

# **GSP Reform: a longer-term strategy (with special reference to the ACP)**

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## Contents

<b>Executive Summary</b>	<b>v</b>
<b>Introduction</b>	<b>1</b>
1 Evolving the GSP	1
2 The focus of the report	1
<b>Part A. The New GSP</b>	<b>3</b>
3 The status quo	3
3.1 The place of the GSP – and its link to the ACP	3
3.2 The current GSP	4
3.2.1 What was new	4
3.2.2 What was retained	5
4 The new GSP	5
4.1 Broad features	5
4.2 Weighing up the changes	6
5 Graduation	7
5.1 Winners and losers to 2008	7
5.2 What happens in 2008?	9
6 GSP+	11
6.1 What it is – and who is eligible	11
6.2 Limitations on GSP+	11
6.3 The potential effects	12
<b>Part B. Making the GSP Cotonou Equivalent</b>	<b>14</b>
7 Scope and methodology	14
8 Identifying the products	15
8.1 Current ACP exports to the EU	15
8.2 Potential ACP exports to the EU	16
9 Preference erosion	19
9.1 Extending GSP+	20
9.2 Improving the Standard GSP	22
9.2.1 Adding extra competitors for the new products	22
9.2.2 Cutting tariffs	25
10 Conclusions	28
10.1 Creating coherence	28
10.2 Extending GSP+	29
<b>References</b>	<b>31</b>



# Executive Summary

## Scope of the report

What role can the Generalised System of Preferences (GSP) play over the medium term in rationalising the EU's multi-layered and partly conflicting trade policies? What contribution can it make to the development of the 'alternative arrangements' that the EU has promised to make available to those African, Caribbean and Pacific (ACP) countries unwilling to enter into Economic Partnership Agreements (EPAs)? These are the questions raised in this report.<sup>1</sup>

The EU has literally dozens of agreements with developing countries, which often overlap. This differentiation has been a source of controversy in the WTO, most recently with the dispute over the anti-narcotics tranche of the GSP brought by India. The Appellate Body ruling has confirmed that differentiation within the GSP is possible provided that it is related to objective and internationally accepted differences in circumstance. The effective integration of the ACP countries in the GSP would represent the largest possible additional step in the direction of creating a single, coherent framework for trade preferences.

## The new GSP

Now over 30 years old, the GSP has been reviewed and adapted several times, most recently in 2001. Although described as a mid-term review of the ten-year regime 1994–2005, it made radical changes. The proposals made by the European Commission in its July 2004 Communication (CEC 2004a) and its draft Regulation (CEC 2004b) continue the process. Like its predecessor, the GSP regime it proposes will last for ten years (from 2006 to 2015) but with a mid-term review. The Commission's draft Regulation covers the first period to 2008. The only two significant innovations in this initial period are a new formula for graduation and a new superior tranche – GSP+ – to replace three existing regimes.

The graduation formula in the new GSP will replace that in the old. So there will be winners (countries that are reintegrated into the GSP) as well as losers (countries that are graduated anew). In the period to 2008 there are significantly more 'winners'. They include three of the countries most affected by the tsunami – India, Indonesia and Thailand. The revenue these countries will gain as a result of paying GSP rather than MFN tariffs is equivalent to between one-fifth and one-third of one percent of their exports to the EU. All three, though, are excluded from GSP+.

Under the proposed GSP+ simple *ad valorem* or specific duties will be suspended on all products covered by the GSP. For items subject to an *ad valorem* and a specific duty, the *ad valorem* element will be suspended. Duty suspensions will not apply to sections from which any given country has been graduated.

In order to benefit from these additional preferences, a country must have ratified and effectively implemented 16 core human and labour rights UN/ILO Conventions and at least seven (of 11) conventions related to environment and governance principles. They must also satisfy additional criteria related to the value of their exports set out in Article 9.2(a) and (b)

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<sup>1</sup> The views expressed in this report are the authors', and do not necessarily reflect those of DFID.

of the draft Regulation. These specify that a country is vulnerable only if it meets both of two criteria:<sup>2</sup> a diversification criterion and a smallness criterion.

We calculate that 21 states fail the vulnerability tests. Three of the excluded states – India, Pakistan and Vietnam – are classified by the World Bank as low-income. And all of the tsunami-affected states other than Sri Lanka are excluded.

The impact of GSP+ *could* be very substantial, but only if a high proportion of the countries are accepted. There could be three types of effect.

- ◆ **Trade creation.** The number of countries and products facing no tariff barriers in the EU would increase, resulting in more trade.
- ◆ **Trade diversion.** Countries elevated from the ‘middle’ to the ‘most preferred’ group would find that they have a competitive advantage over those that remain in the middle group and that they no longer face a competitive disadvantage compared with those that are already in the ‘most preferred’ group.
- ◆ **Rules of origin.** If take-up were widespread, the origin rules would become a less important determinant of trade.

If large numbers of states are accepted the trade creation effects will be enhanced. If few states are accepted trade diversion is more likely.

## Providing Cotonou equivalence

A first, basic requirement for a GSP providing treatment equal to Cotonou is that it cover all of the products that the ACP currently export and that receive preference under Cotonou. Although a necessary condition, it is not sufficient. But it is an obvious first place to start.

The end of the Cotonou Agreement would leave unchanged the tariff treatment of some 75 percent of ACP exports because they are in items that either enter duty free under the MFN or would do so under the Standard GSP. The report considers the position of the remaining 25 percent, referred to as ‘GSP-relevant’ items.

Just under two-thirds of the GSP-relevant items are included in the Standard GSP but are not accorded duty-free access. All but four are, however, given duty-free access under the proposed new GSP+. All of the remainder are items that are not covered by the Standard GSP or GSP+, and so would have to be introduced into the scheme for it to provide an adequate alternative to Cotonou.

A key advantage of Cotonou for the ACP is that they are treated more favourably than some of their developing country competitors. They are always concerned, therefore, with preference erosion. Clearly, the EU has to take a more rounded view of the development attractions of lower tariffs than do the ACP and cannot simply agree to freeze current trade policy in order to maintain this margin of preference. Even a full extension of Cotonou into EPAs would not achieve the ACP objective of freezing preference margins.

On the other hand, some account needs to be taken of the extent to which the task of improving the GSP solely for the purpose of making it Cotonou equivalent would automatically erode the gains that the ACP might hope to achieve from this process. It would

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<sup>2</sup> The descriptive names have been coined by the authors of this paper.

not be sensible to use considerable political capital pressing for an extension of the Standard GSP if, in so doing, it meant that the ACP saw their preference entirely eroded.

The change to the GSP that would provoke the smallest amount of *additional* preference erosion would be the extension of GSP+ to cover all ACP GSP-relevant exports. The ACP would share their preferential access with all other GSP+ beneficiaries – but so they will regardless of what happens under Cotonou for all products that are not added to the scheme specifically to make it Cotonou equivalent.

There are only a few cases in which the extension of GSP+ would further erode ACP preferences. Bananas, rum and, the most substantial of all, sugar, are the only significant ‘problem commodities’. In all three cases it is not really sensible to try to identify ‘solutions’ purely within the context of this report. It is evident that any fully acceptable ‘solution’ is very difficult to find even without the complication of considering the consequences of the end of the Cotonou Agreement. It is not even certain how sugar can be handled in EPAs.

None of the ACP states is excluded *a priori* from the GSP+, and so would be ineligible only if it fails to ratify and implement all of the required conventions. The only reasons, therefore, for not adopting the ‘extend GSP+’ route would be that some countries for which the EU wishes to continue strong preferences fail to make the ratifications or that it is considered undesirable to follow this route, perhaps because the WTO compatibility of GSP+ is by no means certain.

In that case the principal option would be to extend the Standard GSP. No new products will need to be added to the GSP over and above those already identified as required to make the GSP+ an acceptable Cotonou equivalent. But the erosion potential of including these new products in the Standard GSP is greater. The new preferences would also be available to countries that are excluded from GSP+ because they fail the vulnerability criteria. The main candidates for attention are canned tuna, fresh beans, frozen hake and monkfish, prepared beans, preserved pineapples and pineapple juice. There would be significant preference erosion on all of these.

## Conclusion

The broad conclusion of this report is positive – not only is it feasible to consider the GSP as a post-Cotonou trade option, but there are economic advantages in so doing. The most obvious route for creating a Cotonou-equivalent regime under the GSP is to extend GSP+ (assuming it survives WTO challenge). The analysis in Part B suggests that this is feasible.

As explained in Part A, the economic impact of GSP+ will be heavily influenced by the number of countries that become eligible. In brief, the more the better. If many countries are accepted there are good reasons to expect significant trade creation. There will also be a lessening of the problems of the rules of origin. The additional reform of agreeing full cumulation between all GSP+ beneficiaries would clarify the situation still further. At the extreme it would mean that only inputs from the 21 states excluded *a priori* from GSP+ would cause potential problems with the origin rules.

Provided that the broader issues of contractuality etc. can be overcome, the conclusion to be drawn is that an extension of GSP+ to cover all ACP exports would have beneficial economic effects. Indeed, it is possible to argue that the economic effects would be superior to those likely to arise from EPAs. This is because a broad GSP+ would result in a significant and early liberalisation of the EU – a large market. EPAs, by contrast, since they will exclude

some imports and delay liberalisation of others until 2020 or thereabouts, will probably result in only limited liberalisation of small markets.



# Introduction

## 1 Evolving the GSP

The European Commission has put forward broad proposals for a new Generalised System of Preferences (GSP) to cover the period from 2006 to 2015, but has issued a detailed draft Regulation (COM(2004) 699 final of 20 October 2004 – CEC 2004b) only for the period 1 July 2005 to 31 December 2008. Comment upon this draft Regulation needs to take account not only of changes that should be implemented immediately, but also of the longer-term possibilities for evolving the GSP regime.

What role can the GSP play over the medium term in rationalising the EU's multi-layered and partly conflicting trade policies? What contribution can it make to the development of the 'alternative arrangements' that the EU has promised to make available to those African, Caribbean and Pacific (ACP) countries unwilling to enter into Economic Partnership Agreements (EPAs)?

These are the questions raised in this report. Neither the Commission's July 2004 Communication to the Council (CEC 2004a) nor the draft Regulation provides any clear guidance. This is unsatisfactory given that the current exercise is intended to be a major review. Moreover, it may accidentally foreclose on options that later appear to be desirable.

## 2 The focus of the report

The particular focus of this report is on the possibilities for the GSP to become an acceptable alternative successor regime to the Cotonou Trade Agreement for those ACP states for which it is undesirable or infeasible to join EPAs. The reason for this is twofold.

First, of course, the Cotonou Agreement commits the EU to 'assess the situation' of non-least developed ACP states that decide 'they are not in a position' to enter EPAs in order 'to provide these countries with a new framework for trade which is equivalent to their situation and in conformity with WTO rules' (Article 37:6). Originally scheduled for 2004, this is now to be done in 2006. There are no other known developments in EU trade policy between now and the end of 2006 that could provide a plausible peg for a generalised alternative that is WTO compatible. It may prove possible to create individualised arrangements for odd countries falling outside the EPA network, but this would worsen one of the current features of EU trade policy that an evolution of the GSP would counter. This is the high degree of diversity between different trade instruments.

This provides the link to the second reason to focus on the ACP. The EU has literally dozens of agreements with developing countries, which often overlap. As explained below, this differentiation has been a source of controversy in the WTO, most recently with the dispute over the anti-narcotics tranche of the GSP brought by India. The Appellate Body ruling on the India case has provided an opportunity to move forward. It has confirmed that differentiation within the GSP is possible provided that it is related to objective and internationally accepted differences in circumstance. The GSP+ is designed to take advantage of this ruling. The effective integration of the ACP countries in the GSP would represent the largest possible additional step in the direction of creating a single, coherent framework for trade preferences.

