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Designed by Mary Mwele Kiio

TABLE OF CONTENTS

Foreword

trapca *Trade Policy Review* is an annual publication issued by The Trade Policy Training Centre in Africa (**trapca**). **trapca** was inaugurated in December 2006 with the mandate of providing training and technical expertise on trade issues to professionals in Least Developed Countries (LDCs). The centre is situated in Arusha, Tanzania. It is financed by the Swedish International Development Cooperation Agency and operates under the auspices of the Eastern and Southern Africa Management Institute (ESAMI) and Lund University in Sweden.

The overall aim of the training activities of **trapca** is to bring new perspectives to world trade, to inspire the creation of networks in LDCs and to develop competencies for strengthening the capacity of LDCs to engage within the international trading systems with a view of overcoming the constraints to, and of utilising the development-related opportunities provided by, trade. The training activities of **trapca** are premised on the belief that LDCs are not able to reap the benefits of globalisation and international trade due to inadequate competencies and capacities in trade issues.

trapca offers trade policy training activities at various levels from a foundation course in International Trade and Economic Development (CITD), a number of specialised courses in international trade policy and trade law, to a master's degree programme in International Trade Policy and Trade Law. The courses included in the master's programme can also be studied as individual specialised advanced level courses.

trapca also arranges one more policy-oriented *Annual Conference* and one more academic scientific *Trade Policy Research Forum* directed to researchers in the field of **trapca's** mandate. For more information on these two annual events, please visit our web page www.trapca.org.

trapca *Trade Policy Review* is based on papers presented at the two annual events mentioned above but it is also a channel for our most advanced and qualified participants in our training programmes to reach out with their work as presented in Diploma and Master's theses.

All papers presented at our annual conference and trade policy research forum are available on our web page (www.trapca.org/publications) in an unedited form whereas papers published in ***trapca*** *Trade Policy Review* have been subject to peer reviewing and revision.

Because ***trapca*** *Trade Policy Review* is also directed to our course participants and to practitioners, we welcome reviews of scientific or popular policy-oriented books and reports in the fields covered by **trapca's** mandate.

The papers considered in the trapca trade review journal are subjected to a peer review process. The papers presented during trapca's annual events undergo an initial peer review before presentation. The process starts with potential papers for presentation being sent to selected reviews to give their initial views on the content, analysis and suitability of the paper for the organised event. The comments are sent to the paper author. During the event, each paper presented undergoes a plenary critic out of which the comments and suggestions for revision are forwarded to the paper author. The submitted papers, after presentation, are sent to independent reviewers who evaluate their suitability for publication. Papers that incorporate the comments from the reviewers are then considered for inclusion in the journal once the editorial team approves the final submission.

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FEELING FOR THE STONES: NEW THINKING ON TRADE AND DEVELOPMENT

Sam Laird[1]

("Cross a river by feeling for the stones" - Deng Xiaoping)

1. Introduction

From the mid-1980s, the "Washington consensus" on trade led to the most important trade reforms across the developing world and transition economies in recent history – despite developments in trade theory which had challenged conventional wisdom, notably by Krugman (1980, 1986).[2] However, while there were some notable successes – not all attributable to the application of orthodox trade policies – there were also a number of failures, especially in Africa, and there has recently been some serious re-thinking in the Bretton Woods institutions about trade policy prescriptions. On the other hand, in the WTO many negotiators remain attached to a relatively undiluted version of orthodoxy on trade policy in particular – at least as to what their trading partners should be doing. A hard line on industrial policy and safeguards for agriculture challenges the development intentions of the Doha Round and suggests that the brief of some developed country negotiators is: "Do what I say, not what I do!" The failure of the July 2008 talks in the WTO show that negotiating hard ball has triumphed over the need for cooperation and understanding. Hopes that Aid for Trade might pave the way for a compromise have faded amid concerns about funding and possible new conditionalities.

2. Trade

The "autonomous" reforms among developing countries since the mid-1980s, carried out with varying degrees of enthusiasm under IMF/World Bank structural reform programmes, led to dramatic reductions in trade intervention among developing countries and increased openness of their economies towards foreign investment. Tariffs fell from some very high levels to moderate rates (Figure 1), there was substantial rationalisation of tariff structures (reducing the number of bands, in a few cases to a single level), and non-tariff barriers, such as quotas, were largely eliminated. This process has continued in countries like China and India so that their applied rates are now below 10 per cent. Moreover, under these reform programmes, the dispersion in rates across sectors has been substantially reduced, and tariff escalation is now more marked in developed than developing countries. However, developing countries have now also become major users of WTO consistent trade measures such as anti-dumping actions – often against each other.

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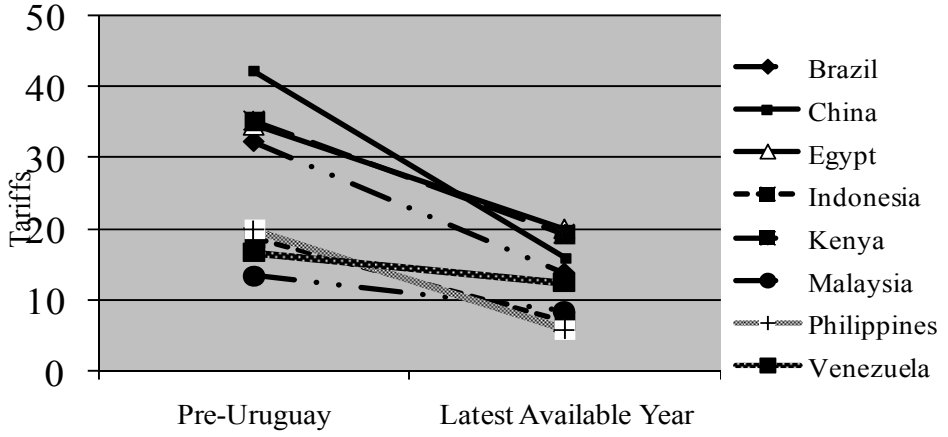
[2] Krugman (1992) expresses disappointment that the "fairly radical change in the way that economists explain international trade has so far at least had relatively little impact on their recommendations about trade policy."

Figure 1: Selected Developing Countries Average Applied MFN Tariffs, Pre-Uruguay Round and Most Recent Year (in most cases 2004)



Source: UNCTAD/World Bank WITS/TRAINS Database.

Apart from traditional trade theory, the reform process was justified by statistical evidence linking openness to growth (Dollar and Kraay, 2004; Sachs and Warner, 1995). However, as David Dollar emphasised on a number of occasions, these were statistical results with a number of countries falling above and below the central finding. Moreover, Rodrik and Rodriguez (2002) roundly criticised the robustness of the statistical results.

It is therefore surprising that not enough attention was paid to why some countries did better and some worse than average. For example, while the reforms brought about some remarkable success, notably in India and China that achieved real growth rates of 9-10 per cent and export growth in the order of 20-30 per cent over a decade, these and other East Asian reforms were scarcely orthodox – indeed in their reliance on pro-active measures they are sometimes considered to be examples of the application of Krugman's strategic trade theory. In Africa, on the other hand, which swallowed the orthodox medicine "straight up", there have been cases of industries closing down with no signs of newly emerging activities. In the Philippines and Brazil, growth rates after the reforms were slower than prior to the reforms, although the situation seems to have improved in Brazil and indeed many other developing countries under the commodity price boom of recent years. (This is discussed further in the section on national trade policies).

Of course, there are many explanations for growth and it would be wrong to attribute poor performance uniquely to changes in trade policy, but since trade policy was a key element in many structural adjustment programmes, there is a perception that the extent and pace of trade

liberalisation has to take at least some of the blame for the negative results (and some of the credit for the positive outcomes!).

A reappraisal of the impact of trade reforms intensified following the global economic slowdown in the wake of the Asian, Russian and Brazil crises of 1997-98 – some two years after the conclusion of the Uruguay Round and establishment of the WTO (as has the role of the state during the 2008 crises). The long overdue revisiting of the orthodoxy represented by the Washington consensus was signalled in a number of ways. First, there was the intellectual challenge by Stiglitz and Rodrik, who queried the emphasis placed on openness and the lack of attention to institutional and governance issues. Second, problems in implementation of the WTO Agreements led to the breakdown of attempts to launch a new negotiating round in Seattle in 1999. Third, the 1990s saw a dramatic increase in the number of regional trade agreements. And, finally, there was an emergence of growing evidence of the failure of the trade reforms, especially in Africa.

2.1 The WTO Processes

After a series of failures to reach agreement, the WTO negotiations remain in a state of stagnation with minimal progress, despite the downscaling of the agenda by removal of contentious issues such as competition policy, investment and transparency in government procurement. After the major success in concluding the Uruguay Round in 1994 and establishing the WTO in 1995, followed by agreements in the areas of information technology (1996), basic telecommunications (1997) and financial services (1997), what has led to the stagnation in the WTO processes and some apparent disillusion with the WTO system in a number of developing countries?

While trade negotiators often seem mercantilistic, the fact is that today most are aware that multilateral liberalisation is more valuable globally than unilateral liberalisation or liberalisation within a regional agreement, bringing about great synergy in economic activity, although of course that is not to say that all players will benefit equally. Obtaining greater access to foreign markets – valuable in itself – may also be presented at home in trying to "sell" domestic reforms. Thus, there are overall net economic and politico-economic gains from the multilateral processes.

In essence, the multilateral process is a cooperative game. In the film "A Beautiful Mind", John Nash – foreshadowing his Nobel-prize-winning work – explains to his male college friends in the bar why Adam Smith is wrong in arguing that competition always produces optimal results. Nash says that if the men all compete for the most beautiful girl, none may finish up with a girl. But if the men cooperate, then they may each get a girl, even if she is not the most beautiful. The difficulty facing trade negotiators is to resolve the conflict between the desire to obtain the maximum gains for one's own country, but in doing so perhaps postponing any gains or failing to achieve any outcome, and the need to cooperate by making greater concessions (offers to liberalise) in order to achieve a successful outcome.

While it is ironical that economists would generally advise making the maximum concessions because that would produce greater economic welfare than no liberalisation, the trade negotiator tends to hold out for others to liberalise as well. But, if negotiators take a hard mercantilist line, the outcome is likely to be minimal liberalisation – as we have seen in the

Doha negotiations with the estimated gains being downgraded by economists as the Round plodded on. It would seem that often the mercantilist instinct dominates, and perhaps the fear of offending powerful special interest groups – such as farmers in some major economies – is greater than the desire to pursue welfare gains which are spread thinly across society.

Another factor that is now being more widely recognised is that not all countries gain equally from multilateral negotiations, and there may indeed be losers. To some extent, the international institutions had been reluctant to acknowledge this reality and there had been a tacit accord over the years to talk up the benefits of trade and the multilateral system, based on earlier research and basic economic theory. It has always been accepted by economists that there would be a contraction and expansion of individual sectors of national economies as their trade interventions and other supports were liberalised, but this was part of the accepted political economy whereby losses in one sector would be offset by gains in others, and this kind of national restructuring would produce overall gains. However, recent research by Fernandez de Cordoba, Laird and Vanzetti (2005) and others shows quite clearly that, on the one hand, the structural shifts are not a seamless, smooth process, and, on the other hand, there may indeed be winners and losers from multilateral liberalisation between, as well as within, individual countries. Apart from structural change, these authors also highlight potentially important tariff revenue losses in a number of small countries that are dependent on trade taxes. In addition, World Bank (2006) findings suggest uneven effect on poverty. Again, Bouët, Fontagné and Jean (2006) in a study for the World Bank suggest that preference erosion may be a problem for some very poor countries.

Most recently, the Commission on Growth and Development (2008) (hereafter the Growth Commission) noted that relying on markets to allocate resources efficiently is clearly necessary but "that is not the same thing as letting some combination of markets and a menu of reforms determine outcomes". The Commission goes on: "Wedded to the goal of high growth, governments should be pragmatic in their pursuit of it. Orthodoxies apply only so far . . . if there were just one valid growth doctrine, we are confident we would have found it." The Commission notes that economists can say with some confidence how a mature market economy will respond to policy prescriptions, "but mature markets rely on deep institutional underpinnings, institutions that define property rights, enforce contracts, convey prices, and bridge informational gaps between buyers and sellers" which, it says, are often lacking in developing countries.

Noting that an important part of development is precisely the creation of these institutionalized capabilities, the Growth Commission states that: "We do not know in detail how these institutions can be engineered, and policy makers cannot always know how a market will function without them. The impact of policy shifts and reforms is therefore harder to predict accurately in a developing economy. At this stage, our models or predictive devices are, in important respects, incomplete. It is, therefore, prudent for governments to pursue an experimental approach to the implementation of economic policy." In this respect, the Commission quotes Deng Xiaoping's oft-quoted dictum to "cross the river by feeling for the stones," and it argues that governments should sometimes proceed step by step, avoiding sudden shifts in policy where the potential risks outweigh the benefits. This will limit the potential damage of any policy misstep, making it easier for the government and the economy to right itself. It also notes that making policy is only part of the battle: policies must also be faithfully implemented and tolerably administered.

While the Growth Commission remarkably says almost nothing about trade policy, it touches on a number of closely related areas including briefly what it calls the "great symbolic importance" of the Doha Round, apparently accepting the downgrading by many economists of the economic significance. In the areas of export promotion (including explicit or implicit subsidies but not trade fairs, etc) and industrial policy (in particular targeting, rather than cluster group formation, etc), the Growth Commission indicates the various sides of the debate that were heard during its work.

While orthodoxy suggests that neither export promotion nor industrial policies work, then the Commission – in a clear break with orthodoxy – suggests that: "If an economy is failing to diversify its exports and failing to generate productive jobs in new industries, governments do look for ways to try to jump-start the process, and they should."[3] However, the Commission hedges its bets by arguing that these efforts should bow to certain disciplines. "First, they should be temporary, because the problems they are designed to overcome are not permanent. Second, they should be evaluated critically and abandoned quickly if they are not producing the desired results. Subsidies may be justified if an export industry cannot get started without them. But if it cannot keep going without them, the original policy was a mistake and the subsidies should be abandoned. Third, although such policies will discriminate in favour of exports, they should remain as neutral as possible about which exports. As far as possible, they should be agnostic about particular industries, leaving the remainder of the choice to private investors. Finally and importantly, export promotion is not a good substitute for other key supportive ingredients: education, infrastructure, responsive regulation, and the like."

Thus, it seems that, at least among professional economists, science is pointing to some serious re-examination of orthodoxy – albeit more than 20 years after the publication of Krugman's work.[4] This reflection looks more and more like scepticism about the benefits of trade liberalisation or at the least the path as well as timing and sequencing, as well as overdue recognition of welfare economics. No doubt many in the developing world are thinking "about time, too" or "we told you so".

Apart from the concern about the failure of reforms in a number of countries, it is also fairly clear that many developing countries felt that they were cheated in the Uruguay Round, where it had been promised by various international organisations that there would be trade gains of $300-500 billion. They asked the question "Where is the cheque?" This is a reference to predictions by the World Bank and the OECD that the Uruguay Round would lead to these huge gains. In fact, it seems likely that these gains were overstated, as the simulations used to make the predictions were based on applying the negotiated MFN tariff cuts to applied rates stored in modelling databases such as GTAP, whereas in the case of developing countries in particular applied rates were already well below legally bound rates. Other concerns related to the back-loading of liberalisation in the textiles and clothing sector to the end of the implementation period in 2005, and, since then, concerns that the gains are mainly being captured by China at the expense of other developing countries which had previously

[3] This was an argument heard in the World Bank while the author worked there in the late 1980s.

[4] Of course, second best argument are not new – look at Pigou's work on Wealth and Welfare published in 1912 – later heavily criticised (although criticism of Pigou's role for the state looks weaker in the light of the financial crisis of 2008) - or James Meade's Trade and Welfare published in the 1960s, but it often seems that policy makers prefer to focus on a naive, simplistic version of theory that appeals to their vision.

guaranteed market shares under their quotas. Similarly, there were other concerns about the application of special and differential treatment for developing countries that often were expressed in the form of "best endeavours" rather than firm legal commitments.

Inevitably, this kind of oversell of the gains from the Uruguay Round leads to the kind of situation envisaged by Akerloff in his theory of "lemons" (a dud car in U.S. usage). Nobel economics laureate George Akerloff focused on the impact that asymmetric information between buyers and sellers has on the market for used cars. The lemons have hidden defects known only to the seller. Since buyers cannot easily distinguish lemons from other cars, they assume that all cars are lemons, and will only be willing to offer a discounted price, with the effect of driving down the prices of all used cars. Analogously, the developing countries feel that they were sold a lemon in the Uruguay Round and it has become correspondingly difficult to persuade them of the benefits of the Doha negotiations and of trade liberalisation, especially when key parts of the Doha Declaration seem to be blithely ignored or reinterpreted.

Other problems facing the WTO that have affected the current multilateral negotiations include the extended scope of the WTO into areas such as farming, services and intellectual property. The new unified, binding dispute settlement mechanism provides protection for smaller players but the process is expensive and large players have dragged their feet on implementing unfavourable decisions. In addition, there have been controversial decisions in the shrimp/turtle, tuna/dolphin, and beef hormone case and more is expected to follow on the use of GMOs. Recent decisions on sugar and bananas have been welcomed by some developing exporters (e.g., Brazil, India, Latin American countries), but others that previously benefited from preferences claim that large sections of their economies will be destroyed (Mauritius, Caribbean countries, etc.). NGOs have also attacked the WTO practice of holding non-public meetings, while some of the smaller WTO members have attacked the use of small group meetings ("green rooms") of key players to resolve issues. Overall, these factors have contributed to an image of the WTO as a powerful, intrusive, non-transparent and non-democratic organisation that is insensitive to the environment and social issues.

In this situation, it is not surprising that attempts to broaden the scope of the WTO to include labour standards, investment, environment, and competition policy failed, while the inclusion of trade facilitation has been treated with suspicion. Delays in allowing developing countries without their own manufacturing capabilities to allow imports of generic drugs to treat AIDS have only served to deepen distrust.

After the failure of the WTO Ministerial Conference in Seattle towards the end of 1999, there was a collective sigh of relief among members when the WTO was able to launch the Doha Work Programme in Qatar in 2001, perhaps due to the conjuncture of the economic slowdown of that year and concerns about the economic impact of the 11th September attack on the World Trade Centre in New York. However, the post-Doha work programme has continued to suffer from delays, up to the failure in July 2008 – despite yet another "July package" that attempts to paint the Ministerial meeting as progress.

Much of the work of the last four years has taken place under the framework agreement of 1 August 2004 (also a "July package"). That package set out general frameworks for negotiations in five core areas: agriculture, market access on non-agricultural products, services, development issues and trade facilitation. Negotiations were expected to produce a package of detailed and specific negotiating modalities (an "end-game document") as the basis for

negotiating outcomes to be adopted at the Hong Kong Ministerial Conference in December 2005 with the Round to be completed by the end of 2006.

However, moving the negotiations forward has been blocked by a series of clashes between developed and developing country groups on a wide range of issues as well as the clashes between exporters and, principally, the EU on agriculture. The expiry of the US Fast Track negotiations authority in March 2007 further complicated matters, and it has been obvious for some time that the deadlines were unrealistic and that there has been repeated failures to recognise the extent of the divide. It is fair to say that developed countries substantially underestimated the determination of the developing countries to stick together and hold them to the Doha promises.

Assuming that the Round is resumed seriously – presumably after the US and Indian elections – any advances are still subject to full agreement on negotiating modalities, and much depends on the formulae to be used in agriculture and non-agricultural products as well as issues such as special safeguards for sensitive products and other flexibilities in agriculture and NAMA. The World Bank has estimated that if sensitive products are sufficiently widely defined, the gains in agriculture will be negligible. However, World Bank and UNCTAD estimates suggest that the welfare gains from the negotiations could be in the order of $80-130 billion both in agricultural and non-agricultural products while welfare gains from liberalisation of the temporary movement of labour (Mode 4) in services could produce gains up to $300 billion. Impressive as this may seem, these amounts are less than 0.5 per cent of global income. However, as noted earlier, some studies note that these modest aggregate results conceal important sectoral movement – with losses in employment up to some 40 per cent in South Asian auto industry, but gains of 30 per cent in Indonesian leather, as two key examples. China would be expected to make further gains in textiles and clothing, provided it is not further restrained by anti-dumping or safeguard measures.

These estimates have led some commentators to suggest that it would not be a disaster if the negotiations were to fail, and there may have been some quiet satisfaction in some quarters after the failure of the July 2008 mini-Ministerial?? However, it is important to recall that the WTO plays an important role in a number of areas other than negotiations on the reduction of tariffs and other interventions. These are the areas of monitoring trade and policy developments, providing a framework for discussions and dispute settlement. Recent decisions on sugar, cotton, bananas and trade preferences have also shown the power of the dispute settlement mechanism to pry open markets. It is also a fact that the WTO was perceived as a forum where there could be continuous improvement of rules irrespective of any negotiations "round", and some substantive negotiations, such as the Information Technology Agreement, were concluded after the end of the Uruguay Round. Nevertheless there are some key areas such as agriculture, textiles and clothing and some service areas where a successful outcome to the multilateral negotiations would eliminate decades of discrimination against developing countries and could provide useful benefits for developing countries and some of the poorer segments of their populations, but inevitably this will entail some tough and political painful decisions.

Development was intended to be central to the Doha negotiations, which will largely be judged on that criterion. There are certainly many references to development and to special and differential treatment in the Doha Ministerial Decision. But it is difficult to predict the extent to which these will be implemented and what will be the development impact. With the constant

downscaling of estimates, perhaps not much will be lost, although there have been concerns that liberalisation forced on developing countries as well as the tightening of WTO rules could limit the ability of developing countries to adopt certain trade and industrial policy measures. Another factor to be taken into account is the significance of the multilateral trade negotiations vis-à-vis other issues such as the development of supply capacity, which may be much more important, especially for the least developed countries. In this context, an Aid for Trade Package, suggested by the UN Millennium Development Project Task Force under Jeffrey Sachs,[5] would go a long way in enabling developing countries, especially LDCs, to meet adjustment costs, build trade-related infrastructure and supply capacity in order to benefit from opportunities opened up by the current negotiations.

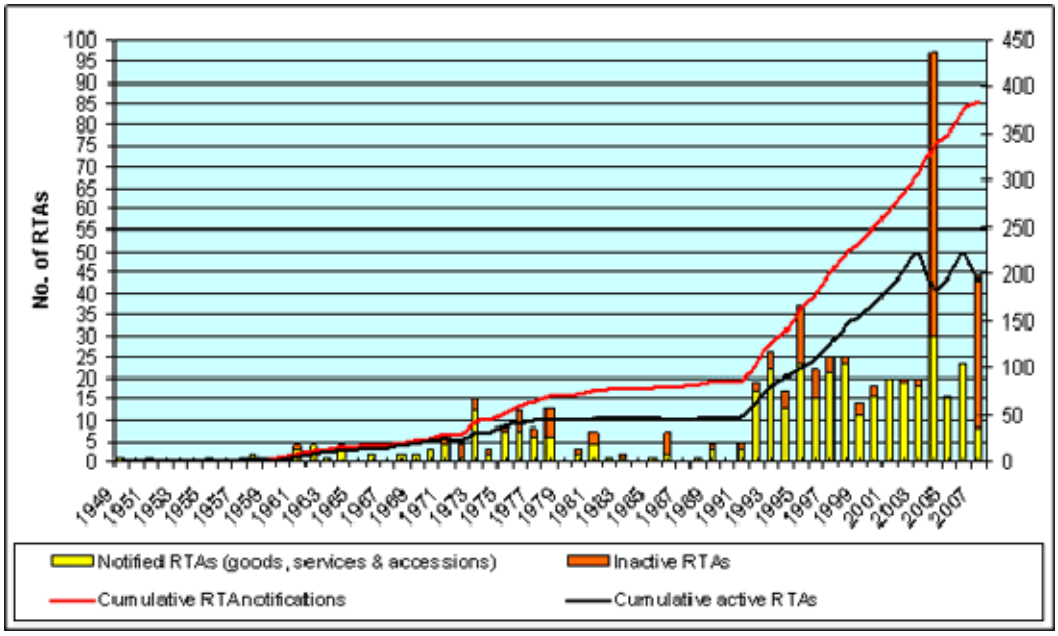
The Hong Kong Ministerial Declaration that Aid for Trade should aim to help developing countries, particularly LDCs, to build the supply-side capacity and trade-related infrastructure that they need to assist them to implement and benefit from WTO Agreements and more broadly to expand their trade. Aid for Trade was seen as a valuable complement to the outcome of the negotiations. Subsequently, the Director-General of WTO created a Task Force to make recommendations on how to operationalise Aid for Trade, consulting WTO members, the IMF, the World Bank, other relevant international organisations and regional development banks on appropriate mechanisms to secure additional financial resources for Aid for Trade. However, while a great deal of information has been collected and reviewed, the bottom line seems to be that no new money will be forthcoming, and developing countries are concerned that any funds that are made available would be subject to the kind of conditionalities that were part of the Bretton Woods institutions' structural reform packages (Laird, 2007).

2.2 Trends in the Formation of Regional Trade Agreements

Another challenge to orthodoxy arises from the proliferation of bilateral and Regional Trade Agreements (RTAs) since the beginning of the 1990s, leading to a number of concerns as to their compatibility with the multilateral system and to the distributions of the welfare effects (Bhagwati, 1992). Figure 2 shows the proliferation of RTAs on a chronological basis by differentiating between two time periods, the GATT and the WTO years; the latter is the period we tend to associate with the current wave of RTAs. Notably, Figure 2 shows that of the total number of RTAs notified to the GATT/WTO up to December 2006, 124 were notified during the GATT years and 243 during the WTO years; this amounts to an annual average RTA notification of 20 for the WTO years compared to less than three during the four and half decades of the GATT. Also significant is the fact that of the GATT notified RTAs, only 36 remain in force today, reflecting in most cases the evolution over time of the agreements themselves, as they were superseded by new ones between the same signatories (most often going deeper in integration), or by their consolidation into wider groupings.

[5] UN Millennium Project 2005, "Investing in Development: A Practical Plan to Achieve the Millennium Development Goals. Overview, UNDP New York 2005

Figure 2: RTAs Notified to the GATT/WTO (1948-2006), Currently in Force, by Year of Entry into Force



Source: WTO Secretariat.

The new wave of RTAs bears some distinct features.[6] Breaking with the past, when RTAs were often signed between countries of the same geographic region, there has been a noticeable rise in the number of overlapping and inter-regional RTAs, with North-South RTAs, under which developing countries offer reciprocal treatment, becoming more common. A substantial number of developing countries have already entered into or signed RTAs with a developed country partner. In addition, these agreements now have substantially enlarged scope, covering services, government procurement, intellectual property, competition policy, labour standards, and so on, although the agricultural sector is often subject to fewer commitments. A few RTAs (e.g. Canada-Chile, Australia-New Zealand, the European Economic Area) take a radical approach in traditional areas, for example, by abolishing contingency protection measures such as anti-dumping.

While these agreements all represent liberalisation beyond the status quo, and seem to offer benefits for participants, a number of different approaches have been followed, especially in the treatment of issues that are not (yet) covered by the WTO, and this could well pose a number of problems for multilateralism. Moreover, third countries may well suffer from negative trade diversion.[7] Bhagwati (2002) also worries about the effects on the multilateral trading system itself, which he believes can

[6] See for example, Cernat and Laird (2005) and Abuggatas (2004)

[7] However, Laird (1999) notes that third countries could well benefit if the creation of the new RTA attracts investment, growth faster than before and draws in trade from third countries, as in the first 6-7 years of MERCOSUR. Similarly Hartler and Laird (1999) note that the EU-Turkey Custom Union was beneficial to third countries as Turkey substantially liberalised its trade and adopted more transparent practice,

be weakened by RTAs. Another concern refers to imbalances in bargaining power when such agreements are negotiated between partners having different levels of development.

However, it seems likely that, in the wake of the various unilateral reforms starting in the mid-1980s, many developing countries wanted to cement their reforms by entering into RTAs that would make policy reversals less likely.[8] The establishment of the new North-South and East West agreements has also been for political and security reasons, as well as economic factors. More generally, it is also likely the most recent mushrooming of RTAs is due to frustration with the slowness of the WTO multilateral processes. It is likely too that there is some kind of knock-on or demonstration effect, with no country wanting to be left out while others are forming such agreements.

Overall, the trends in the establishment of RTAs is perhaps the single most important challenge to orthodoxy in trade, as mainstream economic thinking continues to favour the multilateral route to trade liberalisation, while nations forge ahead with the establishment of new arrangements almost on a day by day basis. The recent failures in the WTO might well give further impetus to RTA formation.

2.3 Revisiting Autonomous Reforms

The Operations Evaluation Department of the World Bank has recently undertaken an evaluation of the effectiveness of trade-related lending operations. In a sense this is long overdue, but the fact that the exercise is being carried out at all suggests that there are some concerns about trade policy reforms. Indeed it is remarkable that after some 15 years of experience with national trade reforms, there is still no magic formula that guarantees monotonically increasing level of welfare under reform. The very existence of "structural adjustment" lending suggests that there was awareness of potential problems, but in practice the focus of such lending was on the design of liberalisation packages and relatively little attention was paid to the design of the adjustment process itself. The funding was essentially seen as the buffer to cope with potential balance of payments problems as countries liberalise and imports expand ahead of the build-up of export supply capacity.

However, apart from some notable examples of success, it is clear that there is still an issue as to how to generate a supply response in the wake of a reform programme. The idea of some kind of proactive support, such as export subsidies, promoted by some Bank staff, largely ran foul of ideological stances (e.g., "if there is a problem, not enough has been done" - and not that the programme has design flaws). Moreover, the possibility of using policy tools, such as subsidies, to overcome market failures are increasingly running up against limitations imposed by expanding WTO rules. Recent work by Laird and Fernandez de Córdoba (2006) also suggests that there is need for caution in asking countries to embark on ambitious reform programmes, since reform-minded governments could risk being replaced by others that take a more protectionist stance, which would result in reforms being stalled, if not reversed.

Laird and Fernandez de Córdoba (op.cit.) reach a number of conclusions on the lessons to be learned from the reform experience, based on eight country studies commissioned under a UK DFID project.[9] A number of the findings do not depart from orthodoxy, at least in its narrowly defined focus on market reforms. However, the studies do confirm commentary from the "non-

[8] Laird (1999) cites this as a reason for Mexico's enthusiasm for participation in NAFTA.

[9] The countries were Bangladesh, Brazil, Bulgaria, India, Jamaica, Malawi, the Philippines and Zambia. The full report is available at http://192.91.247.38/tab/events/namastudy/coping.asp

orthodox" positions as to the importance of institutions, good governance, and so on. Perhaps less well understood are the significance of the greater capacity of large economies to absorb reforms, the importance of investment liberalisation ahead of trade reforms, the importance of substantial targeted funding to facilitate reforms, the tremendous importance of expenditure on transport-related physical infrastructure, and the need to address the high cost of capital that seems to be endemic in many developing countries.

What is also clear from the studies is the almost total lack of attention given to the need for social safety nets to offset the negative effect of reform as labour markets shake out during structural changes. This may be the single most important social issue that has been given scant attention in reform programmes, but one which can make or break governments as public support for reforms are implemented. Martin Rama at the World Bank has been one of the few economists who have focused extensively on the design of adjustment programmes to address the labour market issue and it is clear that much more work is needed along these lines.[10]

The international financial institutions, with their considerable technical expertise in a wide range of projects, can play an important role in helping developing countries to implement or extend programmes to address the wider adjustment issues, fostering supply-side programmes and addressing social safety nets. The WTO process can also help by providing for anticipated liberalisation in areas where the developing countries have comparative advantage. This would help create jobs ahead of job losses in sectors that are likely to suffer from increased competition as their own barriers are lowered. The WTO could also usefully address systemic and rules-related issues with the aim of allowing policy space for development purposes. This was partly envisaged in the original GATT, but it seems that such options, including the use of support policies in the presence of externalities, are being closed off to developing countries.

The GATT/WTO has traditionally been silent on the issue of adjustment, leaving this entirely up to national policies to address, with or without the support of the Bretton Woods institutions in the case of the developing countries. Unfortunately, while attention has been given to the importance of "aid for trade", as discussed earlier it is not evident that new funding will be found and there are concerns that such funding as becomes available may be tied to the same kind of programmes that caused some of the adjustment problems in the past. The challenge is – still – to design efficient adjustment mechanisms, as well as to ensure their funding and find ways to effectively integrate them into the negotiating outcomes.

3. Conclusion

The substantial re-think now being seen about trade policy prescriptions for developing countries is based on a revaluation of effects – empirical results – rather than any revision of theory, although Krugman certainly deserves credit for his early challenge to conventional wisdom. Of course, much of the economics profession and the international lending agencies still consider free trade as the optimal policy in the longer term. However, this has always been subject to some qualifications – for example, the theory of the second best has been an important qualifier for many decades (see Meade's Trade and Welfare written in the 1960s), and the carefully crafted comments by the Growth Commission are a welcome reminder of theory and the limits of economic science.[11]

[10] See, for example, Rama (2003).

[11] The cautious case for industrial policy interventions by such a respected body would certainly have taken much of the heat out of the debate raging in Geneva about "policy space" in the last few years.

Moreover, for at least 20 years there have been concerns about the timing and sequencing of reforms, with widespread if not universal agreement on the need for macro-economic stability before launching into more far-reaching trade reforms. The fine-tuning of the Washington consensus to include attention to the quality of institutions and building supply-side capacities is also welcome, but in practice these have also been part of World Bank programmes for many years (although Mr Wolfenson certainly gave them greater prominence in public statements).

The unfortunate experience of some developing countries, especially in Africa, did not go unnoticed by the anti-globalisation movement, which has been effective in inhibiting the reach of the WTO and the progress in the current negotiations. This reaction has some justification, although equating the WTO system with free trade really misses the point that, beyond the basic GATT articles on MFN and national treatment, many of the WTO rules are less about free trade than about setting a framework for trade intervention, e.g. for health and safety reasons, for national security, to stop dumping or unfair subsidisation (not always very effectively) and so on. On the other hand, the pressure placed on developing countries by developed country negotiators to open their markets – despite the emphasis in Doha on development, including "less than full reciprocity" – shows a sad lack of awareness of recent experiences in Africa and elsewhere and the consequent re-thinking of policy, as well as scant regard for the letter and spirit of the Doha Ministerial Declaration. Equally serious is the failure of delegates to appreciate that international negotiations are not a football match with each side trying to score a goal at the other's expense, but a cooperative game in which the participants are trying to strive towards a solution that is of general benefit and takes full account of each other's concerns.

