	1997	205.3	47.3	8.6	4.7	18.2	54.7	2.3
	1998	256.0	92.1	9.8	5.8	10.6	59.2	2.3
	1999	154.6	60.7	8.2	4.9	13.5	59.8	3.2
	2000	180.1	75.9	9.9	7.2	13.0	72.7	4.0
	2001	243.2	94.6	11.4	8.0	12.1	70.2	3.3
EU	1994	2 471.2	1 823.4	1 791.7	748.1	98.3	41.8	30.3
	1995	2 814.6	2 277.8	2 246.3	1 077.6	98.6	48.0	38.3
	1996	3 219.0	2 580.3	2 520.1	1 196.8	97.7	47.5	37.2
	1997	3 614.8	2 926.3	2 888.8	770.8	98.7	26.7	21.3
	1998	3 519.4	2 932.1	2 908.0	761.8	99.2	26.2	21.6
	1999	3 562.2	3 100.9	3 075.2	1 035.0	99.2	33.7	29.1
	2000	4 247.1	3 671.7	3 633.6	1 499.5	99.0	41.3	35.3
	2001	4 372.4	3 958.1	3 935.7	1 847.4	99.4	46.9	42.3
Japan	1994	1 120.5	695.5	211.2	200.5	30.4	94.9	17.9
	1995	1 309.8	912.7	241.9	230.1	26.5	95.1	17.6
	1996	1 504.3	939.8	388.9	269.9	41.4	69.4	17.9
	1997	1 204.9	757.3	306.3	222.1	40.4	72.5	18.4
	1998	1 045.4	643.8	364.0	189.9	56.5	52.2	18.2
	1999	989.0	679.6	366.2	231.9	53.9	63.3	23.4
	2000	1 236.5	881.3	615.3	236.0	69.8	38.4	19.1
	2001	1 001.3	398.1	278.3	228.4	69.9	82.1	22.8
USA	1994	1 755.3	1 398.4	68.1	50.4	4.9	74.0	2.9
	1995	1 787.5	1 474.3	69.7	49.4	4.7	70.9	2.8
	1996	4 896.1	3 896.5	69.7	48.3	1.8	69.3	1.0
	1997	5 609.1	4 432.5	2 719.4	790.6	61.4	29.1	14.1
	1998	4 974.9	4 247.1	2 282.4	1 747.0	53.7	76.5	35.1
	1999	5 780.7	5 109.2	2 419.7	2 215.7	47.4	91.6	38.3
	2000	7 695.5	7 086.6	3 577.2	3 247.5	50.5	90.8	42.2
	2001	7 221.3	6 716.3	2 960.1	2 836.1	44.1	95.8	39.3

Source: UNCTAD, 2004:251



Table 2 shows that, in 2001 only 68.5 per cent of total imports from LDCs eligible to enter Quad markets at a preferential duty rate actually did so. The rest paid MFN duties. Although this might seem quite low, the utilization rate increased by 20 percentage points between 1994 and 2001. But this was mainly based on an increase in the utilization rate of the United States, which was driven by an increase in oil. If oil imports are excluded, the utilization rate in the United States drops from 95.8 per cent to 47 per cent in 2001.<sup>9</sup> According to UNCTAD (2004:250), the low utilization ratios are basically explained in the context of the

*“insignificant magnitude of the potential commercial benefits; the lack of technical knowledge, human resources and institutional capacity to take advantage of preferential agreements, which require in-depth knowledge of national tariff systems in various preference-giving countries, and conditions attached to the realization of the potential benefits of the preferences. The effective benefits of market access preferences provided by Quad countries are being significantly limited also by their unpredictability and by non-tariff barriers, notably rules of origin and product standards.”*

Recently, however, a number of authors have challenged these results on the low rate of utilization. Candau, Fontagne and Jean (2004) point out that many of the EU’s partners are eligible for different schemes, and thus it is difficult to identify in a particular case under which scheme an export is entering the EU market. In an extensive evaluation of the effectiveness of the different preferential schemes available, the OECD (2004) confirms this point of view – utilization rates are much higher than commonly thought when competing schemes are taken into account. These findings imply that the alleged underutilization of preferences, as reflected by utility and utilization rates, is somewhat of a statistical ‘red herring’, giving a misleading impression of the uptake of the preferences on offer. We will return to this point later.

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<sup>9</sup> The dramatic decline of almost 20 per cent in the utilization rate of the EU scheme between 1997 and 1998 may be imputed to the implementation of graduation policy since a number of beneficiaries have lost

Of course, the evaluation of preferences goes beyond simple analysis of utilization and utility rates. What about the econometric evidence of the effectiveness of the GSP? A recent paper by Ozden and Reinhardt (2003) provides econometric evidence using a data set of 154 countries from 1976 to 2000 that developing countries within the GSP tend to be systematically more protectionist than non-GSP countries. This is considered as negative from the point of view of global welfare, because consumers either end up paying higher prices for their imports, or consuming less.

**Table 3: Benchmark Results of Rose’s Regression Analysis, on data for 178 countries over the period 1948-1999**

	Default	No Industrial Countries	Post '70	With Country Effects
Both in GATT/WTO	-.04 (.05)	-.21 (.07)	-.08 (.07)	.15 (.05)
One in GATT/WTO	-.06 (.05)	-.20 (.06)	-.09 (.07)	.05 (.04)
GSP	.86 (.03)	.04 (.10)	.84 (.03)	.70 (.03)
Log Distance	-1.12 (.02)	-1.23 (.03)	-1.22 (.02)	-1.31 (.02)
Log product Real GDP	.92 (.01)	.96 (.02)	.95 (.01)	.16 (.05)
Log product Real GDP p/c	.32 (.01)	.20 (.02)	.32 (.02)	.54 (.05)
Regional FTA	1.20 (.11)	1.50 (.15)	1.10 (.12)	.94 (.13)
Currency Union	1.12 (.12)	1.00 (.15)	1.23 (.15)	1.19 (.12)
Common Language	.31 (.04)	.10 (.06)	.35 (.04)	.27 (.04)
Land Border	.53 (.11)	.72 (.12)	.69 (.12)	.28 (.11)
Number Landlocked	-.27 (.03)	-.28 (.05)	-.31 (.03)	-1.54 (.32)
Number Islands	.04 (.04)	-.14 (.06)	.03 (.04)	-.87 (.19)
Log product Land Area	-.10 (.01)	-.17 (.01)	-.10 (.01)	.38 (.03)
Common Colonizer	.58 (.07)	.73 (.07)	.52 (.07)	.60 (.06)
Currently Colonized	1.08 (.23)		1.12 (.41)	.72 (.26)
Ever Colony	1.16 (.12)	-.42 (.57)	1.28 (.12)	1.27 (.11)
Common Country	-.02 (1.08)		-.32 (1.04)	.31 (.58)
Observations	234,597	114,615	183,328	234,597
R <sup>2</sup>	.65	.47	.65	.70
RMSE	1.98	2.36	2.10	1.82

Regressand: log real trade.  
 OLS with year effects (intercepts not reported).  
 Robust standard errors (clustering by country-pairs) in parentheses.

*Source: Rose, 2002.*

beneficiary status following the implementation of the graduation policy of the EU-GSP scheme.

The orthodox view defended by Ozden and Reinhardt has been challenged by Rose (2002). Using a gravity model specification, Rose reaches the conclusion that membership of the WTO *per se* does not seem to have any positive impact on the volume of trade. In other words, his results suggest that it is the international system of reciprocal, multilateral liberalization is failing developing countries.<sup>10</sup> In contrast, according to Rose's econometric results, *the GSP approximately doubled the volume of trade between signing partners* (Table 3). This is of course exactly the opposite view to which orthodox economists would usually subscribe, and suggests that, far from being damaging, bilateral mechanisms of trade concessions might actually contribute to export growth and, by implication, poverty reduction.

Similar support for the effectiveness of the GSP is found in a study by Nielsson (2002) who, like Rose, uses a gravity model for data between 1973-92 between the OECD and developing countries. The dummies included for GSP and Lome membership are both significant. Nielsson estimates that the GSP raised developing countries' exports by 34 to 59 percent, and Lome by 45 to 69 percent. In cross-section, the impacts were estimated to be particularly large at the beginning of the period, but fell to near zero for 1980. According to the author, this was due to the NTBs and preference erosion. Since then, however, the impact of the preferences has recovered – presumably, this was because preference erosion was reduced by the process of tariffication (the converting of quotas into tariffs) which begun under the GATT. Although the orders of magnitude may be in doubt, studies like these provide strong support to the idea that preferential market access has indeed been more effective than is commonly assumed.

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<sup>10</sup> Of course, it could be argued that a dummy variable to reflect WTO/GATT membership is not the most appropriate way of measuring the impact of the multilateral system: particularly in Africa, in the 1980s and 90s many countries liberalised unilaterally, due to the conditionalities placed upon them under Structural Adjustment Programmes. This does not mean, however, that membership of the WTO does not exert a significant influence of trade policy.

**b) The ACP/Cotonou Agreements**

Since 1975, the African, Caribbean and Pacific Countries (ACP) have enjoyed the greatest preferential access to the EU market, compared with the rest of the EU's preferential trading partners. The agreements include all SSA countries, with the exception of South Africa. These agreements, originally called the Lome agreements, and since 2000, renamed the Cotonou Accords, are currently under revision. The EU has proposed that developing countries convert these preferential arrangements into free trade agreements, the Economic Partnership Agreements. Ostensibly, the EU argued that this is to make the agreements WTO-compatible. In fact, most analysts agree that it reflects a general disillusion with the meager results of the preferential agreements, as well as the desire on the part of the EU to promote their own trading interests more energetically.

**Table 4: Share of ACP countries in EU Imports**

	1980	1990	2000
Mlns Euro/ECU	21,721	20,986	28,551
Share of EU Total	7.7	4.7	2.7
Trade balance	-3,736	-3,579	-2,217

*Source: EU Commission*

Like the aforementioned studies into the value of the GSP, the evidence regarding the ACP agreements is often contradictory and difficult to interpret.<sup>11</sup> In 2000, the overall preferential margin enjoyed by the ACP on the basis of the present regime was about 2 percent in relation to the GSP, not precisely a huge margin. But the most disappointing stylized fact regarding the utility of the ACP agreements is that whereas between 1988-97 the ACP countries' total exports to the EU grew by less than 4 percent in volume, those of other developing countries grew by some 75 percent (EU, 1999). As a result of these trends, the share of ACP countries in total EU imports has decreased from 7.7 percent of the total in 1980, to only 2.7 percent in 2000 (Table 4).

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<sup>11</sup> We draw here on an official EU report CE/TFN/GCEC3/09-EN ACP/61/002/99 – “An Analysis of Trends in the Lome IV Trade Regime and the Consequences of Retaining it”

However, it would be too simple from this data to conclude that the ACP has not been effective for ACP countries. Clearly, the aggregate results are disappointing, with an apparent inability to maintain even existing market shares. But a better form of analysis would be to study the impact of the ACP on a product-by-product basis – African countries may have been over-proportionately locked into the production of primary commodities, with low and declining terms of trade, something which has little to do with the effectiveness of preferences. The correct way to evaluate the impact of preferences would thus be to analyse the specific cases of preferences on products where the margins may be large. In 1996, the proportion of ACP exports enjoying a preferential margin of over 3 percent was 29 percent. *These products revealed a much greater dynamism, growing in volume by some 62 percent in the period 1988-97.* Clearly, therefore, the effectiveness of the agreements is dependent to a large extent on the margin of preference in particular products. It is also evident from Annex Table 4 that *the vast majority (98 percent) of products from the African ACP countries enter the EU market duty-free.* The calculated utilization rates show that there is a wide variation between different countries in the usage of the Cotonou tariffs, with countries like Mozambique, Swaziland and Malawi benefiting significantly from Cotonou tariffs. Others (e.g. Angola, or the Democratic Republic of Congo) hardly benefit at all. But this is principally because the MFN tariff on the bulk of the exports from the latter group of countries (on average 75 percent) is simply zero. Thus it would seem that the effective usage of the schemes by African countries depends not so much on deficiencies in their operational characteristics, but rather on the structure of exports of the country in question. In the light of these figures, the idea that exports from these countries are not benefiting from preferential access is difficult to sustain.

Kennan and Stevens (1997) attempt to quantify the loss of preferences, if beneficiary countries had been transferred to the standard GSP after the termination of Lome IV in 2000. They show that there would have been widespread effects from any preference loss. Every single non-LDC ACP country would have been affected by loss of relative preference if it had been transferred from Lome to the GSP. *The countries with the largest*

*losses would be Cote d'Ivoire and Nigeria. But other non-LDCs would have been also seriously affected, such as Mauritius, Ghana, Senegal, Cameroon, and Kenya. In many cases, the deterioration would be in relation to non-traditional exports from ACP states. In most cases, the ACP's major competitors which would gain from the change are middle-income or rich states. Alarmingly, Kennan and Stevens estimate that the resulting transfer of revenue from the ACP export chain to the EU treasury (following the increase in tariffs) would be equivalent to a large proportion of aid received from the European Development Fund.*

**c)     *The EBA Initiative***

The European Union's "Everything but Arms" (EBA) initiative is a different kind of market access agreement to the ACP, in the sense that it opens up the EU market nominally to *all* products from participating countries. Beneficiaries of the special arrangements for least developed countries require formal recognition by the United Nations. At present, 50 developing countries belong to the category of LDCs, 35 of which are located in Africa. This is not a sufficiently recognized fact, but *in so far as sub-Saharan African countries have been calling for duty-free access to the European market, many have already achieved their aim.* Of course, this has repercussions for the seven SSA countries which are not LDCs, and have thus been left outside the list of beneficiaries of EBA (South Africa, Kenya, Botswana, Zimbabwe, Namibia, Nigeria, Cote D'Ivoire). It also, as we shall see, has some negative implications for regional integration within the African continent.

Roughly 2100 products already enter the EU market duty-free for all countries. Practically all other products are covered by EBA and are granted duty free access (zero duty rate) to the EU market if they fulfill the rules of origin requirements. Only Chapter 93 (arms and ammunition) of the EU's Combined Nomenclature is not covered by EBA. However, following a concerted campaign by European producers and traditional Caribbean exporters, who feared they would lose market share to LDC exporters, the proposal was modified to postpone the imports of fresh bananas, rice and sugar (Oxfam, 2002:101).

Duties on those products will be gradually reduced until duty free access will be granted for bananas in January 2006, for sugar in July 2009 and for rice in September 2009. In the meantime, there will be duty free tariff quotas for rice and sugar. These quotas will increase annually.<sup>12</sup> For products that do not fulfill the GSP's rules of origin requirements, the normal third country duty rates (MFN duty rates) apply or any preferential duty rate agreed by separate agreement by the country in question and the EU.<sup>13</sup>

With the introduction of the EBA, a number of examples of African countries which have benefited have begun to emerge. For example, Mozambique now has some (quota-limited) access to the EU over the eight-year transition period to 2009. This is expected to provide a new export market for several thousand tonnes of Mozambique's sugar per year, which is expected to create 8000 new jobs in the sugar mills and plantations. According to some evaluations, the jobs will benefit poor people living in rural areas where there are few alternative employment opportunities, and help to stimulate the wider rural economy (Hanlon, 2001, cited in Oxfam, 2002:102).<sup>14</sup>

However, as the Oxfam report points out, the benefits of unrestricted access would have been far greater. The exclusion of rice and sugar until 2009 in particular clearly limits the potential benefits from the EBA for LDCs. In production terms, rice and sugar are precisely the most important agricultural crops for LDCs (Table 5). According to Cernat, Laird, Monge-Roffarello and Turrini (2003:18), the expected increase in sugar exports is by far the most important to emerge at the end of the transition period, to such an extent that EBA could be better labelled '*nothing but sugar*'. Cernat et. al. (2003) use a computable general equilibrium model and partial equilibrium simulations to estimate the impact of the EBA,

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<sup>12</sup> The rules for opening and administration of the annual tariff quotas for rice (for the marketing years 2002/3 to 2008/09) and sugar (for the marketing years 2002/03 to 2005/06) are detailed in Commission regulations No 1401/20023 and No 1381/20024 respectively.

<sup>13</sup> European Commission, "EBA" - Everything But Arms initiative: User's guide to the EU GSP's Special Arrangements for Least Developed Countries <http://europa.eu.int/comm/trade/issues/global/gsp/eba/ug.htm>

<sup>14</sup> The Mozambican sugar industry is an interesting case because in 2001 the Mozambican government won an important battle with the IMF to retain import tariffs to protect its sugar interest from cheap subsidised

and come to the conclusion that Sub-Saharan Africa is the main beneficiary, but again, on a sectorial basis the gains are concentrated in the sectors of paddy rice, sugarcane, sugar and processed rice. The authors particularly cite the rise in sugar exports, which they estimate as rising as much as ten-fold, with large gains for Tanzania, Malawi, Uganda and Zambia.

**Table 5: Products supported by OECD countries and their Importance for LDCs, 1991-2000**

Rank	Average annual output of LDCs			
	In metric tons		In kilogram/capita	
<b>Top 10</b>				
1	Rice	61 155 943	Rice	102.7
2	Sugar	34 289 431	Sugar	60.8
3	Maize	15 628 671	Maize	26.1
4	Milk (cow)	10 267 425	Milk (cow)	17.1
5	Sorghum	9 844 374	Sorghum	16.5
6	Wheat	6 522 028	Wheat	10.9
7	Potatoes	5 637 666	Potatoes	9.4
8	Cotton	3 248 227	Cotton	5.4
9	Beans	3 134 699	Beans	5.2
10	Beef and veal	2 189 747	Beef and veal	4.3

*Source: UNCTAD (2004:226)*

Duty-free entry to the LDCs will undoubtedly accelerate reform of the EU's sugar protocol (Wolf, 2002). The main beneficiaries will be those ACP countries which have little or no quotas under the current sugar agreement. Thus the principal beneficiaries will be Malawi, Tanzania and Zambia. Milner, Morgan and Zgovu (2004) generally coincide with this evaluation, but stress that countries will be affected by the sugar reform in a very non-uniform manner. While some countries' transfer will fall, others may gain due to the impact that sugar reform has on world prices. These differences are due to the very uneven allocation of preferential quotas across protocol countries, and the highly differential dependence of the countries on EU and non-EU export markets. For African countries, they calculate that the main beneficiaries will be Congo, Cote D'Ivoire, Zambia and Zimbabwe, all countries less dependent on the EU market for their sugar exports. The principal loser of the reallocation of rents from the sugar protocol would be Mauritius.<sup>15</sup>

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imports. This was published as the first time that the IMF had openly conceded the legitimacy of a developing country government to protect a strategic sector in order to protect the interests of the poor.