The bulk of the report is divided into two parts. Part A reviews what is in the GSP reform proposal as described in the draft Regulation (updated to include changes where these are known). Part B takes the proposed new GSP as its starting point and assesses the additional changes that would be required to make it an acceptable alternative to EPAs. As it appears now to be too late for these changes to be incorporated into the present review they should be a target for achievement between now and the end of 2007.

# Part A. The New GSP

## 3 The status quo

### 3.1 The place of the GSP – and its link to the ACP

The EU's GSP is the broadest element of its preferential trade policy. Because it applies to almost all developing countries, the GSP provides a 'safety net': no developing country (other than the richest and most competitive) is offered less favourable access to the European market than that provided under the GSP.

Because of this, though, the GSP is not always the most favourable of the EU's import regimes. Lower tariffs are often paid by parties to the EU's older preferential trade accords – not only the Cotonou Agreement, but also the more recent free trade agreements (FTAs), such as those with Mediterranean countries, South Africa and Chile. Kenya, for example, would pay tariffs of up to 10.1 percent on its sales of fresh/chilled peas if they were imported into the EU under the GSP but it does not do so because they are imported instead under the Cotonou Agreement and enter duty free.

In broad terms the EU's trade partners fall into three categories:

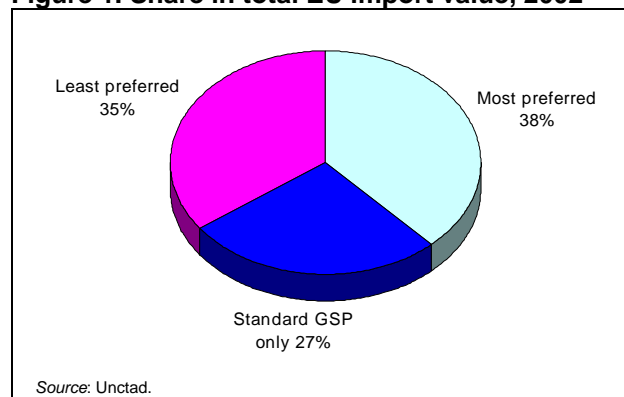
1. **the most preferred** – that benefit from a trade agreement that is superior to the Standard GSP<sup>3</sup> (including, but extending well beyond, the ACP);
2. **the middle group** – that are party to the Standard GSP but to no other regime (mainly South and East Asia, the Middle East and parts of Latin America);
3. **the least preferred** (mainly industrialised countries) – that trade on the so-called 'most favoured nation' (MFN) terms.

Of the three groups, the middle one accounts for the smallest share of EU imports (see Figure 1). It is favoured by the EU in cases where a beneficiary country competes with members of the third group, but disfavoured when competition is with a member of the first.

The term 'standard' is used in the description of the group's access to the EU because the GSP does not provide equal treatment to all developing countries. There are special, more favourable, tranches not only for the least developed countries (LDCs), but also for those fighting illicit narcotics and those with favourable social and environmental policies. These states fall into the 'most preferred' group.

It is this differentiated nature of EU trade policy towards developing countries that has underlain a number of disputes taken to the WTO over the past decade. The most recent of

Figure 1. Share in total EU import value, 2002



<sup>3</sup> The term 'Standard GSP' is used throughout this report to denote what is termed in the Regulation the 'general arrangement', i.e. excluding the more favourable special arrangements (four in the current GSP and two – for sustainable development and good governance (the GSP+) and for LDCs – in the proposed GSP).

these, with India, has contributed directly to some of the reforms in the current Commission proposal.

The GSP affects the ACP in two ways. Any change to the GSP, therefore, is of potential commercial importance if it alters either of these two effects. They are:

- ◆ to establish the market access terms potentially available to the ACP's competitors in the EU and, hence, the size of the ACP's margin of preference over them;
- ◆ to set the 'safety net' for the future access to the European market of any ACP state which declines to enter into an EPA and is not able to negotiate any other alternative trade arrangement with the EU.

## 3.2 The current GSP

### 3.2.1 What was new

Now over 30 years old, the GSP has been reviewed and adapted several times, most recently in 2001.<sup>4</sup> Although described as a mid-term review of the ten-year regime 1994–2005, it made radical changes. It greatly simplified the old system under which covered items (see Box 1) fell into four categories according to their sensitivity and the applicable GSP tariff was 85, 70, 35 or zero percent respectively of the MFN tariff. There are now only two categories for covered items. Tariff duties on those classified as non-sensitive are entirely suspended.<sup>5</sup> For those classified as sensitive:

- ◆ the simple *ad valorem* GSP tariff is 3.5 percentage points lower than the MFN rate for all except clothing and textiles (Chapters 50 to 63) – for which the reduction is 20 percent.
- ◆ specific duties are reduced by 30 percent<sup>6</sup> unless in combination with an *ad valorem* duty, in which case the specific duty is not reduced;
- ◆ duties are totally suspended where the application of the GSP reduction formula results in *ad valorem* duties of 1 percent or less or in specific duties of € or less.

#### Box 4. A GSP lexicon

The term **covered imports** includes imports of all items included in the GSP that originate in a beneficiary country, regardless of whether that country has been graduated out of the sector concerned. **Eligible imports** are limited to products for which the originating country has not been graduated. **Preferential imports** are products for which GSP treatment has been actually claimed.

The EU's **total imports** from a country include, in addition, all the products for which there are no GSP preferences. At present almost one tenth of dutiable products in the Common Customs Tariff are not covered by the GSP.

<sup>4</sup> The first European Community GSP was for an initial phase of ten years (1971–81), subsequently renewed for a second decade (1981–91). The third ten-year offer was delayed pending the outcome of the Uruguay Round, the 1991 scheme being extended with various amendments until 1994. The scheme for 1995–2004 was adopted on 1 January 1995, the legislative acts being Council Regulation 3281/94 in respect of industrial products and Council Regulation 1256/96 in respect of agricultural products. The scheme was revised for the period 1 July 1999–31 December 2001 on the basis of Council Regulation 2820/98. The basic structure of the offer was not substantially modified until the end of 2001, with the adoption of Council Regulation (EC) No 2501/2001 of 10 December 2001 (OJ L 346, 21.12.2001, p. 1), which covered the period 2002–4 and fully incorporated the EBA amendment. Council Regulation (EC) No 2211/2003 of 15 December 2003 (OJ L 332, 19.12.2003) subsequently extended this until 31 December 2005.

<sup>5</sup> Except for agricultural components.

<sup>6</sup> 15 percent in the case of HS 2207 (ethyl alcohol).

The new regime also incorporated the 'Everything but Arms' (EBA) scheme proposed in 2000. This extended a pre-existing special tranche of the GSP for LDCs that already offered duty-free access for all industrial goods but not for all agricultural ones.

### 3.2.2 *What was retained*

Three of the features of previous GSPs that were retained are:

- ◆ special, additional tariff cuts (most resulting in duty-free access) for states fighting narcotics (Andean and Central American states plus, for the first time, Pakistan);
- ◆ further tariff reductions, generally of 5 percentage points (in addition to the 3.5 percentage point Standard GSP reduction) on some items for countries meeting the requirements for inclusion in special incentive regimes for the protection of labour rights and the environment;
- ◆ a graduation mechanism that made some states ineligible for GSP tariffs on specified products if they fell foul of criteria related to share of preferential imports, development index and export-specialisation index.

In 2002 India complained to the WTO that the anti-narcotics arrangement contravened the EU's multilateral obligations. The WTO Appellate Body found in India's favour in April 2004 (WTO 2004a) and subsequent arbitration (WTO 2004b) has requested the EU to amend its trade policy by 1 July 2005.

## 4 The new GSP

### 4.1 Broad features

In its July Communication the Commission seeks to deal with the criticisms that have been levelled at the GSP and with the WTO ruling. Like its predecessor, the GSP regime it proposes will last for ten years (from 2006 to 2015) but with a mid-term review. The Commission's draft Regulation covers only the first period to 2008 – and it also brings forward by six months the proposed start date to July 2005 in order to comply with the WTO ruling; this starting point has subsequently been brought forward even further, notionally to assist the countries worst affected by the Indian Ocean tsunami.

Among the key reform objectives foreseen in the July Communication are to make the GSP:

- ◆ stable, predictable, objective and simple;
- ◆ targeted on the countries that most need it, such as the LDCs and the most vulnerable developing countries (small economies, land-locked countries, small island states, and low-income countries) as well as the countries that would need preferences most after the Multifibre Arrangement (MFA) textile-quota system comes to an end in December 2004;
- ◆ supportive of regional co-operation between developing countries.

Further, argues the July Communication, the GSP must strike the right balance between development through trade and through industrialisation via origin rules that reflect the balance but are less strict than at present. It should assist countries to attain a level of competitiveness that could make them self-supporting economically and full partners in international trade.

This can be done by maintaining and improving the Community offer. The accession to the Community of ten new Member States has already improved substantially the value of the GSP, but the July Communication also considers extending the GSP to cover new products and to reclassify others from the sensitive to the non-sensitive category. Preferential margins are to be at least maintained.

One way for the GSP to focus on the countries most in need is via graduation. The July Communication argues that certain beneficiaries should be graduated for the groups of products in which they are most competitive. Given the high level of competitiveness, there is no further justification for a continuation of preferential tariff treatment.

## 4.2 Weighing up the changes

The July Communication presented a balance of changes, such as limiting preferences to the most competitive states whilst extending and deepening preferences to the remainder. But it did not provide the details needed by observers to weigh up the partly offsetting reforms and to determine whether or not the 'balance' was to their liking.

The draft Regulation has provided these details for the first period of implementation, but not for the second. Table 1 lists the main areas of change proposed in the July Communication and summarises the relevant changes in the draft Regulation. The following three sections then review the details.

**Table 1. The objectives of GSP reform**

Objective (as stated in July Communication <sup>a</sup> )	Extent of change (in draft Regulation <sup>b</sup> )
Improved stability and predictability	<ul style="list-style-type: none"> <li>• Standard GSP is both stable and predictable to 2008</li> <li>• Incidence of special incentives unclear</li> <li>• Substantial uncertainty post 2008</li> </ul>
Improved objectivity	<ul style="list-style-type: none"> <li>• The criteria for graduation have been changed, but are neither more nor less objective than the criteria replaced</li> <li>• Criteria for special incentives more objective than before</li> </ul>
Simplification	Number of regimes reduced
Targeted on: LDCs Small economies Land-locked countries Small island states Low-income states  MFA-affected	No change Potential availability of GSP+ <sup>c</sup> Potential availability of GSP+ <sup>c</sup> Potential availability of GSP+ <sup>c</sup> Potential availability of GSP+ <sup>c</sup> (but not for India, which is excluded <i>a priori</i> ) Potential availability of GSP+ <sup>c</sup>
Rules of origin change: Form Substance Procedures	No change No change No change
Extending product coverage	243 new items (of which 151 fish/fisheries) <sup>d</sup>
Reclassification of sensitive items	None
<i>Notes:</i> (a) CEC 2004a. (b) CEC 2004b. (c) All countries have been eligible for the special labour and environmental incentives incorporated into the GSP in the 1990s, but the margin of preference under the proposed GSP+ is more substantial, and the product coverage broader. (d) General Secretariat of the Council 2004. Four of the items on the list (two in HS 190420 and two in 210610) do not, however, appear in Annex II to the draft Regulation, and 27 are covered only under GSP+.	

There are two areas of major uncertainty. These affect not only achievement of the objective of improved stability and predictability but also assessment of the new GSP's likely impact. One concerns the number of countries that will apply for the special incentives and meet the EU's criteria. Whilst Table 1 recognises the potential importance of GSP+ for the countries identified in the July Communication for targeting, most other developing countries would

also be eligible. Wide usage of special incentives could transform the GSP's impact (see Section 6); modest take-up could reduce its trade effects. There is also a question mark over whether the regime would survive a WTO challenge.

The other uncertainty is over what will happen in the 2009–15 period. Neither the July Communication nor the draft Regulation specifies in sufficient detail, for example, how the graduation mechanism will be applied. As the 2001 reform demonstrates, 'mid-term reviews' can be substantial. Hence, while the outlook to 2008 is stable and predictable, any exporters requiring an investment pay-back period of over three years may view the regime as very unpredictable.

Moreover, the ACP states will find no guidance in the draft Regulation on the likely impact of not joining EPAs. Part B returns to this issue.

## 5 Graduation

The graduation formula in the new GSP will replace that in the old (see Box 2). So there will be winners (countries that are reintegrated into the GSP) as well as losers (countries that are graduated anew). And, of course, for some countries there will be no major change: they are currently graduated and will remain graduated.<sup>7</sup>

### 5.1 Winners and losers to 2008

The draft Regulation indicates which countries will be graduated for which sections on the first application of a new formula (Table 2). Graduation from a section applies to any country which accounts, on average over three consecutive years, for more than 15 percent (or 12.5 percent for Section XI, textiles and clothing) of the total value of covered imports within that section. Table 2 lists them and shows how the new regime will compare with the *status quo*.

The absolute 'losers' (countries not currently graduated that will be under the new regime) are listed in column 4. There are not very many of them. Only six of the 19 Harmonised System (HS) sections<sup>8</sup> would see any countries graduated out for the first time. China is graduated out of four sections which, between them, cover all wood and pulp, plus jewellery and vehicles. India is graduated out for jewellery, Algeria for mineral products and Russia for base metals. The section that sees the greatest 'first-time graduation' is vehicles. No fewer than three significant sources of EU imports (Thailand, South Africa and China) are graduated out.

#### Box 3. Types of graduation

'Old graduation' is what applies at present through the application of the formula in the current GSP Regulation linking market share, level of development and specialisation. Countries that fall foul are graduated out for a variable range of products: in some cases a single Harmonised System (HS) chapter; in others, two or more chapters. For example, Brazil is graduated out *inter alia* for GSP Sector VI, which is Chapter 9 of the HS (coffee, tea, etc.) while China is graduated out *inter alia* for Sector XXVII, which covers all of Chapters 74–83 plus eight 6- or 8-digit items within HS 7202 plus 7217, 7223, and 7323–7326.

The second is **exclusion**. A country which is otherwise eligible for the GSP is simply excluded for some products. Unlike 'old graduation' this is not related to any stated criterion and hence will not be reversed if the criterion no longer applies. South Africa, for example, is simply excluded from the GSP for iron and steel and Greenland is excluded for fisheries.

Third, there is '**new graduation**'. This is the application in future of the formula that has been proposed by the Commission and which is the central concern of this study.

<sup>7</sup> Since the old graduation applies to different product groups from the new graduation there could be some change even for this group (if the new graduation excludes a wider range of products than did the old).

<sup>8</sup> Although the HS is divided into 21 sections, two – Sections XIX (arms and armaments) and XXI (works of art) – contain no items covered by the GSP.

**Table 2. The effects of the new graduation formula**

HS		Brief description	Change from <i>status quo</i>		Remain graduated <sup>a</sup>
Section	Chapter		Graduated for the first time	Reintegrated <sup>b</sup>	
1	2	3	4	5	6
I	1-5	Live animals; animal products	—	Argentina, Brazil, China, Thailand, Uruguay	—
II	6-14	Vegetable products	—	Brazil, Chile, China, Costa Rica, Ukraine	—
III	15	Animal or vegetable fats and oils and their cleavage products	—	Philippines	Indonesia, Malaysia
IV	16-24	Prepared foodstuffs; beverages; tobacco	—	Mexico, Thailand	Brazil
V	25-27	Mineral products	Algeria	Kuwait, Libya, Russia, Saudi Arabia	—
VI	28-38	Products of the chemical or allied industries	—	Belarus, Chile, Mexico, Russia, Ukraine	China (HS 28-38 excl. 31)
VII	39-40	Plastics and rubber and articles thereof	—	Malaysia, Thailand	China
VIII	41-43	Raw hides and skins, leather, furskins and articles thereof	—	Argentina, Brazil, India, Pakistan, Thailand	China (HS 42-3)
IX	44-46	Wood and articles thereof	China	Malaysia	Brazil, Indonesia
X	47-49	Pulp of wood or of other fibrous cellulosic material	China	Brazil	—
XI	50-63	Textiles and textile articles	—	India, Macao, Mauritius, Pakistan	China (HS 61-3)
XII	64-67	Footwear, headgear, umbrellas etc.	—	Brazil, Indonesia, Thailand	China
XIII	68-70	Articles of stone, plaster, cement asbestos, mica or similar	—	Mexico	China
XIV	71	Precious or semi-precious stones; precious metals and articles thereof	China, India	Brunei	Thailand
XV	72-83	Base metals and articles thereof	Russia	Brazil, Mexico	China
XVI	84-85	Machinery and mechanical appliances; electrical equipment	—	Malaysia, Thailand	China
XVII	86-89	Vehicles, aircraft, vessels and associated equipment	Thailand, South Africa, China	—	—
XVIII	90-92	Precision instruments; clocks; musical instruments	—	—	China
XX	94-96	Miscellaneous manufactured articles	—	—	China

*Note:*

(a) Countries shown in this column may not currently be graduated from as broad a range of items as they will be under the draft Regulation. This is because the 33 sectors from which countries may currently be graduated are reduced in the draft Regulation to the 21 HS sections. In most cases, therefore, the HS sections are broader than the current sectors. Where this is the case for countries in this column, the HS Chapters from which they are currently graduated are shown in brackets.

(b) For the reason given in (a), countries shown in this column are not necessarily currently graduated for *all* items in the relevant HS section.

Source: CEC 2004b, and information received subsequently.

There are significantly more ‘winners’ (countries currently subject to old graduation that will not be caught by new graduation). Listed in column 5, they include three of the countries most affected by the tsunami. The revenue these countries will gain as a result of paying GSP rather than MFN tariffs is equivalent to between one-fifth and one-third of one percent of their exports to the EU.

Brazil and Thailand regain their rights to the GSP on the largest number of products – in six sections apiece. Mexico does so on four, Malaysia on three and Argentina, Chile, China, India, Pakistan, Russia and Ukraine on two apiece.



China remains graduated out for ten sectors, three of which do not overlap exactly with the product scope of its old graduation.<sup>9</sup> Brazil and Indonesia remain graduated on two sections (which correspond exactly with their old graduation), whilst Malaysia, and Thailand remain graduated out in just one.

## 5.2 What happens in 2008?

The draft Regulation lists all the graduation that will be implemented before 2008, but what about after? Presumably the graduation exercise will be repeated (or else countries will begin to exceed the import share thresholds yet not be graduated). But against which imports will the share be calculated? The answer is of potential importance to the ACP. Clearly, graduation affects ACP exporters' competitive position by altering the terms on which other suppliers enter the EU market. It is also possible that any ACP state might be graduated in future – which would, at a stroke, make the GSP an inadequate alternative to EPAs.

It would be logical to calculate each state's share of eligible imports for each section (i.e. to exclude from the denominator imports from countries that have been graduated this time). But doing this tends automatically to push some countries above the threshold (even if their exports have not grown relative to those of the others). Given sufficient time, eventually all countries could be graduated as a result of this simple arithmetic process! How might this affect the ACP?

If the graduation exercise were undertaken in 2008 on the basis of the current 15 and 12.5 percent thresholds and in relation to eligible imports, and if the eligible countries retained their 2003 relative trade shares, an additional 23 country/sector graduations would occur. This is over twice the number that will be graduated for the first time in 2005, but it includes no ACP states. The affected countries would be India (in four sections), Russia and South Africa (in three), Indonesia, Thailand and United Arab Emirates (in two), plus Argentina, Brazil, Malaysia, Mexico, Philippines, Saudi Arabia and Ukraine. In addition, of course, there would be 'genuine' graduations, i.e. the removal of countries whose exports had increased relative to their peers'.

One way to avoid this would be to use covered rather than eligible imports in the exercise. This would be possible, and would avoid any 'graduation creep' from this source – but not from another. The other potential source arises from the Commission's intention to remove from the GSP countries with bilateral or regional trade agreements with the EU that provide equally or more favourable market access. Since these countries would no longer be listed in the GSP, they would not contribute to covered imports.

This reform is presented as a sensible 'tidying up' exercise but, of course, it is also a move away from the creation of a single, universal umbrella for EU trade policy towards developing countries. The draft Regulation does not remove any countries on this criterion for the period to 2008. This is presumably because even those agreements that foresee more favourable market access are still in their implementation period; they will be more favourable than the GSP only once fully implemented. This is the case, for example, with the Trade, Development and Co-operation Agreement (TDCA) with South Africa. South African exports of roasted groundnuts to the EU under the TDCA enter duty free, whereas the GSP rate is 7.2 percent; some South African car bumpers, on the other hand, currently pay a tariff of 2.2 percent under the TDCA even though the GSP rate is zero.

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<sup>9</sup> The HS chapters from which it is now newly graduated (because they were not covered by the old graduation) are 31 (fertilisers), 41 (leather, raw hides and skins) and 50–60 (textiles).

Because no country has been removed this time, the draft Regulation provides no guidance on how it might be done and whether any ACP state would be affected directly. This gives rise to two queries: one concerning apparent inconsistencies between the July Communication and the draft Regulation (see Box 3) and the other on how the graduation formula will be applied from 2008.

Since countries that are no longer in the GSP cannot contribute, by definition, to covered imports, an unchanged graduation formula would apply the 15 and 12.5 percent thresholds to a smaller basket of imports. Evidently, some GSP beneficiaries that currently fall below the threshold will in 2008 be above, even if their exports have not increased relatively.

Any attempt to identify such effects must be speculative. Not only is it unclear which countries might be deemed to have 'GSP-equivalent' accords, but who knows which states' exports will increase fastest. None the less, Table 3 provides an illustration of the possible implications. It shows the extra countries that would be graduated from the regime after 2008 if all the main countries which currently have a bilateral or regional trade agreement with the EU were removed from the GSP.

### Box 2. Future exclusions from the GSP

Will countries be removed from the GSP only if their specific agreement has become as favourable as the GSP, or will their specific agreement be 'improved' up to GSP levels to facilitate their removal? The July Communication and the draft Regulation appear to say different things.

The draft Regulation would exclude an FTA member from the GSP 'if this agreement covers at least all the preferences provided by the present [GSP] scheme for this country' (preamble: para. 15). But the July Communication argues that, when making removals from the list, 'the Community *would of course ensure* that no country would lose as a result of this because GSP benefits for any particular product which formerly received GSP treatment should be consolidated into the FTA in question' (para. 6.3, emphasis added).

The difference could be critical to the negotiations on EPAs. It might imply, for example, that EPAs including LDCs must offer access to the EU for all members that is equivalent to EBA.

**Table 3. Countries vulnerable to graduation from 2009 due to beneficiary removal<sup>a</sup>**

HS		Brief description	New graduation in 2009
Section	Chapters		
I	1-5	Live animals; animal products	Argentina
II	6-14	Vegetable products	—
III	15	Animal or vegetable fats and oils and their cleavage products	—
IV	16-24	Prepared foodstuffs; beverages; tobacco	—
V	25-27	Mineral products	Russia, United Arab Emirates
VI	28-38	Products of the chemical or allied industries	Russia
VII	39-40	Plastics and rubber and articles thereof	—
VIII	41-43	Raw hides and skins, leather, furskins and articles thereof	India
IX	44-46	Wood and articles thereof	—
X	47-49	Pulp of wood or of other fibrous cellulosic material	—
XI	50-63	Textiles and textile articles	India
XII	64-67	Footwear, headgear, umbrellas etc.	—
XIII	68-70	Articles of stone, plaster, cement asbestos, mica or similar	—
XIV	71	Precious or semi-precious stones; precious metals and articles thereof	—
XV	72-83	Base metals and articles thereof	—
XVI	84-85	Machinery and mechanical appliances; electrical equipment	—
XVII	86-89	Vehicles, aircraft, vessels and associated equipment	—
XVIII	90-92	Precision instruments; clocks; musical instruments	—
XX	94-96	Miscellaneous manufactured articles	—

Note:

(a) The table covers only 'main countries', i.e. those that are among the top 15 sources of GSP imports in any section. It is based on the values of covered imports in 2003 according to Commission figures with those for countries with bilateral/regional agreements with the EU removed (the latter having been identified from UK Tariff).

Six new country/sector graduations occur (compared with nine first-time graduations in 2005) but, again, there are no ACP graduates. This is just as a result of this ‘tidying up’ exercise, since no other changes have been assumed.

As with the query over the use of covered or eligible imports as the denominator, it is perfectly possible for the EU to avoid this ‘graduation creep’. It could decide simply to maintain the denominator as at present or to raise the 15 and 12.5 percent thresholds proportionately. But in the absence of any guidance, the effect of the draft Regulation must be to create uncertainty – not least in the minds of potential investors.

## 6 GSP+

### 6.1 What it is – and who is eligible

The proposed GSP+ (special incentive arrangements for sustainable development and good governance) replaces the current scheme’s three types of special arrangement relating to labour rights, protection of the environment and illegal drug production and trafficking. It offers substantially improved preferences over the Standard GSP, and covers a broader range of products. For those countries included in the special arrangements, simple *ad valorem* or specific duties will be suspended on all products covered by the GSP. For items subject to an *ad valorem* and a specific duty, the *ad valorem* element will be suspended. Duty suspensions will not apply to sections from which any given country has been graduated.

In order to benefit from these additional preferences, a country must:

- ◆ have ratified and effectively implemented:
  - 16 core human and labour rights UN/ILO Conventions; and
  - at least seven (of 11) conventions related to environment and governance principles;
- ◆ commit itself to ratify and effectively implement the remainder of the conventions;
- ◆ undertake to maintain the ratification of the conventions and their implementation, and to accept regular monitoring and review of its implementation record;
- ◆ be classified as ‘vulnerable’ (see below).

Beneficiaries must have ratified all 27 conventions by 31 December 2008.

### 6.2 Limitations on GSP+

GSP+ will not be available to every developing country that ratifies all the agreements. Countries must also satisfy additional criteria related to the value of their exports set out in Article 9.2(a) and (b) of the draft Regulation. These specify that a country is vulnerable only if it meets both of two criteria:<sup>10</sup>

- ◆ **a diversification criterion** – the country is not classified as high income *and* the five largest HS sections account for over 75 percent of its covered imports (Article 9.2 (a)); and

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<sup>10</sup> The descriptive names have been coined by the authors of this paper.

- ◆ **a smallness criterion** – the country’s covered imports represent less than 1 percent of the EU’s total covered imports (Article 9.2 (b)).<sup>11</sup>

Two questions are whether the GSP+ criteria are ‘development friendly’ and whether they would sustain a WTO challenge. Table 4 lists the countries that would not be eligible for the special incentive arrangements – even if they ratified and implemented all the stipulated conventions – because they do not meet either of the two criteria. There are no ACP states in the group.

Three of the excluded states – India, Pakistan and Vietnam – are classified by the World Bank as low-income countries; the July Communication identified low-income countries as one of the categories on which the GSP should focus. Twelve of the twenty-one have *per capita* incomes of \$2,000 or less, which means that 30 richer developing countries will be eligible for GSP+ (if they sign up to the conventions). Five GSP beneficiary countries are richer than all of the countries listed in Table 4; such statistics might be relevant to any WTO challenge (see Box 4). And all of the tsunami-affected states other than Sri Lanka are included in the table.

### 6.3 The potential effects

The impact of GSP+ *could* be very substantial, but only if a high proportion of the countries not listed in Table 4 are accepted. The new regime replaces two very different types of arrangement.

- ◆ **Deep but geographically restricted preferences** under the special anti-narcotics regime that provided substantial additional preferences to nominated countries. They have been well used by the beneficiaries.
- ◆ **Shallow but geographically unrestricted preferences** under the special regimes for protection of labour rights and the environment that provided modest additional preferences and have not been much used. Only two countries (Moldova

**Table 4. *A priori* exclusions from GSP+**

Country <sup>a</sup>	GNI per capita 2003 (US\$) <sup>b</sup>
Argentina	4,220
Brazil	2,860
China	960
Egypt, Arab Rep.	1,470
India	470
Indonesia	710
Jordan	1,760
Lebanon	3,900
Malaysia	3,550
Mexico	5,940
Morocco	1,170
Pakistan	420
Philippines	1,030
Russian Federation	2,130
Saudi Arabia	8,530
South Africa	2,630
Thailand	2,000
Tunisia	1,990
Ukraine	780
United Arab Emirates	n/a
Vietnam	430

Sources: Data provided by the Commission; World Bank.

#### Box 1. The WTO dimension

The unfavourable WTO ruling on the special ‘anti-narcotics’ preferences in the current GSP has contributed to the design of the GSP+ (WTO 2004a). Importantly, the Appellate Body ruled against a claim by India that the GSP must offer ‘identical’ tariff preferences to all beneficiaries. It confirmed that different preferences may be given provided that the difference responds ‘to a widely-recognized “development, financial [or] trade need”...’ (para. 164). But it also found that the justification given for the anti-narcotics regime failed to satisfy this criterion.

The Commission argues that the eligibility conditions for GSP+ do satisfy the criterion. But it remains to be seen whether the *a priori* exclusion of the countries listed in Table 5 would lay the scheme open to a further WTO challenge.

The Appellate Body gives an example of the ‘objective standard’ that could justify differential treatment for sub-groups within the GSP. The required ‘[b]road-based recognition of a particular need...’ that would justify such differentiation is exemplified by recognition ‘set out in the WTO Agreement or in multilateral instruments adopted by international organizations...’ (para. 163). Whilst the conventions that eligible countries must apply appear plausibly to have such recognition, the same does not appear to apply to the diversification and smallness criteria.

<sup>11</sup> To be calculated using the data available on 1 September 2004 for an average over three consecutive years.

and Sri Lanka) currently benefit under the former, and none under the latter. Two possible (linked) reasons for the low take-up are that: first, countries have been unwilling to accept the conditions (which are in areas considered contentious in the WTO), especially, second, when the gains from so doing are modest.

Will the applications for GSP+ be more substantial than for the labour/environment protection schemes? And will the applications succeed? If the answer is 'yes', the impact could be profound. GSP+ beneficiaries will be among the EU's 'most preferred' group. There could be three types of effect.

- ◆ **Trade creation.** The number of countries and products facing no tariff barriers in the EU would increase, resulting in more trade.
- ◆ **Trade diversion.** Countries elevated from the 'middle' to the 'most preferred' group would find that they have a competitive advantage over those that remain in the middle group and that they no longer face a competitive disadvantage compared with those that are already in the 'most preferred' group. They can expect to acquire some market share from both types of competitor. By the same token, if some current beneficiaries of the anti-narcotics regimes fail to obtain GSP+ they will fall from the 'most preferred' to the 'middle' group – and lose markets.
- ◆ **Rules of origin.** If take-up were widespread, the origin rules would become a less important determinant of trade. The more countries that have identical access terms to the EU market, the less significant it is where the product 'originated'. If, for example, a manufacturer in Pakistan uses inputs from Malaysia, the origin rules will determine whether or not the EU classifies the resulting good as Pakistani or Malaysian. But if the tariff for both Pakistan and Malaysia is 0 percent, the classification has no commercial importance. This is an important point for the ACP, taken up in Part B.

The relative scale of these effects will be determined by the extent of GSP+ uptake. If many countries become eligible, the trade creation and rules of origin effects will predominate. If few countries become eligible, then trade diversion will be more marked, especially if beneficiaries of the anti-narcotics regime fail to obtain GSP+.

The two changes that appear of greatest potential importance to the ACP are those that foresee a focusing of GSP benefits and their enhancement for certain states. Graduation is the primary mechanism for 'focusing the GSP'. The GSP+ is the main vehicle for enhancement.

## Part B. Making the GSP Cotonou Equivalent

### 7 Scope and methodology

As the report of the WTO Appellate Body on the EU–India dispute makes clear (Box 4), differentiation within the GSP is acceptable provided it reflects ‘a widely-recognized “development, financial [or] trade need”...’. How could the GSP be differentiated or otherwise changed? There are three main options, of which two are researched in this paper. The option that is not covered is to create a special tranche of the GSP just for the ACP.<sup>12</sup> The reason this option is not researched in this report is that the problems of feasibility that would flow from a special ‘ACP tranche’ of the GSP do not arise in any way from technical concerns about the product composition and preferential treatment of the regime. This is self-evident: the regime would need to be available to all ACP states not entering EPAs and would offer tariff treatment at least as good as that under Cotonou. Rather, questions over feasibility would be concerned with the WTO acceptability of such a move. This is an issue that falls outside the current study.

The second option is to integrate the ACP into GSP+ and to alter its provisions (mainly through adding new products) so that it offers Cotonou equivalence in relation to tariffs. The third option is to improve the Standard GSP to bring it to the level of Cotonou.

This report identifies which products would need to be brought into the GSP net, what changes would need to be made to their tariff treatment, and which non-ACP states would benefit most. This last point is necessary to assess how far the changes would erode ACP preferences.

And therein lies an important methodological point. There is the world of commerce – and there is the world of trade policy and statistics. The latter provides a mirror of the former, but a distorted one. These distortions need to be understood. This report, based on an analysis of trade statistics and of proposed changes to public policy, helps to identify the framework within which trade takes place. But there are other factors – that will be known to active traders – that also have a bearing (often very strong) on who sells what to whom. Two clear limitations of a study such as this need to be understood.

First, it can deal only with the products that the ACP actually exports to a significant extent at the present time. Only for these is it possible to identify competitors – and the competitors’ terms of access to the EU market. However, if there are products which the ACP expects to export in the future, and these can be specified, an analogous exercise could be done for them as well.

Second, the report identifies the ACP’s ‘competitors’: whether or not the countries are really competitors with the ACP depends on a range of other market-related factors (such as quality, delivery times, niche markets, national markets). It is beyond the scope of this study to identify which areas of competition exist within these products. By the same token, there may actually be competition between, say, ACP exports of preserved pineapples and another country’s exports of fresh pineapples, or other preserved fruits. This type of market-related

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<sup>12</sup> The analysis contained in this part of the report is of relevance only to those ACP states – the non-least developed – which do not benefit from duty-free access to the EU under its EBA scheme (which will continue after the expiry of Cotonou). Thus, unless indicated otherwise, the use of the term ‘ACP’ refers only to the 36 non-LDC members of the group.

information is known by those engaged in the trade but cannot be judged from the trade statistics.

Moreover, for reasons of practicality the report considers only competitors that supply 10 percent or more of EU imports. It is assumed that these are the ones most likely to affect market prices. If a major exporter of beef such as Brazil or Argentina, for example, sees a duty cut their competitive response may well affect the prices available to all other suppliers. This generalised effect is less likely in the case of a country supplying only a few percent of EU imports. On the other hand, of course, they may be competing in precisely the niche market targeted by the ACP! For this reason, as well as others that become apparent, the report should be seen as a first step in assessing the feasibility of the GSP as a Cotonou equivalent.

## **8 Identifying the products**

A first, basic requirement for a GSP providing treatment equal to Cotonou is that it cover all of the products that the ACP currently export and that receive preference under Cotonou. Although a necessary condition, it is not sufficient. Attention also needs to be given to the relative treatment of the ACP and their competitors. But it is an obvious first place to start.

This section identifies the products for which the GSP at present and the proposed new GSP provide less favourable treatment than does Cotonou. The message to be conveyed is that the number of products involved is not huge – and hence it may be feasible to extend the GSP appropriately. On the other hand, neither is it minuscule nor, as might be predicted, uncontentious. So there are certainly obstacles to be overcome.

### **8.1 Current ACP exports to the EU**

Table 5 provides summary details of the range of products that the ACP currently export in other than insignificant amounts to the EU and their treatment under the GSP. The table was compiled by analysing EU import statistics twice: once to pick up products that are relatively important to any ACP state, and the second time to identify any overlooked item that is exported to a substantial value.

The first ‘trawl’ identified any item accounting for 5 percent or more of an individual ACP country’s total exports to the EU in 2003. The choice of a criterion linked to the relative share of a country’s exports ensured that the study did not overlook any items that are important only for a very small ACP state (and therefore are exported in relatively small values). So, for example, the analysis included frozen herring (Combined Nomenclature (CN) code 03049022) which was exported only by Niue, and only to a value of \$2,000 – but which accounted for 40 percent of Niue’s total exports to the EU in 2003. This trawl identified 89 items.

The problem with this approach is that it overlooks some of the items that are exported by the larger ACP states. Five percent of EU imports from, for example, Côte d’Ivoire is \$143.4 million; we did not wish to exclude all imports from Côte d’Ivoire of less than this amount. The second trawl, therefore, identified items which are exported in aggregate by the 36 ACP countries<sup>13</sup> to a value of \$10 million or more. This added a further 105 items.

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<sup>13</sup> The 36 countries are: Antigua and Barbuda, Bahamas, Barbados, Belize, Botswana, Cameroon, Congo Republic, Cook Islands, Côte d’Ivoire, Dominica, Dominican Republic, Federation of Micronesia, Fiji, Gabon, Ghana, Grenada, Guyana, Jamaica, Kenya, Marshall Islands, Mauritius, Namibia, Nauru, Nigeria, Niue,

Table 5 presents the findings on the resulting 194 items which the EU imported from the ACP to a value of \$22 billion in 2003. Since the total imports of the EU from these 36 states in 2003 was only \$23.3 billion, it can be seen that the two trawls have picked up between them items that account for 94 percent by value of European imports from the ACP group other than the least developed.

**Table 5. Non-LDC ACP exports to EU, 2003**

	Value (\$ bn)	Share
<b>Total</b>	<b>23.3</b>	
'Significant' items <sup>a</sup>	22.0	100.0%
Of which:		
MFN zero	15.4	70.2%
Standard GSP zero	1.0	4.7%
Standard GSP not zero (GSP+ zero <sup>b</sup> )	3.4	15.7%
Not covered by GSP or GSP+	2.1	9.5%
<i>Note:</i>		
(a) Any item accounting for 5 percent or more of any individual non-LDC ACP country's total exports to the EU in 2003 (89 items) or not meeting this criterion, but which the 36 non-LDC ACP countries in aggregate exported to the EU to a value of \$10 million or more in 2003 (105 items).		
(b) Other than 4 items – see footnote 14.		
<i>Source:</i> UNCTAD TRAINS, January 2005.		

Seventy percent of these imports came in duty free because the EU's MFN tariff is set at zero. Preferences are neither given nor possible on such products. Just under 5 percent were already accorded duty-free access under the GSP.

Hence, the end of the Cotonou Agreement would leave unchanged 75 percent or so of ACP exports because they are in items that either enter duty free under the MFN or would do so under the Standard GSP. The purpose of this report is to consider the position of the remaining 25 percent. These are referred to in the rest of the report as 'GSP-relevant' items.

Just under two-thirds of the GSP-relevant items are included in the Standard GSP but are not accorded duty-free access. All but four are, however, given duty-free access under the proposed new GSP+.<sup>14</sup> All of the remainder are items that are not covered by the Standard GSP or GSP+, and so would have to be introduced into the scheme for it to provide an adequate alternative to Cotonou.

## 8.2 Potential ACP exports to the EU

Table 5 identifies those products currently exported by ACP states that are imported from the ACP and would face positive tariffs under the GSP, but what of products that the ACP do not currently export to the EU? One of the attractions of the Cotonou Agreement is that it is largely a 'negative list' preference agreement. Except in the case of items covered by the Common Agricultural Policy (CAP) it offers duty-free access for all ACP products that meet the rules of origin. This means that if an ACP country develops a new line of export it can be certain (so long as the item is not covered by the CAP) that it will enjoy duty-free access to the EU. The GSP, by contrast, is a positive list: it specifies precisely which products are covered, and any item that is not mentioned is excluded.

Since it is not possible to identify all the products that the ACP might export in future, a flavour of the range of items that might emerge in their trade with the EU has been obtained by looking at their exports to non-EU markets. In order to keep the task within reasonable limits, a slightly different methodology was employed from that used for Table 5. Instead of identifying all imports that met the two significance criteria and then establishing the EU's tariff treatment, the order of business was reversed. First we produced a list of all the items that are not covered by the GSP, and then we interrogated UNCTAD's TRAINS database to

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Palau, Papua New Guinea, Seychelles, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname, Swaziland, Tonga, Trinidad and Tobago, Zimbabwe.

<sup>14</sup> The four exceptions to duty-free access under GSP+ are chocolate (for which the *ad valorem* duty is suspended but the agricultural component (AC) remains), and three shrimp items (for which the GSP+ tariff is 3.6 percent).



identify all ACP exports of these non-covered items to the world<sup>15</sup> in 2003. The analysis of exports to non-EU markets has necessarily had to be undertaken at the HS 6-digit level. This is because the HS is common only to 6 digits. It is not possible to identify which US or Japanese imports from ACP states fall into each of the EU's CN 8-digit categories.

This exercise identified an additional 10 items (at the HS6 sub-heading level). These are products of which the ACP had exports of at least \$5 million to the world and which had not been thrown up in the trawl of EU import statistics (either because they were not exported at all to the EU, or because their 8-digit components failed to meet either of the criteria).

Taking the two exercises together, Table 6 provides information on the full list of current ACP exports (to the EU and elsewhere) that are not given duty-free access to the EU under the GSP. For reasons of practicality (there are 85 CN8-digit items derived from EU import statistics and 10 HS6-digit items derived from other countries' import statistics), the table aggregates similar products. Hence, for example, the first row is for a single 8-digit item (fresh or chilled boneless beef) because this is the only GSP-relevant meat item within this HS4 heading that ACP countries export either to the EU or elsewhere. The third row, though, provides data only for the HS4 digit heading fresh or chilled fish, for which there are two separate 8-digit EU imports (with different tariffs).

Columns 4–6 of the table indicate the way in which the GSP is currently deficient as a substitute for Cotonou. Column 4 shows the cases where the product is excluded from the Standard GSP altogether. Column 5 covers products that are included in the Standard GSP but do not receive duty-free access. Finally, Column 6 lists for every item in the table the coverage proposed under GSP+.

**Table 6. The main products for attention**

Product	# observations <sup>a</sup>	Description	Standard GSP		GSP+ <sup>b,c</sup>
			Excluded <sup>b</sup>	Positive tariff <sup>b</sup>	
02013000	1	fresh or chilled bovine meat, boneless	ø		
0202	1	boneless, frozen meat of bovine animals	ø		
0302	2	fish, fresh or chilled		5.2 or 11.5	0
0303	3	frozen fish		5.2 or 11.5	0
0304	4	fish fillets and other fish meat, whether or not minced, fresh, chilled or frozen		0, 4, 5.5 or 11.5	0
0306	4	crustaceans		4.2 or 4.3	3.6 or 0
0307	3	molluscs,		2.8 or 3.8	0
0603	2	cut flowers and flower buds of a kind suitable for bouquets or for ornamental purposes		5 or 8.5	0
0708	2	leguminous vegetables, shelled or unshelled, fresh or chilled		4.5-10.1	0
07099090	1	fresh or chilled vegetables n.e.s.		8.9	0
08030019	1	bananas, fresh (excl. plantains)	ø		
0804	2	dates, figs, pineapples, avocados, guavas, mangoes and mangosteens, fresh or dried		0-2.3	0
0805	2	citrus fruit, fresh or dried	ø		
ex 08061010	1	fresh table grapes	(ø) <sup>d</sup>		
09050000	1	vanilla		2.1	0
10062098	1	long grain husked -brown- rice, length/width ratio >=3 (excl. parboiled)	ø		
1101	1	wheat or meslin flour	ø		
1107	1	malt	ø		
15119099	1	palm oil and its liquid fractions, whether or not refined, but not chemically modified		3.1	0

<sup>15</sup> The 'world' being the 72 countries which have so far reported their 2003 imports to UNCTAD.

Product	# observations <sup>a</sup>	Description	Standard GSP		GSP+ <sup>b c</sup>
			Excluded <sup>b</sup>	Positive tariff <sup>b</sup>	
1513	2	coconut 'copra', palm kernel or babassu oil and fractions thereof, whether or not refined, but not chemically modified		2.2	0
1604	3	prepared or preserved tunas, skipjack and atlantic bonito, whole or in pieces (excl. minced)		20.5	0
1701	3	cane or beet sugar and chemically pure sucrose in solid form	ö		
1703	2	molasses resulting from the extraction or refining of sugar	ö		
1803	2	cocoa paste, whether or not defatted		6.1	0
18040000	1	cocoa butter, fat and oil		4.2	0
18050000	1	cocoa powder, not containing added sugar or other sweetening matter		2.8	0
18062010	1	chocolate and other food preparations containing cocoa		4.8% + AC max 18.7%	0 + AC
20055900	1	unshelled beans 'vigna spp., phaseolus spp.', prepared or preserved otherwise than by vinegar or acetic acid		15.7	0
2008	2	pineapples, prepared or preserved, whether or not containing added sugar/other sweetening matter/spirit, nes.		14.9 or 15.7	0
20094930	1	pineapple juice, unfermented		11.7	0
21011111	1	solid extracts, essences and concentrates of coffee		3.1	0
2208	2	undenatured ethyl alcohol	ö		
2302	1	bran, sharps and other residues of wheat	ö		
ex 2309	1	preparations of a kind used in animal feed	(ö) <sup>e</sup>		
2401	3	unmanufactured tobacco; tobacco refuse		3.9% max 56 €/100 kg or 14.9% max 24 €/100kg	0
24021000	1	cigars, cheroots and cigarillos containing tobacco		9.1	0
2501	1	salts, including table and denatured salt, and pure sodium chloride	ö		
28141000	1	anhydrous ammonia		2	0
28182000	1	aluminium oxide (other than artificial corundum)	ö		
29051100	1	methanol 'methyl alcohol'		2	0
29161220	1	ethylacrylate		3	0
29321200	1	2-furaldehyde 'furfuraldehyde'		3	0
39041000	1	polyvinyl chloride, in primary forms		3	0
41051010	1	skins of sheep or lambs, in the wet state 'incl. wet-blue', tanned, without wool on, unsplit	ö		
4105	1	skins of sheep or lambs, in the dry state 'crust', without wool on, whether or not split	ö		
4106	3	goat or kidskin leather, dehaired	ö		
4412	2	plywood, veneered wood and similar laminated wood		3.5 or 6.5	0
54025200	1	filament yarn of polyester, incl. monofilament of < 67 decitex, single, with a twist of > 50 turns per metre		3.2	0
61051000	1	men's or boys' shirts of cotton, knitted or crocheted		9.6	0
61061000	1	women's or girls' blouses, shirts and shirt-blouses of cotton, knitted or crocheted		9.6	0
61091000	1	t-shirts, singlets and other vests of cotton, knitted or crocheted		9.6	0
6110	5	jerseys, pullovers, cardigans, waistcoats and similar articles, knitted or crocheted		9.6	0
6203	2	men's or boys' suits, ensembles, jackets, blazers, trousers, bib and brace overalls, breeches and shorts		9.6	0
62046231	1	women's or girls' cotton denim trousers and breeches		9.6	0
62052000	1	men's or boys' shirts of cotton		9.6	0
62121090	1	brassieres of all types of textile materials, whether or not elasticated, incl. knitted or crocheted		5.2	0
76011000	1	aluminium, not alloyed, unwrought	ö		
79011100	1	unwrought zinc, non-alloy, containing by weight >= 99.99 % of zinc	ö		
7601	1	aluminium alloys, unwrought	ö		

Product	# observations <sup>a</sup>	Description	Standard GSP		GSP+ <sup>b,c</sup>
			Excluded <sup>b</sup>	Positive tariff <sup>b</sup>	
85299081	1	parts suitable for use solely or principally with television cameras, receivers of radio-telephonic/telegraphic signals, or for radio or television, n.e.s.		1.5	0
87032390	1	motor vehicles for transport of persons, with spark-ignition internal combustion reciprocating piston engine, cylinder capacity >1 500 but =<3 000cc		6.5	0

*Notes:*

(a) An observation = 1 CN8 item or 1 HS6 sub-heading.  
(b) Only exclusions and tariffs relating to the specific CN8 items (where known) included in any HS4 or HS6 headings shown are listed.  
(c) 'AC' = agricultural component.  
(d) There is GSP coverage from 1-31 January for Emperor variety and from 1 January to 20 July and 21 November to 31 December for other varieties.  
(e) There is GSP coverage for 4 out of c.16 8-digit components of this HS6 sub-heading. It is impossible to know from the trade statistics whether the items being exported are covered or not.  
*Sources:* UNCTAD TRAINS, January 2005; CEC 2004b; UK Tariff 2005.

Of the two options for achieving Cotonou equivalence investigated in this report, the simpler is if all ACP countries become eligible for the GSP+ and its product coverage is extended to include the 28 observations included in Table 6 that it does not cover. This approach would work if all ACP states achieved GSP+ eligibility.

If this did not happen – or was considered undesirable – then the Standard GSP would need to be improved in order to make it Cotonou equivalent. In addition to the requirement that the GSP be extended to include the 28 observations that are not covered by GSP+, all of the items would have to be given tariff treatment commensurate with that available under the Cotonou Agreement.

## 9 Preference erosion

A problem for the ACP is that a key advantage for them of Cotonou is that they are treated more favourably than some of their developing country competitors. Clearly, the EU has to take a more rounded view of the development attractions of lower tariffs than do the ACP and cannot simply agree to freeze current trade policy in order to maintain this margin of preference. Even a full extension of Cotonou into EPAs would not achieve the ACP objective of freezing preference margins.

Indeed, the extension of liberal access by the EU to a larger number of countries will enhance the economic impact of a broader GSP+. This enhancement could go further if the EU 'compensated' the ACP by providing new trade support measures. This could be in the form of positive assistance to improve ACP supply capacity and help countries meet EU technical and health requirements. It could also be via 'new preferences' in areas less subject to WTO challenge, such as short-term visas and work permits for service providers under modes 1 and 3.

The scale of these economic gains may be substantially larger than any to be obtained from reciprocity under EPAs. There is a likelihood that the requirement of WTO Article XXIV that a free trade area liberalise on 'substantially all' trade will be interpreted as requiring ACP states to remove tariffs on only about 80 percent of their imports from the EU. This will allow them to continue to shelter many sensitive items. And even for those items that will be liberalised, implementation will take place over a transition period of at least 12 years from 2008.

At the same time, though, some account needs to be taken of the extent to which the task of improving the GSP solely for the purpose of making it Cotonou equivalent would automatically erode the gains that the ACP might hope to achieve from this process. It would not be sensible to use considerable political capital pressing for an extension of the Standard GSP if, in so doing, it meant that the ACP saw their preference entirely eroded.

Evidently, the change to the GSP that would provoke the smallest amount of *additional* preference erosion would be the extension of GSP+ to cover all ACP GSP-relevant exports. The ACP would share their preferential access with all other GSP+ beneficiaries – but so they will regardless of what happens under Cotonou for all products that are not added to the scheme specifically to make it Cotonou equivalent.

If this is the ‘least eroding’ approach, then the ‘most eroding’ avenue would be to extend the Standard GSP. To the extent that this is successful it will extend to countries excluded from GSP+ the same benefits as Cotonou currently provides to the ACP (unless such countries are graduated out). Because of their different implications both in terms of political feasibility and ‘preference erodability’, the two approaches of extending GSP+ or the Standard GSP are dealt with in turn.

## 9.1 Extending GSP+

The objective of this section is to identify the products for which inclusion in the GSP+ would result in an erosion of ACP preferences that has not occurred, and will not occur, anyway. This requires us to identify the competitor countries that would benefit from a favourable change in their access to the EU market as a result of the extension of GSP+. No LDC will fall into this category; EBA provides all LDCs with virtually free access regardless of what happens to GSP+. Nor *may* countries which have a bilateral agreement with the EU – if the agreement already provides duty-free access on the items in question (now or by the end of the implementation period) then the extension of GSP+ is irrelevant. A third group of countries that would be unaffected by an extension to GSP+ is those that are ineligible because they fail the ‘vulnerability’ test, because they are graduated out of the GSP for the relevant section, or because they are not GSP beneficiaries.

Table 7 summarises the preference erosion potential of extending GSP+ and provides a pointer to the next step of competitor identification. The shaded rows show products that were identified (at HS6) through analysing ACP exports to the ‘world’.

**Table 7. Extending GSP+: implications for preference erosion**

Product	Description	# ACP exporters to EU	Current non-LDC ACP treatment better, worse or same as main competitors <sup>a</sup>	Competitors eligible for GSP+
02013000	fresh or chilled bovine meat, boneless	4	Better	None
020230	boneless, frozen meat of bovine animals	5	Better	None
08030019	bananas, fresh (excl. plantains)	14	Better	All
08051030 <sup>b</sup>	fresh navels, navelines, navelates, salustianas, vernas, valencia lates, maltese, shamoutis, ovalis, trovita and hamlins	6	All three	None
08051050 <sup>b</sup>	fresh sweet oranges (excl. above)	5	All three	None
ex 08061010	fresh table grapes	3	All three	Some
10062098	long grain husked -brown- rice, length/width ratio >=3 (excl. parboiled)	3	Better	None
110100	wheat or meslin flour	0	No GSP competitors	
110710	malt	1	No GSP competitors	
17011110	raw cane sugar, for refining (excl. added flavouring or colouring)	13	No non-ACP competitors	

Product	Description	# ACP exporters to EU	Current non-LDC ACP treatment better, worse or same as main competitors <sup>a</sup>	Competitors eligible for GSP+
17011190	raw cane sugar (excl. for refining and added flavouring or colouring)	5	No non-ACP competitors	
170199	cane or beet sugar and chemically pure sucrose in solid form	6	No GSP competitors	
17031000	cane molasses resulting from the extraction or refining of sugar	3	Same	None
170390	beet molasses resulting from the extraction or refining of sugar	0	No GSP competitors	
22084051	rum with a content of volatile substances of $\geq 225$ g/hl of pure alcohol 'with a 10% tolerance', in containers holding $> 2$ l	7	No non-ACP competitors	
22084099	rum and tafia, of a value $\leq 2$ ecu/l of pure alcohol, in containers holding $> 2$ l	9	Better	All
230230	bran, sharps and other residues of wheat	1	Better	None
ex 230990	preparations of a kind used in animal feed	0	No GSP competitors	
250100	salts, including table and denatured salt, and pure sodium chloride	7	Same or worse	None
28182000	aluminium oxide (other than artificial corundum)	2	No non-ACP GSP competitors	
41051010	skins of sheep or lambs, in the wet state "incl. wet-blue", tanned, without wool on, unsplit	4	Same or better	Some
410530	skins of sheep or lambs, in the dry state 'crust', without wool on, whether or not split	1	No non-ACP competitors	
41062110	skins of goats or kids, in the wet state "incl. wet-blue", tanned, without wool on, unsplit	4	Same or better	None
41062190	skins of goats or kids, in the wet state "incl. wet-blue", tanned, without wool on, split	3	Better	None
41062290	hides and skins of goats or kids, in the dry state "crust", without wool on, whether or not split	3	Better	None
76011000	aluminium, not alloyed, unwrought	3	Same or better	None
760120	aluminium alloys, unwrought	3	No GSP competitors	
79011100	unwrought zinc, non-alloy, containing by weight $\geq 99.99$ % of zinc	1	No GSP competitors	
<p>Notes:</p> <p>(a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003. 'All three' in this column denotes that the ACP's treatment is potentially the same as, better or worse than its competitors' – according to the date of entry and entry price.</p> <p>(b) Both these codes now (2005) fall under CN 08051020.</p> <p>Sources: UNCTAD TRAINS, January 2005; UK Tariff 2005.</p>				

The table takes each of the items identified in Table 6 as being outside GSP+ and indicates the status of all non-ACP, non-LDC, GSP-beneficiary competitors which accounted for 10 percent or more of EU imports of the item in 2003. Column 5 is the critical one. It indicates whether or not one of these main competitors would be eligible for GSP+ if it were extended. When the column returns 'None' it means that GSP+ extension would not erode ACP preferences – at least in respect of the major competitors. In cases where the response is 'All' there will be full erosion, and where it is 'Some' it means that some competitors would benefit from GSP+ while others would not.

This approach of identifying the main sources of erosion does not work with sugar. The table indicates no non-ACP competitors. This is not because no developing country can export sugar competitively, but because none can export over the EU's high tariffs. Sugar is considered separately below.

Table 8 takes the products for which 'All' or 'Some' is returned in column 5 of Table 7, and provides further information on the identity of the main competitors and their treatment. There are four problem commodities in addition to sugar. Overwhelmingly the most important (in terms of the value of ACP exports and the number of exporters) is bananas – for which the issues and problems are well known. The key issue is whether or not the extension

of the GSP will have any additional effects on the commercial viability of banana exports from the Caribbean on the one hand and West Africa on the other, over and above the changes that are expected to occur following the EU's WTO-induced changes to the banana regime and the lifting of all import restrictions from LDCs from next year.

Similar considerations also apply to rum, which is the next most important item in the table (in both value and number of exporters). Any change to the GSP will need to take account of the accommodations that have been reached as a consequence of the EU's 'zero-for-zero' deal under the Uruguay Round for spirits.

Bananas, rum and, the most substantial of all, sugar, are all known 'problem commodities', for which it is not really sensible to try to identify 'solutions' purely within the context of this report. It is evident that any fully acceptable 'solution' is very difficult to find even without the complication of considering the consequences of the end of the Cotonou Agreement. It is not even certain how sugar can be handled in EPAs.

The other two products in Table 8, though, are less well recognised. Both of the main suppliers of grapes to the EU market (South Africa and Chile) have concluded FTAs with the EU which are likely to reduce the margin of preference of the ACP in due course. One of them, South Africa, is not eligible for GSP+, and so the focus of attention is the EU–Chile Agreement. However, since ACP exports are small, and for climatic reasons unlikely to ever become substantial, it seems plausible that the item could be added to GSP+ without substantially eroding the Cotonou acquis.

This applies even more strongly to the fourth item in Table 8, lamb skins. The only major competitor that would be eligible for GSP+ already has duty-free access to the EU market.

## **9.2 Improving the Standard GSP**

As explained above, none of the ACP states is excluded *a priori* from the GSP+. Hence, the only reason why an ACP state might be ineligible is if it fails to ratify and implement all of the required conventions. Unlike non-ACP states, the ACP will have until end-2007 to do this. The only reasons, therefore, for not adopting the 'extend GSP+' route would be that some countries for which the EU wishes to continue strong preferences fail to make the ratifications or that it is considered undesirable to follow this route, perhaps because the WTO compatibility of GSP+ is by no means certain.

In that case the principal option would be to extend the Standard GSP. Two sets of analysis are required to determine how far the Standard GSP could make an acceptable 'non-eroding' platform for a Cotonou-equivalent system. The first is to re-open the analysis of extending product coverage in Table 7. The second is to consider the effects of reducing tariffs to the Cotonou level.

### **9.2.1 Adding extra competitors for the new products**

No new products will need to be added to the GSP over and above those already identified as required to make the GSP+ an acceptable Cotonou equivalent. But the erosion potential of including these new products in the Standard GSP is greater. In addition to the erosion potential noted in Section 9.1, account needs to be taken of the fact that the new preferences

**Table 8. GSP+: the key areas of potential preference erosion**

CN8	Description	# ACP exporters	ACP export value 2003 (\$000)	Cotonou tariff	Main EU suppliers 2003 <sup>a</sup>	Value 2003 (\$000)	Competitor tariff	Competitor eligible for GSP+?
08030019	bananas, fresh (excl. plantains)	14	547,866	0 in quota (380 €/1000 kg net otherwise)	World Costa Rica Ecuador Colombia	2,363,109 546,578 530,490 463,940	75 €/1000 kg net in quota (680 €/1000 kg net otherwise)	Yes Yes Yes
ex 08061010	fresh table grapes	3	12,044	0-MFN	World South Africa Chile	677,977 262,269 165,037	5.8-MFN 4.6% to 12.8%+9.6€/100 kg net	No Yes
22084099	rum and tafia, of a value <= 2 ecu/l of pure alcohol, in containers holding > 2 l	9	22,845	0	World Cuba	43,516 16,535	0.6 €/ % vol/hl	Yes
41051010	skins of sheep or lambs, in the wet state "incl. wet-blue", tanned, without wool on, unsplit	4	15,759	0	World Syria Saudi Arabia	138,501 45,042 17,629	0 2	Yes No
<p><i>Note:</i> (a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003. <i>Sources:</i> UNCTAD TRAINS, January 2005; UK Tariff 2005.</p>								

**Table 9. The Standard GSP: areas of potential preference erosion on 'new products'**

CN8	Description	# ACP exporters	Value of ACP exports 2003 (\$000)	Cotonou tariff	Main EU suppliers 2003 <sup>a</sup>	Value 2003 (\$000)	Competitor tariff	Competitor eligible for GSP+?
02013000	fresh or chilled bovine meat, boneless	4	72,449	0%+24.2 €/100 kg net (Beef Protocol)	Brazil Argentina	249,066 240,001	} 20% in quota } (12.8%+303.4€/100 kg } net otherwise)	No No
020230	boneless, frozen meat of bovine animals	5	16,123	0%+17.6 or 24.3 €/100kg net (Beef Protocol)	Brazil	227,963	20% in quota (12.8%+221.1 or 304.1€/100 kg net otherwise)	No
08051030	fresh navels, navelines, navelates, salustianas, vernas, valencia lates, maltese, shamoutis, ovalis, trovita and hamlins	6	16,519	0-3.2+7.1€/100 kg net	South Africa Morocco	116,975 73,983	2.6%-(16%+7.1€/100kg net) 0-(3.2%+7.1€/100 kg net)	No No
08051050	fresh sweet oranges	5	11,377	0-3.2	South Africa <i>Swaziland</i>	29,356 6,081	2.6%-(16%+7.1€/100kg net)	No
10062098	long grain husked -brown- rice, length/width ratio >=3 (excl. parboiled)	3	33,783	Reduced levy	India Pakistan <i>Guyana</i>	113,908 55,164 25,186	Rate in force on day of import	No No
17031000	cane molasses resulting from the extraction or refining of sugar	3	11,570	0	Pakistan	82,676	Rate in force on day of import	No
230230	bran, sharps and other residues of wheat	1	482	36.8 or 81.8 €/t	<i>Austria</i> Russia	947 641	44 or 89 €/t	No
250100	salts, including table and denatured salt, and pure sodium chloride	7	83	0 or 1.7 or 2.6 €/1000kg	Tunisia <i>Poland</i> <i>Israel</i>	9,620 8,333 6,351	0	No
41062110	skins of goats or kids, in the wet state "incl. wet-blue", tanned, without wool on, unsplit	4	23,270	0	<i>Nigeria</i> China <i>Ethiopia</i> Saudi Arabia	19,042 17,816 12,473 8,364	2 0 2	No No No
41062290	hides and skins of goats or kids, in the dry state "crust", without wool on, whether or not split (excl. further prepared and pre-tanned only and vegetable pre-tanned indian goat or kid hides and skins of subheading 4106.22.10)	3	11,900	0	<i>Nigeria</i> India Pakistan	11,680 9,077 8,095	2 2	No No

*Note:*  
(a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003.  
*Sources:* UNCTAD TRAINS, January 2005; UK Tariff 2005.



would also be available to countries that are excluded from GSP+ because they fail the vulnerability criteria.<sup>16</sup>

Table 7 returned ‘None’ in the right-hand column for 12 of the 28 rows. In how many cases was this because all of the main competitors fail the GSP+ vulnerability criteria? The answer is ten; in the other two all of the main competitors (China and Russia) were also ineligible because of graduation, and would continue to be excluded on this basis from enjoying the benefits of a reduction in Standard GSP tariffs.

Table 9 provides the same data as in Table 8 for the new products that could result in preference erosion if Cotonou equivalence were to be achieved by improving the Standard GSP. The key products are beef, oranges, rice and molasses. Apart from the last (which is part and parcel of ‘the sugar problem’) these are additional to the contentious products thrown up by the extension of GSP+. But the number of ACP exporters is limited.

### 9.2.2 Cutting tariffs

Having extended the product scope of the Standard GSP to include all relevant items for the ACP, the next step would be to reduce the import duty payable to that provided under Cotonou. A similar approach has been taken to identify competitors and the extent to which preferences would be eroded as was done for the GSP+ above. However, for reasons of practicality (since the list of products is much longer) the information has been split into three tables. Table 10 deals with the items other than clothing and textiles for which the potential preference erosion is greatest, Table 11 covers clothing and textiles, and Table 12 deals with the remaining items where the potential scale of the erosion is smaller. ‘Main suppliers’ that have been graduated out of the relevant section are indicated in all three tables through the use of *strikeout*.

Table 10 lists all the items (other than textiles and clothing) for which the Standard GSP tariff is 5 percent or more. It is here that any preference erosion would be the most substantial. For example, the GSP tariff on fresh or chilled hake (CN 03026966) is 11.5 percent – and it is paid by South Africa, which is the main supplier, since no lower rate is currently offered under the EU–South Africa TDCA. Since the Cotonou tariff on all of the products covered in Table 10 is zero, it follows that the reduction of the Standard GSP rate to zero would erode ACP preferences by 11.5 percentage points.

**Table 10. Standard GSP preference erosion potential: major items (other than textiles/clothing)**

CN8	Description	Standard GSP	Main EU suppliers 2003 <sup>a</sup>	Competitor tariff
03026966	fresh or chilled hake	11.5	South Africa	11.5
03026999	fresh or chilled saltwater fish, edible	5.2	Morocco	0
03037811	frozen hake	11.5	South Africa	11.5
03037981	frozen monkfish	11.5	South Africa China	11.5 11.5
03037998	frozen saltwater fish, edible	5.2	Argentina	5.2
03041019	fresh or chilled fillets of freshwater fish	5.5	<i>No non-ACP</i>	
03049022	frozen meat of herring	0 or 11.5	<i>No GSP beneficiaries</i>	
06031010	fresh cut roses and buds	5 or 8.5	Ecuador	0
06031080	fresh cut flowers and buds	5 or 8.5	Ecuador	0
07081000	fresh or chilled peas "pisum sativum", shelled or unshelled	4.5-10.1	<i>No non-ACP</i>	

<sup>16</sup> Those countries that are excluded from GSP+ because they are graduated out for the relevant section will continue to be ineligible for preference on the additional items.

CN8	Description	Standard GSP	Main EU suppliers 2003 <sup>a</sup>	Competitor tariff
07082000	fresh or chilled beans "vigna spp., phaseolus spp.", shelled or unshelled	6.9 or 10.1	Morocco Egypt	0, 6.9 or 10.1 4.1 min 0.6€/100kg net, 6.9 or 10.1
07099090	fresh or chilled vegetables n.e.s.	8.9	<i>No non-ACP</i>	
16041411	prepared or preserved tunas and skipjack, whole or in pieces, in vegetable oil (excl. minced)	20.5	Philippines Thailand	20.5 20.5
16041416	loins of tunas or skipjack, prepared or preserved	20.5	Ecuador Colombia	0 0
16041418	tunas and skipjack, prepared or preserved	20.5	Thailand Ecuador	20.5 0
18031000	cocoa paste (excl. defatted)	6.1	<i>No non-ACP</i>	
18032000	cocoa paste, wholly or partly defatted	6.1	Indonesia Malaysia	6.1 6.1
18062010	chocolate and other food preparations containing cocoa	4.8% + AC max 18.7%	<i>No non-ACP</i>	
20055900	unshelled beans 'vigna spp., phaseolus spp.', prepared or preserved otherwise than by vinegar or acetic acid	15.7	China	15.7
20082079	pineapples, prepared or preserved, containing added sugar but no added spirit, with sugar content of =< 19 %, in packings of =< 1 kg	15.7	Thailand Indonesia	15.7 15.7
20082099	pineapples, prepared or preserved, in packings of < 4.5 kg (excl. added sugar or spirit)	14.9	Thailand Indonesia Philippines	14.9 14.9 14.9
20094930	pineapple juice, unfermented, brix value > 20 but <= 67 at 20cc, value of > 30 {euro} per 100 kg, containing added sugar	11.7	Thailand Indonesia	11.7 11.7
24012010	partly or wholly stemmed or stripped flue-cured virginia type tobacco, otherwise unmanufactured	14.9% max 24 €/100kg	<del>Brazil</del>	18.4% min 22/max 24 €/100kg net
24021000	cigars, cheroots and cigarillos containing tobacco	9.1	Cuba	9.1
44121310	plywood with at least one outer ply of: dark red meranti, light red meranti, white lauau, sipo, limba, obeche, okoume, acajou d'afrique, sapelli, etc.	6.5	<del>China</del> Morocco	10 0
87032390	motor vehicles for transport of persons, with spark-ignition internal combustion reciprocating piston engine, cylinder capacity >1 500 but =<3 000cc	6.5	<i>No GSP beneficiaries</i>	
<p><i>Note:</i> (a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003. Those graduated out of the GSP for the relevant section are indicated by the use of strikeout. <i>Source:</i> UNCTAD TRAINS, January 2005; UK Tariff 2005.</p>				

For four of the 26 items in the table the main competitors already have duty-free access, and so there would be no preference erosion for the ACP with respect to them. In a further two the competitors are either graduated from the sector or face zero tariffs outside the GSP. And in seven cases there are either no GSP states or no non-ACP states that meet the threshold of 10 percent of EU imports. In none of these cases does the Standard GSP tariff appear to be so high that it could plausibly have suffocated imports (although other features of the GSP such as origin rules might have done).

The main candidates for attention, therefore, are the remaining 13 items. Only two of these face stiff tariffs, the removal of which would plausibly improve the competitiveness of GSP states *vis-à-vis* the ACP. Both are varieties of canned tuna (with a 20.5 percent tariff). The Standard GSP suppliers that face discrimination, Philippines and Thailand, have already been given a reduced-tariff (12 percent) quota as part of the deals associated with the extension of the Cotonou waiver in the WTO. And for the ACP, rules of origin are an important constraint; easing of these might offset the loss of tariff preference.

A group of six items face mid-range tariffs of between 10 and 20 percent (plus one – fresh beans – with a range of tariffs one of which just tops 10 percent). They are frozen hake and monkfish, prepared beans, preserved pineapples and pineapple juice. There would be significant preference erosion on all of these.

Finally, a group of three items (miscellaneous frozen fish, cocoa paste and cigars) face Standard GSP tariffs of under 10 percent. Given that this exercise is concerned only with ACP states that are unwilling to accept EPAs, it seems unlikely that modest preference erosion on this limited group of products would prove a stumbling block to acceptance of an improved Standard GSP as the alternative.

Table 11 provides similar information for clothing and textiles. In all except two of the 14 GSP relevant items the Standard GSP tariff is 9.6 percent. However, in four of these 14 the only competitor exceeding the 10 percent threshold is Tunisia, which has duty-free access (and in one of the others it is one of two suppliers with China, which is graduated). In a further six there are either no GSP-beneficiary or no non-LDC suppliers that meet the 10 percent threshold. As with the discussion of Table 10, a Standard GSP tariff of 9.2 percent cannot plausibly have suffocated trade, and so the removal of the tariff is unlikely to encourage major new suppliers to emerge from the woodwork.

In any case, the impact of any GSP changes to the pattern of world trade in clothing will be dwarfed by the reverberations from the phase-out of the Multifibre Arrangement. By 2008, when the Cotonou trade provisions expire, the pattern of ACP clothing exports is likely to be very different from what it is now.

**Table 11. Standard GSP preference erosion potential: textiles/clothing**

CN8	Description	Standard GSP	Main EU suppliers 2003 <sup>a</sup>
54025200	filament yarn of polyester, incl. monofilament of < 67 decitex, single, with a twist of > 50 turns per metre	3.2	<i>No non-ACP GSP beneficiaries</i>
61051000	men's/boys' shirts of cotton, knitted or crocheted	9.6	<i>No non-LDC</i>
61061000	women's/girls' blouses, shirts and shirt-blouses of cotton, knitted or crocheted	9.6	India
61091000	t-shirts, singlets and other vests of cotton, knitted or crocheted	9.6	<i>No non-LDC</i>
61101130	men's/boys' jerseys, pullovers, cardigans, waistcoats and similar articles, of wool, knitted or crocheted	9.6	Tunisia
61101190	women's/girls' jerseys, pullovers, cardigans, waistcoats and similar articles, of wool, knitted or crocheted	9.6	<i>No GSP beneficiaries</i>
61102091	men's/boys' jerseys, pullovers, cardigans, waistcoats and similar articles, of cotton, knitted or crocheted	9.6	<i>No GSP beneficiaries</i>
61102099	women's/girls' jerseys, pullovers, cardigans, waistcoats and similar articles, of cotton, knitted or crocheted	9.6	<i>No non-LDC</i>
61103099	women's/girls' jerseys, pullovers, cardigans, waistcoats and similar articles, of man-made fibres, knitted or crocheted	9.6	<i>No non-LDC</i>
62034231	men's/boys' trousers and breeches of cotton denim	9.6	Tunisia
62034235	men's/boys' trousers and breeches of cotton	9.6	Tunisia
62046231	women's/girls' cotton denim trousers and breeches	9.6	Tunisia
62052000	men's/boys' shirts of cotton	9.6	India
62121090	brassieres of all types of textile materials, whether or not elasticated, incl. knitted or crocheted	5.2	<del>China</del> Tunisia

*Note:*  
(a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003. Those graduated out of the GSP for the relevant section are indicated by the use of strikeout.  
Source: UNCTAD TRAINS, January 2005; UK Tariff 2005.

Table 12 deals only with the minnows – products that already face such low Standard GSP tariffs that any preference erosion will be minor. Even such impact as there might otherwise

have been, however, will be reduced still further since for six of the 21 items all the major competitors are graduated out of the relevant section. In a further four there are no major non-ACP or GSP-beneficiary suppliers. Of the remainder, the maximum tariff is just 4.2 percent (for cocoa butter).

**Table 12. Standard GSP preference erosion potential: minor items**

CN8	Description	Standard GSP	Main EU suppliers 2003 <sup>a</sup>
03061340	frozen deepwater rose shrimps 'parapenaeus longirostris'	4.2	Morocco, Tunisia
03061350	frozen shrimps of the genus 'penaeus'	4.2	Argentina
03061380	frozen shrimps and prawns	4.2	Argentina, India
03074918	frozen cuttle fish 'sepia officinalis' and 'rossia macrosoma'	2.8	India, Thailand, Morocco
03075910	frozen octopus 'octopus spp.'	2.8	Morocco
03079100	live, fresh or chilled molluscs, fit for human consumption	3.8	Tunisia, Indonesia
08043000	fresh or dried pineapples	2.3	Costa Rica
08044000	fresh or dried avocados	0 or 1.6	South Africa, Mexico
09050000	vanilla	2.1	<i>No non-ACP</i>
15119099	palm oil and its liquid fractions, whether or not refined, but not chemically modified	3.1	<del>Malaysia, Indonesia</del>
15131199	crude coconut oil, in immediate packings of > 1 kg	2.2	Philippines, <del>Indonesia</del>
15132190	raw palm kernel oil and babassu oil	2.2	<del>Indonesia</del>
18040000	cocoa butter, fat and oil	4.2	Indonesia, Malaysia
18050000	cocoa powder, not containing added sugar or other sweetening matter	2.8	<i>No non-ACP</i>
21011111	solid extracts, essences and concentrates of coffee	3.1	<del>Brazil</del> , Colombia, Ecuador
24012080	partly/wholly stemmed/stripped flue-cured tobacco, otherwise unmanufactured	3.9% max 56 €/100kg	Argentina
24013000	tobacco refuse	3.9% max 56€/100 kg net	<del>Brazil</del>
28141000	anhydrous ammonia	2	Russia, Ukraine, Algeria
29051100	methanol 'methyl alcohol'	2	Chile, Libya, Russia
29161220	ethylacrylate	3	<i>No GSP beneficiaries</i>
29321200	2-furaldehyde 'furfuraldehyde'	3	<del>China</del>
39041000	polyvinyl chloride, in primary forms, not mixed with any other substances	3	<i>No GSP beneficiaries</i>
44121390	plywood consisting solely of sheets of wood <= 6 mm thick, with at least one outer ply of a tropical wood specified in subheading note 1 to this chapter	3.5	<del>Indonesia, Brazil</del>
85299081	parts suitable for use solely or principally with television cameras, receivers of radio-telephonic/telegraphic signals, or for radio or television, n.e.s.	1.5	<del>China</del>

*Note:*  
(a) All non-LDC, non-ACP GSP beneficiaries supplying 10 percent or more of the EU market in 2003. Those graduated out of the GSP for the relevant section are indicated by the use of strikeout.  
Source: UNCTAD TRAINS, January 2005; UK Tariff 2005.

## 10 Conclusions

### 10.1 Creating coherence

The broad conclusion of this report is positive – not only is it feasible to consider the GSP as a post-Cotonou trade option, but there are economic advantages in so doing. The renewal of the GSP provides an opportunity to consider whether the EU's multifarious trade agreements with developing countries could be brought coherently under one umbrella. The WTO ruling in the case brought by India has provided confirmation that differentiation within the GSP is possible. The EU's commitment in the Cotonou Agreement to provide ACP countries not

willing to join EPAs ‘a new framework for trade which is equivalent to their situation’ lends an urgency to the task.

The draft Regulation currently under review provides details for the GSP only to 2008, although the scheme is to continue until 2015. This report has considered whether the architecture of the new GSP could provide a framework for offering ACP countries equivalent treatment to that which they obtain under Cotonou.

By ‘equivalent treatment’ we mean a situation in which EU import tariffs are the same and the process of creating the new GSP regime does not result in additional preference erosion that negates the gain for the ACP. Other significant features of a post-Cotonou trade regime have not been given detailed consideration, including most importantly the issues of contractuality and joint decision-making on future change. The reason for the neglect of these points is that the issues are quite clear; what is not clear – and is subject to detailed analysis in this report – is the feasibility of creating from the existing architecture of the GSP a regime that offers equivalent treatment on tariffs without accelerating preference erosion to an unacceptable extent.

Also excluded from detailed analysis is the option of creating a special ‘ACP tranche’ within the GSP. The current Regulation does not provide a direct peg for this, but the GSP+ demonstrates that differentiation is permissible. The key issue would be the political acceptability of a special ACP tranche and its WTO compatibility. The second of these may well be tested over the coming years through the reaction of WTO members to the GSP+. It cannot be assumed that there will be no WTO challenge – nor that if there is such a challenge it will be unsuccessful.

## **10.2 Extending GSP+**

The most obvious route for creating a Cotonou-equivalent regime under the GSP is to extend GSP+ (assuming it survives WTO challenge). The analysis in Part B suggests that this is feasible. There will be problems with sugar, bananas and rum – but these are commodities that face serious difficulties regardless of the future trade regime. And until more is known about the way in which these difficulties are to be handled – and, crucially, which ACP countries decide not to join EPAs – it is not feasible to go much further than is done in this report in assessing the scale of the difficulty.

There are some advantages to the idea of merging Cotonou and GSP+. As explained in Part A, the economic impact of GSP+ will be heavily influenced by the number of countries that become eligible. In brief, the more the better. If only a few countries are accepted for GSP+ the results are more likely to be trade diverting than trade creating. By contrast, if many countries are accepted there are good reasons to expect significant trade creation.

There will also be a lessening of the problems of the rules of origin. The additional reform of agreeing full cumulation between all GSP+ beneficiaries would clarify the situation still further. At the extreme it would mean that only inputs from the 21 states excluded *a priori* from GSP+ would cause potential problems with the origin rules.

Provided that the broader issues of contractuality etc. can be overcome, the conclusion to be drawn is that an extension of GSP+ to cover all ACP exports would have beneficial economic effects. Indeed, it is possible to argue that the economic effects would be superior to those likely to arise from EPAs, under which liberalisation by ACP states is likely to be partial and long drawn out.

The alternative of improving the Standard GSP to Cotonou levels is more problematic. The number of problem commodities increases to include fish, horticulture and processed tropical fruits. Whilst not insurmountable, the extent to which this approach would erode ACP preferences is increased.

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