It is clear that some of the criticisms of the liberal trade orthodoxy are valid, and, in trade, there have often been programmes that were implemented too quickly, based on a standardised approach, and again the Growth Commission highlights the need for caution, commending Deng Xiaoping's dictum to "cross the river by feeling for the stones". In effect the Commission is confessing our ignorance and emphasising the need for constant monitoring of the implementation of policy reforms. While there have been some highly positive results – and we need to learn better how to emulate those cases – trade reforms have been implemented without adequate attention to supporting polices and measures in a number of cases. If we have learned anything from the experience of the last 10-15 years, it is that one size does not fit all, and greater attention needs to be paid to the specificity of cases in tailoring effective reform programmes. In this context, proposals to provide "aid for trade" in support of future reforms are a welcome recognition of the need to address the development challenges in trade reforms, but the debate gives rise to concerns about the adequacy of funding for this initiative as well as concerns that aid for trade does not become an excuse for ideologues to press forward with conditionalities that repeat the mistakes of the past.

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AID FOR TRADE FOR LEAST DEVELOPED COUNTRIES IN THE GLOBAL TRADE SYSTEM

*William M. Lyakurwa**

1. The Objectives of Aid for Trade

Although developing countries are witnessing economic progress, their gains from trade have been uneven. One outcome has been the two faces of developing countries that we see today: one of robust growth built on outward-looking policies that encourage trade and the other where the potential for enhanced trade remains constrained and therefore suboptimal. These two faces are due partly to the opportunities trade liberalisation creates for development, but other factors determine the extent to which those opportunities are realised. In addition, any gross welfare gains from trade liberalisation must be balanced against its associated costs. To realise the full benefits of global trade opportunities, least developed countries (LDCs) must incur production costs, marketing costs and policy costs. These costs are automatic and usually up front, and may be beyond the reach of entrepreneurs and governments in poor countries, thus inhibiting participation in global trade.

To help close the gap, the proposal that World Trade Organisation (WTO) members develop an aid for trade (AfT) package arose in the context of negotiations on the Doha Round. AfT was officially put on the WTO agenda at the 6th Ministerial Conference in Hong Kong in December 2005. The objective of the Hong Kong mandate is "to help developing countries, particularly LDCs, to build the supply capacity and trade-related infrastructure that they need to assist them to implement and benefit from WTO agreements and more broadly to expand their trade". AfT is also expected to assist developing countries in trade policy reform. This includes, for example, training trade negotiators, improving customs procedures and ensuring countries implement laws to comply with the Trade-Related Intellectual Property Rights Agreement (TRIPs).

At the Hong Kong Ministerial Conference, WTO members instructed the WTO Director-General, Pascal Lamy, to set up a task force to provide recommendations on how to make AfT work. The first set of recommendations was submitted to WTO members on 27 July 2006. The task force recommended, among other things, that AfT be guided by the Paris Declaration on Aid Effectiveness, applicable to all parties (WTO AfT Task Force, 2006). The task force also said that country approaches were key, including mainstreaming trade in national development strategies; that donors should integrate trade more fully into aid programming, strengthen trade expertise and coordinate their efforts better. The role of regional development banks was emphasised, and assistance for regional integration and monitoring and evaluation of AfT was termed a critical component.

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The Task Force recommended several additional guidelines for the implementation of AfT. These included strengthening country ownership of aid programmes and country-based formulation of trade-related needs and priorities, and strengthening the donor response to trade-related needs and priorities. In short, the bridge between country demands and donor responses at the country, region and global level needs to be stronger.

While these challenges should motivate donors and help identify recipients, aid disbursements should serve the purpose of promoting future exports, not compensating the loss of past exports. The objective should be to put resources into increasing the volume and value-added of exports, diversifying export products and export markets, and attracting foreign investment to generate jobs and exports and reduce poverty.

This paper is intended to point out the crucial and necessary connection between aid for trade and more trade in the development process of the poorest countries. It was apparent in the WTO agenda at the 6th Ministerial Conference in Hong Kong that LDCs need both more aid and more trade, but will more aid imply more trade and economic growth? After this brief introduction, the remainder of the paper is organised as follows: in the next section we discuss possible institutional frameworks for the delivery of aid for trade, then move on to areas in which AfT is needed. The next stage is to analyse what can be done, then to examine AfT priorities and assess the challenges in AfT operations. Drawing on this foundation, the presentation makes some recommendations on the way forward for both donor and recipient countries, and then provides a brief concluding statement.

2. Institutional Framework for Aid for Trade Delivery

In most LDCs, the political economy jeopardises the use of trade as a tool for growth and the capacity for sophisticated economic interventions is limited. Any institutional framework for implementing aid for trade should consider alternative models and theories. Of particular importance here are the aid effectiveness principles of the Paris Declaration, the spirit of which requires donors to tailor their approach to building trade capacity and level of ambition to a country's political and economic reality and its capacity to design and run effective programmes. The Drivers of Change (DoC) approach articulated by the Department for International Development is one method of applying such an analysis to the development of donor strategy. The DoC approach is not intended to manipulate local political economy conditions per se, but rather to ensure that the country and the donors understand the nature of the obstacles posed by political economy, including both formal and informal institutions, power bases and vested interests. One way of facilitating this effort is by involving local research institutions and publishing the results of the studies. The DoC approach can provide an explicit evidence base for the assumptions that inform programmes. It can also determine the nature and extent of "political will" for reform or the lack thereof, and the role this may have in the success of a programme. Other aspects of the DoC approach are the identification of the role of non-poor groups in change processes and collaboration with non-traditional partners. It is also necessary to take steps to discontinue programmes that have little chance for success.

In the case of small, localised projects for which a full scale DoC analysis may not be practical, other tools may have to be used. These could include analyses of the key stakeholders in the effort – the actors and institutions that need to own the programme to ensure a minimum level of effectiveness – and the development of pilot projects that are likely to deliver good results relatively quickly. Finally, when a state is weak, projects aimed at building capacity in the private sector and civil society might perform better. Adapting initiatives such as the one village-one product approach developed by Japan to work directly with local authorities or the private sector can tangibly increase the benefits from trade, and may also stimulate and strengthen the demand for change and better policies from the private sector and civil society (OECD, 2006).

More formally, the most comprehensive institutional AfT approach is the Integrated Framework (IF) for Trade-Related Technical Assistance to LDCs, which brings together multilateral agencies (the International Monetary Fund [IMF], International Trade Centre [ITC], United Nations Conference on Trade and Development [UNCTAD], United Nations Development Programme [UNDP], WTO and the World Bank) and bilateral and multilateral donors. The IF has two objectives: to integrate trade into national development plans such as the poverty reduction strategies (PRS) of the LDCs and to assist in the coordinated delivery of trade-related technical assistance in response to needs identified by these countries. The basic principles of the IF are country ownership and partnership. Financing is through a two-window Trust Fund, Window I finances the Diagnostic Trade Integration Studies (DTISs), and Window II, created in May 2003, provides a special facility to finance high priority projects. To date, however, the IF has had very limited success. The main problem lies in poor implementation at the country level. For example, a June 2006 report from the IF Task Force found significant shortcomings including lack of finance and human resources, low levels of implementation, disjointed governance structures, inadequate donor responses, and very weak country ownership (IATP, 2006).

Other frameworks for assisting LDCs include the Joint Integrated Technical Assistance Programme (JITAP), which helps African members participate in the Trade Integration Mechanism (TIM) of the WTO and IMF, a policy to make it easier for countries to access IMF funds to help with problems arising from multilateral trade liberalisation. To date, only two countries, Bangladesh and the Dominican Republic, have made use of the TIM. Evaluations of existing trade-related technical assistance programmes have highlighted serious weaknesses including unsystematic or incomplete needs assessments; weak project management; fragmented technical assistance interventions with insufficient linkages to broader development programmes; and weak linkages to poverty reduction (IATP, 2006).

Even the few developing countries and particularly LDCs that have accessed the available programmes have not experienced an optimal aid for trade effect. The best institutional structure for managing aid for trade would therefore address some of the most urgent challenges facing these countries, especially those related to development objectives. While the IF's Trade Diagnostic Studies form a solid basis for identifying needs, each country needs to develop a coherent trade strategy within which additional projects to support trade facilitation and adjustment could be planned. A modality towards this goal could be devoted to building sustained capacity within Ministries of Trade and other key agencies responsible for advocating and implementing trade policy reforms to engage in this kind of policy design and implementation. The IF could also assist with programmes intended to eliminate constraints to

trade expansion, like poor infrastructure and high transaction costs. Extending IF activities beyond LDCs to other low income countries could support regional trade integration by addressing supply-side constraints at a multi-country level. Such an expansion of the IF, coupled with better integration into the poverty reduction strategy paper (PRSP) process would require increased donor resources, most particularly for the IF Secretariat (within the WTO Secretariat) and for the needed research to support linkages to the PRSPs. Another priority resource demand would be the institutional strengthening of in-country IF focal points and AfT Trust Fund management and fiduciary functions (IMF and WB, 2005).

3. Where Aid for Trade Is Needed

Aid for trade is important for LDCs because integration is critical to the realisation of the benefits of trade in globalisation. The productive capacity challenges, marketing constraints, trade policy and regulation challenges are key reasons why LDCs need AfT to realise their optimal trade potential in the global trading system.

3.1 Production Constraints

Productive resources, entrepreneurial capabilities and production linkages together determine not only the overall capacity of a country to produce goods and services, but also what goods and services the country can produce. The reason for this is that productive capacities are not always generic – rather, they are often activity-specific. Notwithstanding, LDCs' productive capacity is characterised by low productivity as a result of rudimentary tools, primitive techniques, lack of production skills, and limited application of research and development in the sector. For example, outside South Africa and Mauritius, training institutions are weak and their programmes are poorly endowed with necessary skills and tools to promote product diversification (Lyakurwa, 2007b).

Inadequate infrastructure is also an important source of supply constraints. Poor transport infrastructure can prevent local farmers from accessing large domestic markets and international ports; unreliable energy and water supplies can disrupt production or increase costs. In Uganda, for example, poor infrastructure cripples local exporters. More than 50 per cent of Ugandan roads are in poor condition placing a large burden on farmers. Transport costs associated with poor roads add the equivalent of an 80 per cent tax on exported clothing. Most companies rely on generators to bridge periods of blackout and to avoid damage to equipment from power fluctuations. This is far more costly than grid power, since the average generator installed by small and medium-sized enterprises in Uganda costs about US$25,000 and requires considerable ongoing maintenance and fuel costs. Power generation can increase business start up costs by more than 30 per cent (Juma, 2005).

Furthermore, despite the spectacular development of technology around the world, the technology divide between developed and developing countries is widening. The current research and development (R&D) model is one that largely precludes LDCs from defining or benefiting from the research agenda, and is instead dominated by international partnerships that do not interact effectively with indigenous knowledge systems. In LDCs themselves, capacity constraints and competing priorities mean that as little as 0.01 per cent of GDP is

allocated to R&D activities. This has implications for both promoting international competitiveness and fostering the link between traditional knowledge and innovation – a copy-cat approach with little innovation. Moreover, some new technologies are often not suitable or affordable to the LDCs who need them the most. Technology development agendas are driven by the needs of developed countries and the consumers who can afford to buy the technology. This has led to the stark contrast between the global research agenda and the needs of LDCs. For example, 90 per cent of pharmaceutical research is focused on products for conditions prevalent in developed countries, while 90 per cent of the disease burden is concentrated in developing countries (UNCTAD, 2006). In the global trading system, these incongruities prompt the challenge to focus AfT towards enhancing the ability of firms to meet production requirements by building production infrastructure and capacity conducive to international trade.

3.2 Market Constraints

While the share of developing country and LDC trade is largely determined by a country's ability to produce high quality goods and services and bring them competitively to international markets, market share is also affected by de facto tariffs. Typical developing country exports face higher barriers, both in the markets of industrial countries and in those of other developing countries, than industrial country products. For example, applied simple average tariffs for merchandise imports into industrial countries are approximately 3 per cent; for textiles and clothing and for agricultural products, which represent a relatively large share of developing country exports, average tariffs are 8 per cent and 27 per cent, respectively. Tariffs on imports into other developing countries are substantially higher, except for agriculture. Within product groups, tariff peaks that often exceed 50 per cent or, in agriculture, 100 per cent, are concentrated in labour-intensive products where least developed countries have comparative advantage. Furthermore, tariff escalation in which tariffs on processed goods exceed those on primary products substantially reduces the returns to developing country entrepreneurs engaged in activities with higher value-added. This hampers the diversification of exports, limits the accumulation of skills and capital, and thus helps to perpetuate dependence on a small number of unprocessed goods whose world demand grows little and whose prices are volatile (UNCTAD, 2006).

In addition, while liberalising access to developed economy markets points to significant benefits for developing countries, the benefits are unevenly spread. Some LDCs enjoy de facto protection in third markets as a result of preference margins and bilateral quotas under the Uruguay Round Agreement on Textiles and Clothing (ATC), but liberalisation erodes these preferences, causing LDCs to lose out to more competitive suppliers. A case in point is China's recent accession to the WTO, which allowed it to compete on equal terms with other developing countries, with sometimes disastrous results for the competitors. ATC quotas on textiles and clothing have constrained Chinese exporters, but upon conversion of quotas into multilateral tariffs, they are expected to gain market share from other suppliers, including low-income countries (UNCTAD, 2006).

Non-tariff measures further increase the barriers faced by developing country exporters, and reduce the transparency of market access conditions. For example, 40 per cent of LDC exports face substantial non-tariff barriers (NTBs), including import quotas and licensing, domestic

content requirements, sanitary and phytosanitary (SPS) requirements, customs procedures in developed country markets, and contingency measures. According to UNCTAD (2006), these NTBs doubled in the period 1994–2004, and there has been a sevenfold increase in testing and certification requirements since the conclusion of the Uruguay Round. Technical and SPS standards are increasingly complex and are generally developed with little involvement by developing countries; they have strained the capacity of developing countries to meet them. Furthermore, there are concerns about the scope for the discriminatory use of these measures. Together, non-tariff measures can add considerable uncertainty over market access – a market that appears accessible at the time of an export-oriented investment can close if the activity proves "too" successful.

Furthermore, product diversification in many LDCs, whether in agriculture, manufacturing or services, is hampered by low capacity. The export competitiveness of LDCs in particular indicates that the basic productive capacity in these countries is often rudimentary, with limited technological or export value added. Very few have been able to move away from the syndrome encompassing commodity dependency, low value addition and realisation, lack of viable diversification, and unfavourable terms of trade. The result is that their ability to cope with the emerging complex of sophisticated market access and entry conditions is negligible. Target areas of intervention by AfT could include trade-related infrastructure funding – including help to fund warehouses, cold chains, grading systems, marketing and promotion bodies, roads and port infrastructure, energy grids, and so on (UNCTAD, 2006).

A European Union evaluation of a selection of Latin American countries brings this point home. The analysis found that only 27 per cent of commitments had been disbursed over the study period, and resources dedicated to diversification were not used. Besides indicating weak strategies for diversification, the report also found that the scope of disbursed funding was limited. Support went mostly to large exporters rather than small ones because the bigger businesses were able to anticipate the necessary investments needed for increasing productivity, thus bypassing domestic smallholders whose productivity was much lower (OECD and WTO, 2007).

3.3 Policy Constraints

The implementation of relevant policies can lead LDCs to competitive participation in the global trading system, resulting in economic growth. However, trade policy capacity building is often narrowly focused on encouraging these countries to participate in the negotiations of interest to rich countries. It is often targeted at one-off issues, rather than contributing to building national capacity to understand, negotiate and implement trade agreements in a way that maximises development (Stiglitz and Charlton, 2006). Furthermore, WTO regulations designed to create a level playing field circumscribe traditional as well as innovative approaches to development. For example, there is concern that the kinds of strong industrial policies that played such an important role in the success of the East Asian countries may be circumscribed by current WTO rules.

In addition, developing countries are subject to the interpretations of regulations demanded by the advanced industrial countries. In the agriculture negotiations, net food importing developing countries have been assured that assistance will be provided in the event of rising

food import bills (IATP, 2006), but they face a core need that AfT should address: Many lack trade policy capacity and simply do not have the staff, finance or depth of skills to adequately represent their interests in trade negotiations – or to implement agreements and integrate their own trade policies into the changing global trade environments.

At the country level, actions of private persons who bribe and otherwise attempt to influence public officials so as to gain an undue competitive advantage or secure profitable government contracts corruptly skew trade advantage. In customs services, one of the major corruption risks is a high rate of duty to be paid, especially if the duty is discretionary. In such a situation it is easier and cheaper and often faster for businesses to bribe a customs officer rather than pay the duties or to avoid paying customs duties by under-declaring goods at customs – although such declaration is arguably riskier because customs officers may reveal the cheating during the verification of cargo (UNECA, 2005).

Furthermore, according to the World Bank (2005), administrative hurdles (for example, customs and tax procedures, clearances, and cargo inspections) contribute to 75 per cent of trade facilitation delays. Africa suffers from the highest average customs delays in the world, 12 days on average. Estonia and Lithuania require one day for customs clearance; Ethiopia averages 30 days. Unstable electricity supplies, congested borders and bureaucratic procedures make it a challenge to run a business in Africa (UNCTAD, 2006). It is logical therefore to conclude that actions by governments and the private sector to remove these administrative barriers are urgently needed. Moreover, where possible, the assistance of intergovernmental and international organisations like the World Customs Organisation, United Nations Economic Commission for Africa (UNECA), the African Development Bank (AfDB) and the Bretton Woods institutions can significantly improve the situation with customs procedures (UNECA, 2005).

4. What Can Be Done

Despite the range of existing trade facilitation programmes, many developing countries and particularly LDCs do not have easy access to these programmes. Moreover, existing programmes fail to address some of the most urgent challenges facing developing countries, especially those related to development objectives, including trade competitiveness and the need to increase productivity in their agriculture, manufacturing and service sectors with a view to increase employment and hence reduce poverty. For trade to strengthen LDCs' development processes, these countries must be enabled to address the challenges they face in production and trading with each other and with the rest of the world. AfT thus becomes an essential complement to international trade liberalisation as it can help these countries to realise the potential development gains and to mitigate the costs of adjustment and implementation. Developing countries need aid for trade designed for reducing transaction costs of various kinds (production costs, marketing costs, policy costs and infrastructure costs), many of them "behind the border", and for alleviating the social cost of trade liberalisation (UNCTAD, 2005; World Bank, 2005).

4.1 Build Productive Capacity

Productive capacities, trade and investment are interlinked and are mutually reinforcing elements of the national and international economic structure. The various production complementarities to which all kinds of production linkages give rise mean that the competitiveness of particular activities and individual enterprises depends not only on the productive resources and entrepreneurial capabilities within those activities and enterprises, but also on the competitiveness of the production system as a whole (Porter, 1990). Building international competitiveness in tradeable sectors should be a basic objective to be pursued in a step-by-step way focusing on real economy targets.

4.2 Improve Quality

Selling to the world requires that there be concerted efforts to benchmark quality of output, mindful of the competition in the markets. Production and quality can both be increased through staff motivation but also require technical capacity, including relevant and appropriate technology acquisition for improved performance. Quality assurance schemes and conformity with standards will address the issue of quality. Investing in full-scale research and development can be done with the aim of un-packaging and adapting technology to local conditions and addressing the needs of local producers to enable them to compete in international markets. However, there is also a need to reorganise institutions and set appropriate targets, while ensuring that there are adequate resources for arising challenges. Examples of institutions that would play a key role are national research institutes and agricultural research organisations. Clustering for benefits deriving from economies of scale is another way to strengthen the capacity of local producers. In agriculture, the creation of conditions for technology-based production capable of producing meaningful volumes would be desirable. Compliance with standards can be the only basis on which products will be accepted and ensure expansion (Juma, 2005).

4.3 Harness Technology

LDCs should build their technological capabilities in order to increase productivity, competitiveness and profitability and to address a changing external environment in terms of supply and demand conditions (Dahlman and Westphal, 1983; Dahlman and Amsden, 2001; Lall, 1992, 2004). Aid for trade can improve African business environments by contributing to the removal of supply-side constraints and the provision of trade-related infrastructure. This is the case in Germany and Spain, where although donor strategies are implicit, support for trade is expressed in many ways, from aid for agriculture and infrastructure to support for private sector development. Sometimes an agency-wide strategy paper on development cooperation overall has trade as a core component, e.g., the Australian Government White Paper (as noted in OECD and WTO, 2007). AfT in Africa should be seen in terms of its role in developing the capacity of the private sector.

4.4 Improve Skills

Improving access to labour markets, particularly by enhancing workers' skills, is a powerful tool for poverty reduction and a fundamental source of economic progress. Combining LDCs'

lower-cost labour with improved skills would enable these countries to compete more effectively in the global market. One of the classic success stories here is Singapore. Fifty two per cent of Singapore's real GDP per worker growth rate is explained by an increase in capacity to absorb new technology by investing in quality education and effective links to the world's technological leaders through trade (particularly machinery imports). Investment in R&D and technological cooperation at the regional and international level are also needed to build the scientific and technological basis for future economic relations. Coe et al. (1997) show that how much any single follower economy benefits from international R&D positive externalities depends on its distance from the frontier and its stock of human capital, as well as its integration with technology leaders through trade and foreign direct investment (FDI). These improvements can be achieved by channelling AfT to promote tertiary education, formal training, learning by doing and innovation (R&D).

4.5 Enhance Information and Communication

Information and communication technologies (ICTs) are unique in the way they can allow newcomers to leapfrog to state-of-the-art technologies. For one thing, ICTs play a critical role in the fragmentation of the global value-added chain and in shifting parts of production to different geographical locations. By using ICTs, firms are able to exchange knowledge and information online from anywhere in the world, communicate just-in-time with clients and suppliers, and deliver services efficiently and promptly. Biggs and Shah (2004) argue that members of ethnic networks do not have to rely on establishing long-term relationships with suppliers to get credit, as their reputation in the network provides enough information to lenders. It is also an indication that with readily available information, smaller firms in the business network have access to credit. The *2006 Global Competitiveness Report* (World Economic Forum, 2006) presents striking evidence to conclude that investment in ICT boosts competitiveness. In order not to hinder international competitiveness, both the trading communities and the public administrations in developing countries need to be institutionally and technologically aligned with their counterparts in neighbouring and overseas trading partner countries.

4.6 Seek Technical and Financial Assistance

Technical and financial assistance should be provided for improving infrastructure, productivity and diversification, and for development of facilities and systems to achieve compliance with SPS requirements and technical barriers to trade (TBTs). The Integrated Framework (IF) discussed earlier has considerable potential to assist these countries in identifying their trade needs. Strengthening export promotion agencies through technical assistance and institutional capacity building is crucial for attaining the objective of improved exports in the LDCs, moving from resource-based exports to value-added and high technological-content exports. It should be recognised that trade, investment and domestic reform, not aid alone, were the main drivers of economic development, but that financial assistance, strategically invested, could provide an important catalyst for export growth and competitiveness.

Most developing countries have limited access to overseas development assistance (ODA) grant resources and concessional lending. Non-concessional lending and equity investment will therefore be key in addressing the region's trade-related capacity and infrastructure needs. AfT

grants can provide crucial seed money for – and thus help activate – larger infrastructure programmes and other supply-side interventions that require non-concessional financing. Among the challenges are how to make multilateral lending more accessible, for example by facilitating "blending" with donor assistance, and how to increase the incentives for private investment in trade capacity building and expand the scope for public-private partnerships. There are ongoing policy decisions (and announcements) about infrastructure funding, but these are generally outside AfT discussions. One example is the Infrastructure Consortium for Africa jointly supported by African countries and by the European Commission, Group of 8 and key multilaterals (UNCTAD, 2006). A challenge is how to bring these issues together.

Further, there is potential for large returns from regional investments, as coordination failures may create a gap in the optimal provision of regional public goods. The availability of grant financing for regional public goods may help to bridge this gap. Likewise, the complexity of aligning national sovereign guarantees to access lending facilities for regional projects calls for the development of new regional financial instruments. The identification of a small number of pilot projects to test new instruments may help to build support for further regional initiatives.

4.7 Build Marketing Capacity

Given the untapped trade, investment and development potential for LDCs, proposals for building their market access take many forms. Several policy initiatives can be implemented to reduce the negative impact of such trade barriers and make market access and entry more effective. One major challenge for LDC producers and exporters, therefore, is the increasing prevalence of anti-competitive practices by foreign enterprises in their own markets and in international markets. In areas such as food and agriculture exports, where LDC exports are concentrated, these exports often face monopolistic and oligopolistic situations and are therefore at the mercy of price, quality and other stipulations set by large buyers with concentrated economic power rather than any WTO agreements. There is a need for capacity building in LDCs to create awareness about competition policy and establish their own legislation and mechanisms to deal with such anti-competitive practices. The international community should also be sensitive to the vulnerability of LDCs to anti-competitive practices and take measures to afford international consultation and cooperation as required. UNCTAD has been working with LDCs in this area (UNCTAD, 2005).

This is not to say that standards are not important; reasonable standards must be observed as they may enable LDCs to improve the technical quality of their products and processes. This is becoming critical for entry into high-income markets. But the imposition of standards in major markets that affect key products of export interest to LDCs needs to be disciplined, and positive measures need to be taken to build capacity in LDCs to monitor and comply with such standards. For example, the provision of WTO-bound duty free quota free treatment (DFQF treatment) by developed countries, coupled with effective standards-related capacity building in LDCs to overcome market entry barriers, is a move in the right direction (UNCTAD, 2005). More specifically, effective awareness raising, notably among LDC producers, particularly small and medium enterprises, of existing and upcoming standards and regulations should be promoted. This can be done through effective communication with governments and standard-setting bodies in importing countries about the impact of environmental requirements on the

compliance costs and profitability of producers in developing countries. The envisaged billion-dollar Aid for Trade Fund would provide much needed finance for meeting adjustment costs arising from trade reform, help provide the hardware and software of trade-related infrastructure, and supply capacity and competitiveness building in commodities, manufacturing and services (UNCTAD, 2005).

4.8 Build Trade Policy Capacity

A good policy environment is a key requirement for trade development, and it can also help ensure that the gains from trade are distributed equitably. But many poor countries need help to build the institutional capacity to address policy challenges and to participate optimally in globalisation and the continuing trend towards trade liberalisation and regional economic integration. Perhaps the most basic move would be a clear commitment by developing countries themselves to create appropriate policy and institutional conditions. To this end many low-income countries have developed PRSPs in which national policies and donor priorities converge.

Notwithstanding, a fundamental goal of capacity building is to enhance the ability to evaluate and address the crucial questions related to policy choices and modes of implementation, based on an understanding of environment potentials and limits and of needs perceived by the people of the country concerned (UNCED,1992). Efforts by WTO, the African Development Bank (AfDB) and UNECA to organise joint trade policy courses for African countries and the Trade Policy Training Centre in Africa (trapca) are steps towards trade development. To achieve trade-related policy objectives, infrastructure improvements have to be coupled with good policies. Research indicates that returns to infrastructure projects can vary widely and are affected by the quality of the business environment. Good roads and port facilities, for example, do not by themselves guarantee an expansion of trade. The value of such infrastructure projects is easily eroded by poor economic policies, or inefficient and corrupt customs services.

As the global marketplace becomes increasingly liberalised and competitive, countries also need to constantly upgrade their technological capabilities. Governments need to regularly assess the policies governing the transfer of technology and the requirements for upgrading technological capacity. They also need to identify weaknesses in their science and technology policy, including in their innovation policies, and ensure they have the appropriate institutions to support their science and technology strategy (UNECA, 2005).

4.9 Curb Corruption

Urgently reforming customs services could go a long way towards improving the trade environment by eliminating corrupt practices that hinder trade. As noted earlier, clearing agents may connive with customs officials to demand facilitation fees and other payments from importers and exporters, especially when documentation is not fully in order. If customs procedures are not defined clearly and are complicated, or if there are no clear terms of reference for customs officers, or the procedure of running some activities is not clearly defined, then the freedom of action of officers is virtually unlimited. The challenge is to limit

the freedom of action of officers in order to eliminate the risk of corruption. Partnership agreements with the European Union or WTO commitments can go a long way to intensify the existing internal systems of control and outward audit leading to the elimination of corruption risk. Up to 75 per cent of the delays experienced by business can be controlled through actions by customs authorities, other government agencies and the private sector. Better still, singly and within coalitions, the private sector can actually provide impetus to customs reform procedures (UNECA, 2005). Companies should also develop and implement Codes of Ethics specifying clearly what is acceptable and unacceptable in dealings with government officials and third party service providers like clearing agents since fraud and corruption are not confined to Customs.

5. Aid for Trade Priorities

The challenges facing AfT limit its ability to deliver efficient trade development. The demand for AfT in least developed countries is seemingly infinite, but having failed so far in the Doha Round the concept seems in danger of dying a slow death. AfT priorities and limits need a rethink and re-evaluation by the participants, as suggested ahead, so as to regain momentum and commitment. This is perhaps even more urgent given the current crisis that is gripping the global economy.

5.1 Adjustment Assistance

Trade liberalisation prompts changes in relative prices that, in turn, trigger structural adjustment, which occurs as more productive firms – especially export-oriented ones – expand their outputs as less productive enterprises in sectors that face greater import competition begin to contract. In many developing countries, adjustment is constrained by the degree of rigidity in the economy and export patterns – high dependence on a few export commodities and markets. Also the costs of implementing new WTO agreements can be disproportionately higher in developing countries where previous practice and regulation might differ substantially from international standards. Empirical evidence suggests that stringent standards can have a negative effect on trade. For example, African exports of cereals will decline by 4.3 per cent and that of nuts and dried fruits by 11 per cent with a 10 per cent tighter EU standard on contamination levels of aflatoxin in these products (Lyakurwa, 2007a; Wilson and Otsuki, 2003). The EU has also estimated the costs of technical standards as being equivalent to a tax of 2 per cent of the value of goods traded (Otsuki et al., 2001).

Complying with international standards requires additional efforts that might be impossible to afford in sub-Saharan economies. Finger and Schuler (2001), for example, show that the World Bank spent US$82.7 million between 1991 and 1996 in Argentina on a project to assist in the implementation of sanitary and phytosanitary regulations. In accomplishing standards, LDC exporters face administrative, technical and financial burdens that can act as an entry barrier for individual suppliers (Sanchez et al., 2007; Lyakurwa, 2007a).

Chen et al. (2004) find that technical regulations adversely affect a developing country firm's propensity to export and impede market entry for exporters, reducing the likelihood of exporting to multiple countries. Three years ago, fish harvest from Lake Victoria was worth

more that US$400 million. But unless the fish meet specific standards in the destined market, such as in the EU, then the duty-free quota-free market access would not count for much, with serious impact on the three East African countries of Kenya, Tanzania and Uganda. African countries therefore should consider the adjustment of standards as a priority area for their AfT activities.

Because so many low-income countries depend heavily on trade revenue, liberalisation may also entail significant losses of government revenue. Under the new Non Agriculture Market Access Agreement (NAMA), for example, lost trade revenue could account for more than 40 per cent of all government revenue in the Dominican Republic, Guinea, Madagascar, Sierra Leone, Swaziland and Uganda to name a few (*Reality Check*, 2008).

Additionally, liberalisation may make it more difficult for net food-importing developing countries to afford necessary food imports, because the reduction in rich country agriculture subsidies will push up world food prices. The World Bank has estimated that total losses for net food importers would be between US$300 million and US$1.2 billion per year (Mitchell and Hoppe, 2006). Depending on assumptions, between 7 and 16 countries risk having food import bills increase by 5 per cent or more (Stiglitz and Charlton, 2006). These additional costs threaten food security and add to existing balance of payments difficulties.

Preference erosion – the trade losses resulting from liberalisation in other countries – is another potentially serious concern for many poor countries (UNCTAD, 2005). From these perspectives, facilitating structural adjustment should be at the heart of efforts to eliminate supply-side constraints, and as such should be fully included in the Hong Kong Declaration on AfT.

5.2 Harmonisation

In the new move on AfT, partner countries confirmed the importance of harmonisation and encouraged coordinated analyses of trade development needs. According to this principle of aid effectiveness, donors are expected to work aggressively to reduce transaction costs by increasing complementarities, making greater use of local systems, expanding the use of delegated cooperation and better integrating their programmes with local spending plans.

But, although harmonising donor procedures and aligning their support is rising, more remains to be done. Many donors – including the AfDB, Australia, Denmark, the ITC, Japan, New Zealand, the Netherlands, the United Kingdom and the United States – do support coordinated country-level programming and analysis as a matter of course. Others, like Portugal, Korea and Spain, have not yet done so, and Korea plans to expand coordination in the future. Finland has undertaken such coordination, but not in all countries. Because of its small size, the Czech Republic builds on the analytic work performed by others (OECD and WTO, 2007).

The WTO, in close collaboration with the World Bank and IMF, is the focal point of the AfT agenda at the international level. There has been limited consultation with other agencies, such as UNCTAD, the Food and Agriculture Organisation (FAO), or the UN Development Programme (UNDP). At the national level, trade ministries have assumed the main responsibility for AfT. This puts a very narrow trade-driven focus to the agenda. If WTO

members are serious about tackling weaknesses in productive capacities and infrastructure in developing and least developed countries, they will have to take a much broader and more integrated approach that actively involves other stakeholders, other national ministries and the wider multilateral system, including UN special agencies.

