

Is the "Everything But Arms" Initiative all good news and everything the EU can do for the LDCs?

The European Union (EU) has recently adopted the "Everything But Arms" initiative (EBA), under which all restrictions on its imports (except arms) from the Least Developed Countries (LDCs) are to be removed on a non-reciprocal basis. This initiative is a continuation and further enhancement of the preferences granted in the past and is considered by the EU as a significant step in fulfilling the objective of the Doha Development Agenda.

Both the EU and the African countries have placed this initiative eminently in their respective WTO negotiation proposals, suggesting that the evaluation of the EBA should be conducted in the context of the negotiations. Multilateral liberalisation as an outcome of the negotiations will likely erode the attractiveness of such preferences. In the case of the EBA, this implies that relying on trade preferences might be a dangerous route for the LDCs, as preference margins will be eroded and eventually disappear during the multilateral process. Moreover, such preferences are insecure due to the attached safeguard clauses and rules of origin, which may result in potential poverty-creating adjustment cost for the LDCs.

In light of these considerations, a better understanding of the potential effects of the EBA with and without probable MFN reforms by the EU is essential for policy makers and trade negotiators. A recent study published by the Danish Research Institute of Food Economics (Yu and Jensen, 2003), upon which this brief is based, tackles these issues. The analysis shows that the benefits of the EBA to the LDCs amount to less than US\$300 million and that these benefits will likely be eroded if the EU reforms its agricultural policy. The study concludes that in order to ease the difficulties faced by the LDCs, it is imperative that additional measures be made available to the LDCs in conjunction with successfully concluding the Doha agenda.

The EBA Initiative

As a direct extension of the General System of Preferences (GSP), the EBA differs from its predecessor in several ways. First, it expands the quota and duty-free access to virtually all exports from the LDCs, effectively affecting 919 HS-8 tariff lines, 876 of which will get the quota and duty-free access with immediate effect whereas the remaining 43 tariff lines (sugar, banana and rice) are subject to gradual liberalisation. Second, it expands the preferential coverage to all the 49 LDCs. Third, all the LDCs are equally given this free access, whereas the GSP provides different treatments for different countries and products. Last, unlike the GSP, the EBA has no time limits although the EU promises to review its performance.

Despite these differences, the EBA does share many similarities with the GSP, especially with respect to safeguard measures and rules of origin. In addition to the safeguard measures already included in the GSP, the situation of "massive imports into the EU market" is added as a trigger for withdrawing the preferences. Furthermore, the EU is allowed to suspend the preferences concerning the three sensitive prod-

ucts entirely if imports cause serious disruptions to the EU market. Also, the rules of origin of the GSP apply to the EBA. Whether or not the objective of the EBA can be achieved is certainly contingent on how these measures are applied in practice. As such, some cautions should be exercised when evaluating the potential effects of the EBA.

Potential impact of the EBA on the LDCs

Potential impact of the EBA can be elicited by examining the pre-EBA trade and protection data. In 1999, total agricultural exports from the LDCs to the EU amounted to about US \$2.5 billion, of which 100 million (4 percent) were exports of the EBA-affected products. Sugar is the largest exportable good affected by the EBA (US\$67 million, see Table 1), followed by vegetable and fruits and cereal grains. Judging from the pre-EBA tariff rates, there seems to be some scope for expanding exports of the above products. However, the special arrangement regarding sugar, rice and banana will likely delay such gains. For other EBA products, the tariff rates have already been low and/or the current exports are quite small, pointing to their limited export potentials.

TABLE 1. TARIFF AND TRADE FOR SELECTED PRODUCTS FROM LDCs

	Pre-EBA Tariff rates	EBA exp. 1000 \$	Total exp. 1000 \$	EBA as % of total
Sugar	75 - 103	67,618	67,618	100.0
Veg. & fruits	2.3	17,203	124,124	13.9
Cereals	37.1	11,283	11,283	100.0
Vegetable oil	0.2	1,667	88,401	1.9
Proc. food products	2.1 - 2.5	475	680,237	0.1
Processed rice	87.4	399	399	100.0
Other meat products	9.7 - 19.2	378	940	40.2
Bovine meats	9.7 - 19.2	217	217	100.0
Other animal products	2.8 - 4.5	149	39,055	0.4
Other crops	0	0	946,585	0
Plant fibres	0	0	245,746	0

Quantitative assessment of the EBA supports the above speculation. If the protections imposed on exports from the LDCs are removed, cereal grains, meats, rice and sugar (the products with higher initial tariffs) will have the highest export expansion. The most notable changes are for sugar, whose exports will reach US\$117 million for Malawi and 472 million for rest of Sub-Sahara African. In contrast, exports of oil seeds, plant fibre, other crops, and vegetable oil (products with smaller tariff cuts) decrease slightly, due to inter-sectoral resource reallocations in the LDC countries. Production patterns in the LDCs are similarly impacted by the EBA (e.g. sugar output increases dramatically).

Implementing the EBA leads to welfare improvement for the LDCs (Table 2). The gains range from US\$169 million (representing 0.12% increase in utility) in rest of Sub-Sahara Africa to US\$2.4 million (0.04% of utility) in Uganda, of which the most is attributed to improved allocation efficiency (due to reallocation of resources to the products with more trading possibilities) and terms of trade (due to higher relative export prices). All the LDCs benefit from terms of trade im-

RESEARCH PROJECT MISSION

This research project analyses the economic consequences for developing countries of changes in agricultural and trade policies in relation to the WTO negotiations.