<sup>15</sup> Stevens (2003) points out an important limitation to gains in the sugar sector – the monopoly position of the Tate and Lyle as an importer of raw sugar. Tate and Lyle is the only feasible purchaser of African exporters to the EU. Unlike the Sugar Protocol, by 2009 there will be no quantitative limits on the sugar that least developed African countries are able to export to the EU. But neither is there any built-in protection against



One of the most methodical reviews of the evidence on the impact of the EBA to date has been by Brenton (2003). By analysing and comparing trade data for the years 2000 and 2001, he shows that the changes introduced by the EBA in 2001 were relatively minor for the currently exported products, primarily because over 99 percent of EU imports from the LDCs are in products which the EU had already been liberalised and removed barriers. This opinion is also shared by Yu and Jensen (2004), who carry out a simulation exercise, using indicate that total welfare impacts of the EBA are less than US\$300 million for all the LDCs and that a great deal of these gains are associated with three "sensitive" products that are subject to gradual liberalization. From this point of view, then, the EBA alone is not expected to have a significant impact on the exports of African LDCs.

**Table 6: EU tariffs used by African countries\***

Regime Used	Import Eligible	Share of Regime	frequency Eligibles	share of frequency used
	GSP	%	*	%
MFN (tariff >0)	209 317	4.5	920	29.9
Cotonou (ACP)	4 289 623	93.1	1951	63.3
EBA (GSP)	54 581	1.2	106	3.4
GSP	54 010	1.2	100	3.2
OCT	196		4	0.1
Total	4 607 728	100	3081	100

*Source: OECD, 2004:53*

\* excluding South Africa and North African countries

Research by the OECD (2004:37) into utilization rates supports this view, and notes that most African countries have hardly ever used the scheme, with a utilization rate of less than 3 percent. This is either because the main export products of these countries are already duty-free, or because they are entering the European market under the Cotonou scheme. These figures show that operators make extensive use of preferences, especially Cotonou, since 93% of qualifying imports enter under the Cotonou scheme (Table 6). Why exporters should prefer one agreement over another is not altogether clear. EBA is in competition with Cotonou for around 86% of EBA-eligible imports. In 60% of EBA-eligible import

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the sole feasible large-scale importer (Tate and Lyle) playing off one supplier against another and driving the price received.

operations (products and countries), the LDCs' preferential margin in relation to Cotonou is low.<sup>16</sup>

So the choice of a scheme must be based on other factors. The requirements of compliance with rules of origin appear to be decisive, especially for processed products (OECD, 2004:40). The rules of origin for the EBA are certainly more restrictive than in the Cotonou agreement. Under the Cotonou agreement, with some exceptions, full cumulation within the ACP countries is allowed for. Thus products that undergo further processing in ACP countries, although the original goods may not have originated in the ACP region, are still eligible for duty-free access. This is not the case with the EBA agreement – since the EBA is an extension of the GSP, the concept of diagonal cumulation applies, meaning that although products can move within the EBA countries for further processing, sourcing outside the EBA, including with other ACP countries, is not an option for products to enter the EU duty-free (Kipe, 2003:5).<sup>17</sup>

The OECD (2004) attempt an interesting empirical investigation into the choice of the EBA scheme using a Probit econometric model (Table 7). The dependent variable takes a value of 1 if the EBA is used, and 0 if not. The independent variables used to express the choice of use of the EBA are: the preferential margin offered over MFN tariffs (*marge*) ; a discrete variable reflecting the size of the transaction (*size*), which takes 1 for all import flows under 20,000 euros (used to capture the influence of the transaction size on EBA utilization). Finally, the existence of a competing Cotonou scheme for a large number of Cotonou-eligible products is taken into account by a discrete variable (*cotonou*) which takes the value 1 if the product and country use Cotonou rather than GSP. Expressed formerly, then,

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<sup>16</sup> The margin turns negative for ACP banana quotas.

<sup>17</sup> There are three regional exceptions to this listed in the Official Journal of the European Communities, L 134/1, May 29, 2003. In the fishing industry, too, the EBA is more restrictive than the Cotonou Agreement. Under Cotonou, ships can be registered in the EU or in any ACP country, independent of which country the products are exported to, and the master and officers along with 50 percent of the crew must be nationals of ACP countries or the EU. Under the EBA, however, the ship must be registered to the EU or the direct beneficiary country, and the master and officers along with 75 percent of the crew must be from the beneficiary or the EU. Because many EBA are landlocked or too poor to have a significant merchant marine, EU ships are de facto required in order for the beneficiary country to export to the EU (Kipe, 2003:6).

the model analyses the probability that the event  $y_j = 1$  (utilisation of the preference) will occur conditionally on the influence of the exogenous variables:

$$\Pr_j(y_j = 1) = \Phi(\alpha.\text{marge}_j + \varepsilon.\text{size}_j + \eta.\text{cotonou} + \mu.\text{const})$$

The results show quite clearly that the preferential margin under EBA has a positive effect on the utilization of the scheme, whereas dual eligibility for both Cotonou and EBA appears to have a negative effect, confirming our earlier observations. Similarly, the low-value of imports seems to have a negative impact on EBA utilization.

**Table 7: Use of Everything But Arms Initiative**

Probit estimat : EBA utilization	
	1=Yes And 0 Otherwise
<b>EBA Used</b>	
<b>Preference margin</b>	5.82421** (.9719)
<b>Size</b>	-.2200088** (.1395)
<b>Cotonou impact</b>	-1.515552** (.1347)
Constant	-.0052216** (.1920)
Obs	1756
Pseudo-R2	0.33
Standard deviation in parenthesis	
Size : dummies for import <20 000 Euros	
** and * respectively significant at the 5% and 10% level	

Source: OECD, 2004: 41

What about the impact of the EBA on the EU itself? Does the measure justify the possible costs? Yu and Jensen find that the impacts of the EBA on the EU and third countries appear to be negative but quite small. This coincides with the conclusion of Mold (2003), who surveys the evidence regarding the potential impact of the EBA on the Spanish economy (one of the southern European economies with a relatively large agricultural base). He notes that LDC imports represent only 1.62 percent of total agricultural imports for Spain, and that the 'sensitive' products (rice, bananas, garlic, and beef) represent under one percent of total imports. Only sugar imports reached 1 percent of the total. Moreover, prior to the EBA, in 1999, Spain had a positive trade balance with these countries. Contrary to

the fears of agricultural lobbies, then, these facts suggest a fairly negligible impact on the Spanish agricultural sector.

In fact, the Spanish case is generalisable - although the EU as a whole is a net agricultural importer, *it is a large net exporter to the EBA countries* (Table 8).<sup>18</sup> From a strictly neoclassical point of view, this does not matter – trade is assumed to be generating static gains through a more efficient allocation of resources, and balance-of-payments problems are assumed away. However, for many African LDCs with serious balance-of-payments constraints, the fact that they are substantial net importers of European agricultural products should be a cause of concern. Whether the preferential market access under EBA is sufficient to help offset this constraint is debatable.

**Table 8: EU and US Net Exports with World and Countries receiving Preferential Treatment, Million euros, 2002**

	EU net Agricultural exports	US net Agricultural Exports
World	-924	12,730
GSP	-14,359	4,473
ACP	-4,749	-1,093
EBA	1,115	416

*Source: Kipe, 2003:3*

Some additional potential handicaps of the EBA agreement need to be borne in mind when assessing its effectiveness. While it is true that the preferences under EBA are given for an unlimited time period, if there are significant increases in imports relative to *usual* levels, temporary suspension of preferences is an option for the EU. Given their weak supply-side capacity, it is questionable whether this is much of an issue for African LDCs. However, it does again underline the uncertainty generated by unilateral preferences of this kind. The question to consider here is whether these safeguards go against African interests. Generally, in the past, safeguards on preferential access have been used against developing countries with considerable export capacities (like Brazil and India). To some extent, therefore, it could be argued that safeguard mechanisms prevent too much of the benefits of

these schemes being taken by the largest players, rather than militating against the interests of small African exporters. However, this has to be offset against the uncertainty that such safeguard mechanisms create.

All these points testify to the fact that, with preferential agreements, their potential effectiveness is contingent on the small print- as is so often the case, the devil is in the detail. Negotiators need to be aware of all the potential drawbacks, and make the appropriate comparisons with existing schemes. This is as true of the United States' African Growth and Opportunity Act as it is of the EU's EBA – although AGOA confers some additional advantages above and beyond the standard GSP, it has a number of limitations which contribute to undermine its developmental impact.

**d) *The African Growth and Opportunity Act***

This agreement was signed into law on May 18, 2000 as Title 1 of The Trade and Development Act of 2000. According to AGOA's webpage ([www.agoa.gov](http://www.agoa.gov)), "*the Act offers tangible incentives for African countries to continue their efforts to open their economies and build free markets.*" Once again, however, because most African countries already enjoyed preferential treatment due to their status as Least Developed Countries, for most products the preferences offered to African countries do not represent a significant improvement over the existing GSP agreements. There are exceptions to this, of course, and for some products, like textiles and apparel, where tariffs and quotas are higher, there are significant advantages in belonging to the scheme.

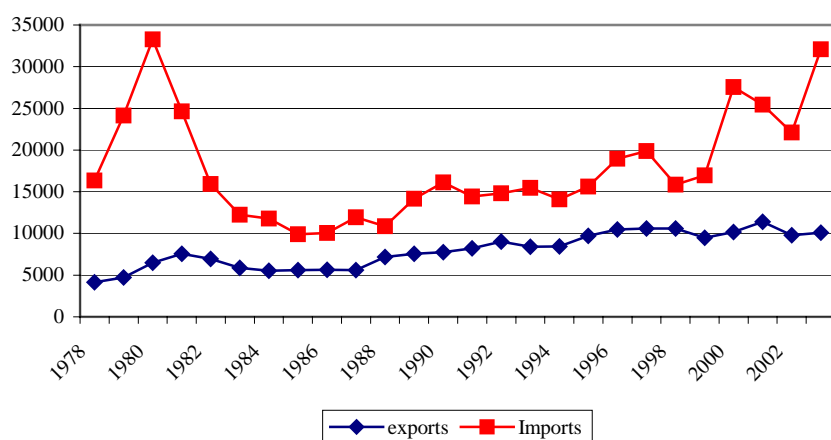
Circumstantial evidence certainly suggests that some African countries have benefited from the access agreement. For instance, South African exports under AGOA to the USA were

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<sup>18</sup> The primary exports from the EU to the LDCs are skim milk powder and wheat. Other main export products include cigars and cigarettes, beer, wine and ethanol, malt and poultry (Kipe, 2003:3).

45% higher in 2002 than in the preceding year.<sup>19</sup> Nigeria, too, has been a big winner in its trading relations with the US, accounting for more than 60% of all AGOA exports to the USA (though the bulk of this trade is related to the oil industry). There is also evidence to suggest that beneficiary countries have seen an increase in export-oriented FDI linked to AGOA. For example, companies from Taiwan Province of China are the main investors in Lesotho's garment industry (UNCTAD 2002:199).<sup>20</sup>

**Figure 2: US Exports and Imports from Sub-Saharan Africa, 1978-2003**



Source: [http://www.bea.gov/bea/international/bp\\_web/list.cfm?anon=75&registered=0](http://www.bea.gov/bea/international/bp_web/list.cfm?anon=75&registered=0)

Nonetheless, all this has to be set against the backdrop of a 16 percent fall of total US imports from sub-Saharan Africa in 2002 (Figure 2). Africa exports to the US subsequently surged in 2003 to over \$32.1 billion. However, oil exports were responsible for the bulk of this increase. Moreover, although the trend in exports to the US market is encouraging, it should be realized that African exports to the US market were higher still in 1980, at \$33.4 billion.

<sup>19</sup> "AGOA Gives Strong Boost to South African Exports to US", [www.allafrica.com](http://www.allafrica.com), 8/8/2003.

<sup>20</sup> As an example of the constraints of the AGOA, the textiles used are at present imported primarily from East Asia. However, after 2004, to benefit from preferential access under AGOA, the fabrics will have to be of United States or AGOA-beneficiary-country origin.

In the year following the announcement of AGOA, there was an apparent increase in a number of countries in the amount in export-oriented FDI (Box 1) by firms apparently wishing to take advantage of the enhanced market-access possibilities.

**Box 1: New Trade and Investment Initiatives in sub-Saharan Africa in response to AGOA**

- In Cape Verde, a fish-processing company was acquired by a United States company, and two new investments in the garment industry were announced by Portuguese companies.
- In Ghana, a United States company is investing in a tuna-processing plant
- In Malawi, AGOA has led to FDI in two garment factories (by a European company and a Taiwanese company) and the creation of at least 4,350 jobs. Total employment could increase eventually by 10,000, for a total of 20,000 workers
- In Mauritius, FDI worth \$78 million has already taken place. In the near future, there are prospects of Asian and European companies building cotton-yarn spinning mills. In addition , there are reports of substantial new orders from major United States retailers
- In Senegal, a leading Senegalese apparel and textiles company plans to enter into partnership with a United States textile manufacturer and a Malaysian firm to export to the United States with the potential creation of 1,000 jobs.
- In South Africa, the establishment of a new \$100 million clothing facility expected to employ 13,000 workers has been announced by a Malaysian company.
- In the United Republic of Tanzania, reports indicate the expansion of a textile mill in partnership with a United States firm involving 1,000 jobs.

*Source: UNCTAD, 2002b:54.*

Clearly, the creation of new jobs in labour intensive sectors such as textiles or food processing has a potentially strong impact on poverty reduction. In the first two years of operation, AGOA may have led to the creation of 200,000 jobs in the apparel industries alone (UNCTAD, 2003b:37). However, it is very difficult to gauge whether the type of investments identified in Table 2 would have been made in any case, regardless of the AGOA.

It is worth stressing that, in spite of the preferences granted by AGOA and GSP, the US imports very little from Africa. Only a handful of countries (South Africa foremost among them) have significant exports to the US. The African LDC trade flows are practically negligible, and exports under AGOA account for only 0.2 percent of US imports. The value of exports of agricultural and food products to the United States from all African countries (including North Africa) in 2002 was only \$1.12 billion. This figure included \$717 million of exports that are duty-free under the multilateral framework anyway (OECD, 2004:84).

Systematic research thus leads to a more somber conclusion about the impact of the AGOA. In the first place, the benefits are limited because only "non-sensitive" products are included in the agreement. Secondly, the regime expires in 2008, something which obviously tempers the reaction of potential investors. Thirdly, as in the other cases of market preference agreements that we have been analysing, there is concern that AGOA's benefits will be diluted as the US government seeks to negotiate free trade agreements with other regions such as the Middle East and Central America.

Finally, much concern has been expressed about rules of origin. Kenya stands to be excluded from the AGOA initiative owing to its continued dependence on imported raw materials to make textiles exported to the US under the act. In 2003, Kenya exports to the US reached 185 million US dollars, and this was expected to rise to 240 billion in 2004. But four years after the AGOA preferences became available, Kenya was still only producing 20,000 bales of cotton against the estimated 500,000 needed by the country's textile producers currently making apparels for export to the United States. As a result, and in contravention of the strict rules of origin of AGOA, manufacturers have imported raw materials from the Far East, Egypt and Sudan. The United States has subsequently threatened to suspend Kenya from AGOA.<sup>21</sup>

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<sup>21</sup> See 'Kenya to be Excluded from AGOA', by Samuel Maina, *Sub-Saharan Informer*, Friday, 20<sup>th</sup> August 2004, page 8. Maina also notes that the benefits to indigenous Kenyans have been minimal – besides the use of imported raw materials, traders making textiles do it in tax havens of the Export Processing Zones on the outskirts of Nairobi, and nearly all of them are of Chinese or Asian origin.



There are considerable controversies over the way the textiles and apparel sector has been included in the agreement. A recent paper by Additya Mattoo et. al. (2003) argues that the gains are very much limited by the rules of origin provisions - they require essentially that apparel be assembled in eligible sub-Saharan countries and that the yarn and fabric be made either in the United States or in African countries.<sup>22</sup> In addition, a number of customs requirements need to be satisfied. To receive the apparel and textile benefits of AGOA, the USTR-chaired inter-agency committee must determine, *inter alia*, that countries have an effective system and enforcement procedures to prevent unlawful transshipment and the use of counterfeit documents. According to the calculations of Additya Mattoo *et. al.*, the absence of these restrictions would have magnified the impact of AGOA nearly five-fold, resulting in an increase in non-oil exports of \$540 million, instead of the \$100-140 million increase expected in the presence of these restrictions.

In this context, it is interesting to note that almost half of South Africa's clothing exports to the USA do not receive AGOA preferences – not because of a failure by South African exporters to claim but because of a deliberate choice. Producers choose not to fulfil the rules of origin because they find it more profitable to use imported rather than domestically produced cloth/yarn and to forgo the tariff cut. As Stevens and Kennan (2003:2) point out, if the South African garment industry cannot use originating cloth and remain competitive, what hope is there for other African states?

One of the most exhaustive analyses of AGOA so far has been a UNCTAD commissioned report (UNCTAD, 2003). This study emphasizes once again that because the majority of the sub-Saharan countries are classified as LDCs and already enjoy duty-free access in a wide range of products due to their adhesion to the GSP, the additional benefits of the

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<sup>22</sup> An additional concession applies only to 28 poorer SSA countries (with a GNP per capita in 1998 under US\$1500). Unlike the richer group, these poorer countries can use cloth from anywhere. This of course increases considerably the value of the concessions. Unfortunately, this concession expires at the end of September 2004, and is unlikely to be renewed.

AGOA scheme are modest.<sup>23</sup> It is worth stressing that AGOA is not an all-comprehensive agreement - of a total of 12,750 tariff lines, 1,067 are not covered by the agreement, representing 8 percent of the total. Indeed, once energy products are eliminated from the analysis, AGOA's only significant benefits for African LDCs appear to be in the textile and apparel provisions.

Annex Table 4 shows the utilization rates of AGOA for individual African countries and reveals quite clearly the large dispersion in the usage which is made of AGOA or GSP tariffs. For countries like Ethiopia, a mere 9 percent of exports to the US enter under these schemes. For Uganda (a country often touted as one of the success stories in the usage of AGOA), a mere 4.3 percent of the country's exports qualifies for these schemes. However, other countries, such as Mozambique (90 percent), Swaziland (83 percent) and Lesotho (95 percent) are clearly benefiting from preferential access. In the same way that the vast majority of the GSP benefits are concentrated on a few countries, so too are the majority of benefits of AGOA gained by a few countries. According to Brenton and Izezuki (2004:3), seven of the beneficiaries account for 96 percent of the estimated transfer under AGOA in 2002, with the remaining 31 beneficiaries receiving very little.

But perhaps the most important criticism of AGOA is that the market access granted under the agreement is conceded with strings attached. African countries seeking eligibility under the AGOA face extensive conditions, such as opening their market to US trade and investment, and implementing market based reforms (Oxfam, 2002:102).<sup>24</sup> Given the significant external pressure under which they are already subject due to IMF, World Bank and donor conditionalities, this can only reduce further still the freedom of policy makers in the region to adopt their own economic strategies. Not only this, but each country's

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<sup>23</sup> Precisely because of this, the greatest benefits are likely to go to countries such as Cameroon, Gabon and Nigeria, which had previously been subject to duties on most of their exports to the United States and now enjoy virtually complete duty-free access to the US market.

<sup>24</sup> In fact, the way in which benefits from AGOA are tied to a better treatment of US investments and exports from the beneficiary country is potentially in conflict with WTO rules on MFN treatment.

eligibility must be reviewed annually, giving rise once more to uncertainty in the application of the preferences.

## **5. How Can Preference Schemes Be Improved to the Benefit of Africa?**

Summarising the evidence we have reviewed in the previous sections, then, it is clear that the record of preference schemes for African countries has been mixed. Nevertheless, we have found scant evidence in support of one of the most commonly voiced criticisms of preference schemes – namely, that they suffer from underutilization and therefore are not particularly useful or valued by African countries. The evidence cited here shows quite the contrary - individual preference schemes made are often apparently under-utilised because a competing scheme is preferred. If utilization rates have in fact been so high, this raises the question then of why the evidence on the developmental impact of preferences is so mixed? As explained earlier, one of the reasons is that the analysis of utilization rates is restricted to current, not potential, exports – *the fact that an export receives preferential access in itself reveals nothing about the ability of the schemes to encourage new exports*. In this context, from our review of the evidence for African countries, we would stress the following problems with existing schemes:

- a) **Rules of Origin** Even in cases where the size of the margin of preference remain large (because of tariff peaks or excluded products), it has often been difficult to take advantage of these market access opportunities due to problems associated with the *rules of origin*. Rules of origin oblige beneficiary countries to prove that a high percentage of the value-added has been created within national territory, thereby restricting sourcing from third countries. For small, structurally relatively un-diversified developing countries in Africa whose manufacturing sector is dependent in large measure on production inputs, this obviously limits the capacity to export.<sup>25</sup> Rules of origin and related

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<sup>25</sup> Data taken from EC document AIDCO/825/2002-EN.

administrative procedures have almost remained the same since the early 1970s, when preferential margins were significantly higher than at present. Some earlier studies conducted in developed countries quantified the cost needed to comply with administrative requirements related to origin as 3 per cent of the value of the goods concerned. Estevadeordal and Suominen (2003) estimate that the administrative costs of compliance correspond to a tax (i.e. a duty) of between 2% and 5.7%. In some sectors, this is enough to completely offset any advantages from the preferential access. Moreover, the total economic cost of applying strict rules of origin impeding the utilization of most competitive inputs is expected to be much higher in LDC beneficiaries. As a result, manufacturers and exporters may export under MFN conditions and forgo preferences (UNCTAD, 2003: xii). Excessively strict rules of origin has been a repeated criticism of market access agreements signed by the EU, which have ended up undermining the developmental potential of the said agreements (Brenton, 2003; Inama, 2003; Kipe, 2003). The same criticism has often been made of AGOA. Mattoo et. al. (2002) estimate that the benefits of AGOA for Africa would be about five times greater if exporting countries were not subject to the restrictive rules of origin imposed by the United States.

- b) **The Use of Non-Tariff Barriers** Non-tariff barriers represent a significant threat to maintaining the advantages from preferential access. Botswana, for instance, has built up an export industry of chilled a frozen boneless beef: its exports to the EU are substantial and probably would not occur in the absence of preferences (Latin America has a comparative advantage). But it is threatened by the loss of the foot and mouth disease status (Stevens and Kennan, 2003). There is little predictability in these issues: EU standards and import rules are often changed during the course of a few months. Salvador Namburete, Vice Minister of Industry and Commerce for Mozambique, called

the EU standards a “moving target”.<sup>26</sup> The much-vaunted Kenyan cut-flower export industry is, for instance, reportedly at risk from a change in regulation regarding the use of pesticides.

- c) **Lack of Permanence of Preferences** Because of continual changes in the conditions of entry under preferential regimes, there has been an underlying lack of faith in the permanence of the preference agreements. Entrepreneurs and policy makers in developing countries are understandably reticent to channel resources towards sectors where the competitive advantage rely on advantages which could prove ephemeral. This has been the case, for example, with the introduction of the system of “graduation” by the EU, whereby countries are excluded from the benefits of the preference agreement when exports in a particular sector reached a pre-determined level, or when the beneficiary country reaches a specified level of development.<sup>27</sup> Similarly, on five occasions, the US GSP has elapsed on five occasions without being immediately renewed (OECD, 2004:78).<sup>28</sup> It is hardly surprising, under such circumstances, that the supply-side response to preference schemes of most African countries has been disappointing. Neither foreign nor national investors would be willing to risk the sunk costs on the basis of ephemeral preferential market access. Regrettably, EU trade policy towards developing countries seems to be heading in the direction of greater, not less, discretionality. Pascal Lamy has recently announced new rules, to be applied from January 2006, which will open EU markets as a reward to developing countries that adopt progressive environmental and labour policies. Developing nations that wish to qualify must implement a list of 27 “*key international conventions on*

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<sup>26</sup> Cited by Kipe (2003: 4). The Minister recalled the story of a shrimp exporter who met all standards and import regulations when the ship left the port, but by the time the ship reached the EU the standards had changed and the cargo was not unloaded.

<sup>27</sup> The new generation of market access agreements, such as the EU’s EBA, in theory are all-encompassing and permanent and are thus intended to avoid this problem. Unfortunately, as we have seen, in practice fall far short of expectations.

<sup>28</sup> For example, GSP expired on 30 September 2001 and was not renewed for almost a year

*sustainable development and good governance*” by 2008.<sup>29</sup> Measures such as these can only increase the uncertainty and discretionality which continues to undermine the long-term impact of preferential market access agreements.

- d) **Complexity of Existing Systems** In their study of 179 products exported from Africa to the Quad countries, Stevens and Kennan (2003) noted that there were few examples of similar products being exported to more than one Quad market. According to the authors, this reflects the complexity of each Quad country’s scheme, and the independent promotion by each preference-giver of ‘their regime’ adds unnecessarily to the confusion. The evidence reviewed here coincides with that evaluation: while established exporters can work the system, many of the poorest African countries hardly benefit at all from preferences, due to the complexity and lack of knowledge of the different schemes.

In the face of these problems, a bold policy stance on the part of African countries would be a call to homogenize all existing preference schemes within the framework of the WTO, and the gradual phasing out of the current ‘patchwork quilt’ of preferences. This would remove the current discretionary and arbitrary application of rules and provide the much needed stability of preferences. Moreover, such an agreement would provide an important impetus to regional integration if rules of origin were made cumulative between all African states – outsourcing between manufacturing strongholds in the continent, such as South Africa, Ghana, or Kenya and neighbouring countries with more resource-intensive endowments would then become a real possibility. As a model for such an agreement, the EU’s EBA is clearly the most comprehensive scheme currently on offer. The deficiencies of the EBA identified this study would need to be addressed, but as a basis for negotiation with the other Quad countries, it would provide a good starting point.

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<sup>29</sup> “Brussels to reward ‘good’ poor countries” by Tobias Buck, *The Financial Times*, 21 October 2004, page 1.

This proposal is broadly supported by CGE modeling estimates. A simulation carried out by Ianchovichina, Mattoo and Olarreaga (2003) suggests that whereas as deepening of the AGOA to include all products would produce only a small increase in welfare for SSA, the gains would be much larger from the simultaneous liberalization of all the QUAD countries – a \$2.5 billion (14%) increase in non-oil exports and a \$1.8 billion (1.2%) increase in welfare for SSA. The decline in QUAD welfare, through trade diversion, was calculated to be insignificant (less than 0.01 percent) – in other words, a virtually costless initiative for the QUAD countries. In a similar vein, Bora, Cernat and Turrini (2002) estimate gains for 4 SSA countries and rest of SSA of \$392 million from the EBA initiative, but that they would rise to \$1320 million if the EBA were generalised to all Quad countries.<sup>30</sup> A more ambitious agenda with regard to market access agreements would clearly seem to be called for.

Another important reform in the current system would be a move towards a legally enforceable system of preferences. We have seen that one of the major problems of the current systems of preferences is the fact that they are unilateral, highly discretionary policy instruments. Developing countries have no way of seeking legal redress if the rules of applying the system are not followed. A recent example is the ‘graduation’ of the Central American country Costa Rica from the GSP+ preferences of the EU. Graduation occurred because just one of the products in a sector (pineapples) has exceeded the 25% limit of total EU-imports. The EU’s own regulations do not make it clear whether graduation occurs when just one product in the sector surpasses the pre-established limit, or whether all the products in the sector have to exceed the said limit. Moreover, there are a number of technical discrepancies about the application of graduation.<sup>31</sup> Cases like this suggest that a legally-enforceable set of preferences is not only desirably, but required. Again, this would probably entail the intervention of the WTO. If the QUAD countries offering these schemes

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<sup>30</sup> The gains are focussed on paddy and processed rice, cereals and sugar – the ‘downside’ of their results is that textiles and manufacturers actually contract. As mentioned earlier, however, these results are usually inevitable from the kind of assumptions underlying CGE modelling, and do not take into account how the additional rents generated from enhanced market access are actually used.

<sup>31</sup> For a fuller discussion of this case, see Freres and Mold (2004).

are convinced of their virtues, they should be prepared to submit preferential systems to a system of legal redress.

## **6. Preference Erosion – What can be done?**

One final question which needs to be dealt with regarding the effectiveness of preferential agreements for Africa is the issue of preference erosion. The conventional wisdom is that during and after the Uruguay Round the value of trade preferences to developing countries was decreasing because of the erosion of the preferential margins as a result of MFN tariff reductions and the lack of legal stability of GDP rates. However, after the Uruguay Round, in most cases the erosion of preferential margins has been rather limited, since major tariff liberalisation only took place in sectors of interest to developed countries. Furthermore, the tariffication process brought into being by the *Agreement on Agriculture* created additional room for preferences where traditional and new tariff peaks still exist in the post-Uruguay Round (Inama, 2003:ix).

As Table 9 shows, overall protection in agriculture among the Quad countries does indeed continue to be very high, especially if subsidies are taken into account. Moreover, tariff peak products (such as bovine meat products, dairy products, processed rice, sugar, and paddy rice), where tariffs are sometimes in excess of 100 percent, imply enormous advantages to African countries if they are conceded preferential access (Annex Table 5).

**Table 9: Overall protection in agriculture (Percent tariff equivalent)**

Type of protection	United States	Canada	European Union	Japan
Tariffs	8.8	30.4	32.6	76.4
Subsidies	10.2	16.8	10.4	3.2
<b>Total</b>	<b>19.9</b>	<b>52.3</b>	<b>46.4</b>	<b>82.1</b>

*Source: Cline, 2004*

As a result, the *effective* preferences of the Quad countries for Africa are concentrated on a single manufactured good (clothing), a range of (mainly temperate) agricultural products,



and fish. Other products that receive effective preferences are sugar, fresh and prepared fruit and vegetable, fresh and preserved fish and meat (Stevens and Kennan, 2003:2). The disadvantage of this pattern of high preference margins is readily apparent – it means in effect that, beyond textiles, Africa gains few incentives to diversify out of manufacturing. Moreover, after the gradual liberalization of the textile sector (Table 10), and the imminent ending of the MFA arrangement, even in textiles African countries have a very short window of opportunity to establish a viable clothing industries before facing what is likely to be a much more competitive international environment (Stevens and Kennan, 2003:2).

**Table 10: Export-tax equivalent of textile and apparel quotas under the Multi-Fiber Arrangement (percent)**

Period	United States		European Union	
	Textiles	Apparel	Textiles	Apparel
Mid-1980s	12.4	26.5	17.2	22.8
1998-99	9.1	11.4	5.1	5.2

*Source: Cline, 2004*

Three further trends in international trade need to be borne in mind which relativises the potential gains through preferential access:

- **The Growth of Free Trade Initiatives.** Given the rapidly changing international situation, with many (often overlapping) free trade initiatives, a preferential agreement like AGOA or EBA can quickly become obsolete. The vigour with which the US and the EU have been promoting free trade deals suggests that future trade agreements will move forward as bilateral or quasi-bilateral processes. The European Union’s Economic Partnership Agreements (EPAs) with the signatory countries of the Cotonou Agreement are but one instance of this.
- **Preferences are being generalized to a larger number of countries.** The extension of sugar preferences to all least developed countries under the EBA is an example. Countries already benefiting under the EU-ACP Sugar Protocol (Congo, Cote d’Ivoire, Madagascar, Malawi, Mauritius, Swaziland and Zimbabwe, plus Tanzania

and Uganda that do not have a surplus to export, and Kenya, which has only recently resumed its exports) (Stevens, 2003:674).

- **Reforms within the EU to the Common Agricultural Policy are making preferences progressively less valuable.** Far from satisfying the aspirations of developing countries, EU “*liberalization*” in agriculture aims to sustain European production but to reshuffle the subsidies and taxes to make them less costly to the European budget and more easily defensible in the WTO. The Commission proposal of 2002 seeks to shift €25 billion of direct EU-level income support from one type of support to another. This will have very limited effects on the EU’s overall agricultural trade since it will neither decrease production nor increase market access. But by decreasing the support prices, it *will* erode the value of African preferences (Stevens, 2003).

To some extent, the convergence of these circumstances puts African trade negotiators in the horns of a dilemma – on the one hand, African countries have been pushing hard for liberalization of the agricultural sector in the QUAD countries. On the other, however, there has been an insistence in maintaining preferential market access. Strictly speaking, the two goals are not compatible: further multilateral liberalization of agriculture will inevitably erode the margin of preferences. The challenge, therefore, is to pursue both goals in a way which does not harm African interests. African trade negotiators will have to use a lot of skill and judgment to strike a balance between the two objectives.

## **7. Conclusions and Policy Recommendations**

Past experience does indeed suggest that trade preferences can be a powerful engine of growth under the right circumstances. In the 1960s and 70s, countries like Spain or South Korea achieved phenomenal export and income growth simultaneously through reaping advantage of their respective preference schemes. But the results of preferential trading agreements have been dependent on the appropriate supply-side response to the opportunities opened up by the market access agreements, and have often owed at least a part of their success on contingent policies, such as the provision of structural funds and Common Agricultural Policy in the case of Spain, or the adoption of an aggressive and comprehensive industrial policy on the part of the state in Korea.<sup>32</sup> This is perhaps the reason why preferential access agreements have been less successful in SSA – the contingent policies, in the shape of adequate external support for structural diversification, and internal policies to facilitate structural diversification, have not been in place.

A certain parallel exists between the criticisms expressed here regarding existing preferential agreements and those which are made of aid systems – the lack of predictability and clear commitment from donor countries undermines aid in the same way as it does for preferential market access. And without the necessary support for capacity-building, both aid and trade instruments are likely to disappoint. What then would be the principal policy recommendations deriving from this survey of the empirical evidence? The following points should be highlighted:

1. **Preference systems need to be strengthened and improved** Despite the mixed nature of the evidence surveyed here, and despite all the weaknesses in the present systems which we have identified, it is clear that the take-up rate of preferences by African countries has been high. Thus we conclude that preferences do not need to

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<sup>32</sup> On Korean industrial policy, see Chang (1994). For a review of the measures provided to compensate poorer developing regions of Europe, see Molle (1994), Chapter 18.

be minimized, or eliminated, as some commentators suggest, but rather strengthened and improved.

2. **Preference schemes are presently too complex** Certain characteristics of preferential schemes, such as rules of origin, product exemptions and safety-guards against import surges all undermine their potential impact. These agreements need to be simplified if their developmental potential is to be realized, particularly with regard to the rules of origin. One proposal would be to allow for automatic cumulation between African countries. This would have the added advantage of supplying a much-needed boost to regional integration within Africa.
3. **OECD Countries should make an effort to harmonize and make legally-binding their respective preference systems.** One of the inherent problems of current preference systems is their concessionary nature. Because the economic stakes are high for exporters, preference systems need to be contestable in the courts – as unilateral measures, currently no country can take any action against a sudden withdrawal of the preferences, whether this is justified or not. Firm commitments, over long time-horizons, by the Quad countries would minimize the uncertainty that has so far undermined the potential impact of these agreements. In this sense, QUAD countries should endeavour to *‘take politics out of preferences’*.
4. **Free market access for all products?** Our final proposal is that the EU’s EBA should be generalized to all sub-Saharan Africa, and should be granted by all the QUAD countries. This could constitute a major pillar of the ‘New Deal’ for African development which is currently unfolding, in the shape of the recommendations of the ‘Commission for Africa’, the Millennium Development Project and the ECA/OECD ‘Mutual Review’ in 2005.

Beyond these recommendations, it should be borne in mind that preferential market access has the added advantage for most African countries of not further threatening the fragile

situation regarding the balance of payments. A recent comparison carried out on the LDCs shows that liberalization measures have been accompanied by a deterioration in the trade balance – import growth has generally been much stronger than export growth (UNCTAD, 2004; Santos-Paulino, 2003). To some extent, this was a fairly predictable outcome of trade liberalization for countries with weak supply-side capacities.<sup>33</sup> There is simultaneously a general feeling in the continent that the efforts that African countries have made to liberalise over the last decade and a half have not been sufficiently acknowledged. In such a context, it could be argued that further reductions are untenable unless African countries receive adequate compensation in the form of enhanced market access. A bold initiative on preferential market access on the part of the QUAD countries would seem to be called for if African countries are to remain convinced of the benefits of the multilateral system of trade liberalization.

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<sup>33</sup> And, as Santos-Paulino and Thirlwall stress “*while trade liberalization may promote growth from the supply side through more efficient allocation of resources, it may constrain growth from the demand side unless a balance between imports and exports can be maintained through currency depreciation or deficits can be financed through sustainable capital inflows*” (2004, cited in UNCTAD, 2004:201).

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## 9. Annex

**Annex Table 1: AGOA Eligible Countries**

Angola <sup>2</sup>	Liberia <sup>2</sup>
Benin	Madagascar * (6 March 2001)
Botswana * (27 August 2001)	Malawi * (15 August 2001)
Burkina Faso <sup>2</sup>	Mali
Burundi <sup>2</sup>	Mauritania
Cameroon * (1 March 2002)	Mauritius * (19 January 2001)
Cape Verde	Mozambique * (6 February 2002)
Central African Republic	Namibia * (3 December 2001)
Chad	Niger
Comoros <sup>1</sup>	Nigeria
Republic of Congo	Rwanda
Democratic Republic of Congo <sup>2</sup>	Sao Tome and Principe
Côte d'Ivoire	Senegal * (23 April 2002)
Djibouti	Seychelles
Equatorial Guinea <sup>2</sup>	Sierra Leone
Eritrea	Somalia <sup>1</sup>
Ethiopia * (2 August 2001)	South Africa * (7 March 2001)
Gabon	Sudan <sup>1</sup>
Gambia <sup>2</sup>	Swaziland * (26 July 2001)
Ghana * (20 March 2002)	Tanzania * (4 February 2002)
Guinea	Togo <sup>2</sup>
Guinea-Bissau	Uganda * (23 October 2001)
Kenya * (19 January 2001)	Zambia * (17 December 2001)
Lesotho * (23 April 2001)	Zimbabwe <sup>2</sup>

Notes: <sup>1</sup> Non-beneficiary countries. These three countries have not requested beneficiary status; <sup>2</sup> Non-beneficiary countries. These nine countries have been reviewed but not yet been granted beneficiary status; \* Textile and apparel beneficiary, with date of textile and beneficiary status in parentheses. Note that the implementation of beneficiary status for Sierra Leone has been delayed pending USTR decision; Countries in italics are currently UN-designated LDCs. Botswana was an LDC from 1971 to 1994.

Source: Office of the United States Trade Representative with the Assistance of the Trade Partnership (2000), Office of the United States Trade Representative (2001b and 2002), and Federal Register (various Issues).

**Annex Table 2: EBA Eligible African Countries**

Angola	Liberia
Benin	Madagascar
Burkina Faso	Malawi
Burundi	Mali
Cape Verde	Mauritania
Centr. Africa	Mozambique
Chad	Niger
Comoros	Rwanda
Congo (Dem. Rep.)	S. Tome, Princ
Djibouti	Samoa
Equat. Guinea	Senegal
Eritrea	Sierra Leone
Ethiopia	Somalia
Gambia	Sudan
Guinea	Tanzania
Guinea Biss.	Uganda
<b>Lesotho</b>	<b>Zambia</b>

Notes: sub-Saharan African countries excluded Botswana, Cameroon, Congo, Gabon, Ghana, Ivory Coast, Kenya, Namibia, Nigeria, Swaziland, and Zimbabwe.

**Annex Table 3: Utilization of Cotonou Agreement by African Countries, 2002**

Country	1,000	in 1000€		in %		
	Total Imports	MFN= zero	MFN + Cotonou zero	% use of preferences	MFN = 0	Cotonou Preferences
Nigeria*	4,989,988	4,689,188	4,988,985	100.0%	94.0%	6.0%
Ivory Coast*	2,600,303	1,652,511	2,470,654	95.0%	63.6%	36.4%
Angola	2,264,214	2,194,183	2,264,203	100.0%	96.9%	3.1%
Cameroon*	1,562,555	1,263,631	1,422,321	91.0%	80.9%	19.1%
Congo (Dem. Rep.)	1,232,089	1,228,309	1,231,733	100.0%	99.7%	0.3%
Ghana*	1,106,461	665,270	1,103,340	99.7%	60.1%	39.9%
Liberia	872,724	870,522	872,609	100.0%	99.7%	0.3%
Kenya	845,305	281,319	834,662	98.7%	33.3%	66.7%
Equat. Guinea	738,680	692,593	738,680	100.0%	93.8%	6.2%
Zimbabwe*	605,677	147,957	562,705	92.9%	24.4%	75.4%
Gabon*	602,526	515,314	602,456	100.0%	85.5%	14.5%
Mozambique	582,737	25,265	573,894	98.5%	4.3%	95.7%
Madagascar	525,793	120,162	523,513	99.6%	22.9%	77.1%
Congo*	501,811	455,465	490,707	97.8%	90.8%	9.2%
Guinea	475,845	417,784	475,843	100.0%	87.8%	12.2%
Namibia*	447,903	147,293	386,153	86.2%	32.9%	67.1%
Tanzania	409,639	197,943	398,197	97.2%	48.3%	51.7%
Senegal	404,990	81,540	399,211	98.6%	20.1%	79.9%
Mauritania	371,579	249,718	371,532	100.0%	67.2%	32.8%
Botswana*	313,098	243,572	276,016	88.2%	77.8%	22.2%
Sudan	262,512	219,853	243,111	92.6%	83.7%	16.3%
Uganda	259,375	127,682	259,310	100.0%	49.2%	50.8%
Ethiopia	183,860	139,661	175,019	95.2%	76.0%	24.0%
Malawi	176,548	31,580	151,107	85.6%	17.9%	82.1%
Centr. Africa	172,183	171,839	172,183	100.0%	99.8%	0.2%
Swaziland*	127,374	5,459	39,719	31.2%	4.3%	95.6%
Zambia	99,936	32,726	84,578	84.6%	32.7%	67.3%
Sierra Leone	83,048	54,643	82,930	99.9%	65.8%	34.1%
Niger	78,961	75,548	78,935	100.0%	95.7%	4.3%
Togo	67,974	43,101	67,923	99.9%	63.4%	36.6%
Mali	65,450	55,334	65,107	99.5%	84.5%	15.5%
Benin	57,688	32,076	57,476	99.6%	55.6%	44.4%
Burkina Faso	52,541	30,974	48,753	92.8%	59.0%	41.0%
Chad	45,499	40,774	45,499	100.0%	89.6%	10.4%
Cape Verde	23,945	11,301	23,940	100.0%	47.2%	52.8%
Gambia	23,651	6,104	23,521	99.5%	25.8%	74.2%
Rwanda	21,453	20,119	21,366	99.6%	93.8%	6.2%
Comoros	18,896	4,179	18,896	100.0%	22.1%	77.9%
Burundi	18,481	17,829	18,481	100.0%	96.5%	3.5%
Lesotho*	10,255	6,573	10,255	100.0%	64.1%	35.9%
Guinea Biss.	7,523	3,829	7,523	100.0%	50.9%	49.1%
S.Tome,Princ	6,246	4,634	6,242	99.9%	74.2%	25.8%
Eritrea	5,110	2,142	4,521	88.5%	41.9%	58.1%
Djibouti	4,293	1,991	4,255	99.1%	46.4%	53.3%
Somalia	2,685	1,153	2,685	100.0%	42.9%	57.1%
African ACP Countries – Total	23,326,717	17,279,488	22,698,061	98.0%	74.10%	23.20%

Source: Own Elaboration, from data supplied by the European Commission

**Annex Table 4: Utility rates of AGOA for Individual African Countries, 2002-3**

	Total Exports to US (1000's US\$)		AGOA incl GSP (1000's US\$)		% of imports under AGOA or GSP	
	2002	2003	2002	2003	2002	2003
Nigeria	5,819,603	10,113,618	5,409,660	9,356,012	93.0	92.5
Angola	3,231,266	4,176,429	0	0	0.0	0.0
South Africa	4,235,974	4,887,962	1,342,594	1,668,573	31.7	34.1
Gabon	1,622,021	1,927,715	1,145,627	1,177,458	70.6	61.1
Lesotho	321,475	393,056	318,029	372,674	98.9	94.8
Chad	5,700	22,434	0	14,478	0.0	64.5
Kenya	189,156	249,137	129,210	184,441	68.3	74.0
Madagascar	215,923	383,329	79,728	187,879	36.9	49.0
Cameroon	172,057	193,319	115,804	147,011	67.3	76.0
Congo (ROC)	223,824	407,186	106,633	340,790	47.6	83.7
Swaziland	114,464	162,033	81,252	133,975	71.0	82.7
Mauritius	280,433	298,096	114,292	143,077	40.8	48.0
Namibia	57,353	123,249	1,717	46,755	3.0	37.9
Cote d'Ivoire	381,860	490,248	49,733	88,037	13.0	18.0
Congo (DROC)	189,692	173,867	0	119,471	0.0	68.7
Guinea-Bissau	35	1,912	0	0	0.0	0.0
Botswana	29,732	13,642	4,578	6,324	15.4	46.4
Ethiopia	25,659	30,496	2,320	2,885	9.0	9.5
Uganda	15,197	34,883	32	1,509	0.2	4.3
Tanzania	25,343	24,234	1,293	1,569	5.1	6.5
Cape Verde	1,811	5,640	51	2,465	2.8	43.7
Mozambique	8,160	8,711	5,916	7,917	72.5	90.9
Zambia	7,790	12,469	83	510	1.1	4.1
Senegal	3,799	4,326	499	720	13.1	16.6
Sierra Leone	3,833	6,478	217	75	5.7	1.2
Mali	2,583	2,394	342	262	13.2	10.9
Guinea	71,600	69,226	68	194	0.1	0.3
Djibouti	1,915	615	23	27	1.2	4.4
Niger	897	4,034	22	63	2.5	1.6
Gambia	0	134	0	20	0.0	14.9
Benin	680	602	0	0	0.0	0.0
Rwanda	3,086	2,623	10	6	0.3	0.2
Seychelles	26,291	15,324	0	3	0.0	0.0
Sao Tome & Prin	391	91	0	0	0.0	0.0
Mauritania	929	929	35	3	3.8	0.3
<b>Total</b>	<b>17,474,282</b>	<b>24,404,120</b>	<b>8,991,502</b>	<b>14,105,025</b>	<b>51.5</b>	<b>57.8</b>

Source: Elaborated from data from [www.agoa.info](http://www.agoa.info) (accessed 18/11/2004)

**Annex Table 5: Agricultural tariff rates (per cent)**

Sector	Weight	United States	Canada	European Union	Japan
Paddy rice	2.94	4.9	0.0	64.9	409.0
Wheat	2.01	2.6	62.7	61.4	249.2
Cereal grains n.e.c.	2.76	0.6	8.9	38.6	20.2
Vegetables, fruits, nuts	8.63	4.7	1.9	14.5	44.9
Oil seeds	1.85	17.7	0.0	0	76.4
Sugar cane, sugar beet	0.95	0.7	0.0	251.4	0.0
Plant-based fibers	0.93	9.7	0.0	0	0.0
Crops n.e.c.	3.14	21.5	2.4	3.1	22.1
Cattle, sheep, goats, horses	4.03	1.1	0.2	36.6	149.1
Animal products n.e.c.	5.71	0.6	19.8	6.7	5.0
Raw milk	3.96	0.0	0.0	0	0.0
Wool, silk-worm cocoons	0.45	0.9	2.3	0	54.7
Forestry	2.53	0.8	0.7	0.4	0.2
Fishing	2.80	0.6	0.4	9	4.9
Bovine meat products	4.83	5.3	16.3	88.9	36.4
Meat products n.e.c.	5.40	3.6	72.4	30.9	58.2
Vegetable oils and fats	3.17	4.3	8.6	11.4	6.6
Daily products	5.61	42.5	214.8	87.7	287.0
Processed rice	3.05	5.3	0.7	87.4	409.0
Sugar	1.93	53.4	4.9	76.4	116.1
Food products	21.73	11.4	14.1	28.8	38.3
Beverages, tobacco products	11.59	3.0	62.5	8.3	16.2
<b>Total</b>	<b>100.00</b>	<b>8.8</b>	<b>30.4</b>	<b>32.6</b>	<b>76.4</b>

a. Weighted by the GTAP estimates of world output value for the corresponding products.  
 Source: Cline, 2004, from GTAP5 database

**Annex Table 6: Summary of Selected Empirical Studies into the Impact of Preferential Agreements**

Study	Sample	Methodology	Key Results
Cline (2004)	100 developing countries, 1981-2001	Pooled OLS	Dummy variable for Lome/Cotonou Agreement highly significant and large coefficient, boosting exports 8.8 percent for Lome countries. However, this is offset by the SSA dummy, which is negative and also highly significant, implying that a typical SSA country had a 10.7 percent lower real export growth annually than would have otherwise been expected
Nielsson (2002)	1973-92 (over three year periods)	Gravity model between OECD and developing countries	Dummies for GSP and Lome both significant. GSP raises developing countries' exports by 34 to 59 percent, and Lome by 45 to 69 percent. Impacts started large, but fell to near zero for 1980, due to NTBs and preference erosion. Since then, it has recovered.
Ianchovichina, Mattoo and Olarreaga (2003)	37 SSA countries	GTAP Simulation	Results dependent on the region granting unrestricted market access: To US market – only 0.4 percent increase in non-oil exports and no change in welfare To Japanese market – negligible benefits To EU market – a \$513 million (2.8 %) increase in non-oil exports and a £317 million (0.2%) increase improvement in welfare. Benefits would derive principally from increase in exports of meat, fibres and sugar. Greatest gains from QUAD liberalisation – \$2.5 billion (14%) increase in non-oil exports and a \$1.8 billion (1.2%) increase in welfare. Insignificant decline in QUAD welfare (less than 0.01 percent).
Bora, Cernat and Turrini (2002)	Data for LDCs (Bangladesh, Malawi, Tanzania, Uganda, Zambia and rest of SSA (including some non-LDCs)	GTAP simulation of EBA and a 'generalised' EBA	Estimated gains for 4 SSA countries and rest of SSA of \$392 million, rising to \$1320 if the EBA is generalised to all Quad countries. Gains are centred in paddy and processed rice, cereals and sugar – textiles and manufacturers actually contract. Losses for EU mount to \$250 million, rising to \$546 million if EBA is generalised. The US would lose a similar amount.
Cernat, Laird, Monge-Roffarello and Turrini (2003)		SMART ex-ante partial equilibrium model	
Yu and Jensen (2003)	As for Bora et. al. (2002)	GTAP model	Under full liberalisation scenario, authors estimate a \$169 million gain in GDP for SSA (equivalent to 0.5 percent of GDP. Gains are proportionately much larger for Malawi (4.7%), Tanzania (3.5%), Zambia (2.4 %) and Mozambique (1.1%). However, if the delay on the liberalisation of sugar, banana and rice is taken into account, then gains for SSA is only \$41 million

			(0.1% of GDP), and all the other SSA countries enjoy welfare gains of less than \$6 million. Authors also experiment with preference erosion – with a reduction on tariff rates from all other trading partners of 50 percent, for SSA welfare losses arise of -\$25 million, compared to gain of \$169 million under full liberalisation effect. Authors similarly show that the elimination of export subsidies would compound losses for SSA (-\$71 million).
Rose (2002)	1948-98 data for 175 countries	Gravity model using OLS and GMM estimator	Author detects a significant and substantial effect of GSP on trade volumes, approximately doubling trade between partners. At the same time, the GATT/WTO is not found to be significant in any of the samples. Author concludes that multilateral system does not necessarily induce greater trade, but preferential agreements do.
Romalis (2003)	1960-98 data for 120 countries	OLS cross-sectional and panel regressions	Author specifies an equation to determine per capita growth rates as a function of two variables – the GSP impact, being the value of the country-specific measure of the US and EEC tariff reductions, and a variable that captures export composition. Also included is an African dummy. Author calculates a “growth dividend” over a fifteen year period of 10 percent for the average African country through the working of the GSPs.
Ozden and Reinhardt (2002)	1976-2000 data for 154 developing countries using US data	OLS regressions	Three dependent variables are chosen to represent whether a trade regime is ‘open’ or not – <i>closure</i> are imports as % of GDP, <i>Duties</i> are duties as percent of total trade, and <i>Tariff</i> is the unweighted nominal tariff. These are regressed on a GSP-membership dummy and various control variables (market size, conditionality, income, geography, growth). Authors find that countries removed from GSP adopt more liberal trade policies than those remaining.