5.3 Financing

Finance can to help countries to achieve the necessary developmental pre-conditions for trading by alleviating the external constraints on development. In his speech to the 2007 AfT Regional Review Conference in Manila, WTO Director-General Pascal Lamy highlighted the need to focus on the required financing, how to mobilise it, and how to deliver it more efficiently and effectively – getting donors and international agencies to focus more on trade and growth. However, even though the potential for aid and trade to work together to help developing countries seems obvious, there has been a history of mistrust and apparent conflict between them (Page, 2007). Aid agencies in developed countries and finance ministries in developing countries are normally separate from trade ministries, so that there is rarely an institutional spur to consider the possibility of using trade measures. Again, the inadequacy of grant funding for trade-related assistance to middle-income countries is a serious challenge, and what is available is not predictable because it is budgeted annually. And finally, the lack of regional finance and a flexible rapid response facility contrast with the long-term programming suggested by the World Bank and the IMF. LDCs, through a WTO agreement, should ask for financial certainty through AfT mechanisms.

6. The Challenges in Getting the Delivery of AID for Trade Right

The Paris Declaration on Aid Effectiveness is built around broad principles on how to deliver and manage aid accompanied by action plans that can be monitored to improve aid for trade delivery. Delivering on these principles means overcoming a number of challenges, as described in the next section.

6.1 Insufficient Funds to Accomplish Objectives

The Hong Kong WTO Ministerial Conference and the G8 summits in Gleneagles (in 2005) and St. Petersburg (in 2006) pledged to increase AfT. At the Hong Kong conference, Japan pledged US$10 billion over three years, the United States pledged US$2.7 billion a year by 2010 and the EU pledged €2 billion (US$2.6 billion) a year by 2010. In St. Petersburg, G8 leaders said they expected spending on AfT to increase to a total of US$4 billion. However, the money pledged to date is insufficient to cover the proposed AfT agenda: The current pledges amount to around US$4–8.6 billion, yet according to calculations by the Organisation for Economic Cooperation and Development (OECD), the estimated costs stood at US$22.8 billion in 2004 (IATP, 2006). In addition, OECD members have already made their ODA commitments until 2010 and thus prospects for additional money are unlikely (OECD, 2006).

There is also no negotiating momentum behind the initiative and it might be hard to shift aid more towards improving the trading and productive capacities of developing countries. From the pledges announced so far, there appears to be little or no increase in total AfT and its share

of total aid may actually fall (ODI, 2007). Concerned about the limited progress in the area of funding, the Agency for International Trade Information and Cooperation (Aitic) remarked that the political will of the major players to deliver on their Hong Kong promises is weak and will need to be tested (Aitic, 2006). Aitic also indicated that the conditions attached to enhance trade-related aid will have to be watched carefully and that the means of delivery and coordination among agencies remain a concern.

Regarding other questions, it is clear, as indicated earlier, that trade-related infrastructure has not been well defined. It is therefore important to find a common understanding which parts of infrastructure are to be considered AfT (Olanrewaju, 2007). Additional funds also come with the challenges of the Dutch disease and absorptive capacity. To harness effective pledges, the Aid for Trade Task Force should clarify how much money is being pledged and which programmes the AfT money will prioritise, if the full agenda proves too big – as seems likely (Olanrewaju, 2007).

6.2 Skewed Trade Negotiations

There should be no link between AfT and countries' negotiating positions. Yet promises of aid are used to pressure developing countries to accept greater commitments in the WTO. Developed countries consistently use their aid budgets to pressure developing countries to move closer to developed countries' trade negotiating positions. In the agricultural market access (NAMA or industrial tariff) negotiations, for example, the IMF assured many developing countries that there would be suitable mechanisms for addressing any balance of payment problems that might arise from lost tariff revenues. In the trade facilitation negotiations, which include improving customs procedures, developing countries were similarly assured that assistance would be available to help them implement their obligations. Furthermore, the Aid for Trade Task Force consumes time and resources from developing countries, leaving them with less capacity to engage in the trade negotiations (IATP, 2006). The challenge is that the pressure on developing countries distracts them from pushing for better trade rules and they may end up signing agreements they would rather not sign.

6.3 Mutual Accountability

Arguably, the accounting of AfT and its effectiveness is ultimately more important than the amounts available. The Aid for Trade Task Force argued that a global picture of AfT flows is important to assess whether additional resources are being delivered, to identify where gaps exist, to highlight where improvements should be made, and to increase transparency on pledges and disbursements. Furthermore, the design, implementation and review of trade development strategies, and the associated aid for trade, are challenged by the involvement of a wide spectrum of stakeholders. Although some Aid for Trade Committees or equivalent bodies have been established to review progress on AfT commitments, there are challenges yet to be addressed (OECD and WTO, 2007). In Peru, for example, a large number of public entities are involved in supporting the National Competitiveness Plan, but there is no AfT committee as such; the Peruvian Agency for International Cooperation takes a lead role in coordination of AfT. Mauritius also has no AfT committee, although a designated body meets as often as required to monitor progress and review strategy. In Uruguay there is no AfT committee. Malawi does follow general aid-related processes that encompass the trade sphere and the

budget framework and key policies are discussed with representatives of the private sector, donors and civil society (OECD and WTO, 2007).

Donors and partners should be more committed to enhance mutual accountability and transparency in the use of development resources. Partner countries should reinforce participatory processes by systematically involving a broad range of development partners when formulating and assessing progress in the implementation of national development strategies. Donors should be committed to provide timely, transparent and comprehensive information on aid flows.

6.4 Alignment

Partner countries should help facilitate donor alignment through national planning and budgeting frameworks with the development priorities and results-oriented strategies set out by the partner country. This process needs to be strengthened in some countries, however, which may require investment in capacity development on the part of partner countries.

In Mauritius, Panama and Peru, the major donors do work through national planning and budgeting frameworks. Mauritius's external partners align their interventions with the government reform programme. External resources – in the form of general budget support – are channelled to the government on the basis of mutually agreed performance indicators. A significant proportion of Malawi's overall support is deemed extra-budgetary (i.e., involving finances not directly managed by a government institution). The Philippines does not verify whether all external partners use its policy planning and budgeting framework (OECD and WTO, 2007).

Furthermore, many partner countries are unable to specify how well AfT matches their overall priorities, and more work is required in the development of aid management information systems. In 2005, some 80 per cent of AfT to Peru went to different forms of capacity development, with 19 per cent going to trade-related infrastructure. Peru's experience affirms that infrastructure is a priority, but does not indicate whether the overall composition of AfT is striking the right balance. No aid management information system is referred to. Malawi uses the Commonwealth Secretariat Debt Recording Management System for capturing information on external loans. No other type of information management system is used (OECD and WTO, 2007).

In delivering this assistance, donors may have to progressively depend on partner countries' own systems – and provide capacity-building support to improve these systems – rather than establishing parallel systems of their own. Partner countries should undertake the necessary reforms that would enable donors to rely on their country systems.

6.5 Managing for Results

Partner countries embrace the principles of managing for better results, starting with their own results-oriented strategies and continuing to focus on results at all stages of the development cycle – from planning through implementation to evaluation.

A range of achievement indicators is used for trade development and AfT strategies. While some partner countries in consultation with donors do describe and frequently review an array of achievement indicators in these areas, this management measure is lacking in others. In Mauritius, partners collectively agree on strategies and benchmarks with line ministries and external partners make their own independent assessments of progress. Mandatory consultations are held with partners collectively three times a year to take stock of progress and agree on new indicators and targets. Cambodia, however, does not have formal mechanisms to monitor and evaluate the results and impacts of its AfT. Uruguay appears to have no overall AfT achievement measures; objectives are said to vary according to each ministry (OECD and WTO, 2007).

The Aid for Trade Task Force recommended that the WTO should convene a global periodic review of Aid for Trade. Yet the WTO lacks the necessary expertise to assess aid delivery and effectiveness and so will not be able to effectively evaluate AfT, at least not without help from other agencies. To date, WTO member governments have been reluctant, and occasionally hostile, to WTO cooperation with UN agencies, raising the question of whether the WTO is the most appropriate forum to hold a periodic review of AfT activities (OECD and WTO, 2007).

7. The Way Forward

If there is any landmark in the development process of LDCs' participation in the WTO initiative, it is the new attention in the linkages between aid and trade. LDCs should nevertheless observe that this success is so far suboptimal, given the challenges facing the implementation process, and must be reinforced by both the donor community and developing countries in the AfT space. Both players should take the opportunity to criticise and propose reforms that improve the present level of AfT delivery.

7.1 Way Forward – Donor Community

To make AfT work, donors need to rely on and support partner countries' own priorities, objectives and results. They should also work together to strengthen partner countries' institutions, systems and capabilities to plan and implement projects and programmes, report on results, and evaluate development processes and outcomes – all the while avoiding parallel donor-driven mechanisms (Stiglitz and Charlton, 2006). AfT funds should be additional, predictable and sustainable. Donors should clearly distinguish existing commitments from AfT pledges.

7.2 Maintaining the AfT Focus

It should be noted that AfT did not feature in the 2001 WTO Doha Ministerial Declaration that launched the Doha Development Agenda and therefore falls outside the negotiating mandate that was agreed at Doha. But as the negotiations progressed, it became evident that a major effort was required to provide assistance not only to build trade capacity to help LDCs take advantage of improved market access from a more development-oriented Doha Round agreement, but also to address supply-side constraints and adjustment costs. To this extent, the

main AfT focus was to complement but not to be technically a part of the Doha Development Agenda.

Thus, it is necessary to take real, measurable steps to meet the most pressing challenges so that the momentum that remains is not lost. Three things must characterise AfT: the funds should be additional to existing aid, they should be predictable and they should be sustainable. Existing donor commitments need to be honoured and at the same time AfT pledges need to remain distinct so that they can be applied as intended – to build LDCs' trade-related capacity. One way to ensure additionality is to use AfT funding to leverage additional financial resources such as non-concessional lending and equity investment. Non-concessional multi-lateral financing could be used for larger infrastructure programmes and other efforts to overcome supply-side constraints. In this regard, regional financing instruments are also needed to facilitate grant financing of regional public goods. They would also reinforce national sovereign guarantees to access lending facilities and serve as a means of identifying pilot projects with broad regional appeal, thus building support for regional initiatives.

7.3 Harmonising Priorities

The Paris Declaration clearly showed the way here: Donors committed to a more harmonised, transparent and collectively effective aid process. Aid for trade should not be an exception, and assistance to LDCs in their efforts at building trade capacity could be magnified by simplifying and harmonising international trade procedures. Both multilateral financial institutions and bilateral donors should ensure consistency between a partner's macroeconomic framework and creditor/donor plans.

Donors need to implement the good practice principles they have committed to in the provision of development assistance. The Drivers of Change (DoC) approach discussed earlier is instructive, as it favours a more consensus driven, less top-down framework for delivering aid. Donors should aim at streamlining and harmonising their policies, procedures and practices and intensify delegated cooperation. It is also necessary to increase the flexibility of country-based staff to manage country programmes and projects more effectively and to develop incentives within their agencies to foster management and staff recognition of the benefits of harmonisation.

It is also important for the international financial agencies, in particular the World Bank, to take coherence seriously, and recognise that trade can have legitimate policy and lending priorities. The IMF has done this with its Trade Integration Mechanism, but the World Bank has not yet altered its position that it has no responsibility for WTO-related needs.

7.4 Supporting the Development of Technological Capabilities

Building international competitiveness in tradeable sectors should be a basic objective to be pursued in a step-by-step way focusing on real economy targets. In this regard, African countries lack value- added production capacity. According to the World Bank's *Doing Business Survey for 2006/07*, only three African countries are among the top 50 countries in terms of ease of doing business ranking among the 178 countries surveyed. These are Mauritius (27), South

Africa (35) and Namibia (43). Even when the list is extended to the top 100 countries, only nine African countries are included (IMF and World Bank, 2005).

7.5 Way Forward – Developing Countries

Developing countries are particularly vulnerable to policy shocks because their export industries are the least diversified – many are dependent on the exports and hence the world price of just one or two commodities. A deficient policy environment will not stimulate the development required to take advantage of new global trading opportunities. There is need to intensify economic reforms aimed at removing barriers that impede optimum performance of businesses.

7.6 Making Trade a National Priority

Certain economic orientations, such as what sectors or activities ought to be given priority, are important policy options but they are derived from, and therefore subordinate to, the ultimate goal of broad economic development. In this regard there is need for political commitment to making trade a central national priority. There should be a strategy for getting there; and that this strategy needs to be shared across government and business and mainstreamed in all facets of national trade development policy. Cambodia, for example, has prepared its Diagnostic Trade Integration Study (DTIS) to guide its trade development during the next three to five years. One way of ensuring a focused and sustained national commitment to trade-led growth is to mainstream into poverty reduction strategy programmes or national development programmes (PRSPs/NDPs) (World Bank, 2005).

7.7 Increasing Private Sector Involvement

For rapid capital accumulation and technological progress, the nature of the relationship between the entrepreneurial class and the state is very important. But this is a question of the nature of the private sector as much as it is of the nature of good governance. Very poor countries face the problem of underdeveloped markets and a paucity of firms. In this situation the policy challenge is not to get the government out of the way but to create markets. Private sector advice will strengthen trade policy since the exporters know their markets, they pay the price for delays, bottlenecks and red tape, and hence they are best placed to identify the right set of priorities. AfT should be used to leverage private sector resources and dynamism since aid alone can never provide the whole answer to LDCs' trade capacity dilemmas.

7.8 Enhancing Infrastructure

The poor state of internal transport infrastructure in LDCs has deterred most countries from taking full advantage of the global market opportunities. Infrastructure projects to address specific bottlenecks need to be financed, but they should also be driven by local users. There is a critical need to ensure that good projects are identified and matched quickly to finance and implementation. Latin America, for example, emphasised regional programmes such as the Initiative for the Integration of Regional Infrastructure in South America (IIRSA), which supports the development and integration of energy, transport and telecommunications infrastructure that covers 12 countries spanning two different regional trading blocs (ADB and WTO, 2007). In most cases, however, projects will require significant subsidies; in many

developing countries, basic infrastructure projects are either not commercially viable at all or are not profitable unless they charge fees, which severely inhibits universal access.

7.9 Mobilising Finance

High levels of risk in developing countries are a major barrier to investment. In particular, political risk and exchange rate risk deter foreign investors. There are several ways that multilateral finance could be mobilised to reduce risk and enhance credit in developing countries. A multilateral credit insurance facility, for example, could subsidise financial guarantee insurers of projects in developing countries, which would facilitate access to large volumes of credit. Currency risk is perhaps the greatest threat to developing countries' ability to trade and to attract investment. The development of multilateral assistance programmes to pool currency risk and subsidise hedging costs should be a subject of research. The Global Trade Facility (GTF) could work with existing initiatives, e.g., the Asian Bond Fund, as well as expanding such initiatives to other regions. At the same time, the GTF could work with the World Bank and other multilateral banks to encourage bond markets in local currencies and/or baskets of local currencies (Stiglitz and Charlton, 2006).

7.10 Adopting a Regional Outlook

In many LDCs, the regional dimension of global integration is likely to be important. International regimes governing private capital flows and aid, technology transfer and intellectual property rights, and international migration, both globally and regionally, enhance the opportunities provided by globalisation and reduce its risks. One way of narrowing priorities is to concentrate on regional needs and projects – from transport corridors to customs modernisation and power pools. The New Partnership for Africa's Development (NEPAD) has started to address this issue and efforts need to be intensified in this direction (World Bank and IMF, 2007).

Improving both national and international institutions is an important policy pressure point to promote the development of productive capacities within LDCs. The design and implementation of AfT strategies towards this end can be a beneficial factor if domestic policy works to ensure that foreign enterprises crowd in, rather than crowd out, domestic enterprises, and if there are dynamic linkages between them promoting learning and investment.

7.11 Building Institutional Capacity

Most donors now have institutional remits, dedicated structures, and professional teams and operational guidance that are specifically focused on delivering "more and better" AfT. Some have long experience in fields relevant to AfT, while others are relative newcomers, relying on the larger donors to guide the way. In this regard LDCs should realise that support for institutional capacity building is an essential complement to enterprise development. In the short run, a key feature of an expanded AfT agenda should be to promote investments in new productive capacity. Support should also be extended to programmes to enhance in-country

expertise and policy formulation, as well as research and trade development diagnostic studies. In the long run, regulatory and legal frameworks are essential to successful business environments (World Bank and IMF, 2007).

8. Conclusion

This paper has indicated the importance of AfT to the economic prosperity of underdeveloped countries. The widening gap between the developed countries and LDCs can be eliminated only if the latter can achieve higher growth rates than the former. Aiding trade is one way of achieving development, and while it is necessary it is insufficient. Good policies are important for growth. Aid will have positive impact on growth if developing countries have good policy environments – fiscal and monetary as well as trade policies.

Donors should realise that development cannot be imposed but facilitated. Therefore, trade related assistance should respect country ownership. The donor community should respect the right – and responsibility – of partner countries to exercise effective leadership over their development policies and strategies and to coordinate development actions. In addition, donor countries should respect their pledges and enhance management for results to ensure that expanding AfT delivers larger benefits to the LDCs and enables them to effectively increase their trade competitiveness.

Finally, the Paris Declaration on Aid Effectiveness is built around five broad principles on how to deliver and manage aid. Those principles are accompanied by clearly defined action plans to increase the impact of aid on overcoming export supply capacity constraints and contributing to the economic development of LDCs. As has been highlighted, AfT participants on both sides have not effectively followed these principles. Thorough application of the general principles of the Paris Declaration on aid effectiveness should be the way forward for all parties.

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TRADE, DEVELOPMENT AND REGIONAL INTEGRATION IN AFRICA: EPA'S CONTRIBUTION TO REGIONAL (DIS) INTEGRATION IN DECISION-MAKING IN SUB-SAHARAN AFRICA PUBLIC SPHERE

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I: Introduction

Trade liberalisation and openness, as linchpins for development have been flagships of conventional economic policy advices to most African countries over the last few decades. In the late eighties and early nineties, decision-making on liberalisation in African public sphere were overshadowed by IMF/World Bank failed Structural Adjustment Programmes (SAPs). There has been a gradual paradigm shift and African countries nowadays tend to rely mostly on the prescriptions of the World Trade Organisation and related regional trade regimes for liberalisation. About half of world trade nowadays occurs under preferential tariff rates. Among other reasons for this worrying fragmentation of international trade rules is the belief that regional trade agreements are easy to negotiate and perhaps offer the possibility of permeating areas that multilateral trade negotiations cannot. While some of the fragmented trade regimes have been enlarged to include new partners, others are in the process of metamorphosis from non-reciprocal trade regimes to reciprocal trade regimes. This is the case with the African, Caribbean and Pacific Group of States (ACP) and European Union (EU) trade relationship established under the 2000 Cotonou Partnership Agreement (CPA) that superseded the original 1975 Lomé Convention.

The CPA calls for the new trading regime to be supportive to current regional integration processes within Africa and should be placed in the context of the overall development objectives of ACP countries. As witnessed in the Agreements initialled by 35ACP countries by year-end 2007, the European Commission has relied on GATT Article XXIV to justify its claim for reciprocity in the impending trade regime (popularly known as the Economic Partnership Agreement-EPA). Consequently, if development concerns can be factored into EPA, what would be an acceptable threshold for such RTAs to conform to GATT Article XXIV requirements of "substantially all trade" and "reasonable period of time"?

Although by the end of December 2007, when the Cotonou waiver was supposed to expire, about 35 of the 77 ACP countries had initialled interim or full[2] goods-only EPAs, they largely disagree with any form of FTA with the EU made on the basis of an inflexible interpretation of GATT Article XXIV. Inevitably, the prevailing view in ACP countries is that an FTA between the EU and the ACP countries must be a development instrument and supportive of their regional integration initiatives. In view of the fact that thus far, interim EPAs contain no clear details in terms of the commitments given by the parties, the possibility remains that agreement

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[2] The Caribbean is the only region that initialled a full EPA with the EU by 31 December 2007.

on EPAs will not be reached by the end of 2008 as some of the initialled agreements claim.[3] In this situation of uncertainty, individual exporters from the ACP countries are likely to be more concerned about the long-term delivery terms of the contracts they may be entering into now. Assuming that on the basis of the initialled interim goods-only agreements between the EC and a cluster of ACP countries, the rights and obligations under the CPA are still valid; ACP non-LDCs will be expected to continue to benefit from the Cotonou preferences until such time as an agreeable EPA is put in place. Consequently, the question left to be answered is whether in case of any dispute arising from a non-compliance with a provision of the CPA, the EC will be absolved of its legal obligation under the Cotonou Agreement to continue to give Cotonou-equivalent preferences to these countries. This paper discusses the idea of development and WTO compatibility in the context of the current EPA negotiations. The paper also examines why and how EPA should have been a building block to the multiple regional integration processes in Africa. In view of the flawed dispute settlement provisions under the CPA, the paper further tries to answer the question of whether the CPA contains rights and obligations that need protection by individual EU member courts and may necessarily be enforced before the ECJ. The paper ends with some thoughts on post-EPAs adjustment programme and how EPAs will impact decision-making in Africa's public sphere.

2. The Permissibility of Regional Trade Agreements under the GATT/WTO Rules

The clustering of states by a common bond of policy has occurred for many years,[4] although the current fragmentation of international trade rules has generated a lot of concern about the effectiveness of multilateralism.[5] Regionalism allows like-minded states or states with similar concerns, such as security or trade, to align themselves with each other. Yet, whenever multilateral trade negotiations move toward reducing most-favoured nations (MFN) tariffs, countries benefiting from trade preferences are concerned about the impacts of such reductions on their trade preferences. The principles and rules pertaining to Free Trade Agreements (FTAs) and Preferential Trade Agreements (PTAs) laid down by the WTO and binding upon its current 151 members are therefore very relevant in light of the increasing number and complexity of worldwide preferential agreements. On the basis of the General Agreements on Tariffs and Trade (GATT) of 1994 and General Agreements on Trade in Services (GATS),

[3] The application of the SADC EPAs by the EU was scheduled for 1 January 2008 and 1 June 2008 for the SADC EPA States. See statement of the Chief Negotiators On the initialling of the Economic Partnership Between the SADC EPA Group of States on the one hand and the European Union on the other hand, Brussels, November 2007.

[4] Article 21 of the Covenant of the League of Nations provided that '[n]othing in this Covenant shall be deemed to affect the validity of international engagements such as treaties of arbitration or regional understanding like the Monroe doctrine for the maintenance of peace'. The corollary of this provision is Article 52(1) of the UN Charter, which encourages regionalism among members of the UN.

[5] For an extensive discussion on RTAs and the puzzles surrounding their formation and existence, see Lorand Bartels & Federico Ortino, *Regional Trade Agreements and the WTO Legal System*, Oxford (2006); and Roberto Fiorentino et al., 'The Changing Landscape of Regional Trade Agreements: An Update of WTO', Discussion Paper (2006).

these principles shape the conditions, requirements and limitations of such agreements.[6] For the purpose of the creation of trade, the requirements and limitations of GATT/WTO rules on Regional Trade Agreements (RTA) seek to establish a balance between multilateralism and regionalism.

GATT Article I (MFN) is regarded as a cornerstone of the multilateral trading system as it obliges all the 151 WTO members to treat each other equally.[7] However, in the field of goods, GATT Article XXIV establishes an exception to this obligation for the purpose of creating Custom Unions and FTAs. While Custom Unions such as the Southern Africa Custom Union (SACU),[8] East Africa Community (EAC),[9] the European Union (EU), and the Cooperation Council of the Arab States of the Gulf (GCC) are structures establishing common external tariffs and trade policies toward third countries, FTAs such as the Economic Community of Central African States (ECCAS),[10] the Southern African Development Community (SADC)[11] and the North America Free Trade Area (NAFTA) establish free trade among members.[12] The deviation from Article XXIV is conditioned to the meeting of the requirements laid down in paragraphs 5 and 8 of Article XXIV regarding trade coverage, length of time for internal liberalisation within the regional arrangement and the level of trade liberalisation maintained with third countries.[13]

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[6] Similarly, in the context of the Agreement on Trade Related Intellectual Property Rights (TRIPs), Members may also deviate from the MFN rule to the extent that the conditions laid down under TRIPs Article 4 are met.

[7] GATT Article III also requires similar obligations from the perspective of an individual WTO member's treatment of products within its territory.

[8] See http://www.dfa.gov.za/foreign/Multilateral/africa/sacu.htm.

[9] See http://www.eac.int/EAC_customs_U.htm.

[10] See http://www.iss.co.za/AF/RegOrg/unity_to_union/eccas.html.

[11] SADC's 14 members are Angola, Botswana, the Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, United Republic of Tanzania, Zambia and Zimbabwe. As the name suggests, SADC portrays itself as more of a development regional institution than just an FTA. Article 5 of the SADC Treaty sets the following as its objectives: achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the people of Southern Africa and support the socially disadvantaged through regional integration; evolve common political values, systems and institutions; promote and defend peace and security; promote self-sustaining development on the basis of collective self-reliance, and the interdependence of Member States; achieve complementarities between national and regional strategies and programmes; promote and maximise productive employment and utilisation of resources of the Region; achieve sustainable utilisation of natural resources and effective protection of the environment; strengthen and consolidate the longstanding historical, social and cultural affinities and links among the people of the Region. See Treaty of SADC at http://www.sadc.int/english/documents/legal/treaties/amended_declaration_and_treaty_of_sadc.php.

[12] Under the Agreement on Technical Barriers to Trade (TBT) and the Agreement on Sanitary and Phytosanitary Measures (SPS), WTO Members are also encouraged to enter into bilateral mutual recognition preferential agreements (TBT Article 6(3) which must be in conformity with paragraph 1 of the same provisions, and SPS Article 4.2 respectively).

[13] Consequently, according to the AB report in the *Turkey – Textile*, paras. 5 and 8 are the operative paragraphs under GATT Article XXIV.

The requirements of trade coverage as provided for under GATT Article XXIV(8) for the purpose of compatibility with WTO rules on FTAs[14] and CUs[15] need to cover substantially all the trade in products originating within members of the RTAs. There is at present no provision in the GATT/WTO Agreement defining "substantially all trade". An agreed understanding of the meaning of this term has so far eluded the GATT/WTO membership.

As a consequence, the only sources of interpretation we can rely on to ascertain the meaning of "substantially all trade" is the DSB jurisprudence and existing common practice. In this regard, in drawing attention to the problem in the *Turkey-Textile* case, the AB stated that, "neither the GATT CONTRACTING PARTIES nor the WTO Members have ever reached an agreement on the interpretation of the term 'substantially' in this provision. It is clear, though, that 'substantially all trade' is not the same as all the trade, and also that 'substantially all trade' is something considerably more than merely some of the trade. … Thus we agree with the Panel that the terms of sub-paragraph 8(a)(i) offer 'some flexibility' to the constituent members of a customs union when liberalising their internal trade in accordance with this subparagraph."[16]

GATT Article XXIV(8)(a)(i) is seen as establishing a standard for the internal trade between constituent members to fulfill the requirements of a "customs union". And the constituent members of a customs union are required to apply a common external trade regime relating to both duties and other regulation of commerce.

So far, the ruling of the AB in the *Turkey-Textiles* clarifies Article XXIV(8)(a)(i) dealing with customs union and not Article XXIV(8)(b) on FTAs. But, since the phrase "substantially all trade" has a similar function in both subparagraphs and the relevant difference between Custom Unions and Free Trade Areas in this connection is only on the origin of covered goods, it may be assumed that the AB interpretation could be applicable *mutatis mutandis* to Article XXIV(8)(a) and Article XXIV(8)(b). Regarding the views of members, in the examination of the Treaty of Rome, the six-member states opined that the test for "substantially all trade" would be satisfied if 80 per cent of the volume of trade between the parties were liberalised. But in the EU-South Africa Trade and Development Cooperation Agreement (TDCA), the threshold seems to be slightly different. The EU gives 95 per cent of South African exports improved access to its markets, while South Africa does so for 86 per cent of EU exports. For its part, the United States argued in the *Line Pipe* case that since NAFTA covered 97 per cent of the trade between the parties, it was in conformity with the provisions of Article XXIV(8)(17).

[14] See GATT Article XXIX(8)(b) for the definition of Free Trade Area used here simultaneously with Regional Trade Agreement (RTA).

[15] For a definition of Customs Union, see GATT Article XXIV(8)(a).

[16] Appellate Body Report, *Turkey – Restrictions on Imports of Textile and Clothing Products*, WT/DS34/AB/R, para. 48. See further the communication of Botswana on behalf of the ACP Group to the Negotiating Group on Rules at document TN/RL/W/155 dated 28 April 2004. See also a similar proposal by China at document TN/RL/W/185, dated 22 July 2005.

[17] Appellate Body Report, *United States - Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea,* WT/DS202/AB/R, adopted 8 March 2002.

2.1 The Quantitative and the Qualitative Approach Interpretation

The question that usually arises when examining the requirements of Article XXIV(8) is whether a regional trade agreement may decide to consider "substantial coverage" as only a qualitative requirement while ignoring it as a quantitative requirement. These two approaches are not mutually exclusive and there is generally no consensus on either.[18] With regard to the quantitative approach, WTO members engaging in FTAs sometimes argue that to the extent that the lion's share of the overall trade is covered it may be justified to exclude an entire goods sector. Arguments in support of a quantitative approach seem to suggest a definition that will incorporate a statistical benchmark, such as a certain percentage of the trade between the contracting parties to demonstrate that the coverage of the RTA in question fulfils the requirement. The percentages that have been commonly suggested in this context range from 80 to 90 per cent.

Conversely, members in favour of the qualitative approach interpret "substantially all trade" to mean that no major sector of intra-RTA trade should be excluded from liberalisation.[19] The difficulty with this approach might stem from the definition of "sector".[20] The question may arise as to whether the inclusion of a minute component of a major sector will be able to fulfill the requirement of the qualitative approach. In an attempt to clear up ambiguities and shed more light on the interpretation of Article XXIV, in 1994 WTO members adopted an "Understanding on the Interpretation of Article XXIV". The preamble of the 1994 Understanding recognises that the "contribution of custom unions and free trade areas" to the "expansion of world trade that may be made by closer integration" is "diminished if any major sector of trade is excluded". Despite this wording, the Understanding does little to settle the controversies over the interpretation of "substantially all trade". Yet, the requirement is relevant in circumventing selectivity and limitations to goods of a particular interest.

While the quantitative approach has some positive aspects, it also has some conspicuous drawbacks. It can permit parties to an agreement to exclude so-called sensitive sectors such as agriculture and textiles and clothing.[21] To reduce the selectivity associated with the quantitative approach, Australia made a proposal to the WTO Committee on Regional Trade Agreement in 2002 that the threshold figure should be 95 per cent of all the six-digit tariff lines listed in the harmonised system. Australia argued that the main advantages of its proposal were that: (i) it

[18] At least in the domain of services, there is no such problem of definitions. For instance, footnote 1 to GATS Article V is to the effect that '[t]his condition is understood in terms of number of sectors, volume of trade affected and modes of supply. In order to meet this condition, agreements should not provide for the a priori exclusion of any mode of supply.'

[19] The objective of the qualitative approach is to prevent the exclusion of an RTA from the liberalisation of any sector which, prior to the formation of the RTA, contained restrictive trade policies. See Compendium of Issues Related to Regional Trade Agreements, Background Note by the WTO Secretariat, TN/RL/W/8/Rev.1 (1 August 2002). This is also reflected in the preamble to the Understanding on the Interpretation of GATT 1994 Article XXIV.

[20] In the context of GATS, 'sectoral commitments' may be understood as entries covering specific service sectors or sub-sectors in WTO Members' specific Schedule of Commitments under GATS; e.g. life insurance and accountancy.

[21] Comments by New Zealand over the exclusion of agriculture from the free trade agreement between Singapore and Japan.

would obviate the need to establish the extent to which trade in a given product may have been affected by other measures in place; (ii) it was unlikely that this approach would permit the carving-out of any major sector because of the strong possibility that the permitted exemptions would have to be spread out over a range of potentially sensitive sectors; and (iii) the suggested approach was easily verifiable without requiring complex econometric studies.[22]
In addition to the general request on a concrete definition of RTAs that covers all sectors; some suggestions have been put forward to resolve the differing views arising from the quantitative and qualitative approach debates. In this regard, the product coverage of RTAs should be characterised not only in the light of trade flows, but also in terms of a certain percentage of tariff lines.[23] Similarly, as a modification of the quantitative approach, the calculation of the percentage of trade between member states could be carried out under RTA rules of origin or exploring some clarifications of the concept of "substantially all trade" on the basis of footnote 1 of GATS Article V.[24]

Clearly, some benchmarks are relevant for considering these different approaches. In *Turkey – Restrictions on Imports of Textile and Clothing Products*,[25] in agreeing with the views of the Panel on this issue, the Appellate Body stated that "[t]he ordinary meaning of the term 'substantially' in the context of subparagraph 8(a) appears to provide for both qualitative and quantitative components. The expression 'substantially the same duties and other regulations of commerce as applied by each of the Members of the [customs] union' would appear to encompass both quantitative and qualitative elements, the quantitative aspect more emphasised in relation to duties.'[26] To this extent, the AB's view in the *Turkey-Textile* case does not only provide a relevant precedent for future cases, but would certainly influence future interpretations of CUs, especially those relating to goods or falling within the ambit of GATT Article XXIV.

In view of the analysis set out earlier, one may reasonably question the necessity of subparagraph 8(a) of GATT Article XXIV. A possible explanation would be that these provisions were originally aimed at delineating the extent to which certain products may be omitted from the coverage of a FTA or CU. By implication, a comprehensive approach is required and there is no room for pick-and-choose or *à la carte* policies. Similarly, limited liberalisation is excluded and discrimination is acceptable only to the extent that it is extensive in sectoral coverage.[27]

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[22] See Negotiating Group on Rules, submission by Australia on Regional Trade Agreement, TN/RL/W/15, 9 July 2002.
[23] Negotiating Group on Rules, Compendium of Issues Related to Regional Trade Agreements, TN/RL/W/8/Rev.1, para. 69.
[24] With reference to substantial coverage of RTAs on services, footnote 1 of GATS provides the following clarifications: 'This condition is understood in terms of number of sectors, volumes of trade affected and modes of supply. In order to meet this condition, agreements should not provide for the a priori exclusion of any mode of supply.' World Trade Organization Legal Texts, the Results of the Uruguay Round of Multilateral Trade Negotiations, p. 289.
[25] WT/DS34/AB/R, adopted 19 November 1999.
[26] AB report Turkey-Textile case, para. 49 and panel report para. 9.148
[27] This view is echoed in the Chairman's report for Hong Kong Ministerial delineating the views of Members regarding the Substantially all Trade (SAT) debates and the length of time liberalisation should take place in an RTA. See Report by the Chairman to the Trade Negotiating Committee (TNC), TN/RL/15 (dated, 30 November 2005).

The WTO rules also require constituent members of RTAs to eliminate all tariffs and quantitative restrictions within the RTA. Such elimination should be completed within a reasonable length of time. So far, a time frame of ten to twelve years has been considered as reasonable transitional period for the abolition of such internal trade restrictions.[28] However, it is important to note that there may be scope for flexibility when it comes to North-South non-reciprocal trade arrangements. For instance, the foregoing requirement may not apply when it comes to RTAs entered into in the context of the WTO Enabling Clause.[29] Although the wording of paragraph 2(c) of the Enabling Clause is not very precise on this issue, it seems to allow a more gradual elimination of tariffs than would be in the context of Article XXIV:8 which calls for the drastic elimination of all tariffs on substantially all trade between constituent members of RTAs.

3. Prospects and Challenges of Regional Integration in Africa

As mentioned earlier, there are diverse reasons for the existence of regional clustering. Regional Trade Agreements (RTA will be used here simultaneously with regional integration) may be formed because of the need of economic and political integration, national security and foreign policy as well as members' willingness to have access to greater external markets.[30] The problems of regional integration have long been recognised in Africa's political circles. Many decades ago, Nkrumah forcefully stated the case for regional integration in Africa. Over the last half century, there has been the development of over ten different regional trade blocs in Africa. Most African countries belong
to at least three or more separate regional integration agreements.[31] Yet, there has been very limited progress towards meaningful trade enhancement.[32]

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[28] This is the case with the current EPA negotiations between the European Commission and the four groups of African members of the ACP, where the EC is currently pushing for a FTA with a transitional period of ten to twelve years for implementations. For analyses on RTAs and compatibility with WTO rules, see Gabrielle Marceau and Cornelis Reiman, 'When and How is a Regional Trade Agreement Compatible with the WTO?', Legal Issues of Economic Integration, Vol. 28 issue 3, pp. 297-336 (2001); James Mathis, 'WTO, Turkey – Restrictions on Imports of Textiles and Clothing Products', Legal Issues of Economic Integration, Vol. 27, Issue 1, (2000) .

[29] For the sake of clarity, this is the decision of the Contracting Parties adopted at the end of the Tokyo Round in 1979 which allows for deviation from the MFN rule in favour of imports from developing countries. The 1979 decision entitled 'The Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries', allows intra-developing countries preferential trade arrangements and North-South preferential trade agreements in favour of the developing countries.

[30] See Bernard Hoekman and Michael Kostetecki, The Political Economy of the World Trading System – From GATT to WTO, Oxford University Press, (1995), chapter 9. It is important to note that in the absence of a fast-track multilateral process, RTAs may arguably be a useful linchpin for trade liberalisation.

[31] Some of the regional integration processes include; the Economic Community of West African States involving 16 West African States (ECOWAS), West African Economic and Monetary Union (WAEMU/UEMOA) made up of seven countries, Economic and Monetary Community of Central African (with the French acronym CEMAC) states made up of six CentralAfrican states, Common Market for Eastern and Southern African States, (COMESA) involving 21 states, the East African Community (EAC), involving five members, Southern Africa Custom Union (SACU), involving five members and the Southern African Development Community (SADC) involving 14active and non-active

While different integration mechanisms have been successfully launched by other regions to improve their economic welfare, Africa lags behind with regards to economic growth and general living standards. In spite of the existence of a whole range of regional arrangements and a plethora of policy plans, regional integration is yet to be a feature of Africa political economies. The Lagos Plan of Action and the Final Act of Lagos were adopted almost three decades ago setting out the vision for an integrated Africa by the beginning of the third millennium. The Lagos Plan envisaged that, via regional economic communities, the challenges of Africa's poverty and underdevelopment would be overcome. Some of the milestones of the Plan included the strengthening of existing regional economic institutions, creation of new ones, tariffs stabilisation and harmonisation of tariffs system across the different regional economic communities. Among the new initiatives is the New Economic Partnership for Africa's Development (NEPAD).[33]

Among the features of the discourse on regional integration in Africa are the absence of political constituencies in the business and labour movements that push for regional integration, lack of focused regional integration and overlapping memberships. With regard to the former, at the domestic constituency, there has not been any real debate on the national costs to benefit integration. At best, it is often some pan-Africa sentiments that provide a modicum of ideological support nationally to intra-Africa rapprochement. Regarding the problem of overlapping membership, apart from the vision of the African Union to achieve common markets among its members, one can hardly find a coordinated plan to harmonise the existing numerous regional integration agreements spread around the continent. Such plan may make sense, as the pursuit of further integration by sub-group would eventually be absorbed by a larger group. Yet, the intricacies of the current situation do not make such a scenario easy unless there were to be major rationalisation of the existing agreements. The issue of rationalisation and overlapping memberships will be taken up in the subsequent section.

However, it is very clear that what African leaders have not achieved domestically through sound economic development policies would be difficult to achieve regionally. If the first attempts by the post-colonial African leaders had been unsuccessful, we may rationally start questioning the reasons for the current optimism that characterises the present proponents of Africa's integration. The fact that this very question is a good basis for reengaging African leaders in a new strategic partnership among themselves, means that Africa's vision for regionalism must be a fallback of encompassing and frank debates in their different domestic constituencies.

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members. Others with less significant role include the Arab Maghreb Union (UMA), the Economic Community of the Great Lakes Countries (CEPGL), Indian Ocean Commission (IOC), Intergovernmental Agency on Development (IGAD) etc.

[32] Although authors like Venter et al, attribute lack of this progress to political turmoil in most of the African countries, I rather see political turmoil as only a minimal part of the problem. See Venter Dani and Ernst Neuland, NEPAD and the African Renaissance, Johannesburg, (2005) at pp. 178-181.

[33] A considerable amountof literature exists on the NEPAD initiative. Some of these literature include Celliers J. Peace and Security through Good Governance: a Guide to NEPAD's African Peer Review Mechanism, Institute for Security Studies Occasional Paper 70, Pretoria (2003), Venter et al, ibid, Argo, EF. Forging New Partnerships: NEPAD SMMEs and the Challenge of Globalisation, Pretoria (2005), Institute for Business Innovation

4. Existing Frameworks for Trade between the African ACP States and the European Union

For the African countries in general, and the LDCs among them in particular,[34] it is not only the commitments enshrined in the WTO treaty system that determine their trade relations with the developed countries. While under certain conditions the WTO permits its members to engage in preferential trade agreements, since the 1970s most industrialised countries – by way of the Generalised System of Preferences (GSP) – have accorded discriminatory market access to products originating in developing countries. Under the European Communities GSP scheme,[35] "non-sensitive" products benefit from duty-free treatment while sensitive products are granted a 3.5 per cent reduction on the normal tariff duty rate.[36] To the extent that developing countries can demonstrate that they have complied with specific environmental and labour standards, they may also apply for additional preferences for sensitive products. As opposed to the Cotonou preferences (which are discussed below), the EC standard GSP is available to all developing countries. It provides a number of products with preferential access to the EU market but its coverage is significantly lower than those under the trade provisions of the Cotonou Partnership Agreement (CPA). In addition to trade preferences under the GSP scheme, the European Communities in 2002 introduced the "Everything But Arms" (EBA) initiative for all LDCs.[37]

Furthermore, there is the Trade and Development Cooperation Agreement (TDCA) between the EU and South Africa entered into in 1999,[38] and the CPA signed in 2000 to supersede the original Lomé Convention. Thus, in the context of the 48 members of the African, Caribbean and Pacific Group of States, there are currently four separate frameworks guiding their EU trade relations. Among these frameworks, the Cotonou Agreement is the principal one, as it provides extensive trade preferences to African countries on a non-reciprocal basis. With the exception of the EU-South Africa Trade and Development Agreement (TDCA), the common thread running through all these frameworks is the idea of non-reciprocal trade preferences and quota free market access. However, for the purpose of this paper, only the Cotonou trade arrangement will be discussed.

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[34] Under the UN classifications, there are currently 48 LDCs. The African LDCs are: Sudan, Mauritania, Mali, Burkina Faso, Niger, Chad, Cape Verde, Gambia, Guinea-Bissau, Guinea, Sierra Leone, Liberia, Togo, Benin, Central African Republic, Equatorial Guinea, Sao Tomé and Principe, Democratic Republic of Congo, Rwanda, Burundi, Angola, Ethiopia, Eritrea, Djibouti, Somalia, Uganda, Tanzania, Mozambique, Madagascar, Comoros, Zambia, Malawi, Lesotho.

[35] EC Regulation No. 2501/2001, currently in force through the amendment by Council Regulation (EC), No. 815/2003.

[36] Article 7 of the GSP Regulation. Of course, there is also the 2005 EU labour and environmental arrangements (popularly known as EU GSP +) where, among other things, potential beneficiaries are required to ratify some human rights and good governance conventions. On the legality of EU GSP +, see Lorand Bartels, 'The WTO Legality of the EU's GSP+ Arrangement', Journal of International Economic Law (2007), Vol. 10, No. 4, pp. 869-886.

[37] Regulation 416/2001 of 26 February 2001, Official Journal No. L 60 of 1.3.2001.

[38] Official Journal of the European Union, No. L 311 of 4.12.1999.

4.1 The Cotonou Preferences

In the ground-breaking *Turkey-Textiles* case, the Appellate Body reminded WTO members that unless otherwise proven, RTAs and preferences accompanying them are incompatible with WTO rules. Implicitly, GATT Article XXIV is inoperative as a discipline, meaning that WTO members may only invoke it in the context of dispute settlement when their existing trade measures or agreements are inconsistent with the GATT/WTO core MFN principle or any other GATT Article. Despite this, clustering of states by common bonds of policy has occurred for many years,[39] although the current fragmentation of international trade rules has generated a great deal of concern as to the effectiveness of multilateralism.[40]

Regionalism allows like-minded states or states with similar concerns, such as security or trade, to align themselves with each other. By the same token, the idea of entering into a free trade agreement between the EU and the ACP countries – as is currently being negotiated in the context of Economic Partnership Agreement – to supersede the non-reciprocal trade preferences that the EU has been granting the ACP countries for the past thirty years has been widely questioned.[41] Although it may be important to discuss the history of the Lomé/Cotonou preferences, this paper will not cover this historical dimension since a great deal has already been written about it.[42]

The exact nature of the link between trade and development is a subject of continuous debate. It is hard to refute the argument that international trade can be a powerful engine for a country's socio-economic development.[43] This is widely observed in the current EC/ACP EPAs negotiations where the European Commission negotiating on behalf of the EU Member States continuously takes the view that by liberalising their markets and boosting economic

[39] Article 21 of the Covenant of the League of Nations stated that '[n]othing in this Covenant shall be deemed to affect the validity of international engagements such as treaties of arbitration or regional understanding like the Monroe doctrine for the maintenance of peace'. The corollary of this provision is Article 52(1) of the UN Charter, which encourages regionalism among members of the UN.

[40] For an extensive discussion on RTAs and the complexities surrounding their formation and existence, see Lorand Bartels & Federico Ortino, *Regional Trade Agreements and the WTO Legal System* (Oxford, 2006); and Roberto Fiorentino et al., 'The Changing Landscape of Regional Trade Agreements: An Update of WTO', Discussion Paper (2006).

[41] In this regard, see Romain Perez, 'Are the Economic Partnership Agreements a First-best Optimum for the African Caribbean Pacific Countries?', Journal of World Trade (JWT), Vol. 40, No. 6, pp. 999-1019 (2006) and a response to this article by Louise Curran, JWT, Vol. 41, Issue 1, pp. 234-244 (2007). For policy perspectives, see the TWN Africa and Oxfam International publication, 'A Matter of Political Will: How the European Union Can Maintain Market Access for African Caribbean and Pacific Countries in the Absence of Economic Partnership Agreements', April 2007.

[42] In this regard, see B. Martenczuc, 'From Lomé to Cotonou: The ACP-EC Partnership Agreement in a Legal Perspective', (2000) 5 EFAR, pp. 461-487; Abou Abass, 'The Cotonou Trade Regime and the WTO Law', ELJ, Vol. 10, No. 4, July 2004, pp. 439-462; Romain Perez, 'Are the Economic Partnership Agreements a First-best Optimum for the African Caribbean Pacific Countries?', Journal of World Trade (JWT), Vol. 40, No. 6, pp. 999-1019 (2006) and a response to this Article by Louise Curran, JWT, Vol. 41, Issue 1, pp. 234-244 (2007) etc.

[43] See Jeffrey Sachs, *The End of Poverty: How can we Make it Happen in our Lifetime* (London, 2005); Jagdish Bhagwati, *In Defence of Globalization* (Oxford, 2004).

reforms in ACP countries, EPAs will foster development in African countries.[44] To realise this objective, the EC considers Aid for Trade as an important component of its dialogue with the African countries.[45] It is with this in mind that the Commission has pointed out that "…trade will be at the service of development, leaving a high degree of flexibility to take account of the development challenges in Africa".[46]

One of the main external reasons for replacing the Lomé preferences with the CPA and then EPAs is the ruling of the WTO Dispute Settlement Body (DSB) in the *EC-Bananas III* dispute where elements of the Lomé preferences were declared incompatible with EC commitments under the WTO Agreement as they provided discriminatory preferences to ACP countries. This represents a major overhaul and shift in the ACP/EC development cooperation as it introduces the idea of reciprocity in a trade relationship that has existed for the last 30 years on a non-reciprocal basis.[47] At the same time, what is legally puzzling in the context of the current negotiation is that while EPAs will be WTO-compatible, they should be development-oriented. And in the worse case scenario where the negotiations on such development-friendly EPAs fail to produce results,[48] the EU must provide alternative trade arrangements for the non-LDCs ACP countries "which is equivalent to their existing situation and in conformity with WTO rules".[49]

In a press release by the EU Council on 20 November 2007, the Council reaffirmed the development dimension of EPAs by stating as follows: "[t]he Council confirms its commitment to the ongoing negotiations on the Economic Partnership Agreements (EPAs), as expressed in its Conclusions on EPAs of April 2006 and May 2007 and reiterates its position of EPAs as being development instruments. EPAs are going to be WTO-compatible agreements, supporting regional integration and promoting the gradual integration of the ACP economies into the rules-based world trading system. This will thereby foster their sustainable

[44] This view may also be seen in the light of Article 178 of the Treaty Establishing the European Community which states that '[t]he Community shall take account of the objectives referred to in Article 177 in the policies that it implements which are likely to affect developing countries'. This was also echoed by the Directorate General for Development in 'EC Report on Millennium Development Goals 2000-2004', 5 (2005).

[45] See Council of the European Union, 'Towards an EU Aid for Trade Strategy – the Commission's Contribution', SEC (2007) 414, COM (2007) 163 final, April (2007).

[46] CEC, 'Speeding up Progress Towards the Millennium Development Goals: The European Union's Contribution', COM (2005) 132 final, Brussels (IV), Annex II, 22 (2005).

[47] For some earlier thoughts on the legal basis of EPAs, see B. Martenczuc, 'From Lomé to Cotonou: The ACP-EC Partnership Agreement in a Legal Perspective', (2000) 5 EFAR pp. 461-487 and Abou Abass, 'The Cotonou Trade Regime and the WTO Law', ELJ, Vol. 10, No. 4, July 2004, pp. 439-462.

[48] The originally agreed deadline was January 2008. This did not happen, but a number of ACP countries entered into interim goods-only agreement with the Commission.

[49] Article 37(6) of the CPA. This was reiterated by the Council of the European Union in a press release on the current state of affairs with regard to negotiation of the EPAs. See 'Council Conclusions on the Economic Partnership Agreement', 2831st External Relations Council meeting, Brussels, 19-20 November 2007, obtainable at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/gena/97189.pdf.

development and contribute to the overall effort to eradicate poverty and to enhance the living conditions in the ACP countries."[50]

Truly, in this context one may argue that despite the difficulties encountered by both the ACP countries and the EC in the negotiations toward the conclusion of EPAs, the EC is legally obliged under the Cotonou Agreement to continue to provide Cotonou preferences – or equivalent – to the ACP countries. This is the case notwithstanding the fact that the EC implementing Regulation does not clearly specify what would be an effective fallback if the transitional period ends without an EPA being reached.[51] To avoid the impasse involved in achieving development-friendly EPAs (or, in other words, Cotonou equivalent EPAs) and making sure that such FTAs fulfill the requirement of GATT Article XXIV,[52] the Commission may jointly with the ACP countries request an extension of the Cotonou waiver from the WTO,[53] and thereafter take relevant action under its own power pending appropriate regulations from the Council to extend the negotiation period.[54]

In theory, one would say that it is not impossible to request a waiver from the WTO if the negotiations are not concluded within the agreed timeframe. This is not totally incompatible with the spirit of the Cotonou provisions on trade, as it is clear from these provisions that the ACP countries would decide the pace of the negotiations.[55] This view contradicts the Commission's current position, as it continues to claim that the chances for extending the current waiver or requesting a new one are minimal and, if it were possible, the political costs would be too high.[56] At the same time, depending on the period of time such extension is possible, the legal uncertainty concerning EPAs which are by nature development-friendly and conform to the current WTO rules would remain unresolved.[57]

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[50] Ibid. para. 1.

[51] See Council Regulation (EC) No 2286/2002 of 10 December 2002 on the arrangements applicable to agricultural products and goods resulting from the processing of agricultural products originating in the African, Caribbean and Pacific States (ACP States).

[52] The difficulties of streamlining development in an EPA can be inferred from the concerns expressed by the ACP negotiators. For instance, in 2006, one of the chief negotiators declared that '[i]n our view, there is a definite contradiction between the narrow focus on trade liberalisation and the EU's arguments that EPAs are instruments for development rather than to force open regional markets. One of our concerns is that EPAs must not become instruments of oppression.' Billie Miller, Chair of the ACP Ministerial Trade Committee and Minister of Foreign Affairs and Foreign Trade of Barbados, Vienna, June 2006.

[53] The assumption here is to the extent that the current initialled EPAs do not lead to comprehensive development-friendly EPAs in 2008.

[54] See Article 300 of the EC Treaty and the chapeau???of Article 9(d) of the proposed New EC Reform Treaty at Draft Treaty Amending the Treaty on the European Union and The Treaty Establishing the European Community, Brussels, 23 July 2007 (30.07).

[55] CPA Article 37(4)-(6).

[56] See http://ec.europa.eu/trade/issues/bilateral/regions/acp/memo010307_en.htm. Pursuant to WTO Charter Article IX (on the WTO decision-making process), a waiver application may be accepted by two-thirds majority votes in the absence of a clear consensus from the Membership.

[57] Unless a miracle occurs and the Doha Development Round proceeds faster and WTO members adopt the kind of proposals tabled by the ACP countries to the CRTA.

4.2. GATT Article XXIV and Mainstreaming Development in EPAs

As seen in the preceding section, GATT Article XXIV allows WTO members to engage in discriminatory regionalism to the extent that those RTAs, among other things, fulfil the basic requirements of (a) covering substantially all the trade in goods among the constituent members of the RTAs;[58] (b) not introducing higher duties or other trade-distorting measures in respect of trade with third countries, excepting those that were in place before the formation of the FTA; and (c) such FTAs should enter into force within a reasonable period of time.[59] From a legal perspective, a GSP-based trade agreement will move EU-ACP trade relations out of the free trade domain into the area covered by the Enabling Clause and they would effectively not be required to conform to the three requirements noted earlier. While FTAs create a wider trading area by removing obstacles to competition, agreements in the context of the Enabling Clause are subject to internal barriers established to confer privileges on underdeveloped members of the agreements. Thus, since the EU-ACP trade relationship seems to have been originally conceived on the basis of transposing elements of the Lomé/Cotonou preferences into EPAs, differentiation in the sense of Special and Differential Treatments (S&D) constitutes a fundamental aspect of the negotiations with regard to EPAs as required by Article 34(4) of the CPA.[60] CPA Article 35(1) further calls for the contracting parties to such negotiations to pay particular attention "…to trade development measures as a means of enhancing ACP States' competitiveness" and in this regard, the Community shall support appropriate development strategies within the ACP States.

4.3 Development as a Yardstick for Understanding the Cotonou Agreement

The issue of how the conditions "text, context and objects and purposes" set out in Article 31 of the Vienna Convention (VC) should be approached when trying to make sense of international trade rules has arisen on a number of occasions in the WTO.[61] If development *par excellence* as an object can be employed as a *modus operandi* for understanding the mindset of the EU and the ACP countries at the time of drafting the CPA, the development dimension, as an objective, must be clearly factored into the EPAs at the moment of drafting and institutionalised in every stage of implementation of the FTA. Pursuant to the CPA, "[t]he Parties shall closely cooperate and collaborate in the WTO with a view to defining the arrangements reached, in particular with regard to the degree of flexibility available".[62] And during the Doha Ministerial Conference, WTO members agreed to negotiations aimed at clarifying and improving disciplines and procedures under the existing WTO provisions applicable to regional trade agreements. Members further agreed that development should be

[58] The only exceptions are those under GATT Articles XI, XII, XIII, XIV, XV and XX.
[59] GATT Article XXIV(5)(b) and 8(b).
[60] Pursuant to CPA Article 34(4), '[e]conomic and trade co-operation shall be implemented in full conformity with the provisions of the WTO, including special and differential treatment, taking into account the Parties' mutual interests and their respective levels of development'.
[61] See AB reports, *US – Shrimp*, para. 114; *EC – Chicken Classification*, para. 176; *Japan – Taxes on Alcoholic Beverages* pp. 11-12, etc.
[62] CPA Article 37(8).

one of the driving objectives of the negotiations on WTO rules relating to regional trade agreements.[63]

Surely, at the time of concluding the CPA, the contracting parties must have been convinced that by the end of 2007, the WTO Doha Development negotiations would be completed so that GATT Article XXIV would provide for possibilities of some sort of S&D treatments in favour of constituent members of the RTA. They were clearly wrong in this regard. When the Doha Development Round was launched in 2001, the non-LDC ACP countries, in particular, welcomed it with enthusiasm. The Round was to be completed by the beginning of 2005, leaving enough time for the expiration of the Cotonou WTO Waiver. At the early stage of the negotiations, the ACP group jointly supported a proposal calling for the negotiations on WTO rules on RTAs to explicitly provide the necessary S&D to developing countries party to RTAs with developed countries.[64] With the slow pace of the Doha development negotiations, the EC for its part sponsored a somewhat half-hearted proposal to the Negotiating Group on Rules, stating that "flexibilities [are] already provided for within the existing framework of WTO rules" and that the current negotiations should "involve further consideration of the relationship between GATT Article XXIV and the Enabling Clause, as well as an examination of the extent to which WTO rules already take into account discrepancies in development levels between RTA parties".[65] The EC and the ACP views have failed to move forward as the negotiations on RTAs have so far concentrated on procedural rather than substantive issues.[66]

Currently, some WTO members are of the view that consistent with GATT Article XXIV, there is very little room, if any, for inserting discriminatory S&D in RTAs entered into between developed and developing WTO members. This is undoubtedly bad news for the ACP countries, especially the non-LDCs among them. In this regard, if EPAs are to be consistent with the development objective of the CPA, they must contain provisions clearly allocating preferential treatments to the ACP countries. However, the views of the EC as expressed in the paragraph above are very much consistent with its earlier submission before the GATT panel in the *EEC-Bananas II* dispute.[67] The EEC earlier in this case argued that the Lomé Convention, which provided discriminatory market access preferential treatment in respect of ACP bananas, undoubtedly created an FTA between the EEC and the ACP countries.[68] According to the EEC, such preferences were in conformity with the criteria and conditions laid down in Article XXIV(5)(b) and XXIV(8)(b), read together with Part IV of GATT. Thus, GATT Article XXIV(5)(b) and XXIV(8)(b) permitted the establishment of FTAs between the EC and the ACP countries without full reciprocity.[69] Similarly, in the *European Community – Export Subsidies*

[63] See paragraph 29 of the Doha Ministerial Declaration.
[64] This was followed by another proposal by the ACP in 2004 on the same issue. See WTO TN/RL/W/155.
[65] Cotonou Article 39(2) calls for both parties to closely cooperate in the WTO to further their mutual interests.
[66] See Decision of the WTO General Council of 14 December 2006 on Transparency Mechanism in RTAs, WT/L/671 and WTO Secretariat Background Notes on Issues related to RTAs, TN/RL/W/8/Rev. 1.
[67] Report of the Panel*, EEC – Import Regime for Bananas*, (DS38/R), 11 February 1994.
[68] Ibid at para. 37.
[69] Ibid at para. 39, p. 14.

on Sugar,[70] the EC argued before the panel that the complainants' challenge of the EC re-export of subsidised ACP/India-equivalent sugar was wrong and tantamount to challenging the commitments of WTO members agreed upon during the Uruguay Round of multilateral trade negotiations (MTNs).[71] Neither the panel nor the AB (though they did not expressly state that this was the case) found this argument a justification for the EC's WTO-inconsistent measures at issue.

If differentiating between ACP countries constitutes[72] an essential element of EPAs, the EC's arguments in the *Bananas II* case would probably still be relevant in the impending EPAs. Such differentiations in this context would be limited to ACP countries and apply to landlocked countries, LDCs, and low-income developing members of the ACP group. Despite the non-adoption of the panel reports in the *EEC-Bananas II* case, the panel rejected the EEC's arguments. The panel findings stated that "…a legal justification for the tariff preference accorded to the EEC to imports of bananas originating in the ACP countries could not emerge from an application of Article XXIV to the type of agreement described by the EEC in the Panel's proceedings". In somewhat suggesting the possibility of intra-ACP differentiation in EPAs, CPA calls for the contracting parties to take into account the development needs of the ACP[73] countries, especially those affected by the WTO provisions on S&D treatments. Such S&D would also include the kind of preferences provided for under GATT Article XVIII:B which provides special treatment to the developing countries as covered by the Enabling Clause[74] of the WTO.

However, assuming that "…[Article XXIV is to be normally read in conjunction with Part IV of the General Agreement] the authorisation of special and differential treatments had been suggested during the negotiations of Part IV", but was paralysed at the time of drafting the final text.[75] In this regard, if preferences are to be accorded to ACP countries under a FTA like EPAs, Article XXIV(5)(b) of GATT covers only the formation of FTAs between WTO Members.[76] Currently, not all ACP countries are WTO members. Consequently, in the present state of affairs, the text of Article XXIV(5) makes it clear that, in the absence of a waiver, the conclusion of FTAs with non-GATT/WTO members may not justify infringement of the MFN rights of other WTO members.[77]

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[70] See documents WT/DS265/21, WT/DS266/21 and WT/DS283/2 of 11 July 2003.

[71] See statement by the European Commission: 'WTO challenge against EU sugar will hurt developing countries', in document DN:IP/03/993 (Brussels, 10 July 2003).

[72] See Francis Matambalya and Susanna Wolf, 'The Cotonou Agreement and the Challenges of Making the New EU-ACP Trade Regime WTO Compatible', JWT, Vol. 35, Issue 1 (2001) at pp. 123-144.

[73] CPA Article 34(4).

[74] GATT CONTRACTING PARTIES decision of 28 November 1979 (L/4903), officially known as Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries.

[75] Panel reports, *EEC-Bananas II*, para.162 at p. 50. This therefore put into question the very purpose of Part IV of the General Agreement. However, it is also important to note the statement of the panel ---if non-reciprocal Article XXIV preferences were allowed in the reading of Part IV, the very objective of the Enabling Clause will be questioned.

[76] '[A]s between the territories of contracting parties' per the wording of Article XXIV(5)(b).

[77] In this regard, see panel reports in *Bananas II*, para. 163, p. 51.

While Part IV of GATT provides for situations where developing countries may place development at the heart of their trade policy formulations, Part IV per se may not be invoked as a justification for actions which would be inconsistent with their obligations under GATT Part II.[78] Therefore, the question as to whether EPAs may move to a different territory in terms of the S&D that it provides to the non-LDC members of the ACP remains open. In other words, the idea of employing a variable geometric approach in EPAs clearly remains uncertain. However, viewed from the perspective outlined earlier, the issue is no longer of specific S&D to a set of ACP countries, but rather to developing countries which are members of the WTO.[79] As opposed to the non-reciprocal preferential treatments under the CPA, EPA preferences will become less internal as they may be available to all developing countries if provided. Although intra-regional differentiation is a vital element of the negotiation of EPAs, in the absence of the necessary progress in the WTO Doha negotiations, such differentiation can only occur if the trade provisions of the CPA are interpreted in the context of their negotiating history and the circumstances of the conclusions.[80]

5. Contesting EPAs Failure in the Context of CPA Article 98 Dispute Settlement Procedure

Effective and unambiguous dispute settlement provision is one of the elements that determine the credibility of any international agreement. Interpretation in the process of Dispute Settlement may also highlight how development concerns were factored into a specific international treaty at the time of negotiations and drafting of the agreement in question.[81] Although we are not suggesting that a state would disregard its international commitments on the basis that no court exists to rule on its actions, an inter-state dispute settlement structure can be an effective means of independent control that effectively limits the conduct of the entities subject to law.[82] A trade agreement which brings into being an effective dispute resolution organ demonstrates the willingness and good faith of the parties to such agreement to enforce it. Dispute settlement provisions *a priori* either deter parties from violating the agreement or prevent the parties from engaging in unilateral countermeasures once it has perceived violations.[83] This is of greatest significance when the parties to such agreement are

[78] The GATT panel had stated in another case that even the *travaux préparatoires* of Part IV of GATT clearly show that the Contracting Parties had not intended that Part IV be a separate exception to the General Agreement. See panel report in *Norway – Restrictions on imports of textiles products*, BISD 27S/119, pp. 125-126, para. 15, adopted on 18 June 1980.

[79] This is in line with CPA Article 34(4) which calls for EPAs to be in conformity with the WTO rules including the WTO provisions on Special and differential treatments.

[80] This is not repugnant to Article 32 of the Vienna Convention.

[81] See Qureshi (2006)'Interpreting WTO Agreements: Problems and Perspectives' for development dimensions in the interpretations of international treaties.

[82] We cannot dismiss the fact, as Koskenniemi has argued, that international treaties are unable to fulfil any function unless they have a degree of autonomy from states' behaviours, will and interests. See Martti Koskenniemi, *From Apology to Utopia: The Structure of International Legal Argument* (Cambridge, 2005), pp. 19-20. See also Markus Burgstaller*, Theories of Compliance with International Law* (Leiden, 2005).

[83] Of course, such dispute settlement provisions need to be introduced in such a way that the penalties for violating the agreement outweigh the possible benefits of doing so.

very much unequal in terms of their relative economic strength. The WTO's DSU and, to some extent, the dispute settlement provisions under NAFTA provide clear examples of such structures. Consequently, in the context of the WTO, it has been asserted: "*A careful reading of the accumulated jurisprudence of the [dispute settlement] system thus far reveals that the interests and perception of developing countries have not been adequately taken into account. The panel and the Appellate Body have displayed an excessively sanitized concern with legalisms, often to the detriment of the evolution of a development-friendly jurisprudence*".[84]

In the context of the CPA, the only recourse available where any of the parties to the agreement fails to respect its obligations are the provisions of Article 98 of the CPA Agreement. While under public international law, parties to a treaty have a choice of means to peacefully settle their international dispute,[85] a quasi-adjudicative or legal process provides a degree of assurance on the binding and definitive nature of the decision.[86] Under the CPA, disputes arising from a violation of the agreement may be referred first to the Council of Ministers, secondly to the Committee of Ambassadors, and in the worst case scenario to the Permanent Court of Arbitration.[87] In the final case, unless otherwise decided, the arbitration procedure shall be those laid down in the "optional arbitration regulation of the Permanent Court of Arbitration for International Organisations and States".[88]

To a large extent, the effectiveness of a dispute settlement organ is determined by the architecture of the very dispute settlement mechanism. Given the vague wording of the CPA, most ACP countries may not even be willing to go through the onerous arbitration process at the PCA at The Hague. Even if they were to pursue such a process, compliance proceedings are not considered by the provisions of Article 98 of the CPA. The Agreement only mentions, and does not clearly specify, what measures must be taken to comply with the rulings of the arbitral proceedings or with the decisions of the Council of Ministers and the Committee of Ambassadors. Nonetheless, arbitration procedure, which Article 98 of the CPA clearly envisages as a method of last resort, allows the respondent party to delay the appointment of arbitrators. Even if the parties manage to agree on the appointment of the three arbitrators on time, the decision of the arbitration is supposed to be binding on both parties. At the same time, no compliance timeframe is given and there are no provisions on reporting on compliance to the member states as exists under some trade regimes.[89]

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[84] See the communication of Zambia on behalf of the LDC Group to the DSB in document TN/DS/W/17,(dated 9 October 2002)

[85] See United Nations Charter, Article 33, para. 1.

[86] For dispute settlement in public international law, see J. G. Merrils, *International Dispute Settlement* (Cambridge University Press, 1998), pp. 1-169; and in the context of international economic law, see Yenkong Ngangjoh H., *WTO Dispute Settlement System and the Issue of Compliance: Perspectives in Remedies Against Non-Compliance* (Helsinki, 2006).

[87] CPA Article 98(2)(a).

[88] CPA Article 98(2)(c). For more on the rules on arbitration by International Organisations and States, see the internet site of the Permanent Court of Arbitration at The Hague at http://www.pca-cpa.org/showpage.asp?pag_id=1061.

[89] See in this case DSU Article 21(6) on surveillance of implementation of the rulings of the DSB.

6. Considering Disputes under the CPA before the European Courts

In view of the fact that thus far only interim EPAs, which contain no clear details in terms of the commitments given by the parties, have been agreed on among some of the ACP countries and the EC, the possibility remains that agreement on EPAs will not be reached by the end of 2008 as some of the initialled agreements claim.[90] In this situation of uncertainty, individual exporters from the ACP countries are likely to be more concerned about the long-term delivery terms of the contracts they may be entering into now. Assuming that on the basis of the initialled interim goods-only agreements between the EC and a cluster of ACP countries, the rights and obligations under the CPA are still valid, ACP non-LDCs will be expected to continue to benefit from the Cotonou preferences until such time as an agreeable EPA is put in place. Consequently, the EC will not be absolved of its legal obligation under the Cotonou Agreement to continue to give Cotonou-equivalent preferences to these countries. At the same time, it is worth pointing out that save for cases in which there is a denunciation of the CPA by one of the parties, the obligations under the Cotonou Agreement remain valid until 2020.

As seen earlier, in the absence of the onerous Article 98 provisions, the CPA does not provide any comprehensive guidelines for settling disputes arising from the agreement. Therefore, a critical issue for individual exporters/importers within the EU would be whether the CPA creates rights and obligations that can be enforced through national courts. In other words, is the principle of "direct effect"[91] in Community law applicable in relation to the CPA? This issue begs another question as to the position of the CPA within the Community legal system.

Pursuant to the EC Treaty,[92] international agreements "shall be binding on the institutions of the Community and on the member States". Thus, international treaties concluded by the Community may be regarded as forming an integral part of Community law.[93] However, the principle of "direct effect" will only apply to the extent that the piece of legislation[94] or provisions of the EC law in question (1) has an addressee; and (2) that the condition is clear, unconditional and precise. As the former is neither necessary nor sufficient to invoke direct effect, the fulfilment of the latter will suffice for the applicability of direct effect.[95] This

[90] The application of the SADC EPAs by the EU was scheduled for 1 January 2008 and 1 June 2008 for the SADC EPA States. See statement of the Chief Negotiators On the initialling of the Economic Partnership Between the SADC EPA Group of States on the one hand and the European Union on the other hand, Brussels, November 2007.

[91] The principle of 'direct effect' in Community law relates to the rights of an individual. Pursuant to the direct effect principle, the citizens of the Union can rely on the provisions of EC law as being directly effective before the national courts.

[92] Article 300(7) of the Treaty Establishing the European Community.

[93] This was clarified by the European Court of Justice as early as 1974 in the case of *Haegeman v Belgium*, ECJ, 181/73 ECR 449, at 472.

[94] Although the use of 'legislation' in international context may be questioned by critics who dispute the nature of international law as law, in 'making treaties or adopting certain patterns of behaviour a state in fact "legislates" and not merely furthers its own national interests in individual circumstances'. See Koskenniemi at p. 145 and Burgstaller at p. 23.

[95] See Kari Joutsamo, *The Role of Preliminary Rulings in the European Communities* (Turku, 1979), p. 224; and more comprehensively, Paul Craig & Gráinne De Búrca, *EU Law, Text, Cases and Materials* (Oxford, 2003) third edition, pp. 178-227.

therefore means that even if the CPA is considered as an enforceable piece of legislation within the Community, individual rights emanating from it must be clear, unconditional and precise.

Let us now return to the issue of whether the CPA *par excellence* confers rights on Community citizens which the national courts are obliged under EC law to uphold. Pursuant to Article 20(3)(d) of Council Regulation (EEC) No 2913/92, "[t]he Customs Tariff of the European Communities shall comprise among other things . . . preferential tariff measures contained in agreement which the Community has concluded with certain countries or groups of countries and which provide for the preferential tariff treatment".[96] And in view of the fact that customs duties within the Community are determined by the Union and not by individual member States, Commission Regulation (EC) No 1549/2006 of 17 October 2006 amending Annex I to Council Regulation (EEC) No 2658/87 on the tariff and statistical nomenclature and on the Common Customs Tariff is to the effect that "conventional duties are applicable to goods, other than those. . . originating in certain countries or where preferential customs duties are applicable in pursuance of agreements".[97] Consequently, the CPA is consistent with the foregoing Regulation. In this regard, the CPA becomes a candidate for the sources of Community Law.[98] Bearing in mind that the principle of direct effect/supremacy essentially renders Community law the "law of the land", the CPA as an international agreement concluded by the Community is "binding on the Member States".[99]

The issue as to the nature of the ACP-EC partnership agreement within Community law has already been highlighted by the ECJ in the context of the 1963 Yaounde Convention.[100] In the *Bresciani* case, the Italian administration had imposed a charge for compulsory veterinary and public health inspections on raw cowhides from the Associated Territories.[101] More importantly, the ECJ had to rule on the nature of individual rights emanating from the Yaounde Convention. Here, the Court conceded that the Yaounde Convention was not concluded with the objective of ensuring the equality of obligations that the Community assumes toward the Associated States. In spite of this clarification, the Court nevertheless, pointed out that "[the] imbalance between the obligations assumed by the Community towards the Associated States, which is inherent in the special nature of the Convention, does not prevent recognition by the Community that some of its provisions have a direct effect".[102]

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[96] Council Regulation (EEC) No. 2913/92, of 12 October 1992, Establishing the Community Customs Code, obtainable at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31992R2913:EN:HTML, last visited on 17 January 2008.

[97] See Section B on General Rules concerning duties, paras. 1 and 2, Official Journal of the European Union, 31 October 2006.

[98] EC Treaty Article 300(7).

[99] EC Treaty Article 300(7). On the issue of Community law as the 'law of the land' see the rulings of the ECJ in Case 26/62 *Van Gend & Loos v. Nederlandse Administratie der Belastingen* [1963], ECR 1; ECJ.

[100] The Yaounde Convention concluded on 20 July 1963 was superseded by the first Lomé Convention (1975) and subsequently by the current Cotonou Partnership Agreement (2000).

[101] Case 87/75, *Bresciani v. Amministrazione Italiana delle Finanze* (1976) ECR, 129.

[102] See paras. 22 and 23 of the *Bresciani* case. For a short analysis of the case see Paul Craig and Gránne de Búrca (2003) at pp. 588-590.

In light of the principle of consistent interpretation, domestic courts are supposed to interpret and apply national law in a manner consistent with EC law.[103] In the case at hand, the ECJ interpreted Article 2 of the Yaounde Convention as imposing obligations on the Community to refrain from imposing charges that may have an automatic equivalent effect. Following this line of reasoning, Article 2(1) of the Yaounde Convention conferred rights on EC citizens, and national courts are obliged to uphold these rights.[104] By implication, from 1970 onwards Community citizens could import goods from Associated States without having to pay charges which have effects equivalent to custom duties.

7. Tentative Conclusion

It is true that whatever form an eventual EPA will take, the general economic and trade framework of the FTA between the EU and the ACP countries that will emerge out of the negotiations will need to be WTO-compatible. At the same time, this by no means assumes that there is any hierarchy between the WTO treaty and an impending trade treaty between the EU and the ACP countries. To be sure, with the exception of peremptory norms or rules that have the status of *jus cogens* or obligations *erga omnes*, there is no hierarchy in international law.[105] However, if there were to be such hierarchy between one or two treaties and another, there would be specific provisions in the treaty in question creating such hierarchy.[106] In the absence of this, we can only have recourse to general principles such as the later in time rule[107] or the requirement that a *lex specialis* treaty takes precedence over a more general one.[108] However, the fundamental principle informing the interpretation of such agreement would relate to the development needs of the ACP countries.[109] It is accordingly incompatible with the spirit of the Cotonou Agreement to assume that the failure to enter into a comprehensive EPA within the timeframe stipulated in the various initialled EPAs will absolve the EU of its obligations under the Cotonou Agreement.

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[103] In the area of competition, despite the direct effect of EC Treaty Articles 81 and 82, and the fact that national authorities have different competition regimes, national legislation must be applied in conformity with EC law.

[104] Para. 26 of the report.

[105] This is contrary to municipal law where there is a clear hierarchy of norms between constitution, ordinances decrees etc. However, Article 53 of the Vienna Convention directs the international community to refrain from entering into treaties that conflict with *jus cogens*.

[106] This is the case with Article 103 of the United Nations Charter.

[107] Even with the later in time rule, international law as a legal system '…act[s] in relation to and should be interpreted against the background of other rules and principles. As a legal system, international law is not a random collection of such norms. There are meaningful relationships between them.' See the International Law Commission on the Fragmentation of International Law: Difficulties Arising from the Diversification and Expansion of International Law, United Nations, ILC, Report on the Work of its 58th Session, (1 May to 9 June and 3 July to 11 August 2006), General Assembly Official Records, Sixty-first Session, Supplement No. 10 (A/61/10).

[108] The Latin maxim *lex specialis derogat legi generali*, as a technique of interpretation and conflict resolution in international law, is to the effect that whenever two or more norms deal with the same issue, the more specific one prevails. On the conflict of norms in international law, see Joost Pauwelyn, *Conflict of Norms in Public International Law: How WTO Law Relates to other Rules of International Law* (Cambridge, 2004).

[109] See Article 34 (4) of the CPA.

8. Conclusion

As the WTO Doha negotiations for further liberalisation and clarification of some of the ambiguous GATT/WTO provisions have failed to be reinvigorated, all eyes in the ACP countries are now on the EPA negotiations. Because of the vagueness of the GATT/WTO provision on RTAs, different interpretations have been given to GATT Article XXIV. No FTA has ever been challenged before the WTO dispute settlement on the basis of compatibility with Article XXIV. This has posed a significant challenge to EPA negotiations in respect of the extent to which development concern can be factored into an eventual EPA. The search for constraints within the WTO through the Doha negotiations to achieve this result seems very unlikely to bear fruit in the near future or before a full EPA is completed. The failure at the multilateral level shifts the burden onto the EU and the ACP countries to deal with the inherent conflict of sustainable development, regional integration and WTO compatibility in EPAs. Although this does not appear to be currently the case, one might have imagined that this issue could have been easily handled even without any progress with the Doha negotiations. This assumption gains support from the fact that WTO members have consistently failed to check the legality of RTAs and in dispute settlement they have shied away from challenging RTAs.

With regards to the question of regionalism, regional integration in Africa needs to come from concerted vision and must be supported by domestic constituencies. For this to happen, transparency and openness in the decision making process in Africa's public sphere are of the essence. Moreover, the current experience from EPA negotiations points to the fact that external actors have the power to either help or hinder the process, and African countries must be aware of the consequences of their international affairs.

AFRICAN COUNTRIES AND THE WTO NEGOTIATIONS ON THE DISPUTE SETTLEMENT UNDERSTANDING

Kofi Addo* & Edwini Kessie**

I. Introduction

The dispute settlement system of the World Trade Organisation (WTO) is recognised as one of the central pillars of the multilateral trading system. The credibility of the WTO owes much to its ability to enforce the commitments entered into by its members. In fact, Article 3.2 of the Dispute Settlement Understanding (DSU) provides that the dispute settlement system is a central element in providing security and predictability to the multilateral trading system. Its uniqueness in the system prompted WTO members to specifically exclude the DSU negotiations from the single undertaking[1]. They were of the firm belief that a strengthened and effective dispute settlement would be beneficial for all members and that it would be inappropriate to make linkages with other negotiating issues. Increasingly, the frequency with which a member has recourse to the dispute settlement mechanism is partly being used to determine the extent of its participation in the multilateral trading system. A look at the statistics reveals that it is mostly the leading trading nations which are making extensive use of the dispute settlement system. African countries and Least Developed Countries have rarely made use of the WTO dispute settlement system, even though other developing countries, particular those in Asia and Latin America, are increasingly making use of it.[2]

The situation under the GATT was no different. African and other developing countries, including those now making use of the WTO dispute settlement system, hardly made use of the GATT dispute settlement system. As a group, developing countries accounted for less than 10 per cent of the cases initiated by the GATT contracting parties.[3] The lack of use of the dispute settlement system by African and other developing countries and its structural weaknesses, including the lack of precise time-limits and the ability of countries to block the establishment of panels and prevent the adoption of panel reports, made the reform of the dispute settlement system one of the priorities during the Uruguay Round. To a large extent, the negotiators achieved their objectives. The DSU introduced fixed time-limits for almost all the stages in the process and, most importantly, circumscribed the right of members to block the establishment

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[1] Paragraph 47 of the Doha Ministerial Declaration. WT/MIN(01)/DEC/1; 20 November 2001.

[2] It should be noted, however, that some leading trading nations such as Singapore, Chinese Taipei and Hong Kong, China have not made extensive use of the dispute settlement system. The only least-developed country to have requested consultations under the DSU is Bangladesh in the case on *India – Antidumping Measures on Batteries from Bangladesh*, WT/DS306.

[3] See GATT, GATT Activities 1991: An Annual Review of the work of the GATT (Geneva: GATT July 1992) p.50.

of panels or the adoption of panel reports. Under the new system, members can exercise this right only when there is a consensus against the establishment of a panel or the adoption of a panel report or an Appellate Body report.

Since the new dispute settlement system went into force in January 1995, there have been an unprecedented number of cases initiated by members. As of November 2008, WTO members had requested consultations in 381 cases leading to the establishment of 161 panels and the adoption of 118 panel reports and 75 Appellate Body reports by the Dispute Settlement Body (DSB). The increase in the number of cases could be interpreted as a sign of confidence in the new dispute settlement system by WTO members, especially considering that developing countries as a group account for nearly 40 per cent of this figure.[4] It could also be interpreted that members have become more protectionist since the implementation of the WTO Agreement in January 1995. In other words, the sharp increase in the number of disputes should not be confused with confidence in the dispute settlement mechanism. It could also well be that the more automatic procedures and the relatively easy access to the dispute settlement mechanism have encouraged members to initiate cases under the DSU. Whereas this view may be plausible, the high number of cases which have been settled "out-of-court" coupled with the decisions that have been handed down by Panels and the Appellate Body seem to suggest that members have generally not initiated frivolous cases.[5]

From an institutional perspective, however, what may be important is the general satisfaction with the operation of the DSU. In other words, whether or not members have become more protectionist after the implementation of the WTO Agreement is not that important, as the DSU has effectively acted as a bulwark against such protectionist tendencies. With the exception of a few cases where implementation has been delayed, almost all the complaints have been satisfactorily resolved either through the WTO system or through bilateral negotiations between the parties. Generally, WTO members seem to be content with the operation of the DSU, insofar as it has reduced significantly the threat of unilateralism in international trade relations and established a rules-based system in which economic and political power have become largely irrelevant in determining the outcome of disputes.[6]

Notwithstanding the improvement in the WTO rules and procedures for the settlement of disputes, African countries have complained that because of their lack of expertise in WTO matters, high legal costs and other impediments, they have not been able to take full advantage of the improved rules and procedures to enforce their rights under the WTO Agreement. A

[4] Lacarte-Muro and Gappah, "Developing Countries and the WTO legal and Dispute Settlement System: A View from the Bench, JIEL (2000) p.395

[5] As at 15 September 2006, 102 panel and 66 Appellate Body reports had been adopted by the Dispute Settlement Body. Mutually agreed solutions had been reached in about 70 cases.

[6] In *European Communities – Measures Affecting Trade in Commercial Vessels*, WT/DS301, the Panel stated that: "...based on an interpretation of Article 23.1 of the DSU in accordance with the ordinary meaning of its terms in their context and in light of the object and purpose of the provision, that the obligation to have recourse to the DSU when Members 'seek the redress of a violation...' covers any act of a Member in response to what it considers to be a violation of a WTO obligation by another Member whereby that first Member attempts unilaterally to restore the balance of rights and obligations by seeking the removal of the WTO-inconsistent measure, by seeking compensation from that Member, or by suspending concessions or obligations under the WTO Agreement in relation to that Member.": para 7.207at p.126.

cursory glance at the cases which have been initiated since the WTO came into force reveals that it is mostly the bigger and the relatively advanced developing countries such as Argentina, Brazil, Chile, India and Thailand which have been involved in the process either as complainants or respondents. It cannot even be taken for granted that these countries have the requisite knowledge and skill in prosecuting or defending cases. It is common knowledge that some of them retain established law firms or the Advisory Centre on WTO Law to represent them in WTO proceedings. To date, African countries which have participated in the dispute settlement process have done so only as third parties and not as complainants.[7] A limited number of cases have been initiated against Egypt and South Africa which happen to have.[8] ?????

For the large number of African countries which cannot probably afford the services of international law firms or are not members of the Advisory Centre on WTO Law, the only options open to them are to seek bilateral negotiated settlements with the opposing parties, abandon any potential claims that they may have, or seek assistance under Article 27.2 of the DSU which relevantly provides that the WTO Secretariat shall make available "a qualified legal expert…to any developing country Member which so requests. This expert shall assist…in a manner ensuring the continued impartiality of the Secretariat". Pursuant to this provision, the WTO Secretariat has recruited two part-time consultants to assist developing countries which may want to have recourse to the DSU.

While these experts have done their best to accommodate all requests, a number of African and other developing countries have questioned the depth of the assistance provided by them. Due to the lack of adequate resources and the proviso that the "impartiality of the Secretariat" should be upheld at all times, important constraints have been placed on the sort of assistance that could be provided to developing-country members. At the pre-Panel/Appellate Body stage, the assistance rendered so far has basically involved making preliminary informal determinations as to the chances of a member successfully initiating or defending a case. At the Panel/Appellate Body stage, the assistance has mainly consisted of commenting on the submissions prepared by a member's team of lawyers and responding to queries on an *ad-hoc* basis.

[7]In *EC – Bananas*, WT/DS27, Cameroon, Cote d'Ivoire, Ghana and Senegal participated as third parties with a view to safeguarding their preferences under the EC's banana regime. In *EC – Export Subsidies on Sugar*, WT/DS265/266/283, Cote d'Ivoire, Kenya, Madagascar, Malawi, Mauritius, Swaziland and Tanzania participated as third parties to defend their preferences under the Sugar protocol. In *US – Subsidies on Upland Cotton*, WT/DS267, Benin and Chad participated as third parties given the importance of cotton to their economies. In *EC – Asbestos*, WT/DS135, Zimbabwe participated as a third party because of its broader export interest in asbestos. In *US – Shrimp*, WT/DS58, Nigeria and Senegal participated as third parties because of their export interest in shrimps.

[8]The two African countries which are relatively active are Egypt and South Africa, which happen to have Africa's biggest economies. Two cases have been initiated against South Africa, namely *South Africa – Anti-Dumping Duties on the Import of Certain Pharmaceutical Products from India*, WT/DS168 and *South Africa – Definitive Anti-Dumping Measures on Blanketing from Turkey*, WT/DS288. Four cases have been initiated against Egypt, namely *Egypt – Import Prohibition on Canned Tuna with Soyabean Oil*, WT/DS205*; Egypt – Definitive Anti-Dumping Duties on Steel Rebar from Turkey*, WT/DS211, *Egypt - Measures Affecting Imports of Textile and Apparel Products*, WT/DS305 and *Egypt – Anti-dumping Duties on Matches from Pakistan*, WT/DS327. Egypt participated as a third party in *EC – Bed Linen*, WT/DS 141 and *EC – Provisional Steel Safeguards*, WT/DS260.

For a significant number of African countries, especially those not conversant with GATT/WTO jurisprudence, the assistance provided by the WTO Secretariat is woefully inadequate. They expect the legal experts to be more proactive in the sense of being involved in all the stages of the process. They expect them to draft their submissions to the Panel/Appellate Body and respond to any queries or questions that may be posed by the Panel/Appellate Body, the parties or third parties. While, in principle, this would be the optimal assistance that could be provided by the WTO Secretariat, it has been ruled out for the reason given earlier.

In the face of this limitation, the crucial issue is what can be done to strengthen the capacity of African countries to make use of the WTO dispute settlement mechanism to safeguard and promote their interests in the multilateral trading system. In the current DSU negotiations, African countries have been quite active and tabled far-ranging proposals with a view to increasing their access to the system and also to obtain favourable rules in the DSU to safeguard and promote their interests.[9] The purpose of this paper is to examine these proposals and assess whether, if adopted, they would increase the participation of African countries in the dispute settlement system.

The paper is divided into five sections. The second section examines some of the reasons why African countries have not been making use of the dispute settlement system and considers the possible consequences for African countries for not participating in the development of jurisprudence which would partly define the rights and obligations of members. The third section examines systemic issues raised by African countries, including the scope of the interpretative powers of the General Council, and also proposals relating to the pre-panel phase. This section considers whether it would be in the interest of African countries if the consultative process were strengthened and whether the present time-frame for consultations is adequate from their perspective. The fourth section examines proposals tabled by African countries relating to the panel and Appellate Body phase. It considers, among other things, whether African countries should press for enhanced third party rights as reflected in the Chairman's text of 28 May 2003 and the feasibility of the proposal relating to the involvement of other institutions such as UNCTAD in the dispute settlement process. The fifth section examines proposals relating to the implementation phase, including those on financial compensation and collective retaliation. The paper concludes with some summary observations and recommendations on how African countries can prepare themselves to benefit from the opportunities that go with membership in the WTO, and how they can seize these opportunities which go hand in hand with a better understanding of their rights and obligations as members of the WTO.

[9] See document TN/DS/W/42. Other proposals considered are the following: Submission of the African Group to the Special Session of the Dispute Settlement Body (TN/DS/W/15, 25 September 2002); Submission of the African Group to the Special Session of the Committee on Trade and Development (TN/CTD/W/3/Rev.2; 17 July 2002) and the Responses of the African Group to questions posed by other Members (JOB (03)/55; 10 March 2003).

2. Possible Reasons for Africa's Low Involvement in the Dispute Settlement Process and its Consequences

There are several possible reasons why African countries have not been making use of the dispute settlement system of the WTO to enforce their rights and legitimate expectations. These include the share of African countries in world trade, which was estimated last year to be around 2 per cent by the WTO. With this low figure, it may be argued that it is not surprising that African countries are not making use of the dispute settlement system. They export mostly a few commodities and the priority for them is to remove supply-side constraints which have prevented them from increasing and diversifying their exports. While this argument may be persuasive, it ignores the fact that African countries do often complain about their exports being subject routinely to arbitrary non-tariff measures such as sanitary and phytosanitary measures, technical regulations and standards and overly stringent rules of origin. More importantly, should the barriers to their exports remain, they would eventually find it difficult to increase and diversify their exports.

It has also been suggested that African countries do not have an incentive to institute proceedings at the WTO given the fact that most of their exports receive preferential treatment in their major export markets – the European Communities and the United States. These preferences are non-reciprocal and could be revoked at any time by the preference-giving country without providing any reasons. Some African countries may entertain the fear that initiating actions at the WTO might irritate their major trading partners and put at risk the preferences which they so much depend on. Associated with this reason is the fact that most African countries depend on their major trading partners for budgetary support. With the value of their trade so small and sometimes far less than the Official Development Assistance (ODA) they receive from donor countries, it would make economic sense to continue receiving support from donor governments rather than to initiate actions at the WTO which might not result in increased export earnings. It has been further suggested that traditional African culture has always exhorted the value of settling disputes through mediation and conciliation as opposed to litigation which is perceived as an antagonistic procedure likely to damage relations between countries.

Another possible reason is related to the lack of expertise and resources to engage international law firms to represent them in dispute settlement proceedings. The Trade Ministries of most African countries are inadequately staffed and several do not even have trained international trade lawyers. While the WTO has tried to address this problem by providing training to African trade officials in line with Article 27.2 of the DSU, the impact has not been very significant. For a start, the duration of the dispute settlement courses is too short; they are usually held over four to five days. With the growing complexity of WTO Agreements and the case law, more time would be needed to build the capacity of African trade officials, especially where the officials have not had any prior exposure to international trade law. Also, there ought to be follow-up courses to keep the trained officials abreast with developments in WTO law.

A complicating factor in building and strengthening the capacity of African trade officials is the high turnover of staff in developing-country administrations. People who obtain knowledge about the WTO and its dispute settlement system are likely to be lured away by the private sector which can offer far more attractive salaries than those offered by the government. The

point has been made that it would be far more cost-efficient for African countries to engage international law firms or the Advisory Centre on WTO Law in the isolated cases they may be involved in in the future, rather than to expend resources training and retaining full-time trade lawyers who may never actually have the opportunity to practice their art. It would appear that in most African countries, the Trade Ministries are staffed by many economists and a few lawyers, probably reflecting this view.

Another related problem is the prohibitive rates charged by international law firms. Given that very few African countries are members of the Advisory Centre on WTO Law, those which are not may have no option other than to seek the services of international law firms which are usually based in Brussels or Washington.[10] According to Gregory Shaffer, the typical hourly rate charged by these firms is US$600. He also asserts that "[l]awyers for Kodak and Fuji in the Japan-Photographic Film case respectively charged their clients fees in excess of US$10 million". For a number of African and poor developing countries, it would simply not make economic sense for them to spend such huge amounts when the total value of their export of a particular product may not significantly be in excess of the legal fees they would be charged.

Unlike many developed or advanced developing countries, where there is a strong partnership between government and industry, in most African countries such partnerships are tenuous at best. It is known that in countries such as Brazil and India, which are among the most active users of the dispute settlement system, the private sector routinely pays the legal fees of international law firms to represent their interests in WTO dispute settlement proceedings. There is also the complicating factor that there are no proper institutional structures or mechanisms in place detailing the procedures to be followed if exporters should encounter any market access problems in foreign markets.

A further reason may be the uncertainty whether the responding member would faithfully implement the DSB's recommendations and rulings within the reasonable period of time either fixed by an arbitrator pursuant to Article 21.3(c) of the DSU or mutually agreed between the parties or approved by the DSB. As a guideline, the reasonable period of time shall normally not exceed 15 months from the date of adoption of the report by the DSB. For many African countries which rely on a few export products and markets, this could prove excessive considering the weak state of their industries. Unless the industry facing barriers is able to find new markets during the period of implementation of the DSB's recommendations and rulings, there is the possibility that it could cease to exist. Given this uncertainty, many African countries prefer to settle disputes through consultations, the advantages being that it is less expensive and could produce results much more quickly. It has also been suggested that there are less incentives for African countries to resort to dispute settlement considering that they cannot effectively retaliate against a country which fails to implement the DSB's recommendations and rulings.

It is clear from the foregoing that there are a number of factors which account for the non-utilisation of the dispute settlement system by African countries to enforce their rights and

[10]Only three African countries are members of the Advisory Centre on WTO Law, namely Egypt, Kenya and Mauritius. Least-Developed Countries can, however, avail themselves of the services provided by the Centre.

legitimate expectations under the WTO Agreement. The question is whether by not participating in the dispute settlement mechanism, African countries are losing the opportunity to contribute to the development of jurisprudence by panels and the Appellate Body. It may be argued that Africa has other priorities and should not waste scarce resources on dispute settlement. Priority should be given to enhancing market access and removing supply-side constraints, which have prevented them from diversifying their exports and markets. That dispute settlement would only become relevant when Africa has the goods and services to sell in global markets.

While African countries have been relatively active in the DSU negotiations, they have been much more active in the negotiations on agriculture and non-agricultural market access. This would appear to endorse the view that they attach more importance to market access than to dispute settlement. Winning cases through the WTO dispute settlement system would not necessarily ensure market access, as the responding member may have some difficulties in implementing the DSB's recommendations or rulings. In fact, it could potentially have the opposite effect when the complaining member has to suspend equivalent concessions or other obligations following the lack of implementation or an agreement on a compensatory package.

Presumably, the reason why African countries are focusing more on the market access negotiations is because they want to ensure that any agreements reached are cast in tight language to prevent future disputes. Their experience with current special and differential treatment (SDT) provisions in the WTO Agreements has reinforced their belief in legal certainty. Many of the SDT provisions are cast in hortatory language and have failed to deliver the market access that African and other developing countries expected. Past attempts to use dispute settlement to enforce the provisions of Part IV of the GATT did not yield any positive results.[11] The wide differences in the views of developed countries and those of developing countries on the scope of paragraph 44 of the Doha Ministerial Declaration and the resulting failure to make significant progress in reviewing and strengthening SDT provisions have also convinced African and other developing countries to focus more on market access issues in the current round of negotiations.

On the other hand, it has been argued that by failing to participate in the dispute settlement system, African countries are losing the opportunity to contribute to the shaping of "international trade principles and jurisprudence that will govern multilateral trade relations for years to come".[12] While participation in the dispute settlement system is important, we do not believe that Africa's trade interests have been prejudiced by its limited involvement in the dispute settlement process. The objective of the dispute settlement system of the WTO is not to create new legal principles that would define or regulate multilateral trade relationships

[11] In *United Kingdom – Dollar Area Quotas*, the argument by the United Kingdom that it was maintaining trade restrictions to further the interests of certain Caribbean countries was rejected by the Panel. In *Norway – Restrictions on Imports of Certain Textile Products*, the argument by Norway that its restrictions on the export of textile products by Hong Kong, China and its preferential treatment of exports from six developing countries were justified by Part IV of the GATT was rejected by the Panel.

[12] Mosoti Victor, "Does Africa need the WTO Dispute Settlement System", ICTSD, 2003 and "Africa in the First Decade of WTO Dispute Settlement", Journal of International Economic Law, 9(2), pp 457-453, 2006.

between countries, but to assist the parties to find a solution to their dispute. While it is conceivable that in discharging this role, panels and the Appellate Body might adopt an interpretation which may be at odds with treaty language and thereby indirectly create new obligations, the instances of that happening are very limited. Indeed, Article 3.2 of the DSU makes it clear that the purpose of dispute settlement is to preserve the rights and obligations of members under the covered agreements and that the recommendations and rulings of the DSB could not add to or diminish the rights and obligations provided in the covered agreements.

WTO members have jealously guarded their rights and have not hesitated to criticise the Appellate Body anytime that they feel that it has strayed from its terms of reference and adopted an interpretation which would upset the balance of rights and obligations carefully crafted during the Uruguay Round. In *EC-Asbestos*, where the Appellate Body broadly interpreted Article 13 of the DSU relating to its right to receive unsolicited *amicus curiae* briefs, WTO members convened a special meeting of the General Council to discuss what they saw as judicial activism on the part of the Appellate Body. The representative of Turkey noted that:

> "The DSU did not empower the Appellate Body to decide on such a crucial issue ... [T]he Appellate Body should have foreseen to a certain extent the reactions its decision would provoke. Article 13 of the DSU did not give a discretionary power to the Appellate Body. The absence of rules concerning *amicus* briefs did not give a free hand to the Appellate Body but showed the limits of its authority as well as the limits of the system. The Appellate Body should have informed members of the need for new rules instead of elaborating on them."[13]

Similar concerns about the additional procedure adopted by the Appellate Body to accept *amicus* briefs were expressed by other delegations, including Jamaica:

> "[Jamaica] was concerned that with its decision, the Appellate Body had expanded access and the rights of non-Members to the dispute settlement process and, by corollary, had diminished members' rights in this critical area of the WTO activities. The Appellate Body had taken this decision without any legislative mandate that could reasonably be construed as a basis to do so . . . The Uruguay Round Agreements were a delicate balance of rights and obligations, and the Appellate Body was a part of that balance. In carrying out its functions, the Appellate Body should act with full regard for legislative authority and for the substantive and procedural rights of members".[14]

[13] WT/GC/M/60; 23 January 2001, para. 79, p.20. See further the *United States – Final Dumping Determination on Softwood Lumber from Canada: Recourse to Article 21.5 of the DSU by Canada*, where the United States expressed serious concerns and disappointment with the reasoning of the Appellate Body in this case: WT/DSB/M/219; 6 October 2006, paras 65-77 at pp 17-20. See also United States criticism of the Appellate Body's report in the case on *United States – Laws, Regulations and Methodology for calculating Dumping Margins*, WT/DS294.

[14] WT/GC/M/60; 23 January 2001, para. 89, p.23.

In *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products: Recourse to Article 21.5 of the DSU by New Zealand and the United States*,[15]some members expressed concern about the interpretation of Article 9.1(c) by the Appellate Body:

> "[T]here were several aspects of the analysis in the Appellate Body Report that ... should be of concern to other Members from a systemic standpoint. First, and most disturbing, was the new test that the Appellate Body had read into the text of the Agreement on Agriculture for purposes of determining whether a 'payment' existed under Article 9.1(c) of that Agreement. The Appellate Body had stated that to determine whether a 'payment' existed, one had to compare the price of the good to the 'proper value' of the good, and for the Appellate Body, 'proper value' meant the cost of production of the good. Cost of production appeared nowhere in the text of the Agreement on Agriculture, nor was it clear why 'proper value', which itself was a term that did not appear in the Agreement on Agriculture equated to cost of production. There were several questions raised by the Appellate Body's reliance on the cost of production. Cost of production was not a general benchmark under the WTO. The Appellate Body had rejected the use of any market price as representing the proper value of a good. It was odd that the WTO would not consider the market as being a good indicator of the value of goods . . . There was nothing in the Agreement on Agriculture to suggest that Members had agreed that the cost of production for a private party, not even a government entity, would be relevant in determining whether another private party was receiving a 'payment' under Article 9.1(c) of the Agreement on Agriculture. Just as a practical matter, it struck the United States as a particularly unworkable standard given that most Members would not have access to a private party's cost of production data."[16]

These cases prove that WTO members fearlessly defend their rights and obligations and that the Appellate Body has little room to manoeuvre. Indeed, the Appellate Body itself has alluded to the fact that its functions are circumscribed and it does not have the authority to make law. In *United States – Wool Shirts and Blouses*, the Appellate Body held that:

> "Given the explicit aim of dispute settlement that permeates the *DSU*, we do not consider that Article 3.2 of the *DSU* is meant to encourage either panels or the Appellate Body to 'make law' by clarifying existing provisions of the *WTO Agreement* outside the context of resolving a particular dispute. A panel need only address those claims which must be addressed in order to resolve the matter in issue in the dispute".

It should also be borne in mind that the principle of *stare decisis* is not embedded in the DSU, meaning that panels do not necessarily have to follow the decisions of other panels or the Appellate Body in subsequent cases. The facts of cases may at times be similar, but there are bound to be some differences underscoring the need for each case to be decided on its own merits. While the arguments of the parties to the dispute and those of third parties might influence the thinking of panels and the Appellate Body on certain issues, ultimately it is the treaty language which is decisive. By focusing more on the market access issues and insisting on tight legal language to reflect the agreed rules and capture the concessions that would be traded

[15]WT/DS103/RW and WT/DS103/AB/RW; WT/DS113/RW and WT/DS113/AB/RW.
[16] WT/DSB/M/116; 31 January 2002, paras 33-34 at p.8.

among members, it could be said that the strategy of African countries is the appropriate one. Not only would it assist them to increase their exports and diversify their markets, but also in the event of disagreement, they are likely to prevail as panels and the Appellate Body would give effect to the ordinary meaning of the terms of the agreement reached by the members in accordance with the Vienna Convention on the Law of Treaties.

In summary, it cannot be disputed that it would be in the interests of African countries if they participated in the dispute settlement mechanism to enforce their rights and legitimate expectations, whenever necessary. However, there is no clear evidence to suggest that non-participation in the system in the past has been damaging to their trade interests. Arguably, some of their exports might have been impeded as a result of unauthorised barriers, but the greater majority of African exports enter their major markets unhindered. The greatest obstacle to the integration of African countries in the multilateral trading system is the existence of numerous supply-side constraints which have prevented them from increasing and diversifying their exports to take advantage of the preferences under schemes such as the African Growth and Opportunity Act (AGOA) and the Cotonou Agreement. In that regard, African countries need to adopt consistent policies which would ensure micro and macro-economic stability and pave the way for sustainable growth and development. The international community must be supportive by increasing aid for trade and improving access for products of export interest to African countries.

African countries realise the importance of the dispute settlement system, hence the submission of detailed proposals to the Special Session of the Dispute Settlement Body to facilitate greater access and ensure the reaping of tangible benefits from the system. To achieve this objective in the medium to long term, it would be advisable for African countries to participate as third parties as often as possible in many disputes so as to become acquainted with the rules and procedures both at the panel and the Appellate Body stages.[17] Since joining the WTO in December 2001, China has participated in almost every case as a third party with a view to building its capacity in WTO dispute settlement. The European Communities and the United States as a matter of routine participate in all cases not directly involving them as third parties.

3. Proposals of Systemic Importance and those Relating to the Pre-Panel Phase

3.1 Issues of Systemic Importance

It is the proposal of African countries that where there is a conflict between provisions of any covered Agreement or between any covered Agreements, "the panel or Appellate Body shall refer the matter to the General Council for a determination. In reaching the determination, the General Council may exercise the authority conferred on it under paragraph 2 of Article IX of the WTO Agreement". This proposal was discussed in the Special Session, but it failed to attract broad support among the membership. Among the concerns expressed were that it

[17]It should be noted that participating as a third party could also be expensive if the Member chooses to engage private counsel in the proceedings. However, the costs should generally be less than participating as complainants or respondents, especially where the third party only addresses issues of direct relevance to it.

would lengthen the process and also put panels and the Appellate Body in a straitjacket, as they could not apply established conflict rules to resolve disputes. In the past, panels and the Appellate Body have been able to resolve such situations of conflict without referring the matter to the General Council. They have adopted an approach that had permitted them to interpret the provisions in a harmonious manner. In *Korea – Dairy*, the Appellate Body observed that:

> In light of the interpretive principle of effectiveness, it is the *duty* of any treaty interpreter to "read all applicable provisions of a treaty in a way that gives meaning to *all* of them, harmoniously". An important corollary of this principle is that a treaty should be interpreted as a whole, and, in particular, its sections and parts should be read as a whole. Article II:2 of the *WTO Agreement* expressly manifests the intention of the Uruguay Round negotiators that the provisions of the *WTO Agreement* and the Multilateral Trade Agreements included in its Annexes 1, 2 and 3 must be read as a whole.

There was the concern that the adoption of this proposal would politicise the dispute settlement process and create unnecessary tensions. Under Article IX:2 of the WTO Agreement, the General Council can adopt authoritative interpretations by a three-fourths majority. This opens up the possibility that the majority can push through an interpretation which is at odds with the treaty language. Panels and the Appellate Body might find it difficult to apply the majority's interpretation if it were not in sync with their overall reasoning in the case. In light of these objections, the African Group's proposal was not reflected in the Chairman's proposal of 28 May 2003.

3.2 Consultations Phase

The basic issue is whether the consultations phase should be strengthened. Some WTO members seem to be of the view that countries use the consultations phase to drag out the process and that there is usually no commitment to genuinely engage in good faith to resolve the dispute. This view is countered by those who believe that consultations play an indispensable role in the process and saves not only time but resources of the WTO and the parties engaged in the dispute. At the DSB meeting on 20 June 2005, the representative of Chile informed the DSB that it was withdrawing its consultations request in the case on *European Communities -- Definitive Safeguard Measure on Salmon*, following the decision by the European Communities to remove the safeguard measures. She said that this case demonstrated that it was not always necessary for cases to go to the panel stage. African countries tend to share this view given their lack of expertise and inadequate financial resources to go through all the phases of the dispute settlement system. They have therefore advocated for a strengthening of the consultations provisions in the DSU.

3.2.1 Request to be Joined in Consultations

African countries have proposed an amendment to the DSU, so that requests by least-developed and developing countries to participate in consultations would always be accommodated. Under the current rules, members do not have an automatic right to participate in consultations, especially when they were requested under Article XXIII of the GATT 1994. While countries can easily join in consultations requested under Article XXII of the GATT 1994, they need to make their request within 10 days after the date of the circulation of the request and demonstrate that they have a "substantial trade interest" in the case. A number of countries have had their requests to participate in consultations rejected either because their request was not made within the stipulated 10 days or they could not demonstrate that they had a "substantial trade interest" in the case.

There is the view among developing countries that the DSU is quite vague and gives too much discretion to the responding member to decide whether or not a country has a "substantial trade interest". The DSU does not define the term "substantial trade interest" leaving it to countries to apply their own criteria. It has also been said that the Article is not consistent as it refers both to "substantial trade interest" and "substantial interest". It is not known if the terms are interchangeable, and if they are not, how each should be interpreted. Under GATT practice in the market access area, a country would be considered as having a "substantial interest" in a product if its market share constituted 10 per cent or more of total trade. It is not clear if this benchmark has any relevance as far as the test under Article 4.11 of the DSU is concerned. While Article 4.11 recognises the right of a country whose request to join in the consultations has been refused to request new consultations in respect of a matter, it has hardly been made use of by developing countries, including African countries for a number of reasons, such as the lack of resources and expertise. Participating in consultations with other countries gives developing countries an opportunity to build capacity and know first-hand how the system operates.

The main reason given by countries which oppose an automatic right to be joined in consultations is that it would lengthen the process, especially where there are many interested countries and also diminish the ability of the parties to reach mutually agreed solutions. They stress that the purpose of the WTO dispute settlement system is to settle a dispute between the disputing parties and that while the interests of other countries may be important, they are not sufficient to supplant the primary objective of the system. There can be no doubt that African and other developing countries would greatly benefit from flexible rules in this area. The challenge therefore seems to be how to find an appropriate balance between the interests of developing countries and that of the parties to the dispute. It should be pointed out that the Chairman's text virtually maintained the status quo; countries wishing to be joined in consultations would need to demonstrate that they have a "substantial trade interest" in the matter. In a recent proposal, Argentina, Brazil, Canada, India, Mexico, New Zealand and Norway have proposed an "all or nothing" approach, under which the responding member could choose either to reject or accept all requests to be joined in the consultations under Article XXII of the GATT 1994.[18]

[18] TN/DS/M/23; 26 May 2005, paras 2-3 at pp 1-2.

3.2.2 Time-frame for Consultations

Although this issue was not directly addressed by the African Group, it would appear that they are in support of maintaining the current time-frame, which allows the parties to consult for 60 days, after which a request for the establishment of a panel could be made assuming that the consultations fail to settle the dispute between them. Some developed countries want the time-frame to be reduced to 30 days. They argue that 30 days are enough if the parties are really interested in finding a solution to their dispute. The view of several developing countries is that given their lack of financial and human resources, they need a longer time-frame to engage in fruitful consultations.

3.2.3 Demonstration that the Special Interests of Developing Countries have been Taken into Account

The proposal by the African Group to the Committee on Trade and Development provides that:

> "In the proceedings developed-country Members shall present evidence of, and in the written decisions, the panels and the Appellate Body shall indicate, how special attention has been given to particular problems and interests of developing country Members during the stage of consultations".[19]

This proposal in effect combines the language of Articles 4.10 and 12.11 of the DSU. The concern of African and other developing countries is that the present language in Article 4.10 is very weak. It uses the word "should" instead of "shall", thus imposing no legal obligation on developed countries to give special attention to the particular problems and interests of developing-country members. The Chairman's text proposes a tightening up of the language in the article by replacing "should" with "shall". This proposal was not received enthusiastically by other developing countries, who pointed out that what was needed was rather operationalisation of the Article in terms of establishing detailed procedures which have to be followed by developed-country members. It was not enough for a developed country to merely assert that it had taken into account the interests of the developing-country member, and later decide to pursue the case by requesting the establishment of a panel to examine the consistency of the measures of the developing-country member with a covered agreement. It is the expectation of African countries that this proposal would oblige developed countries to engage in good faith consultations with them, instead of treating consultations as a mere perfunctory exercise.

3.2.4 Measures Withdrawn before, or in the course, of Consultations

African countries are proposing that Article 3.6 of the DSU should be amended by re-numbering the current provision as paragraph (a) and adding the following paragraphs:

[19] TN/CTD/W/3/Rev.2; 17 July 2002.

> (b) Developed-country members that adopt measures against developing or least-developed country members and withdraw them in the course of consultations or 90 days before the commencement of consultations pursuant to Article 4 of this Understanding shall notify them individually or jointly to the DSB within 60 days of their withdrawal. The notification shall describe the measure and the reason or circumstances for the withdrawal, state whether consultations were held and finalised, and indicate the amount of injury to the developing or least-developed country member resulting from the measure. Disputes over the amount of injury may be referred to arbitration under Article 25 of this Understanding.
>
> (c) Where injury has resulted from the withdrawn measure, and if the developing or least developed-country member so requests, the DSB may recommend monetary and any other appropriate compensation taking into account the nature of injury suffered. The level of compensation shall be determined by arbitration in accordance with Article 25 of this Understanding and shall be implemented *mutatis mutandis* in accordance with Articles 21 and 22.
>
> (d) The requests referred to in paragraph (c) may be made at the meeting of the DSB considering the notification of the withdrawn measures or subsequently within a period of 60 days, unless there are exceptional circumstances justifying the consideration of the request at a later date.

The underlying reason for this proposal seems to be that African and other developing countries should not suffer any damage as a result of inconsistent measures adopted by a developed-country member, which are later withdrawn either before the commencement or during consultations between the parties. For African countries which do not have competitive industries, the mere imposition of trade-restrictive measures could have devastating consequences on the industry affected. Depending on the length of time the measures are implemented, some industries may not survive. Thus, the mere withdrawal of the measures might not be enough. It is in this sense that African countries are seeking retroactive compensation. It should be noted that Mexico has made a similar proposal.

When this proposal was discussed in the Special Session, it received very little support. While some members were sympathetic to the underlying reasons behind this proposal, others thought that it would introduce a very fundamental change to the way the DSU has operated since its inception. For these countries, the mandate of the Special Session was restricted to making improvements and clarifications and that the proposed amendment by African countries was clearly not within the ambit of the mandate. Apart from this philosophical debate, the proposal may raise some practical problems. First, it would be difficult to convince some developing countries that the proposal should be applicable only when the responding member is a developed country. A country whose industry has suffered irreparable damage would prefer to be compensated by the country which has adopted the WTO-inconsistent irrespective of its status as a developed or a developing country. Exempting developing countries from the application of this measure would send a bad signal that it is okay for developing countries to adopt trade-restrictive measures against each other. The increasing number of disputes between developing countries suggests that such a decision would be at odds with the current thinking and practice of several developing countries.

Second, it is difficult to understand why the parties should make an elaborate notification to the DSB when the measure is withdrawn before consultations under the DSU take place. Third, unless a joint notification was made by both parties, it would be difficult to expect the developed-country member to acknowledge in its notification that the measure it adopted was in violation of its WTO obligations and that it had caused injury to a developing-country member. Fourth, the level of compensation need not be determined by arbitration. While arbitration could be resorted to when the parties are in disagreement as to the amount of level of nullification and impairment, compensation in WTO law is always voluntary and a party could not be mandated to provide compensation.

4. Proposals Relating to the Panel and Appellate Body Phase

4.1 Development Perspective in the Terms of Reference of Panels

African countries are proposing that Article 7 of the DSU concerning the terms of reference of panels should be amended by adding paragraphs 4 and 5 as follows:

> 4. Where a developing or least-developed country member is a party to any dispute under this Understanding, the panels, in consultation with relevant development institutions where necessary, shall consider and make specific findings on the development implications of the issues raised in the dispute and shall specifically consider any adverse impact that findings may have on the social and economic welfare of the developing or least-developed country member. The DSB shall fully take those findings into account in making its recommendations and rulings.
>
> 5. This Understanding is an important mechanism for achieving the development objectives of the WTO Agreement. Accordingly, the findings of the panels and the Appellate Body, and the recommendations and rulings of the DSB shall fully take into account the development needs of developing and least-developed country members. The General Council shall review this Understanding every five years in order to consider and adopt appropriate improvements to ensure the achievement of the development objectives of the WTO Agreement.

This proposal received very little support when it was discussed in the Special Session and was not reflected in the Chairman's text. A number of concerns were raised by members. There was the view that it would hamper the work of panels and delay the dispute settlement process. It was also stated this proposal would divert panelists from their primary function which was to settle trade disputes in accordance with the agreements reached by WTO members. By virtue of their background, several panelists may not be well-equipped to undertake such socio-economic analyses. There was the fear that involvement of institutions such as UNCTAD, UNDP and ILO would politicise the dispute settlement process and undermine its rules-based nature much to the detriment of all members.

While the International Monetary Fund has a role to play in Article XV of the GATT 1994 in relation to balance of payments, what is being proposed by African countries goes further than

that. If carried to its logical conclusion, this proposal would oblige panels, for example, to ignore WTO rules when it is adjudged by the relevant development institutions that the withdrawal of an inconsistent WTO measure by a developing country member would harm its country's socio-economic interests. Such a ruling would not inspire confidence in the dispute settlement system and would compromise its role as a central element in guaranteeing security and predictability to the multilateral trading system.

4.2 Third Parties

4.2.1 Definition of 'Substantial Interest'

As previously noted, the DSU does not define the term "substantial interest" nor does it provide useful guidance on how it may be interpreted. As a result of this omission, countries apply different criteria, with some insisting on a higher threshold. Some countries insist on countries having at least a 10 per cent market share in accordance with GATT practice. For African countries, a higher threshold would not be in their interest given the fact that their share in most products in their major markets are below five per cent. It is against this background that African countries have proposed the following definition to be added to the existing paragraph 2 of Article 10 of the DSU:

> "For purposes of developing and least-developed country Members, the term 'substantial interest' shall be interpreted to include, any amount of international trade; trade impact on major domestic macro-economic indicators such as employment, national income, and foreign exchange reserves; the gaining of expertise in the procedural, substantive, and systemic issues relating to this Understanding; and protecting long-term development interests that any measures inconsistent with covered agreements and any findings, recommendations and rulings could affect".

This proposed definition was rejected by the major trading partners who thought that it would make the participation of all developing countries automatic regardless of whether or not they have a substantial interest in the matter. The apprehension is that if you have too many countries participating as third parties, it could lengthen the dispute settlement process and also make it difficult for the parties to explore the possibility of reaching a mutually agreed solution. The Chairman's text leans in favour of requesting countries seeking third party rights to have a substantial interest in the case. From a practical point of view, it is doubtful if this proposal would substantially change the current practice. Member countries that request third party rights at the DSB meeting at which a panel is established are automatically granted third party rights, so are those that communicate interest within 10 days of the establishment of the panel.

4.2.2 Access to Meetings and Documentation

The African Group proposes that paragraph 3 of Article 10 of the DSU should be replaced with the following language:

> "Third parties shall receive all the documentation relating to the dispute from the parties, other third parties, and the panel without prejudice to the provisions of paragraph 2 of Article 18.

> Third parties, if they request, shall have a right to attend the proceedings and to be availed the opportunity to put written and oral questions to the parties and other third parties during the proceedings."

In the discussions in the Special Session, there was a broad consensus on the need to enhance the third-party rights, particularly in terms of improving access to meetings and documentation. The Chairman's text reflects the views of members on this issue by providing that third parties shall be entitled to receive all submissions of the parties and of other third parties, except those portions containing privileged information, up until the issuance of the interim report to the parties. The submissions of third parties shall be made available to the parties, other third parties and the panel, and they shall be entitled to attend all substantive meetings of the panel with the parties preceding the issuance of the interim report, except those meetings or portions thereof, where privileged information would be discussed. The text further provides that third parties shall have the opportunity to be heard by the panel and their submissions shall be reflected in the panel report. They shall be entitled to receive the descriptive part of the report containing their arguments and be able to provide comments within the period specified by the panel. In some respects, the Chairman's text goes further than the proposal by the African Group. A recent proposal by the group of seven countries also recommended an enhancement of third party along the lines in the Chairman's text.[20]

4.2.3 Third Participants in Appellate Body proceedings

The proposal by the African Group advocates the replacement of Article 17.4 with the following language:

> "The parties to the dispute may appeal a panel report. Third parties in the panel proceedings, if they request, shall have a right to attend the proceedings and have an opportunity to be heard and to make written submissions to the Appellate Body. Their submissions shall also be given to the parties to the dispute and shall be reflected in the Appellate Body report."

The language in the Chairman's text does not differ significantly from the proposal by the African Group. Under the Chairman's text, it is stated explicitly that third parties which had notified the DSB of their substantial interest in a matter pursuant to Article 10.2 of the DSU "shall have an opportunity to be heard and make written submissions to the Appellate Body". The text goes further in proposing that a member country which had not notified its substantial interest in a matter pursuant to Article 10.2, but had subsequently notified the DSB and the Appellate Body of its substantial interest in a matter within 10 days of the filing of a notice of appeal, shall also have an opportunity to be heard and to make written submissions to the Appellate Body.

While this proposal was supported by a significant number of developing countries, including African countries, the view was expressed that it could delay the proceedings at the Appellate level, especially where there were many members interested in participating in the proceedings. The argument was made that the primary function of the dispute settlement system was to

[20] TN/DS/M/23; 26 May 2005, para. 4 at p.2.

resolve disputes between the parties in a prompt and satisfactory manner. The counter-argument advanced was that some members may only become aware of the systemic implications of a case after the panel report had been circulated and that it would be unfair to exclude them from the process when their interests would be affected. Given the wide differences in the views of members, consensus could not be reached on the Chairman's proposal. In their recent proposal, the group of seven countries expressed support for the Chairman's proposal, *albeit* indirectly by urging that member countries which did not participate as third parties in the panel proceedings should be allowed to participate as third parties at the appellate stage:

> "Given the systemic interest in issues considered at the appellate stage and the interest of members to make their views known, there was no valid reason for denying them that opportunity. Additionally, amending Article 17.4 of the DSU to incorporate the right of members to join as third parties at the appeal stage would allow Members with limited resources to participate in the process. They would not have to participate in the panel proceedings before they could be allowed to participate in the appellate proceedings".[21]

This proposal has two key advantages for African countries. First, it would help build and strengthen the capacity of African countries in this highly complex area. Having the opportunity to participate as third parties in both panel and Appellate Body proceedings would let them know first-hand how the system works. The experience that would be acquired would become very handy, once African countries start participating actively in the dispute settlement system

4.3 Composition of Panels

The African Group and the LDC Group have proposed that in disputes involving a developing country or a least-developed country, one of the panelists should come from a developing country or a least-developed country, as the case may be. The reason behind this proposal seems to be that a panelist from a developing country or a least-developed country is likely to show greater appreciation of the prevailing conditions in the developing or least-developed country and the arguments presented to the Panel than a panelist from a developed country. The other argument is that the selection of panelists from developing countries helps to build and strengthen their capacity to participate more effectively in the dispute settlement system.

While it may be true that panelists from developing countries are likely to show greater appreciation of the prevailing conditions in the developing or least-developed country and the arguments presented by it to the Panel than one from a developed country, it is doubtful if this would influence the eventual outcome. The rules of the WTO cannot be ignored to give a favourable decision to the developing-country member. The interests of developing countries would be better guaranteed under the relevant WTO Agreements rather than under the DSU. If there is a mandatory special and differential treatment provision in a WTO Agreement, the Panel or the Appellate Body would have no option but to take due account of it regardless of where the panelists come from.

[21] *Ibid*, para. 5 at pp 2-3.

Furthermore, the argument that panelists from developing countries help build and strengthen the capacity of developing countries in WTO dispute settlement is not entirely persuasive. Several of the panelists who have been appointed from developing countries do not have any government affiliation and as such it is difficult to see in which way they could be said to be contributing to the building and strengthening of a country's capacity to participate in the dispute settlement system. Some credence could be given to this argument if the panelists were later to advise their governments. Furthermore, there seems to be a pattern of selecting panelists from a few developing countries. In the case of Africa, most of the panelists have come from either Egypt or South Africa. Thus, it is inaccurate to argue that these panelists are helping to build the capacity of African countries. In any event, what African countries need is sustained training and continued exposure for them to build capacity in this area.

The African Group has not expressed any definite views on the proposal by the EC for a system of permanent panelists. Africa's interests could be safeguarded under the proposed system if the method of selection of the panelists is as transparent as the method for selecting Appellate Body members. Depending on the total number of panelists who will be appointed, the different regions of Africa could each have a representative.

4.4 Scope of Article 13 of the DSU

African countries propose that Article 13 of the DSU should be amended by adding the following as paragraph 3:

> 3. "For purposes of this Article, 'the right to seek information and technical advice' shall not be construed as a requirement to receive unsolicited information or technical advice."

It is clear from the formulation that African countries want Panels and the Appellate Body to give a very narrow interpretation of Article 13 of the DSU. Put in another way, they want the judicial bodies to exercise restraint and reverse their earlier rulings permitting NGOs, IGOs and other bodies to submit *amicus curiae* briefs. The discussion of this issue was polarised in the Special Session with a significant number of developing countries criticising Panels and the Appellate Body for exceeding their authority and adopting a very flexible interpretation of this article. This view was not shared by developed countries which seemed to be of the view that it was within the rights of Panels and the Appellate Body to make such determinations. If the discussions in the Special Session offer a clue, it would be difficult for consensus to be achieved on this proposal. It should be mentioned that India and a group of other developing countries have tabled a similar proposal.

4.5 Separate Opinions of Panelists and Appellate Body Members

The African Group has proposed that panelists and members of the Appellate Body should each deliver a separate opinion, unless they are in agreement. With this in view, the group has called for the replacement of Articles14.3 and 17.11 with the following language:

> "[Each panelist [Appellate Body member] shall deliver a fully reasoned, separate written opinion stating clearly the party which has prevailed in the dispute. Where two or more [panelists] [members] are in agreement, they may decide to provide a joint opinion. The majority opinion shall be the decision of the [panel] [Appellate Body].]"

This proposal was strongly opposed by several members in the Special Session. They argued that it would undermine the authority of the Appellate Body and the collegiality which currently exists among its members enabling them to work together effectively and efficiently. The argument is also made that it is necessary to preserve the anonymity of panelists and Appellate Body members. A further reason is that under the current rules and procedures, it is possible for a panelist or an Appellate Body member to write a separate opinion and that no purpose would be served by specifying this in the DSU. It is recalled that in the recent *EU-GSP* case, one panelist wrote a separate opinion on one of the issues under consideration.

It is the view of African countries that while it is true that under the current system, it is possible for a panelist or a member of the Appellate Body to write a separate opinion, the whole system is structured in such a way as to discourage the issuance of separate opinions. African countries do not share the view that separate opinions would undermine the credibility of the dispute settlement system. Insofar as the decisions are well-reasoned, they could actually enhance the credibility of panels and the Appellate Body.

5. The Implementation Phase

5.1 Development Perspective in the Implementation of Recommendations and Rulings

The African Group has proposed that Article 21.2 of the DSU should be amended by adding the following:

> "In this regard, notwithstanding any finding of inconsistency of measures with a covered agreement, the DSB, if requested by the developing-country Member and fully taking into account the findings of the panel or Appellate Body, as well as the reports of relevant development institutions where appropriate, on the development implications of the issues raised in the dispute, may recommend arbitration in accordance with Article 25 for purposes of drawing up an adjustment programme under which the developing-country Member will gradually implement the recommendations and rulings."

This proposal failed to attract broad support when it was discussed in the Special Session. The view was expressed that it would undermine security and predictability, as its sole objective is to delay the implementation of the recommendations and rulings of the DSB. It should be noted that in determining the reasonable period of time for the implementation of the DSB's recommendations and rulings, arbitrators have in the past taken into account the special situation of developing countries. In *Indonesia - Autos*, the arbitrator, for example, noted that:

> "Indonesia is not only a developing country, it is a developing country that is currently in dire economic and financial situation. Indonesia itself states that its economy is 'near collapse'. In these very peculiar circumstances, I consider it appropriate to give full weight to matters

> affecting the interests of Indonesia as a developing country pursuant to the provisions of Article 21.2 of the DSU. I, therefore, conclude that an additional period of six months over and above the six-month period required for the completion of Indonesia's domestic rule making process constitutes a reasonable period of time for implementation of the recommendations and rulings of the DSB in this case."[22]

5.2 Monetary Compensation and Computation of Injury

The African Group has proposed the amendment of Article 21.8 of the DSU by adding the following:

> "Further, if the case is one brought by a developing-country Member against a developed-country member, the DSB may recommend monetary and other appropriate compensation taking into account the injury suffered. The quantification of injury and compensation shall be computed as from the date of the adoption of the measure found to be inconsistent with covered agreements until the date of its withdrawal."

This proposal did not attract broad support when it was discussed in the Special Session. A number of countries were concerned that it would fundamentally alter the way the DSU operates by introducing retroactivity into the system. There was also some uneasiness about introducing monetary compensation into the system. It must be pointed out that while compensation has predominantly taken the form of reducing barriers on products of export interest to the prevailing Member, there was at least in one case (US – Copyright), where the parties agreed on a financial package. It should be noted that the facts of this case were quite unique and it should not be taken as a precedent for future cases.

In the GATT/WTO, compensation has always been voluntary and it can be expected that the greater majority of members would like it to remain that way. Operationally, it would be difficult for the DSB to come to a consensus decision on this issue, assuming the principle was accepted by members. It is likely that some members would question why injury and compensation should be calculated from the date of the adoption of the measure and not the date of the establishment of the Panel or the date of the adoption of the panel report. If injury and compensation were to be calculated from the date of the adoption of the measure, it could lead to "unjust enrichment", especially where there was no trade to the responding member prior to the initiation of the action or if exports only commenced some years after the introduction of the measure.

5.3 Collective Enforcement of Recommendations and Rulings

The African Group has proposed that Article 22.6 of the DSU should be amended by renaming the current provision as paragraph (a) and adding the following paragraphs (b), (c) and (d) to it:

> (b) "The following principles and procedures shall apply to requests for collective suspension of concessions under paragraph (c):

[22] *Indonesia – Certain Measures Affecting the Automobile Industry*, Award of the Arbitrator, WT/DS54/15, para. 24 at p10.

> (i) Before making such a request, the developing or least-developed country Member shall refer the matter to arbitration for determination of the level of nullification and impairment, which shall be done taking into account the legitimate expectations of the developing or least-developed country Member. The arbitration shall further take into account any impediment to the attainment of the development objectives of the WTO Agreement as further elaborated by the developing or least-developed country Member.
>
> (ii) The arbitration shall consider whether suspension of concessions or other obligations in other sectors by the developing or least-developed country Member would be appropriate to effectively encourage the withdrawal of the measure found to be inconsistent with a covered Agreement, taking into account possible effects on that developing or least-developed country Member.
>
> (iii) Where the DSB grants authorization to Members to suspend concessions or other obligations under paragraph (c), the level of suspension for each Member authorized shall be such as to secure, full compensation for the injury to the developing or least-developed country Member, the protection of its development interests, and the timely and effective implementation of the recommendations and rulings.
>
> (c) Where the case is one brought by a developing or least-developed country Member against a developed-country Member and the situation described in paragraph 2 occurs, and in order to promote the timely and effective implementation of recommendations and rulings, the DSB, upon request, shall grant authorisation to the developing or least-developed country Member and any other Members to suspend concessions or other obligations within 30 days.
>
> (d) The DSB shall review the operation of paragraph 6 of this Article not later than five years after its implementation with a view to ensuring its effectiveness and in this regard may adopt appropriate measures and amendments to this Understanding.

This proposal failed to attract broad support when it was discussed in the Special Session. The view was expressed that it would fundamentally alter the DSU in several respects. It was pointed out in that connection that the primary function of the dispute settlement system was to settle disputes between the disputing members. While other members may have a systemic interest in a particular case, they should not have the right to take action reserved exclusively for the parties to the dispute. This point was stressed by Poland during the discussion on the Mexican proposal under which members would be able to negotiate their right to suspend concessions and other obligations to other members:

> "The introduction of this concept to the DSU would be an unfortunate development for at least three reasons. First, it would undermine one of the basic tenets of the dispute settlement system and the multilateral trading system, which was that the rights of Members should be protected under multilateral surveillance and that it was up to each and every Member to ensure that its rights and legitimate expectations were not being impaired or nullified. Second, if Members were able to negotiate away the remedies that they were entitled to, it might discourage parties from negotiating seriously to find mutually agreed solutions to their disputes, which was also one of the

> objectives of the dispute settlement system. Third, it would diminish transparency of the system, as the surveillance powers of the DSB would be severely compromised."

It is a cardinal principle of WTO law that suspension of concessions must be equivalent to the level of nullification and impairment. It follows that if collective retaliation is to be accepted, it would deprive this principle of its practical significance. From the viewpoint of African and other small and weak developing countries, retaliation has to be massive and disproportional to the level of nullification and impairment if it is to be effective and induce compliance. The underlying reasons of the African proposal are twofold. The first is to bring maximum pressure on the developed country member to implement as rapidly as possible the recommendations and rulings of the DSB. The second is an attempt to deal with the incapacity of most developing countries to retaliate. It would be recalled that in the *Bananas* case, Ecuador chose not to retaliate against the European Union, although it had been given authorisation by the DSB. It realised that retaliatory action would be ineffective in terms of compelling the European Union to implement the recommendations and rulings of the DSB and that it would also harm its own economy. While a number of members were sympathetic to these reasons, they still thought that this proposal was too "revolutionary" and impracticable to implement.

5.3 Responsibilities of the Secretariat

5.3.1 Disclosure of Information to Developing Country Members

The African Group has proposed that Article 27.1 of the DSU should be amended by adding the following:

> "The Secretariat shall provide all relevant legal, historical and procedural research and other material relating to a dispute to the developing and least-developed country Members that are parties or third parties in the dispute. The material shall cover the specific rights and obligations relating to the particular issues raised in the dispute."

This proposal failed to attract broad support when it was discussed in the Special Session explaining its omission from the Chairman's text. The view was expressed that it would not be appropriate for the Secretariat to hand over confidential documents pertaining to the case to a party to the dispute.

5.3.2 Legal Assistance in Dispute Settlement

The African Group has proposed that Article 27.2 of the DSU should be amended by adding the following:

> "The Secretariat shall maintain a geographically balanced roster of legal experts from which developing and least-developed country Members may select experts to assist them in dispute settlement proceedings. Notwithstanding the reference to impartiality in the provision of legal and other services by the Secretariat, the legal expert shall fully discharge the functions of counsel to the developing or least-developed country Member party to a dispute."

A number of countries were supportive of this proposal when it was discussed in the Special Session. The Chairman's text partially reflects this proposal. The view was expressed that with the establishment of the Advisory Centre on WTO, it was not necessary to pursue further this proposal. While it is true that the Advisory Centre has filled a vacuum, it still charges for the services that it renders to developing-country members depending on their state of economic development and ability to pay. African and other developing countries want to have the legal services rendered at no cost. Should donor countries increase funding for the Centre to enable it to provide its services at no cost to African countries, there may not be enough grounds to pursue this proposal. Until that is done, African countries should keep this proposal on the table.

5.3.3 WTO Fund on Dispute Settlement

The African Group has proposed the introduction of a new Article 28 in the DSU:

1. "There shall be a fund on dispute settlement to facilitate the effective utilisation by developing and least-developed country Members of this Understanding in the settlement of disputes arising from the covered agreements.

2. The fund established under paragraph 1 of this Article shall be financed from the regular WTO budget. However, to ensure its adequacy, the fund may additionally be funded from extra-budgetary sources, which may include voluntary contributions from Members.

3. The General Council shall annually review the adequacy and utilisation of the fund with a view to improving its effectiveness and in this regard may adopt appropriate measures and amendments to this Understanding."

Varying degrees of support were expressed for this proposal when it was discussed in the Special Session. The Chairman's text partially reflects this proposal. Some concerns were expressed on the funding coming out of the regular budget of the WTO. It is likely that the developed-country members would like to limit access to this fund, assuming there is a consensus to establish it. They would like the beneficiaries to be least-developed countries and other poor developing countries. There would be the reluctance to fund the legal challenges of advanced developing countries, which have the human and financial resources to participate actively in the system.

6. Concluding Remarks

The active participation of African countries in the negotiations for the reform of the Dispute Settlement Understanding is to be welcomed given the central role played by the system in guaranteeing security and predictability in the multilateral trading system. With a new determination to become active users of the system, it is hoped that African countries would be able to promote and safeguard their interests and legitimate expectations. While some of the proposals of the African Group would strengthen the dispute settlement system in terms of

improving access and the remedies, their adoption would not necessarily lead to increased use of the system by African countries.

Effective participation in the dispute settlement system would require African countries in the medium to long term to put in place measures which would strengthen the collaboration between industry and government. It would be helpful to have a dedicated office for trade complaints staffed with qualified people. The office should be non-partisan and should investigate complaints lodged by exporters. Given capacity constraints, African countries could consider pulling their resources together as they have done in the context of the DDA negotiations and establish a joint office to handle their trade disputes with other countries. An optimal result in the long term, however, would be for each country to develop its own capacity given the increasing trade frictions among African countries.

As an interim measure, it would be advisable for African countries to participate as third parties in as many cases as possible and use the services of the Advisory Centre on WTO Law and other international law firms which are willing to take cases on a *pro bono* basis or at discounted rates.

While greater use of the dispute settlement system by African countries should be encouraged, it is to be noted that the greatest obstacles to the integration of African countries in the multilateral trading system are supply-side constraints which have impeded their efforts to increase and diversify their exports. There is no evidence on record to demonstrate that the limited use of the dispute settlement system has been damaging to the export interests of African countries. In fact, the bulk of African exports enter their major markets unhindered under preferential conditions. Priorities for African countries in the DDA negotiations appear to be the safeguarding of these preferences and the securing of enhanced market access generally for products of export interest to them. They appear to have taken the view that it would be more productive to expend their limited resources on getting cast-iron commitments in their favour rather than litigating on past commitments which are sometimes couched in hortatory language. As African countries increase their share in world trade, it could be expected that they would resort to the dispute settlement system more frequently to protect their rights and legitimate expectations.

According to the World Bank[23], the economic outlook for Africa is improving with growth matching global rates. This indicates that at the present rate it is only a matter of time with sustained growth that African countries would start to take measures to safeguard their trade and developmental interests. African countries from the time of GATT have considered trade as an engine of economic growth, and it was this belief that made many African countries participate actively in the Uruguay Round negotiations. The countries view the multilateral trade negotiations as an essential tool in defining their priorities for trade policy and ultimately impact economic development. Their confidence in the multilateral trading system (MTS) is seen in their active participation in WTO negotiations and their commitment to further participation in multilateral trade negotiations. African countries believe that trade and investment is an engine of economic growth and sustainable development, which leads to the

[23] http://news.bbc.co.uk/2/hi/africa/7093912.stm

creation of jobs and improved standards of living. Trade and investment can also assist the efforts of governments in alleviating poverty.

However, for African countries to seize these opportunities would entail that they have a better understanding of their rights and obligations as WTO members. Since African countries do not have adequate human and financial resources, it would make it difficult to know when their rights have been infringed upon. Understanding WTO Law is a complex exercise, as the law consists of over 20 agreements covering about 20,000 pages. This calls for considerable investments in training African legal experts in WTO Law.

In light of this, we propose the setting up of an "African Centre on WTO Law" to train both public and private legal officers capable of competently handling legal issues. It is accepted that the establishment of the Advisory Centre on WTO Law in Geneva would to some extent alleviate the legal difficulties that African countries face, but the Advisory Centre is not able to provide the assistance needed in first identifying the legal issues when another country violates an agreement with consequences for African countries economic growth. It is this gap that the African Centre on WTO Law is expected to fill.

The functions of this Centre would be twofold: (i) to train African legal officers in both the public and private sectors; and (ii) to provide advice on WTO law and prepare legal opinions and support in dispute settlement proceedings at modest fees. The programme envisaged under the Centre is intended to contribute towards the long-term sustainable capacity building in WTO legal matters, and in so doing enhance the effectiveness of African countries to advance their respective national interests in the emerging multilateral framework.

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ASSESSMENT OF TRADE FACILITATION AND COMPETITIVENESS OF CAMEROON'S COFFEE SECTOR: IMPLICATIONS FOR TRADE LIBERALISATION

Ernest L. Molua[1]

1. Introduction

Changes in the agriculture and food sectors over the last ten years have been heavily influenced not only by world economic events but by both the global trade policy and domestic economic reforms. These have had serious impacts on African economies and on the response of the agricultural sector for agrarian economies such as Cameroon. Cameroon is a small developing country whose economy depends heavily on agricultural export commodities, the most important being coffee (Tambi, 1999; Nchare, 2007; World Bank, 2008). Coffee is a typical global good with a highly competitive market. In Cameroon, coffee revenue accounts for some 20 per cent of total export earnings, 10 per cent of agricultural GDP, and 2 per cent of national GDP. However, sustained fluctuations in export earnings have raised concern on the country's earnings, growth prospects and debt servicing.

Like most Sub-Saharan African economies (see McKay et al. 1999; and Milner and Morrissey, 1999), Cameroon's markets have suffered from inefficiencies in domestic production and trading systems, stemming from inappropriate government policies that inhibit competition and the exploitation of economies of scale. Following its independence in 1960, Cameroon followed an interventionist approach to development (Tambi, 1984). Prices, as well as the rate of exchange and the interest rate, were regulated, quantitative restrictions were imposed on trade, and private-sector activity was controlled. Government was directly involved in the provision of services such as marketing and in some cases were also producers, e.g. banana and oil palm cultivation. The Cameroon National Produce Marketing Board (NPMB) was created to overcome market disruption and price instability. Farmers were guaranteed outlets for their crops and given the opportunity to participate in the cash economy, with everyone being paid the same price for the same product irrespective of their location. Hostility to the private sector and adopted single-channel marketing made it easier for the government to collect export taxes.

Given the then structure of the economy, macro-economic imbalances ensued in the late 1980s and these negatively impacted on demand management, exchange rate, external financing and aggregate output levels. In the early 1990s Cameroon embarked on structural adjustment measures with the purpose of stimulating economic recovery, on the assumption that macroeconomic stability will enshrine economic stability, brought on by reduced internal budget deficits. Since 2000, GDP has grown on average by about 4 per cent a year. The new optimism on the state of Cameroon's economy is founded on the improved public finances. In 2004, receipts of US$ 2.5 billion accrued over expenses of US$ 2.3 billion. Despite the cautious

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optimism that Cameroon is emerging from its long period of economic hardship, the country still has a precarious trade balance with key trading partners such as Spain (recipient of 16 per cent of Cameroon's exports), Italy (14 per cent), France (10 per cent), UK (10 per cent), USA (11 per cent) and Netherlands (6 per cent). Export revenue of US$2.5 billion was realised in 2005, from an export basket that comprised principally: crude oil and petroleum products, lumber, cocoa beans, aluminium, coffee and cotton. Agriculture remains the backbone of the economy, with an average share in GDP and in total exports approximating 25 per cent and 60 per cent, respectively.

Given the foregoing review, some research questions that need to be answered include; does liberalisation facilitate trade? Is competitiveness of coffee trade affected by transport costs? The goal of this paper is to examine the significance of liberalisation in facilitating Cameroon's coffee trade. Specifically, the paper examines whether changes in coffee export prices, foreign exchange rate and transportation costs affect the volume of coffee exported from Cameroon. Reliable estimates of the determinants of coffee export earnings are essential for policy decisions to foster better living conditions of farm families and general welfare of the economy. This hinges on the premise that steps taken by Cameroon to lower trade barriers, including removing obstacles to trade, are critical to expanding product supply and trade. The removal of non-tariff barriers and lower trade costs are increasingly recognised as key factors that affect economic progress. Trade costs, which include international transportation costs, transaction costs, and distribution costs in countries of origin, destination, and transit, are an important barrier to trade. These costs can be more significant than tariffs and other trade policy barriers. Even in rich countries with regional trade arrangements where formal trade barriers are almost fully eliminated, trade costs still remain as strong barriers to exports and imports. In the next four sections of the paper, we review the coffee sector in Cameroon, the extent of trade liberalisation, the nature of trade facilitation and the impact of competitiveness on coffee export values.

2. Cameroon Coffee Sector

Cameroon boasts of advantageous natural conditions to produce export crops, amongst the staple market commodities of coffee, cocoa, rubber and palm oil. Coffee is grown in diverse agro-ecologies, making Cameroon an important player in global coffee production and trade. Cameroon's extensive volcanic soil, high altitude and bimodal rainfall promote the cultivation of Robusta coffee in all agro-ecologies except in the dry sahelian northern part of the country. Arabica coffee is mainly produced in the high altitudes of the savannah grassland of the west and northwest provinces. Production technology is simple and labour intensive, with berries harvested by hand. The farm plots are small, averaging about 5 hectares, with drying principally in the sun. Coffee features prominently in farm enterprise mix, as shade trees for food crops in agro-forestry plantations.

In 1961 total coffee production was 43000 metric tonnes rising steadily to more than 100,000 metric tonnes in 1974. Despite vagaries of weather in the 1982/83 season, 1984 witnessed the highest levels of production (138,000 metric tonnes). As shown in figure 1, declines then ensued from 1987, dropping to about 41,000 metric tonnes in 2002. Today, coffee production levels average 50,000 metric tonnes. A plethora of factors account for variations in coffee

production, these may include environmental constraints, production and marketing infrastructure, the agricultural policy environment, amongst others.

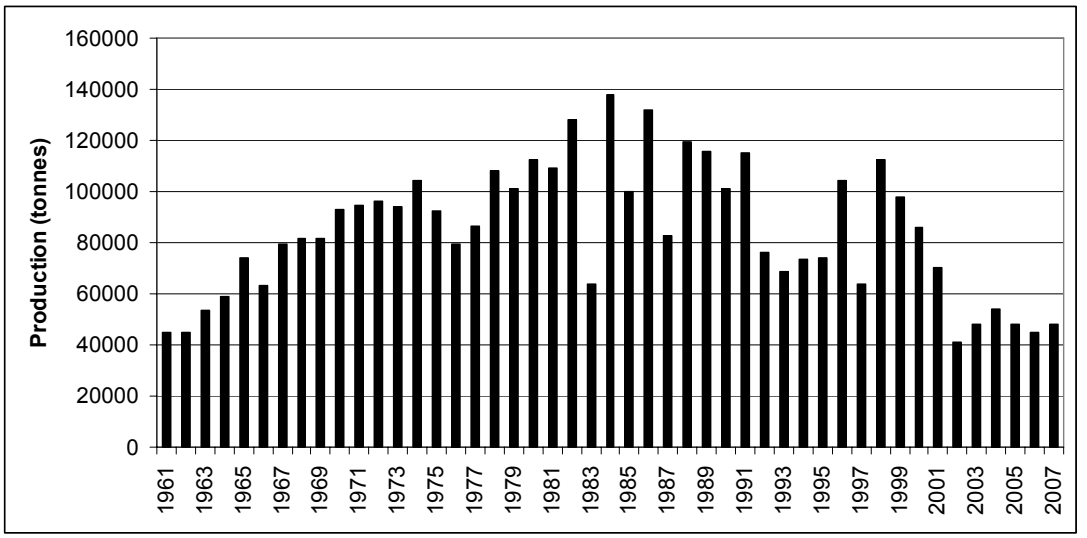

Fig. 1: Coffee Production in Cameroon, 1961 – 2007 (Data Source: FAOSTAT)

The output levels and the farm characteristics (Nchare, 2007) suggest that many growers may be vulnerable to price risks, possibly facing severe financial difficulties when coffee prices drop. Coffee crop is still economically important as the major income earner in subsistence agriculture, the income base for family welfare and as insurance for household income (Minagric, 2003). Coffee cultivation and trade fuels job creation along a producer and marketing chain, creating opportunities in threshing, warehousing, roasting, transporting, marketing, branding, quality control and advertising.

Cameroon experienced a boom in its renewable and exhaustible natural resource exploitation from the mid 1970s to the end of the 1980s. However, since the earnings from natural resource exploitation especially that of crude petroleum were lodged into a stabilisation fund, Cameroon escaped the wrath of the Dutch Disease (Coden, 1984) by concentrating its efforts on the traditional sectors. Agricultural policies were pursued with sustained efforts as if Cameroon were an archetypical agrarian economy. The coffee sub-sector received undue attention during this period given its employment and revenue generation potential. Whether these efforts and programmes promoted agricultural productivity and profitability at the household and farm gate has been the object of some scholarly investigations (Tambi, 1989; Nchare, 2007).

3. Trade Liberalisation in Cameroon

3.1 A Snapshot on Cameroon: Resource Availability and Societal Vulnerability

With a population of about 17 million, Cameroon's human development indicators are those of a middle income developing country (UNDP, 2006). Income per capita is estimated at US$ 800 (US$ 2350, in purchasing power parity terms) and life expectancy at birth is 56 years (UNDP, 2006). Adult literacy is estimated at 63 per cent (75 per cent for males and 53 per cent for females), 82 per cent of the population has access to safe water and 92 per cent to sanitation (UNICEF, 2006). Recently, Cameroon was ranked 125th out of 173 countries in the Human Development Index of the United Nations Development Programme (UNDP, 2006). Compared to other countries in sub-Saharan Africa, Cameroon has one of the most diversified production and resource bases, as it produces and exports a broad range of non-oil commodities.[2] Cameroon is a net petroleum product exporter, with oil exports amounting annually to 37 million metric tonnes representing about 10 per cent of GDP. However, agriculture still remains the mainstay of the economy.[3]

In the period 1961-75, real GDP grew by nearly 5 per cent per year. Beginning 1978, Cameroon's economy experienced a structural change when oil became a major source for foreign earning. GDP grew by about 8.7 per cent per year during the period of 1976-1985 reflecting part of the oil sector's output. With booming economic conditions during this period, the government adopted a development strategy that centred on expanding the public sector. As revealed in Table 1, the period of 1986-95 was marked by severe economic crisis that led to 4.1 per cent average annual drop in per capita real GDP. An overvalued local currency, the CFA Franc[4], compounded the drop in terms of trade as the tradable good sector experienced a cost price squeeze and a fall in public revenue associated with an increasingly insolvent banking sector. Average negative rate of growth of GDP per capita (-4%) observed during the 1987-97 period was the worst in the history of the country's economy. The slowing down of the economy exposed serious deficits in public finance and balance of payments. Deflationary effects of the worsening terms of trade were offset by an increase in budget deficits, which rose to 8.7 per cent of GDP by the early 1990s. Budgetary deficits were financed by a reduction of state deposits in the banking sector and a build up of internal arrears of payment. The balance of payments deficit was funded by an increase in foreign debts and repatriation of external bank assets (Tchoungi *et al.*, 1996). In addition, the sustained weakness of the primary commodity

[2] The principal commercial and staple food crops include coffee, cocoa, timber, cotton, rubber, bananas, oilseed, grains, livestock and root starches. Natural resources include petroleum, bauxite, iron ore and timber.

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[3] The main commercial agricultural crops include; cocoa, coffee, cotton, banana, sugar cane, natural rubber, palm oil, timber, sorghum, groundnut, millet, sweet potato, cassava, rice, maize, wheat, soybean, potato and field beans.

[4] Cameroon is a member of the French African Zone, a monetary union of 15 West and Central African countries. Its currency, the "*Franc de la Communauté Français*"

markets and its attendant consequence for public revenue impeded attempts to halt the downward slide of the country's economic and financial stand. This, no doubt, led to an accumulation of public and private sector debts.[5] In line with recommendations and support from the Bretton Woods institutions [International Monetary Fund (IMF) and the World Bank], the government embarked on a series of measures embodied in an Economic Reform Programme (ERP), designed to spur business investment, increase efficiency in agriculture, re-capitalise the nation's banks and jump-start the economy.

Table 1: Trends in Some Macro-economic Indicators for Cameroon, 1961-2006

Period	GDP [a]	GNP [a]	Consumer [b] Price Index	Rate of [c] Inflation
1965-1975	4.8	8.6	53.3	5.6
1976-1985	8.7	6.5	121.7	10.2
1986-1995	-4.1	-5.1	205.5	2.5
1996-2000	5.2	2.2	250.0	12.4
2001-2005	5.1	2.3	220.0	2.3
1961-2005	3.6	3.1	157.6	7.7

Note: (a): average annual rate of change in real per capita terms. (b): is consumer price level (index 1980=100). (c): is average annual rate of change.
Source: Computed from various issues of National Statistical Accounts (*Comptes Nationaux du Cameroun* and *Note Annuelle de Statistique*) published by the *Direction de la Statistique et de la Comptabilité Nationale* of the Ministry of Economic and Finance (MINEFI), Yaoundé, Cameroon.

The declining trends have been reversed both by the internal adjustment measures (fiscal reforms) and external competitiveness (deregulation and liberalisation of the economy), following the adoption and implementation of the economic recovery programme. The overall objective of the economic reform was to restructure the country's production and consumption patterns with a view to diversifying the sources of foreign exchange earnings and eliminate price distortion to enhance competitiveness. The specific objectives of the programme were to restructure and diversify the productive base of the economy to reduce dependence on the oil sector and imports; achieve viability in the balance of payments (external balance); and achieve fiscal balance by enhancing the government's revenue base and reducing unproductive public sector investments and improve the efficiency of the private sector. This led to the signing of three stand-by arrangements with the IMF in September 1988, November 1991 and March 1994. These have been revisited recently and combined with other arrangements such as the rescheduling of debt repayment and the classification of Cameroon into the Heavily Indebted

[5] This is compounded by the increasing costs of inputs at the farm-level and macroeconomic reforms that removed subsidies and increased supply costs, leading to reductions in profit margins.

Poor Countries Initiative (HIPC).[6] Overall, real GDP turned around from an average decline of 4.1 per cent during 1986-95 to an average growth of 5.2 per cent during the 1996-2000. The acceleration of economic growth in Cameroon since 1996 reflects the strong bounce back in economic activity following the demise of the macro-economic policies that restricted growth in the first half of the decade. The evidence clearly indicates that apart from a noticeable decline in the 1986-95 period, economic progress as measured by real GNP per capita has been growing marginally over the past 40 years. Since 1996, real GNP growth has rebounded in Cameroon, advancing at about 2.3 per cent per year.

3.2 Agricultural Sector Liberalisation and Coffee Trade

More than two decades of steady growth ensued in Cameroon until 1987. Since the mid 1970s, petroleum production complemented the expansion in agricultural production and exports. As a result, Cameroon recorded average real growth rates on the order of 7 per cent over a period of about ten years (World Bank, 2000). In 1970 export revenue of US$ 50 million accrued to the coffee sub-sector. This increased steadily to US$ 30 million in 1970 (Figure 2). As shown in the figure, since 1987 coffee export values have declined from US$ 34 million to about US$ 6 million at par with the mid 1970 levels (see Figure 3).

In the beginning of 1986, export revenues from both petroleum and agricultural commodities declined dramatically by approximately 8 per cent of GDP. The deterioration in economic activity accelerated as a result of the continued decline in the price of the principal exports (petroleum, coffee, cocoa, and cotton). Growth rates of exports turned negative between 1985 and 1988, as the terms of trade deteriorated by half. There was a 40 per cent fall in per capita consumption between 1986 and 1993, and the external debt stock rose, from under one-third, to more than three-quarters of GDP between 1985 and 1993 (World Bank, 2000). Investment declined from 27 per cent of GDP to less than 11 per cent of GDP. To deal with the pronounced deterioration in public finances, marked by unmanageable cash flow pressures, drastic cuts in civil service wages were introduced. The social situation deteriorated sharply by 1995. The restructuring of the public and semi-public enterprise sectors, involving the closing of certain establishments, a civil service hiring freeze, and other labour-shedding measures, led to a significant rise in unemployment.

[6] This is a comprehensive approach to debt reduction for poor countries, designed by IMF and the World Bank. The HIPC framework is designed to provide special assistance for heavily indebted poor countries that pursue IMF- and World Bank-supported adjustment and reform programs, but for whom traditional debt relief mechanisms are insufficient. The HIPC Initiative entails coordinated action by the international financial community, including multilateral institutions, to reduce to sustainable levels the external debt burden of these countries. Central to the HIPC Initiative is the country's continued effort toward macroeconomic adjustment and structural and social policy reforms. In addition, the Initiative focuses on ensuring additional finance for social sector programs—primarily basic health and education (IMF, 2000).

These effects highlight that Cameroon was not immune to the global market downturn observed in Hazell et al. (1990). To restructure the agriculture sector, state subsidies for principal crops such as coffee and cocoa were eliminated. The provision of fertilisers and insecticides to farmers, and the state regulation of coffee trade, its marketing structure, quality control and pricing were halted (see Box 1). The marketing of cocoa, coffee and other export crops was liberalised, and the National Produce Marketing Board (NPMB) restructured into a National Cocoa and Coffee Board (NCCB), with reduced mandate to facilitate production and marketing of cocoa and coffee (Tchoungi *et al.*, 1996).

For the last 20 years, following the withdrawal of government subsidies in 1990, the liberalisation of the coffee trade and the devaluation of the CFA franc have combined to force small farmers to integrate their coffee into traditional family farms, leading to a less intensive and more casual production of coffee (Gilbert et al., 1999). Together with the decline of the coffee price, forced many coffee farmers to abandon or diversify their farms (see Benhin and Barbier, 1999). A combination of endogenous and exogenous factors explains the performance of the sub-sector.

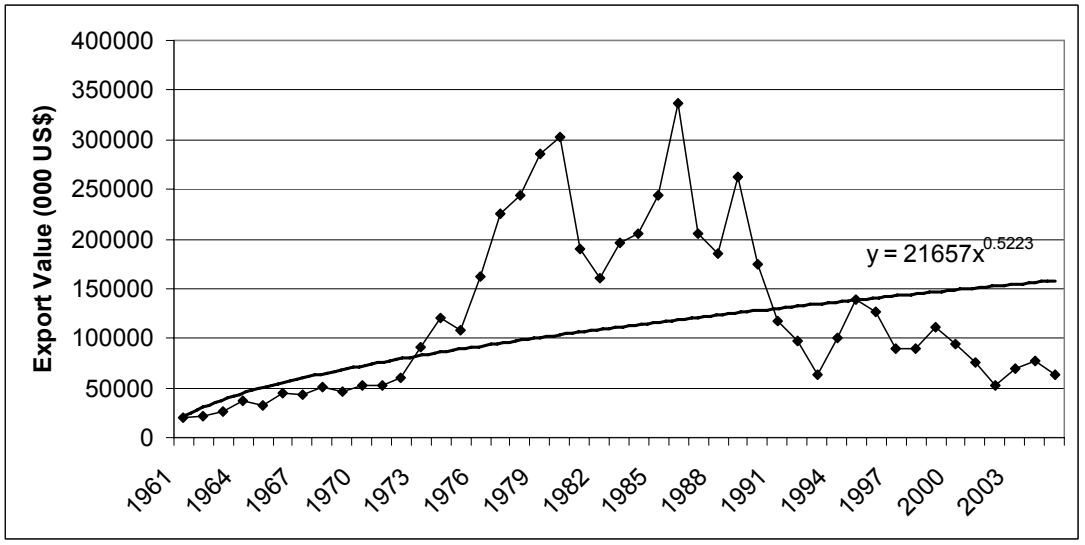

Fig. 3: Export value of coffee from Cameroon, 1961 – 2005 (Data source: FAOSTAT)

The period 1996–2005 in the figure indicate that reducing the limitations on coffee trade in particular and agricultural trade in general through lowering of tariffs and quotas and other non-tariff barriers is not an end to the challenges of commodity trade, whether regional or international. A coherent set of policies aimed at achieving a durable improvement in export earnings is required, and this must acknowledge the importance of reducing the costs to trade and raising awareness on trade opportunities.

Box 1

In analysing the impact of liberalization we do need to distinguish between changes that could have been brought about without privatization and changes resulting from that privatization. For example, in Cameroon farmers are now receiving a much higher share of the FOB price for coffee than they did before, but this stems primarily from a reduction in the high levels of taxation on exported coffee. Such changes could have been brought about while still retaining the state marketing system. Under the previous system, Cameroon set pan-territorial farm prices for export crops, as well as marketing margins up to the FOB level. For arabica and robusta coffee the buying was handled by licensed buyers who had fixed areas of operation where competition was not allowed. Arabica coffee was the monopoly of the *Union Centrale des Coopratives Agricoles de l'Ouest* (UCCAO) in the West Province and the North West Cooperative Association (NWCA) in the Northwest Province. The system as then operated had to support heavy National Produce Marketing Board (NPMB) administrative costs, largely as a result of a bloated payroll, artificially inflated trading margins for the authorized buyers, and the costs of badly managed coffee cooperatives and uncompetitive cocoa processing ventures.

Despite these drawbacks and the fact that producers were heavily taxed, coffee and cocoa quality was considered to be good. Since the liberalization process began there has been some decline in quality. The marketing systems in Cameroon were a mixture of the *Caisse de Stabilisation* (Caistab) system of francophone Africa and the marketing board system of Anglophone Africa. Three different reforms (1989/90, 1991, 1994/95) brought Cameroon to a complete withdrawal of the state from the cash crop sector, through the abolition of the system of state licensing, the abolition of the annual stabilization mechanism and the transfer of quality control prior to export to the private sector. The *Office National du Cacao et du Caf.-cacao* (CNCC) and the *Conseil Interprofessionnel Caf.-Cacao* (CICC) were created in 1991 and 1992 to replace the boards. ONCC was charged with promoting Cameroonian produce on world markets, representing the country in commodity negotiations, carrying out quality control and registering exports and collecting statistics. The creation of the CICC provided a private-sector institutional framework for liberalization as it represented exporters, buyers, processors, cooperatives, producers and even the ONCC.// END (Shepherd and Farolfi, 1999)

4. Transport Infrastructure, Cost and Trade Facilitation in Cameroon

It could be possible that despite the deregulation of coffee marketing and agricultural trade, export earnings never regained their peak levels because of the absence of factors that motivate supply response. There is an inherent relationship between export supply and factors that facilitate trade. International trade holds promise as an important engine for private sector development and reduction in poverty, particularly for small and medium-sized firms in developing countries. However, the extent of trade facilitation determines the ability of firms to deliver goods and services on time, at lowest possible costs to the world economy (Limao and Venables, 2000). Once formal trade barriers come down following liberalisation, other trade issues therefore become more important, with producers and marketers seeking to acquire information on other countries' importing and exporting regulations and how customs procedures are handled. Cutting red-tape at the point where goods enter a country and providing easier access to this kind of information are possible ways of facilitating trade (Helbe et al., 2007; Balat and Porto, 2008).

Transport infrastructure in Cameroon includes an extensive network of roads, limited railway infrastructure, three functioning international airports, underutilised domestic air routes, tough inland waterways, over-utilised coastal shipping facilities at the Douala "shallow" Seaport, undeveloped Limbe and Kribi "deep" seaports, underutilised river ports and oil pipelines running from north to south of the country. However, coffee transportation from farms to marketing centres and international border is predominantly by road, and then shipped out to

international markets from the Douala seaport. The road infrastructure is of paramount importance as it carries the bulk of Cameroon's produce. These include both rural earth roads and urban bituminised roads. The responsibility for road development is shared between the national government and local municipal authorities. Only 4000 kilometres of the 34,000 kilometres of road network is tarred, mostly urban road. This means that rural areas are more difficult to reach, while mountainous terrain and annual torrential rains seriously degrade the road system in many areas. Given the long distances, difficult terrain, and climatic conditions, transportation thus faces enormous challenges whether it is on rural or urban roads. A difficult topography makes the cost of construction or rehabilitation officially generally high. The nature of the soils, poor drainage conditions, the heavy rainfall in the southern humid forest zone where the Air and Sea ports are located, make it difficult and expensive to maintain road and rail transport facilities. This implies coffee products are abandoned in some hinterlands and some proportion only reach export terminals after the value has been affected due to long delays chiefly by inadequate road facility. The rising cost of fuel adds to the challenges faced by both producers and marketers.

Trade facilitation is therefore now at the forefront of recent trade policy dialogue as developing countries look for ways to bolster their economic growth through increased trade performance (Wilson et al., 2004). This includes the transparency of trade policy and regulation, as well as product standards, infrastructure to support trade, and technology as it applies to lowering trade costs (Negri and Porto, 2008). Trade facilitation therefore includes the improvement of transport infrastructure, the removal of government corruption, the modernisation of customs administration, the removal of other non-tariff trade barriers, export marketing and promotion as well as improving the wider environment in which trade transactions take place.[7] Lowering trade-related transaction costs is expected to result in significant improvement in Cameroon's ability to compete effectively in the global economy. Further range of benefits to be realised include: improved revenue collection, improved border controls and security, lower administrative costs, encouragement of more trade and investment, and enhancement of the competitiveness of the domestic business in the home market as well as in the export market.

According to Portugal-Perez and Wilson (2008), "the high costs of trade, i.e. transporting goods and getting them across borders, are a major obstacle to African trade performance. High trade costs have a negative effect on economies enduring them, making producers less competitive as imported inputs are relatively more expensive and the cost of final goods is relatively higher. Although direct evidence on border costs shows that tariff barriers are relatively low across all countries, poor infrastructure and weak institutions contribute in a larger extent to high trade costs along the logistic chain in sub-Saharan African countries." Limao and Venables (2001) identify poor infrastructure as significant deterrents to trade expansion. Transportation accounts for significant costs of delivery and distribution and rise in distance, as each kilometre travelled requires fuel, man-labour and capital expense. Cameroon has a challenging terrain for new road construction or rehabilitation of existing road infrastructure. In this guise, Amjadi and Yeats (1995) observe that transport costs represent a more important obstacle in Africa than import tariffs and trade restrictions. This is corroborated in Buys et al (2006) who assert that if transport infrastructure is improved, then

[7] This relates to transparency and professionalism in customs and regulatory environments, as well as harmonization of standards and conformance to international or regional regulation.

intra-African trade as a whole can be expected to increase from 10 billion to about 30 billion USD per year, while initial investments and annual maintenance costs would be relatively moderate, and significantly increase the volume of trade by 7.93 per cent.

5. Impact of Trade Facilitation on Coffee Supply and Competitiveness

5.1. Analytical Model

To ascertain the effect of trade facilitation and competitiveness on coffee trade, we employ an econometric framework in which indicators and variables are tested on the level of significance on which they influence coffee exports from Cameroon. The general form of the coffee export supply is specified in the log-log form as:

(1)

$$\ln QS_t = \alpha_0 + \beta_1 \ln P_{it}^d + \beta_2 \ln P_{it}^e + \beta_3 \ln PR_{it} + \beta_4 \ln VGT_t + \beta_5 \ln GDP_{at} + \beta_6 \ln ER_t + \beta_7 \ln TR_t + \beta_8 PP_t + \beta_9 EXG_t +$$

Where QS_t is the value of coffee exports, P_t^d is the domestic price, P_t^e is the export price, PR_t is the quantity of domestic production, VGT_t is the net value of agriculture trade, GDP_{at} is agriculture gross domestic product measured at factor cost, ER_t is exchange rate in terms of units of foreign currency (US$) per Cameroon currency (CFA francs), TR_t is the road transport measured as government's annual expenditure on rural road rehabilitation, PP_t is the global price for a barrel of crude petrol, EXG_t is government expenditure on agriculture and μ_t is the stochastic error term assumed to be independently and normally distributed with zero mean and constant variance. The joint inclusion of P_t^e and P_t^d in eq. (1) may lead to multicollinearity. Hence P_t^e and P_t^d are replaced by relative price defined as P_t^e / P_t^d, eq. (1) becomes:

(2)

$$\ln QS_t = \alpha_0 + \beta_1 \ln\left(P_t^e / P_t^d\right) + \beta_3 \ln PR_{it} + \beta_4 \ln VGT_t + \beta_5 \ln GDP_{at} + \beta_6 \ln TR_t + \beta_7 PP_t + \beta_8 \ln EXG_t + \mu_{it}$$

The price ratio P_t^e / P_t^d is expected to have a positive effect on QS_t and is intended to capture the profitability of exports. The sign PR_t is expected to be positive because higher production results in an increase in exports. The net value of national trade can be positive or negative depending on whether or not exports exceed imports. A negative net value implies an unfavourable balance of trade position. A direct relationship is expected between QS_t and GDP_{at}, a reflection of the robustness of the agricultural sector. TR_t and EXG_t are expected to have positive effect on net exports. PP_t is expected to have a negative impact on exports.

5.2 Nature and Source of Data

The data used in this study covers the period from 1961 to 2007. Quantities of coffee exported and net value of national trade are obtained from the Ministry of Trade. Domestic and export prices of coffee are obtained from the Department of Statistics of the Ministry of Agriculture. GDP is obtained from IMF International Financial statistics Yearbook. Information on TR is obtained from the Ministry of Transport. Information on PP is obtained from the Production and Statistics Office of Cameroon's National Oil Refinery Company (SONARA)

5.3 Diagnostic Evaluation

To obtain reliable estimates for our experiment, we first test if there is an equilibrium relationship of the variables in the model, i.e. whether they exhibit similar statistical properties. We employ the Engle and Granger (1987) co-integration tests by testing the Augmented Dickey-Fuller (ADF) statistics. Some studies have provided important expositions on the co-integrating methodology (Hendry, 1986; Johansen, 1988; Hallam et al., 1994; McKay et al. 1999). In table 2 we present DF and ADF test statistics for unit root of the individual series.

Table 2: Univariate Stationarity Properties of the Individual Series

Variable	**DF**	**ADF**	**Variable**	**DF**	**ADF**
$\ln QS_t$	- 2.121	- 1.873	$\Delta \ln QS_t$	- 2.727	- 4.831
$\ln P_t^e / P_t^d$	- 2.265	- 3.433	$\Delta \ln P_t^e / P_t^d$	- 4.211	- 5.277
$\ln PR_t$	- 1.999	- 2.885	$\Delta \ln PR_t$	- 3.830	- 3.978
$\ln VGT_t$	- 0.817	- 1.621	$\Delta \ln VGT_t$	- 2.924	- 3.156
$\ln GDP_{at}$	- 1.261	- 2.388	$\Delta \ln GDP_{at}$	- 2.881	- 3.487
$\ln TR_t$	- 2.316	- 2.111	$\Delta \ln TR_t$	- 2.007	- 3.531
$\ln PP_t$	- 1.962	- 2.910	$\Delta \ln PP_t$	- 2.893	- 3.891
$\ln EXG_t$	- 1.851	- 2.793	$\Delta \ln EXG_t$	- 2.913	- 3.087

Critical Value for the ADF statistic is -3.46

For all the variables, the null hypothesis that each series is I(1) cannot be rejected as the ADF statistics are below the critical value of -3.46. Thus, the variables are non-stationary in their level

form. In the first difference form, however, we can reject the null hypothesis that the variables are I(2), except for VGT_t and EXG_t. We however proceed to examine the long run equilibrium relationship between coffee supply and relative prices and transport variables using the data in their level form. The estimates presented in Table 3 show a positive and significant relationship between coffee exports and P_t^e / P_t^d, PR_t, GDP_{at}, TR_t and EXG_t and an indirect relationship with PP_t.

Table 3: Test for Long-Run Effects of Coffee Exports in Cameroon

Regressors	**Coefficients**
Intercept	2.565 (5.300)
$\ln P_t^e / P_t^d$	0.139 (2.963)
$\ln PR_t$	1.056 (2.009)
$\ln QGDP_{at}$	0.160 (3.524)
$\ln TR_t$	0.115 (3.109)
$\ln PP_t$	- 0.126 (-1.804)
$\ln EXG_t$	0.420 (3.605)
ε_t	- 0.024 (-2.099)
R^2 adj.	0.813
DW	1.961
Box-Pierce χ^2	3.764
J-B χ^2	0.672
Chow – F	1.59

DW is the Durbin-Watson statistic. J-B is the Jarque and Bera statistic with a critical value of 3.71. The critical value for the Box-Pierce statistic is 9.6, while the critical value for the Chow statistic is 2.53.

We employ the Johansen procedure to test for the existence and number of possible co-integrating vectors. The null hypothesis is that the number of co-integrating vectors is less than

or equal to r, where r is 0,1,2,4 or 5. As shown in Table 4, we can reject the null hypothesis of zero co-integrating vectors at the 95 per cent level. The null hypothesis that r≤1 or r≤2 against the general alternative cannot be rejected. The trace test statistic for r≤2 is 95.178 which is greater than the critical value of 24.31. This means that there exist more than two co-integrating vectors.

Table 4: Johansen Test for the Number of Co-integrating Vectors

Ho	Trace test statistic	Maximum eigenvalue statistic (λ_{max}) H_o	H_a	
r = 0	297.585	r = 0	r = 1	92.268
r ≤ 1	175.660	r = 1	r = 2	64.306
r ≤ 2	95.178	r = 2	r = 3	39.741
r ≤ 3	26.232	r = 3	r = 4	23.169
r ≤ 4	13.456	r = 4	r = 5	11.521
r ≤ 5	0.052	r = 5	r = 0	0.095

Critical values are from Johansen and Juselius, 1990

Since some of the data series have a long-run equilibrium relationship, we formulate an error correction representation (ECM) to capture the short-run dynamics. Upon differencing the VGT_t and EXG_t remain non-stationary and therefore not fit for inclusion in the analysis. In Eq. (3) below, the residuals from the equilibrium co-integrating regression are used as an error-correcting regression (EC_t lagged one period).

(3)

$$\Delta \ln QS_t = \beta_0 + \sum_{i=1}^{n1} \beta_{1i} \Delta \ln QS_{t-i} + \sum_{i=0}^{n2} \beta_{2i} \Delta \ln(P_t^e / P_t^d) + \sum_{i=0}^{n3} \beta_{3i} \Delta \ln GDP_{at-i} + \sum_{i=0}^{n4} \beta_{5i} \Delta \ln TR_{t-i} + \sum_{i=0}^{n5} \beta_{6i} \Delta \ln PP_t + \delta \mu_{t-1} + \varepsilon_t$$

The variables are as already defined, and Δ refer to the difference operator. The lagged quantities for cocoa and coffee measure the short-run dynamics, μ_{t-1} is the lagged value of the residuals and is included to measure the long-run equilibrium adjustment with δ as the error correction coefficient and ε_t is a random error term. Eq. (3) is a dynamic ECM of the short-run behaviour of commodity exports.

6. Results and Implications

Results of the ECM and the diagnostic tests are presented in Table 5. The ECM coefficients for coffee export integrate the short-run dynamics in the long-run relationship. Lagged values of coffee exports do not have a significant short-run effect on changes in exports. Changes in exports are determined jointly by export/domestic price ratio, agricultural GDP and foreign exchange. Lagged values of cocoa as substitute crop are tested and dropped since these do not seem to have a significant short-run dynamic effect on changes in coffee exports. In the light of the research objectives, government expenditure on road construction/rehabilitation and the world market price for a barrel of crude oil as proxies for trade costs confirm *a priori* expectations.

Table 5: Error Correction Model Regressions for Coffee Exports in Cameroon

Regressor	**Dependent variables**		
	$\Delta \ln QS_t$	$\Delta \ln GDP_{at}$	$\Delta \ln TR_t$
Intercept	2.178 (4.066)	3.189 (3.278)	1.757 (2.877)
$\Delta \ln P_t^e / P_t^d$	0.134 (2.710)	0.013 (1.997)	0.009 (1.289)
$\Delta \ln QS_{t-1}$	0.336 (2.531)	0.012 (2.096)	0.064 (1.491)
$\Delta \ln GDP_{at-1}$	0.086 (3.011)	0.213 (4.320)	0.118 (2.832)
$\Delta \ln TR_{t-1}$	0.184 (3.268)	0.108 (2.374)	0.216 (2.176)
$\Delta \ln PP_{t-1}$	- 0.142 (-1.759)	- 0.046(-1.698)	- 0.037 (-1.759)
μ_{t-1}	- 0.117 (-2.145)	- 0.078 (-1.867)	- 0.053 (-1.989)
R^2 adj.	0.639	0.537	0.487
DW	1.757	1.863	1.689
Box-Pierce χ^2	3.495	3.996	2.897
J-B χ^2	0.647	0.838	0.915
Chow – F	1.59	1.75	2.69

DW is the Durbin-Watson statistic. J-B is the Jarque and Bera statistic with a critical value of 3.89. The critical value for the Box-Pierce statistic is 13.5, while the critical value for the Chow statistic is 2.65.

Given that the regressants are cast in the first difference, the empirical results indicate a satisfactory statistical fit as judged by the adjusted R^2. The Box-Pierce statistic for residual autocorrelation does not reject the null hypothesis of no autocorrelation in the residual. According to the JB test, heteroscedasticity does not pose a problem in the relationship. These test statistics do not reject the hypothesis that the estimated equation poses a normal distribution. The relation does not fail the Chow (1960) test for structural stability following the removal of subsidies in 1990; hence the relationship is structurally stable.

Whilst acknowledging that coffee trade may depend on existing competition policies, enhanced access to credit, better education and health, and low marketing or intermediation costs,

however, it is plausible that trade costs prevent the full realisation of the gains from trade. The caveat from the study is therefore that road infrastructure and fuel price, and hence transport is important, thus indicating that liberalisation alone cannot improve coffee trade. This reinforces the importance of providing public goods, in addition to price policies, to bring about a sustained agricultural supply response (Schiff and Montenegro 1997). In a developing country such as Cameroon, these costs can also wither the poverty alleviation role of export opportunities.

7. Concluding Remarks

Over the last 15 years Cameroon has embarked on liberalisation that is significantly opening the economy, shifting from a highly regulated and centralised to a more market-based and liberal economic paradigm. Cameroon's policy reforms aimed at building a sound macro-economic environment that would stimulate domestic and foreign investment and enhance productivity, while reducing the role of the state in production. No other sector is embracing these reforms as the export crop sector. The reform programmes were designed to reduce the bias against the sector as a means to reduce poverty and increase economic growth. While the rural economy continues to be highly dependent on cash crops, producers' participation in markets for input as well as output is significantly impacted by the extent of trade facilitation. Road infrastructure and the costs are significantly important, and co-integrate with other factors such as export price and exchange rate to influence returns from coffee exports.

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THE IMPACT OF EAST AFRICA COMMUNITY CUSTOMS UNION ON UGANDA ECONOMY: A COMPUTABLE GENERAL EQUILIBRIUM (CGE) ANALYSIS

Charles Ayai Okello[1]

1. Introduction

In 2005, Uganda, Kenya and Tanzania signed a treaty forming the East Africa Community (EAC) customs union which has now been expanded to include Rwanda and Burundi. The purpose of the customs union is to promote trade and other elements of regional development. The dominant feature of the customs union is that member states agreed to reduce tariffs. The Heads of State reached an agreement to implement a common external tariff with three bands; 0 per cent for meritorious goods, 10 per cent for intermediate goods and 25 per cent for consumer goods (Obwona:2005:15). Uganda and the rest of the members of EAC have imposed a common external tariff of 25 per cent on goods from non-members of EAC (Obwona: 2005:15).

However, the EAC customs union presents uncertain economic impacts on member countries and has generated a great deal of public discussion and debate in Uganda (Obwona: 2002:15). For instance, there is concern that Ugandan industries would be adversely affected under the customs union by import competitition especially from Kenya which has a relatively advanced industrial sector.[2] But, to date, there is limited analysis of the economic impact of the new EAC customs union on member countries. Therefore, a concise analysis of the impact of the EAC customs union is important to guide policy intended for development of trade to benefit the Ugandan economy. The purpose of this paper is to quantify the impacts of the EAC customs union on Uganda's economy using general equilibrium analysis (CGE). This methodology captures fully the chain of interactions in the Ugandan economy that were triggered by the customs union (Dorosh: 2000:11; Mbabazi: 2002:14). The rest of the paper is organised as follows: Section 2 describes the data and the modelling approach of Uganda's economy. Section 3 discusses the simulation results for EAC customs union on macro-economic variables, manufacturing sector, welfare and factor income. Finally, section 4 provides the concluding remarks.

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[2] See Morris Obwona *et al* (2005) "The new EAC customs union: Implications for Ugandan trade, industry competitiveness, and economic welfare". Final Report, prepared for Ministry of Finance, Planning and Economic Development, p.2.

2. The Social Accounting Matrix and the Ugandan CGE modeling

2.1 The Data: A Social Accounting Matrix for Uganda (SAM)

A SAM is a particular representation of macro and meso-economic accounts of socio-economic system, which captures the transactions and transfers between all economic agents in the system (Pyatt and Round:1985:16). The accounts are presented in a square matrix, where the incomings and outgoings for each account are shown as corresponding row and column of a matrix. The transactions are shown in the cells, so the matrix displays the interconnections between agents in an explicit way. It is comprehensive in the sense that it portrays all economic activities of the system (consumption, production, accumulation and distribution), although not necessarily in equivalent detail. A SAM is flexible in that disaggregation is possible and emphasis can be placed on different parts on the economic system. Such transactions are carried out by different economic agents either through market or identifiable transfers.

The concepts and principles of SAM are fairly standard (for details see Pyatt and Round: 1985:16). In CGE modelling we need to construct a SAM or use the existing one. The latest available SAM for Uganda was constructed in 2002.[3] The Uganda SAM contains the block of activities, factors of production, households, government, stocks and the rest of the world (ROW). It is a 193 by 193 matrix, which has 62 activities, 62 commodities, 32 household types, and 16 labour categories, showing GDP at factor cost amounting to 3,389,424 million Uganda shillings at 2002 prices. The various commodities (domestic production) supplied are purchased and used largely by households (40 per cent) for final consumption, but also a considerable percentage (35 per cent) is demanded and used by producers as intermediate inputs. Although only 7 per cent of the domestic production is exported, a considerable amount (11 per cent) is used for investment and stocks, while the remaining 8 per cent is used by government for final consumption.

Households are shown to derive 68 per cent of their income from factor income payments while the rest accrues from government, inter-household transfers, corporations and the ROW. The government account earns a hefty 33 per cent income from import tariffs, a characteristic typical of developing countries. It derives 42 per cent from the ROW which includes international aid and interest. Domestic producers pay 14 per cent in taxes on products, while only 6 per cent is income taxes paid by households and only 5 per cent is corporate taxes paid by corporations.

Government is the main source of investment finance (28 per cent) followed by domestic producers (27 per cent), households (26 per cent) and lastly the corporations that provide only 20 per cent. Imports of goods and services account for 87 per cent of total expenditure to the ROW. The rest is paid to the ROW by domestic household sectors in form of remittances; wage labour from domestic production activity; domestic corporations payments of dividends and insurance claims; income transfers paid by government; and net lending and external debt related payments. It is important to note that net lending and external debt related payment is negative fourteen of total expenditure to the ROW indicating a possibility of a negative trade balance and hence inability to cope with external debt servicing.

[3] Work is in progress to update the 2002 SAM to 2007.

The extent of household disaggregation is very important for policy reform analyses involving representative household groups as opposed to individual households.[4] Pyatt and Round (1985:16) argue persuasively for a household disaggregation that minimises within-group heterogeneity. This is achieved in the Uganda SAM through the disaggregating of households by quartiles within regional, rural and urban classifications. These criteria generated 32 household groups; namely, rural Q1, Q2, Q3, Q4 and urban Q1, Q2, Q3, Q4; distinguished by region (Central, Eastern, Northern and Western).

The Uganda SAM identifies four labour categories disaggregated by gender and skill namely, male and female, distinguished by unskilled, semi-skilled, skilled and highly skilled. These are further classified according to rural and urban as well as by geographic regions. This criterion yields 16 categories of labour classifications. Land and capital are distributed accordingly to the various household groups.[5]

2.2 CGE Modelling of Uganda Economy

CGE technique can capture the interdependence among the various markets and sectors of an economy. The theoretical foundation is the equilibrium theory formalised by Arrow and Debreu.[6] When combined with social accounting matrix or input-output data, it is a standard tool for policy analysis (Shoven:1984:18; Stifel and Thorbecke:2003:19; Reed:1996:17; Dixon, Parmenter, Sutton and Vincent 1982:9; Francois and Reinert:1996:12).

The model of the Uganda economy developed here is a static one of a small open economy. The general structure of this computable general equilibrium model is a familiar one which has been used frequently in numerous studies based on a standard CGE model developed by (Lofgren, Harris, and Robinson:2002:13). The CGE model is calibrated to the 2002 SAM database and GAMS software is used to calibrate the model and perform the simulations.[7] It is assumed that the economy is at equilibrium at the benchmark (2002).

A policy simulation is implemented as a *counterfactual* scenario, which consists of an exogenous set of shocks to the system (Decluwe, Patry, Savad, and Thorbecke: 1999:6; Dervis, de Melo and Robinson:1982:7). Counterfactual shows the state of the economy after all markets have reached a new equilibrium; that is, comparative static analysis. The various components of the CGE model of Uganda are described here.

[4] An overriding feature of a SAM is that households and household groups are at the heart of the framework. This helps to bring data from disparate sources. These households are often classified according to characteristics of either the household head or the principal income earners (gender, employment status), often by location (rural/urban, etc) and sometimes other characteristics including asset or main income source (farm/non farm, etc).

[5] Labour account is usually disaggregated by gender, skill, educational level, location etc. The main focus is on labour market segmentation that may have structural consequences, especially determining impacts on different groups of households.

6The approach is covered in some of the literature in microeconomics. Arrow and Debreu assumed that all market choices are made at once. See David M. Kreps, 1990, *A Course in Microeconomics Theory*, Prentice Hall of India, pp.217-20.

[7] GAMS stands for General Algebraic Modeling System, a software used in CGE analysis.

2.2.1 Productions and Commodities

In our model production makes use of five factors: capital, skilled labour, unskilled labour, land and natural resources. Factor endowments are assumed to be fully employed and their growth rates are exogenous (zero for land and natural resources), except for labour which is based on demographic forecast of the United Nations. Installed capital and natural resources are sector-specific, so that their rate of returns may vary across sectors. The three remaining factors are perfectly mobile across sectors.

The production technology process is represented by a nested production function.[8] At the bottom level, primary inputs are combined to produce value-added using a CES (Constant Elasticity of Substitution) function. At the top level, aggregated value added is then combined with intermediate inputs within a fixed coefficient (Leontief) function to give the output. The profit maximisation gives the demand for intermediate goods, labour and capital demand. A firm can choose the quantity of the commodities it can produce. For all activities, producers maximise profits given their technology and the prices of inputs and output (Lofgren: 20001:13).

2.2.2 International Trade

The allocation of domestic output between exports and domestic sales is determined using the assumption that domestic producers maximise profits subject to imperfect transformability between these two alternatives. The production possibility frontier of the economy is defined by a Constant Elasticity of Transformation (CET) function between domestic supply and export.

To accommodate the possibility that imported commodities are exported, the Armington assumption is applied in combining domestic production and imports, using a CES function.[9] The resulting homogenous "Armington commodities are either sold in Uganda or exported". A CET function determines the scope for the choice between domestic demand and export. The Armington assumption is used here to distinguish between domestically produced goods and imports (Armington:1969:1). For each good, the model assumes imperfect substitutability (CES function) between imports and the corresponding composite domestic goods. The parameters for CET and CES elasticity used to calibrate the functions in the CGE model were borrowed (Devarajan: 1990:5).[10] Exports are traded for foreign exchange which is used to pay for imports. Balance of payments equals net import.

[8] It is a two-layer structure of intermediate inputs and value added.

[9]The Armington assumption is that imported and domestically produced commodities are substitutes for each other, but not perfect substitutes. This solves the problem that the same kind of goods are found to be both exported in actual trade data which is inconsistent with the Heckscher-Ohlin under perfect competition.

[10] One of the most debated issues in CGE literature concerns the validity of the key behavioural parameters. In fact, CGE models prefer to borrow from the handful of estimates available from the literature. Lack of data is often cited as the major reason for the compromise. We use 0.50 for capital-labour substitution; 2.0 for substitution between domestic and imported goods and 5.0 between domestic output and export.

2.2.3 Factor of Production

There are 18 primary inputs: 16 labour types, capital and land. Wages and returns to capital are assumed to adjust so as to clear all the factor markets. Both types of labour are mobile across sectors while capital is assumed to be sector-specific. Economic agents own all these factors of production.

2.2.4 Consumption

Household consumption is modelled using the Cobb-Douglass utility function subject to the budget constraint (Lofgren: 2001:13). Therefore, economic agents respond to price incentives but keep the share of their budget spent on each commodity fixed. The agents demand consumption goods and save the remainder as disposable income. Households receive their income from primary factor payments. They also receive transfers from government and the rest of the world. Households pay income taxes and these are proportional to their incomes. Savings and total consumption are assumed to be a fixed proportion of household's disposable income (income after income taxes). Consumption demand is determined by a Linear Expenditure System (LES) function.[11] Firms received their income from remuneration of capital; transfers from government and the rest of the world; and net capital transfers from households. Firms pay corporate tax to government and these are proportional to their incomes.

2.2.5 Government

Government is an important institution in the model. Government revenue is composed of direct taxes collected from households and firms, indirect taxes on domestic activities, domestic value added tax, tariff revenue on imports, factor income to the government, and transfers from the rest of the world. The government also saves and consumes.

2.2.6 Market Clearing Conditions

Supply in any commodity market must be equal to its demand at equilibrium price. Domestic demand equals demand for intermediate inputs to production, public sector use, final consumer demand plus domestic investment and stock change. The model includes supply-demand conditions for the Armington composite goods. On the supply side, Armington composite goods equal the aggregation of imports and domestic production, whereas the demand side includes domestic and export components. Primary factor endowment equals primary factor demand. Any commodity which commands a positive price has a balance between aggregate supply and demand, and any commodity in excess supply has an equilibrium price of zero.

[11] The study also borrowed LES parameters.

2.2.7 Macro Closure and Welfare Measurement

Equilibrium in a CGE model is captured by a set of macro closures in a model (Dewatripont and Michael: 1987:8; Blake, McKay and Morrissey: 2001:3). Aside from the supply-demand balances in product and factor markets, three macro-economic balances are specified in the model: (i) fiscal balance, (ii) external trade balance, and (iii) savings-investment balance. For fiscal balance, government savings are assumed to adjust to equate the difference between government revenue and spending. For external balance, foreign savings are fixed with exchange rate adjustment to clear foreign exchange markets. For savings-investment balance, the model assumes that savings are investment driven and adjust through flexible saving rate for firms. Alternative closures, described later, are used in a subset of the model simulations.

The consumer price index (CPI) was chosen as the *numeraire*; the price relative to which all prices are evaluated.[12] The price being fixed at one, means the total quantity of consumption equals total value of consumption at all times. In our model we measure welfare focusing solely on private household consumption while the government purchases are fixed. A change in total household consumption therefore equates a welfare change as measured by the Hicksian equivalent variation (EV).

3. Simulation and Discussion of Results

3.1 Discussion of Results

Every simulation results generated by a detailed CGE model such as ours depend potentially on thousands of data items, elasticity values and behavioural assumptions. Nevertheless, as demonstrated in this paper, it is possible to explain the results to policy makers in terms of elementary mechanism, starting from the bigger picture (macro variables) down to the smaller units (micro variables). The approach used to explain results here makes it possible for policy advisers or politicians to understand CGE results without requiring time-consuming absorption of voluminous technical documentation. We performed simulations under three policy scenarios under the assumptions of fixed/ varying fiscal deficit and mobile labour (see Table 1). Tariffs were reduced by 25, 33 and 100 per cent respectively.

[12]Absolute price levels are undermined in the model and only relative prices can be assessed. Fixing the consumer price index to one implies that inflation cannot occur.

Table 1: Summary Scenario for the Impact of Customs Union

Simulation	Code	Fiscal Deficit	Mobility of labour
Scenario 1: Partial tariff reduction			
1. EAC tariff cut 25%	(EAC1)	flexible	mobile
2. EAC tariff cut 25%	(EAC2)	fixed	mobile
Scenario 2: Partial tariff reduction			
3. EAC tariff cut 33%	(EAC3)	flexible	mobile
4. EAC tariff cut 33%	(EAC4)	fixed	mobile
Scenario 3: Complete tariff removal			
5. EAC tariff cut 100%	(EAC5)	flexible	mobile
6. EAC tariff cut 100%	(EAC6)	fixed	mobile

3.1.1 Impact on Macro-economic Variables

Table 2 summarises the impact of the customs unions on the macro-economic variables.

Table 2: Effects of EAC Customs Union on Uganda's Macro-economic Variables (percentage change from 2002—the baseline of the model)

	2002 LEVEL (MILLION SHS) *	EAC1 %	EAC2 %	EAC3 %	EAC4 %	EAC5 %	EAC6 %
Absorption	10,213,837	0.0	0.0	0.0	0.2	0.2	0.2
Private Consumption	8,636,159	0.1	0.1	0.1	0.3	0.3	0.3
Exports	446,538	0.6	0.8	0.3	2.9	2.9	2.9
Imports	1,192,472	0.4	0.5	0.5	0.5	1.9	1.9
GDP at Market Prices	10,859,871	0.0	0.1	0.1	0.2	0.2	0.2
Net Income Tax	1,436,146	0.2	0.3	2.9	1.9	0.2	2.1

Source: Bank of Uganda
Note: * Figures obtained from Bank of Uganda, Quarterly Economic Report, June 2004.

Real GDP

Real GDP increases by a small percentage of not more than 0.2 per cent when all tariffs have been removed under scenario 3, whether the budget deficit is fixed or flexible[13]. With gradual removal of tariffs (scenarios 1 and 2), there was virtually no growth in real GDP. In Uganda investment is scarce (investment equation in the model) and therefore GDP is generally consumption-driven (consumption equation in the model). Promotion of Foreign Direct Investment (FDI) would be a viable policy for the government to pursue.

[13] Uganda has a budget deficit of 12 percent of GDP.

Exports and Imports

Tariff cuts increased exports more than imports. Both import and export volumes have increased by 3 and 2 per cent respectively under scenario 3. Under gradual removal of tariffs (scenarios 1 and 2) exports and imports growth were less than one per cent. The increase in exports is partly as a result of increased availability of capital goods and re-exportation to other countries in the region such as Democratic Republic of Congo (DRC) and Southern Sudan.

This low percentage growth rate in export depicts a weak intra-regional trade.[14] Since increase in government spending primarily affects production of domestic goods, real depreciation of the exchange rate is required to stimulate exports and reduce imports. Since exports increased, the trade balance and balance of payments improved as well, reducing the budget deficit.

3.1.2 Impact on Industrial Sector

Table 3 indicates that the impact on Uganda's industrial sector is mixed. Economic literature has often emphasised the favourable impact of tariff reduction on industries. Some manufacturing industries (food, drink and tobacco, coffee and tea, chemical, apparels) declined as a result of competition from imports and high production cost since intermediate imports are high. Other industries like pulp and paper products, dairy, sugar, leather, metal and cement have positive percentage change of less than one per cent.

Table 3: Impact on Industry Output Activity (percentage change from the base case-2002)

Industry	EAC1	EAC2	EAC3	EAC4	EAC5	EAC6
Pulp and Paper products	0.0	0.0	0.0	0.0	0.1	0.1
Food, Drink and Tobacco	0.0	0.0	0.0	0.0	-0.1	-0.1
Dairy	0.2	0.2	0.3	0.3	0.9	0.9
Sugar	0.1	0.1	0.2	0.2	0.5	0.5
Coffee and Tea	-0.2	-0.2	-0.3	-0.2	-0.9	-0.9
Soft drinks	-0.1	-0.1	-0.1	-0.1	-0.5	-0.5
Chemicals	0.0	0.0	-0.1	-0.1	-0.2	-0.2
Textiles	0.0	-0.1	-.0.1	-0.1	-0.2	-0.2
Apperels	-0.2	-0.2	-0.3	-0.3	-0.8	-0.8
Leather	0.1	0.1	0.1	0.1	0.3	0.3
Printing and Publishing	-0.5	-0.5	-0.6	-0.6	-0.2	-0.2
Petroleum	-0.1	-0.1	-0.1	-0.1	-0.3	-0.3
Rubber	-0.7	-0.7	-0.9	-0.9	-2.7	-2.7
Metal	0.0	0.0	0.0	0.0	0.1	0.1
Clay	0.0	0.0	0.0	0.0	0.0	0.0
Cement	0.0	0.0	0.0	0.0	0.2	0.2

[14] There is very limited intra-trade in the customs union due to complementarities in production and non trade barriers like customs clearance delays.

3.1.3 Impact on Welfare

Table 4 provides the impact of EAC customs union on welfare. There is reduction in the welfare of the poorest households (1st, 2nd, and 3rd quintiles) while the welfare of the 25 per cent of the richest urban and rural households (4th quintile) improved. The poorer members of the society lost because of possible trade diversion. Locally produced goods are relatively more expensive compared to imported products.

However, the welfare of the richest household group increased for a number of reasons. There are two sources of consumption gain.

Table 3: Compensating Variation from the Base Case 2002 (percentage change)

	EAC1	EAC2	EAC3	EAC4	EAC5	EAC6
Central region urban (first quintile)	-0.4	-0.4	-0.5	-0.5	-1.7	-1.8
Central region urban (second quintile)	-0.6	-0.6	-0.7	-0.8	-2.6	-2.8
Central region urban (third quintile)	-0.7	-0.7	-0.9	-0.8	-2.6	-2.8
Central region urban (fourth quintile)	1.2	1.2	1.6	1.6	4.6	4.6
Central region rural (first quintile)	0.1	0.1	0.1	0.1	0.3	0.2
Central region rural (second quintile)	0.2	-0.2	0.1	0.1	0.4	0.4
Central region rural (third quintile)	3.4	4.0	0.3	0.3	0.8	0.8
Central region rural (fourth quintile)	-0.2	-0.3	4.5	5.3	12.9	15.0
Eastern region urban (first quintile)	-0.2	-0.3	-0.3	-0.4	-1.1	-1.3
Eastern region urban (second quintile)	-0.3	-0.4	-0.5	-0.5	-1.7	-1.9
Eastern region urban (third quintile)	-0.3	-0.4	0.7	0.7	2.1	2.0
Eastern region urban (fourth quintile)	0.6	0.5	0.2	0.3	0.2	0.5
Eastern region rural (first quintile)	0.0	0.0	0.0	0.0	0.1	0.1
Eastern region rural (second quintile)	0.0	0.0	0.1	0.1	0.2	0.1
Eastern region rural (third quintile)	0.1	0.1	0.1	0.1	0.4	0.4
Eastern region rural (fourth quintile)	0.1	0.2	0.2	0.3	0.2	0.5
Northern region urban (first quintile)	-0.3	-0.4	-0.4	-0.5	-1.5	-1.7
Northern region urban (second quintile)	-0.2	-0.3	-0.3	-0.4	-1.1	-1.3
Northern region urban (third quintile)	0.0	0.0	0.0	0.0	-0.2	-0.3
Northern region urban (fourth quintile)	0.1	0.1	0.2	0.2	0.5	0.4
Northern region rural (first quintile)	0.1	0.1	0.1	0.1	0.3	0.2
Northern region rural (second quintile)	0.0	0.0	0.0	0.1	0.2	0.2
Northern region rural (third quintile)	0.0	0.0	0.0	0.0	-0.2	-0.3
Northern region rural (fourth quintile)	0.0	0.1	0.1	0.1	0.0	0.2
Western region urban (first quintile)	0.0	-0.1	0.0	-0.1	0.0	-0.2
Western region urban (second quintile)	-0.3	-0.4	-0.4	-0.5	-1.5	-1.7
Western region urban (third quintile)	-0.1	-0.2	-0.1	-0.2	-0.6	-0.8
Western region urban (fourth quintile)	0.8	0.7	1.0	0.9	2.7	2.4
Western region rural (first quintile)	0.0	0.0	0.1	0.0	0.2	0.1
Western region rural (second quintile)	0.0	0.0	0.0	0.0	0.1	0.1
Western region rural (third quintile)	0.1	0.1	0.1	0.1	0.2	0.2
Western region rural (fourth quintile)	0.4	0.5	0.6	0.6	1.5	1.8
Total	**4.1**	**4.1**	**5.5**	**5.3**	**10.7**	**10.7**

The first is the efficiency gain in GDP identified above which translates into consumption increase. The second source of consumption gain is the improvement in the terms of trade. This increase in purchasing power of real GDP by increasing prices of commodities produced in Uganda relative to prices of commodities produced outside Uganda. The term of trade effect is the combination of the following: First, there is improvement in the terms of trade from the elimination of import duties which results in reduction of import prices. Second, there is an increase of exports (although of less than 3 per cent). Third, the welfare for the higher income groups increases as imported products form a significant part of their consumption basket. Because of the reduction in production in activities on which the poor households depend, for example, crop production, their income and consumption levels are also affected. Tariff cuts also reduce government revenue which is likely to reduce government transfers to the poor households.

3.1.4 Impact on Factor Income

Table 4 indicates the percentage change in factor income for labour, capital and land. For labour, the incomes of skilled labour both in rural and urban areas have gone up relatively more than the rural unskilled labour in both rural and urban areas. The changes in income of skilled labour could be as a result of a slight increase in employment in the export sector because they have a high share of employment for the production of these commodities. Unskilled labour suffers smaller factor income change because they have relatively high shares of their employment in the production of commodities for which national production shrinks when tariffs are removed. In addition, this could be as a result of increase in nominal wages.

Factor incomes of land and capital have increased by less than 3 per cent. Land supply is fixed but the demand for land has skyrocketed, pushing its price up. Capital supply has increased over time from direct foreign investment and loans/grants offered to the government from foreign sources, reflecting relative abundance of capital in the new equilibrium, compared to other production inputs. Land and capital are scarce factors and are relatively more expensive.

Table 4: Factor Income (percentage change from the base case 2002)

Factors	EAC1	EAC2	EAC3	EAC4	EAC5	EAC6
Labour unskilled (rural male)	0.8	0.8	1.1	1.1	3.7	3.7
Labour unskilled (rural female)	0.9	0.9	1.1	1.1	3.8	3.8
Labour unskilled (urban male)	0.8	0.8	1.1	1.1	3.3	3.3
Labour unskilled (urban female)	1.3	1.3	1.7	1.7	5.5	5.5
Labour semi skilled (rural male)	1.4	1.4	1.9	1.9	6.4	6.4
Labour semi skilled (rural female)	0.9	0.9	1.2	1.2	3.8	3.8
Labour semi skilled (urban male)	0.9	0.9	1.2	1.2	3.8	3.8
Labour semi-skilled (urban female)	0.8	0.8	1.1	1.1	3.6	3.6
Labour skilled (rural male)	0.8	0.8	1.0	1.0	3.1	3.1
Labour skilled (rural female)	0.7	0.7	0.9	0.9	2.7	2.7
Labour skilled (urban male)	0.7	0.7	0.9	0.9	2.7	2.7
Labour skilled (urban female)	0.7	0.7	0.9	0.9	2.5	2.5
Labour highly skilled (rural male)	0.7	0.7	0.9	0.1	2.8	2.9
Labour highly skilled (rural female)	0.8	0.8	1.0	1.0	3.2	3.2
Labour highly skilled (urban male)	0.7	0.7	0.9	0.9	2.8	2.8
Labour highly skilled (urban female)	0.7	0.7	0.9	0.9	2.7	2.7
Land	0.7	0.7	0.9	0.9	2.9	2.9
Capital	0.7	0.7	0.9	0.9	2.6	2.7

3.2 Sources of Possible Biases in the Results

Does this model adequately explain all these results? What are the biases of this model? Although trade liberalisation can increase economic efficiency, others have shown that different assumptions on factor mobility and macro closures can cause differences in simulation results (Deveranjan, Lewis and Robinson: 1990:5). Other researchers also indicate that different assumptions on economic and social environment may affect the modelling results significantly.

First, the key issue which has not been properly captured in the model is productivity and FDI. Does trade liberalisation affect productivity and FDI in Uganda? Is the present upsurge in foreign investment in Uganda a result of the EAC customs union? These questions need further investigation.

Second, one of the most debated issues in CGE literature concerns the validity of key behavioural parameters used in the calibration process. CGE results have been shown to be sensitive to the values of these parameters. CGE models seldom estimate these parameters, preferring to borrow from estimates available in the literature. The lack of data prevented us from estimating these elasticities. The results of the sensitivity study are not reported here.

For instance, the Armingtonassumption the degree of substitution between domestic and imported, is a key behavioural parameter that drives the results of interest to policymakers. For

instance, trade policy can affect the price of traded goods relative to domestically. Such a price change will affect a country's tradeadvantage, level of income, and employment. The magnitude of these impacts will largely depend on the magnitude of these elasticities, including Armington parameters (Deverajan:1990:5). Thus, it is important to use the true Armington parameters for a study like this one. The estimation of elasticity is a fertile area for future research.

Third, this analysis should have considered other domestic policy reforms like fiscal policy reforms as well as other trade liberalisation initiatives such as the Doha Development Agenda of World Trade Organisation (WTO) in tandem with the East Africa regional liberalisation process. The inclusion of these policy choices would counterbalance the impact of customs unions.

Finally, the effects of trade policies are not immediate, but spread over a long period of time. Such effects are difficult to take into account in a static framework. Dynamic models may be required to study corresponding adjustment period. Indeed, a number of the effects are dynamic as they are linked to accumulation of capital which has impact on capital and savings (Baldwin:1989:2; 1992:3). This will magnify gains or losses, than static effects as evidenced, for example (Baldwin:1992:3). In this context, a cautious approach is necessary in interpreting our results.

4. