The implications of the European Union's EBA for the Caribbean

Developing countries have traditionally benefited from various schemes of the Generalised System of Preferences (GSP). The GSP was originally conceived as an instrument to promote economic diversification in developing countries through enhanced market access. It was in this context that the European Union (EU) introduced its own GSP in 1971, which benefited developing countries, including the least developed countries (LLDCs).[1] The EU GSP has evolved over time, adapting to changes in the global environment. In 1995, the EU moved away from the use of quantitative restrictions in favour of a tariff modulation system, under which fixed reduced rates for sensitive industrial and agricultural products were replaced by reduced rates of duty applied according to product sensitivity. The African, Caribbean, Pacific (ACP) developing countries have also been enjoying preferential treatment in the European Union market through the Lomé Convention. In terms of product coverage and duty preferences, the ACP least developed countries enjoy more favourable access in the EU than other least developed countries. In addition to duty-preferences, they also benefit from generous rules of origin which allow their products to be classified as ACP products, even if they are made from materials originating in the EU or Overseas Countries and Territories (OCT) and have not undergone sufficient processing in the ACP country. The non-ACP LLDCs got improved concessions from the 1998 extension of the GSP coverage. Although the EU pledged in 1996 to offer non ACP-LLDCs trade preferences equivalent to those enjoyed by the ACP-LLDCs, no improvement was made until the "Everything But Arms" (EBA).

The EBA extends duty and quota free access to all the products originating from the least developed countries, most of which are in sub-Saharan Africa. The only products exempted are arms and ammunition. The measure will become effective from January 2002. However, liberalisation for the three most sensitive products: bananas, sugar and rice, will be phased progressively over a period of three years. Full liberalisation for bananas would be achieved in 2006 after progressive reductions of tariffs by 20 per cent annually from 1 January 2002. This also happens to be the time when the new tariff-only system will replace the current quota system of the EU banana regime. The EU market for sugar and rice will be opened up between 2006-2009. In the interim period, LLDCs sugar and rice will be allowed to enter the EU market duty-free within the limits of a tariff quota. The quota for sugar will increase from 74,185 tons in 2001/2002 to 197,355 tons in 2008/2009, while that of rice will grow from 2517 tons in 2001/2002 to 6699 tons in 2008/2009. The EBA presents a significant market-opening opportunity for the least developed countries, particularly the non-ACP LLDCs. The EBA concessions will apply the current GSP rules of origin, which allows regional cumulation between the Association of South East Asian Nations (ASEAN) and the South Asian Association

[1] The ACP-least developed countries are; Angola, Benin, Burkina Faso, Burundi, Cape Verde, Central African Republic, Chad, Comoros, Democratic Republic of Congo, Djibouti, Equatorial Guinea, Eritrea, Ethiopia, Gambia, Guinea, Guinea Bissau, Haiti, Lesotho, Liberia, Kiribati, Madagascar, Malawi, Mali, Mauritania, Niger, Mozambique, Samoa, Sierra Leone, Solomon Islands, Somalia, Sao Tomé and Principe, Sudan, Rwanda, Tanzania, Togo, Tuvalu, Uganda, Vanuatu and Zambia.
The non-ACP LLDCs are: Afghanistan, Bangladesh, Bhutan, Cambodia, Laos, Maldives, Myanmar Nepal and Yemen.

for Regional Cooperation (SAARC).[2] These rules of origin are stricter than those that apply to the ACP countries under the Lomé/Cotonou Agreement, which allows cumulation between the ACP, EU and the OCTs. An ACP country may also cumulate with a neighbouring developing country other than an ACP State. This Issue Brief assesses the possible implications of the EU's EBA on the Caribbean, with special reference to the three sensitive products.