FUNDING
The research project is primarily funded by the Royal Danish Ministry of Foreign Affairs, DANIDA, Denmark.

provement. For example, about US\$117 million of the total gains for Sub-Sahara Africa are due to improved terms of trade. The importance of the three sensitive products deserves some further comments. Should pre-EBA tariff rates for the sensitive products remain, the welfare results would be reduced markedly. For instance, welfare gains would be reduced to US\$41 million and US\$1.3 million for rest of Sub-Sahara Africa and Uganda, respectively.

TABLE 2. CHANGES IN REG. WELFARE (MILLION \$) AND UTILITY (%)

	EBA		EBA + EU reform	
	Welfare	Utility	Welfare	Utility
EU	-184.0	0	12,995.4	0.19
Malawi	30.4	1.18	10.5	0.41
Mozambique	8.5	0.26	-8.0	-0.24
Tanzania	59.7	0.93	27.5	0.43
Zambia	11.4	0.3	2.5	0.07
Uganda	2.4	0.04	-15.5	-0.24
Rest of Sub-Sah. Africa.	169.2	0.12	-396.5	-0.28
World	38.2		14,826.1	

Will EU reforms reduce the value of the EBA?

The attractiveness of the EBA initiative is made possible largely by means of the EU's Common Agriculture Policy (CAP). The ongoing WTO negotiation and the imminent enlargement of the EU exert pressure on the EU to reform the CAP. Against this backdrop, it is conceivable that the EU will at least partially reform the CAP, thereby reducing the preference margins of the EBA.

Further analysis show that the value of the EBA indeed diminishes if the EU across the board reduces its market access barriers by 50 percent, eliminates export subsidies and reduces domestic support by 35 percent (a move in accordance with the "Harbinson proposal"). These reforms lead to welfare losses for all the LDCs concerned in the study, especially for Sub-Sahara African, which will suffer a loss of over half billion dollars from the EU reforms alone, thereby turning the gains from the EBA to losses of nearly US\$400 million (Table 2). In contrast, the world gains from such a scenario (estimated at nearly US\$15 billion), with the EU itself being the biggest beneficiary of nearly US\$13 billion. About two-third of the total welfare gains are attributable to the market access reform, whereas the domestic support reform provides much of the remainder. Removing export subsidies does not generate significant gains for the world. However, it does add to the welfare of the EU.

The above results clearly present a dilemma to policy makers. On the one hand, keeping the existing protection measures of the EU unchanged for the sake of a meaningful EBA would be hard to justify from a purely economic perspective—the world would have to forgo the welfare gains of US\$15 billion, as compared to the benefits of US\$300 million to the LDCs from the EBA. On the other hand, to say that just because the losses of the LDCs are small they can simply be neglected and forgotten is not acceptable, considering that WTO members have agreed that the interest of the LDCs has to be adequately addressed.

So what else can be done to avoid marginalizing the LDCs in the new round of trade liberalisation? The answer might lie in other policy measures. For example, the EU, with all the potential welfare gains, can team up with other developed countries to find ways enabling the LDCs to overcome the short-term losses. Part of the solution could be to increase and perhaps redesign the development aids so as to lift pervasive supply side constraints and infrastructure bottlenecks in the LDCs.

SUMMARY AND POLICY IMPLICATIONS

To sum up, the EBA initiative is unlikely to generate sizable welfare gains for the LDCs, which are estimated to be less than US\$300 million. A great deal of the gains is associated with the three sensitive products. At the same time, the negative impact on the EU and third countries seems to be quite small, indicating that the EBA is not costly for the EU and does not pose a serious threat to third countries. Putting the

EBA in the context of the multilateral trade liberalisation, the analysis further shows that most LDCs will suffer welfare losses under a scenario where the EU cuts its protection measures, indicating that further trade liberalisation may actually harm the LDCs in the short run. However, using this result as an argument for maintaining protections in the EU (and other countries) would be quite mistaken as it entails forgoing welfare gains of US\$15 billion for the whole world.

Based on the above analysis, two sets of policy implications can be drawn out from the perspective of the LDCs. Regarding the EBA initiative, it is important that the trading opportunities provided through the EBA is fully available to the LDCs. To do so, the EU should minimise the uncertainties and complexities associated with the safeguard measures and rules of origin. The presence of these measures in previous preference schemes (such as the GSP) may have contributed to their poor performance. To avoid this problem from happening again, the LDCs should seriously consider taking action to negotiate for unconditional quota and duty-free access to the markets of the EU and other developed countries. As many WTO members have proposed the abolition of Article 5 (special safeguard provisions) of the Agreement on Agriculture, the LDCs may take this opportunity to integrate the EBA into the new WTO agreement and to get rid of the attached safeguard provisions altogether. It should be noted, however, that these benefits are bound to be short-lived, and that long-term solutions should be considered.

Concerning the possible negative impact of the WTO reforms, the negotiation proposal of the African Group emphasises the importance of implementing the Marrakesh Ministerial Decision. Although this decision was meant to primarily tackle the problems resulting from the Uruguay Round reform, many of the mechanisms proposed can also help to ease the problems discussed here. For example, technical and financial assistance and cooperation are much needed in solving many supply side constraints and bottlenecks that the LDCs face. As the LDCs have to compete on level grounds with other WTO members eventually, the key to improve their positions is to break these constraints. Certainly, the EU and other developed countries are in the position to offer such assistances as they stand to benefit the most from further multilateral liberalisation. If the efforts are indeed forthcoming from the rich countries and if the cooperation between the rich and the poor is genuine during the Doha Round, there is no reason to fear for marginalizing the LDCs. If not, the willingness of participation in the negotiations by the LDCs is difficult to envisage.

REFERENCES

Yu, Wusheng and Trine Jensen (2003). "Trade Preferences, WTO Negotiations, and the LDCs: the case of the "Everything But Arms" Initiative of the EU", Working Paper, Danish Research Institute of Food Economics (FOI).

Further information: Wusheng Yu, wusheng@foi.dk.