To assess fully the possible impact of the EBA on the Caribbean countries, one should first examine the production and consumption patterns of the three sensitive products in the LLDCs. This is important since the ability of the least developed countries to take advantage of this new trade concession hinges on their production and institutional capacity. An examination of production patterns of the least developed countries as a group reveals that they are not significant producers of agricultural commodities compared to other countries (*See Table I*). The least developed countries account for a mere 0.003 per cent of EU imports and 0.4 per cent of global trade. In fact, in many least developed countries, the production of agricultural commodities, particularly bananas, sugar and rice, falls consistently below domestic consumption. Although this is the case for the LLDCs as a group, there are some individual countries with substantial surpluses in some of the agricultural products, for example, Myanmar, in the production of rice. In aggregate, the least developed countries are net importers of agricultural products. Furthermore, the exports of the LLDCs to the EU have experienced a substantial decline over the period 1995-1999. This is an issue of great concern in light of the duty preferences, which their exports to the EU have been enjoying through the Lomé Convention. The prospect for increased exports over the short to medium term does not look favourable. This points to a significant supply constraint that has to be overcome if they are to optimise the benefits of the EBA.

Table I
Least Developed Countries' Production and Consumption of Bananas, Sugar and Rice
(Averages for 1996-98)

	Production			Consumption			Production Surplus/Deficit (000 tons)		
	Bananas	Sugar	Rice	Bananas	Sugar	Rice	Bananas	Sugar	Rice
LLDCs	5.69	2.06	40.81	5.69	3.69	43.43	8.00	-1.63	-2.62
EU 15	408.00	17.70	1.80	3.58	13.87	2.11	-3.17	3.83	-31.00
World	56.65	126.95	384.08	55.53	121.51	381.34	1.12	5.44	2.74

Source: European Union

The EBA may prove significant in helping the LLDCs overcome their infrastructural and supply constraints. It will improve market access for the least developed countries only for those products that are currently restricted in the European Union. As indicated earlier, most least-developed countries, with the exception of those in Asia, enjoy trade preferences in the European Union markets as part of the ACP-EU Lomé convention. The ACP sugar protocol, for example,

[2] ASEAN comprises of Brunei Darussalam, Indonesia, Laos, Malaysia, the Philippines, Singapore, Vietnam and Thailand while SAARC comprises of the following countries: Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

gives ACP sugar producers duty-free access to the EU, but with a quota. The EBA, on the other hand, will provide duty and quota-free access to the least developed countries. However, the price the LLDCs will receive for the sugar will be negotiated with the importers in the EU and would most likely be lower than the EU price.

However, the benefits of the EBA to the banana producing least-developed countries would not be significantly different from those the ACP countries presently receive under the current EU banana regime. Although the banana protocol imposed a quota limit on the ACP countries, the quota does not constitute a constraint for them as it far exceeds their supply capacity. For the non-LLDCs ACP countries, under the new Cotonou partnership agreement these benefits will be rolled over for a transitional period of eight years before the new reciprocal regime comes into operation in January 2008. However, the transitional period for bananas will be six years until 1 January 2006 when a new tariff only system will replace the quota regime. During this transitional period, the Caribbean countries should restructure their production activities to achieve dynamic efficiency and competitiveness. At the end of the transitional period, the Caribbean countries will have to compete against other countries for access to the EU market. However, for the least developed countries they will continue to enjoy duty and quota-free access to the EU market for all products, with the exception of arms.

Overall, the EBA will slightly improve on the existing preferences the ACP-least developed countries enjoy. The greatest benefits, however, will accrue to the non-ACP least developed countries, especially the ASEAN/SAARC which currently receive no preference over the standard tariff payable by industrialised countries (the EU's Most Favoured Nation (MFN) tariff). Only Bangladesh receives preferences for sugar exports. Market access will be improved significantly for them. However, these countries are not significant exporters of bananas, sugar and, to a lesser extent, rice (*See Table II*). Only Myanmar is the significant exporter of rice but it will not be eligible for the EBA due to its human rights record. However, the EBA may improve market access for the non-ACP LLDCs in garments, textile and other manufacturing products in which their exports are concentrated. How improved market access for them in these products may affect the Caribbean is beyond the scope of this brief.

Table II
Non-ACP LLDCs Exports of Rice, Bananas and Sugar (Averages for 1996-97)

	Rice (US$'000)			Bananas(US$'000)			Sugar (US$10000)		
	Export	Import	Balance	Export	Import	Balance	Export	Import	Balance
Afghanistan	0	48650	-48650	0	0	0	0	1700	-1700
Bangladesh	47.0	146922.5	-146876	0	4	-4	0	3391	-3391
Bhutan	7.5	4605	-4597.5	0	5	-5	0	140	-140
Cambodia	937.5	5633	-4695.5	0	0	0	0	1356	-1356
Laos	0	12350	-12350	0	0	0	0	785	-785
Maldives	0	5810	-5810	0	0	0	0	335	-335
Myanmar	20424.5	15	20409.5	0	0	0	511	265	246
Nepal	0	10508	-10508	0	30	-30	0	384	-384
Yemen	0	104514.5	-104515	0	0	0	0	22055.5	-22056

Source: Food and Agricultural Organization of the United Nations (FAO), Trade Yearbook, Vol.52, 1998

Since the non-ACP LLDCs are not significant exporters of agricultural products, the brief focuses on the ACP-LLDCs whose exports are concentrated in bananas, sugar and, to lesser extent, rice. Although their exports are concentrated in the three commodities, they are not significant exporters of these products. However, the EBA, as with any trade liberalisation measures could provoke a dynamic response, leading ex ante to increased exports to the EU market. This may arise from diversion of LLDCs' production from domestic consumption and non-EU markets to the EU markets to take advantage of duty preferences and higher prices. This is consistent with the findings of a study[3] on sugar that suggests that the LLDCs would export refined sugar to the EU owing to the high price of white sugar. This would be made possible by importing from third countries for domestic consumption and exporting the entire domestic production to the EU. Furthermore, the trade concessions could potentially lead to a reallocation of resources, including capital and labour, away from producing for domestic consumption to producing exclusively for the European Union, with products tailored to the specific needs of EU consumers. Some argue that in the long run, the effects of the EBA on the least developed countries may arise from increased investment, particularly foreign investment, in industries that benefit from duty and quota preferences. This may be investment in new production facilities or expansion of existing facilities. The direct effects of all these would be to increase EU imports from the least developed countries. Besides the injection of foreign capital, there could also be some domestic investment as the countries begin to derive tangible benefits from the EBA in the form of increased exports, more foreign exchange earnings and, therefore, better mobilisation of domestic resources for domestic investment.

However, the long-run effects of the EBA are limited by the small size of many least developed countries coupled with supply and infrastructural constraints. The prevailing macroeconomic environment and political situation in individual least developed countries will be crucial factors determining whether or not the LLDCs realise the benefits of the EBA. More than 80 per cent of the LLDCs are in sub-Saharan Africa and in many of them political instability has been a lingering problem**.** The problem is not isolated to sub-Saharan Africa alone, although certainly more intractable, but other least developed countries in Asia and the Caribbean (Haiti to be specific) continue to experience some type of political instability. This problem constitutes a major obstacle to attracting foreign investment and may very well prevent them from maximising the benefits of the EBA. The weak supply capacity coupled with the smallness of the least developed countries has been a major factor contributing to their marginalisation in international financial markets, and it is highly unlikely that they will overcome this challenge in the foreseeable future. More so, investments based on duty preferences are riskier because of the inherent uncertainties of GSP schemes, in general, and the EBA, in particular, which is non-contractual and can therefore be changed anytime at the whim of the EU. After all, the LLDCs have not been able to attract a significant amount of investments during the 1990s.[4] This, coupled with the changing nature of FDI away from primary commodities to services and information technology industries, may make it difficult for LLDCs to attract investments in the foreseeable future. Furthermore, the reform of the Common

[3] Association des Organisations Professionnelles du Commerce des sucres pour les pays de l'Union Europeenne (ASSUC), 25 January 2001, "EBA-An impact Assessment for the Sugar Sector" at http://www.acpsugar.org

[4] According to UNCTAD's report, "FDI in the Least Developed Countries at a Glance", the share of LLDCs in global FDI averaged a meagre 0.5 per cent during the 1990s.

Agricultural Policy (CAP) which is already underway and the likely impact of the next WTO Round on agricultural liberalisation could significantly lead to a decline in EU prices, forcing them to converge to equilibrium world prices. This would erode the attractiveness of the EU market vis-à-vis other markets. All these factors could constrain the LLDCs in optimising the benefits of the EBA.

The EBA would have implications for the Caribbean, especially in the long run. Its impact could be felt immediately at the end of the new ACP-EU partnership agreement in December 2007. The three sensitive products, viz., bananas, sugar and rice, have traditionally played an important role in the economies of many Caribbean countries, particularly the Windward Islands. The duty preferences which the Caribbean countries enjoy in the European Union market under the Lomé agreement have had a positive impact on the economies of smaller Caribbean countries as they served to maintain increased export to a protected market, relatively higher income per capita, and increased employment. The three commodities combined accounted for an average 79.0 per cent of CARICOM's total agricultural exports in the period 1990-1997. The share of the three products in CARICOM's total exports has been averaging 13.0 per cent during the 1990s (*See Table III)*.

Table III
CARICOM's Export of Bananas, Rice and Sugar as percentage of Agricultural and Total Domestic Exports (1990-97)

CARICOM's Exports of Bananas, Rice and Sugar as percentage of Agricultural and Total Domestic Exports (1990-97) (US$'000)					
	Bananas, rice & sugar	Total Agric. Exports	Total Domestic Exports	A/B	A/C
	A	B	C		
1990	476,054	581,071	3,861,397	81.9	12.3
1991	452,304	540,958	3,640,894	83.6	12.4
1992	562,231	676,676	3,716,416	83.1	15.1
1993	514,870	647,015	3,514,058	79.6	14.7
1994	511,157	656,835	4,282,777	77.8	11.9
1995	585,230	779,554	4,859,623	75.1	12.0
1996	644,370	830,972	4,920,709	77.5	13.1
1997	582,181	791,744	4,937,960	73.5	11.8
Average	**541,050**	**688,103**	**4,216,729**	**79**	**13**
Source: CARICOM Secretariat					

The vulnerability of the Caribbean's agricultural sector to changes in the global economic environment, in general, and the EBA, in particular, is clearly illustrated by the high dependence of the region's exports on the European Union market (*See Table IV*). The degree of dependence of the three commodities on the European market has varied. The higher the degree of a commodity's dependence on the European market, the more difficult would be the adjustment to the new liberalised, WTO-compatible global regime. Banana is the most dependent on the European Union market. Therefore the challenge of adjusting to the new globalised and competitive environment would be more formidable for the banana industry. For example,

during the period 1990-1997, the European Union market absorbed an average 98.9 per cent of CARICOM's banana exports.

Table IV
Share of CARICOM's Exports of Banana, Rice and Sugar in various markets

	Bananas		Sugar			Rice			
	EU	Other	EU	USA	Other	EU	Caricom	Other Caribbean	Other
1990	98.9	1.1	82.1	11.2	6.7	61.3	35.1	3.6	0
1991	98.7	1.3	95.0	4.9	0.1	20.0	95.6	21.0	0.3
1992	99.3	0.7	85.7	10.6	3.7	9.5	63.8	26.4	0.3
1993	98.3	1.7	87.9	7.0	5.1	27.2	28.4	44.0	0.4
1994	99.2	0.8	85.9	4.7	9.4	26.6	15.2	58.2	0
1995	98.7	1.3	89.7	4.1	6.2	0.4	18.5	81.1	0
1996	98.8	1.2	86.9	8.5	4.6	0.2	27.3	71.9	0.6
1997	99.5	0.5	85.2	10.8	4.0	23.5	39.1	28.2	9.2
Average	98.93	1.08	87.3	7.73	4.98	21.09	40.38	41.8	1.35

Source: CARICOM Secretariat.

The share of CARICOM's sugar exports to the European Union market averaged 87.3 per cent during the 1990-1997 period, with the United States market absorbing an average 7.8 per cent. An impact assessment study[5] shows that in respect of the three sensitive products, the impact of the EBA will be the most significant for the sugar industry in the non-LLDCs ACP countries. Since the EU sugar market is already over-supplied, any increase in the least developed countries' export of sugar may lead to displacement of EU import of ACP sugar. Should the excess EU sugar be dumped on the world market, this could put a downward pressure on sugar prices, resulting in loss of income, government revenue and, potentially, employment.

Rice however, has a well-diversified export market. The share going to the European Union averaged only 21.1 per cent during the 1990s. The bulk of exports is accounted for by regional markets, both CARICOM and other Caribbean countries. A cursory analysis may lead one to conclude that the impact of duty preferences to the least developed countries on the rice industry in the Caribbean will be minimal, owing to its low dependence on the European Union markets. However, the dependence of rice on the European Union market is much higher than suggested in T*able IV*, because the bulk of CARICOM's rice to the other Caribbean countries go to Aruba and the Netherlands Antilles from where they are re-exported to the European Union countries after further processing.[6] However, the impact of the EBA on the Caribbean rice industry would not be significant since neither the Caribbean nor the LLDCs are significant exporters of rice (*See table V*). Guyana remains the only significant exporter of rice. Although the impact of the EBA will vary across products and countries, it is reasonable to assume that the Caribbean stands to lose their shares of their European Union market for bananas and sugar.

[5] See Stevens, Christopher and Kennan, Jane, January 2001, " Impact of the EU's Everything But Arms' Proposal: A Report to Oxfam", Institute of Development Studies (IDS).
[6] See Byron, Blake, June 2000, "Commodity Exports: Agriculture in the post Lomé IV Era, Implications of International Developments", Caricom Perspective, A century of Achievement, p.70-74, Vol. II, No. 69.

Table V
Exports and Imports of Bananas, Sugar and Rice for Selected Caribbean Countries
(Averages for 1996-97)

	Bananas (U$'000)			Sugar (U$10000)			Rice(U$'000)		
Country	Export	Import	Balance	Export	Import	Balance	Export	Import	Balance
Barbados	3.0	903.5	-900.5	3572	667.0	2905.0	918	4415.0	-3497.0
Belize	27409.5	0	27409.5	4655	5.5	4649.5	4	180.5	-176.5
Dominica	17384	0	17384.0	0	154.5	-154.5	0	768.5	-768.5
Dom. Rep	13073.5	0	13073.5	17600.5	630.0	16970.5	0	18650.0	-18650.0
Grenada	351.0	0	351.0	7	238.0	-231.0	0	1342.0	-1342.0
Jamaica	44431	0	44431	2760	10503.0	-7743.0	0	30216.0	-30216.0
St. Kitts	0	49.0	-49.0	0	101.5	-101.5	0	746.0	-746.0
St. Lucia	43728.5	0	43728.5	0	256.0	-256.0	0	2383.5	-2383.5
St. Vincent	17502	0	17502.0	0	246.0	-246.0	0	2341.0	-2341.0
Trinidad	33.5	462.5	-429.0	3519	1209.0	2310.0	1254	13577.5	-12323.5
Guyana	6.0	0	6.0	14061	390.0	13671.0	88189	0	88188.5
Suriname	16676.5	0	16676.5	0	806.0	-806.0	45	62323.0	-62278.0
Haiti	0	0	0	0	4390.0	-4390.0	0	73000.0	-73000.0

Source: Food and Agricultural Organization of the United Nations(FAO), Trade Yearbook, Vol.52, 1998

Although the EBA could have some implications for the Caribbean agricultural sector in the long run, the major threat to the region's economies, particularly the banana industry, will come from the new liberalised, WTO-compatible EU banana regime, which will be based on a First-Come-First-Served basis. This will favour the banana producing countries of Latin America, most notably Costa Rica and Ecuador. Given their high level of efficiency and productivity, their high quality dollar bananas could displace the European Union banana imports from the Caribbean countries. Productivity in the Windward Islands is low compared to the other banana producing countries of Latin America. For example, for Saint Lucia, average productivity is estimated at 8 tonnes per acre compared to 24 tonnes per acre for the Latin American banana plantation.[7] This places the Windward Islands banana producers at a competitive disadvantage. To overcome this constraint, they would need to restructure their production facilities to achieve dynamic efficiency and competitiveness. A recent EU study[8] shows that of all the ACP countries only Cameroon and Ivory Coast have the best chances of competing on cost with Costa Rica and Ecuador. This suggests that even if the Caribbean restructure their production they still may not be able to compete on cost with the dollar bananas of the Central American countries. They would have to develop niche-market products as well as other non-traditional exports.

The three industries (banana, sugar and rice) account for the bulk of employment in much of the Caribbean, with the share of labour in the three industries averaging close to 60.0 per cent for Guyana. A gradual, integrated process of transition away from older to newer industries, such as tourism, financial services and information technology, is required if the region is to survive

[7] See The Economist " Globalisation: Expelled from Eden ", December 20, 1997.
[8] See Nordic Consulting Group/University of Birmingham/Synergie, January 2000, "Evaluation of EU Assistance to ACP Banana Producers under Regulation 2686/94 ".

in the new liberalised globalised world economy. In fact, a number of countries have established dynamic services sectors with tourism and offshore financial services playing a dominant role. The challenge will be more formidable for countries with high shares of agriculture in their Gross Domestic Product, particularly Guyana.

While the EBA may lead to displacement of the EU imports from ACP countries, including the Caribbean, it also presents a market opening opportunity for other countries. The Caribbean should forge trade relations with LLDCs, such as Haiti and other African least developed countries. These countries could become important markets for Caribbean exports. This kind of arrangement already exists between Sudan and the Dutch Caribbean island of Aruba, whereby the latter imports 30,000 tonnes of sugar from the former, from where it is re-exported to the European Union after some light processing. Since it is perfectly legal for the LLDCs to import from third countries to meet their domestic consumption while exporting their entire production to the EU, there is no reason why this type of trade arrangement cannot be fully exploited by Caribbean countries. It would be in the interest of the Caribbean countries to strengthen trade relations with Haiti. Given the magnitude of its current political and economic problems it will take some time before Haiti could begin to realise tangible benefits from the EBA. Should the political situation stabilise, investment may flow in from other Caribbean countries, especially into industries benefiting from the EBA. This investment will be critical in revitalising the moribund sugar industry in Haiti. In the long run, Haiti may also become a significant market for other Caribbean countries, partly offsetting the impact of the EBA. Therefore, the Caribbean Community should work hard at consolidating democracy and good governance in Haiti.

Although it is difficult to predict accurately the possible impact of the EBA on the Caribbean countries, preliminary assessment tends to reinforce the conclusion that the absolute impact would be limited given the LLDCs inadequate supply capacity. Moreover, the EBA will not significantly improve market access conditions for the ACP-LLDCs since they already receive duty-free access to the EU under the Cotonou Agreement, which replaced the Lomé Convention. However, the relative improvement in market access will be the greatest for the non-ACP LLDCs, particularly in Asia since they currently do not enjoy any favourable access to the EU market. These countries however, do not pose any threat to Caribbean bananas, sugar and rice industries since they are not significant exporters of these products. Even if the non-ACP LLDCs manage to increase their exports to the EU, the likely impact will not be so significant as to displace EU imports from the non-LLDCs, including the Caribbean. Therefore, the overall direct impact of the EBA will be limited. Moreover, once the Common Agricultural Policy is reformed, Caribbean producers may not be at a competitive disadvantage vis-à-vis EU producers, which are equally high-cost producers. However, the greatest impact of the EBA on the Caribbean countries would be through the decline in commodity prices as increased competition to export to the EU will force prices to converge to equilibrium world prices. Furthermore, since the EBA comes at a time when the EU banana regime is being overhauled to bring it in conformity with the WTO rules, the Caribbean banana industry will face stiff competition from the dollar bananas of Central American countries, most notably Costa Rica and Ecuador. Therefore, they need to use the transitional period to restructure their industries and diversify into other niche-market as well as non-traditional commodities.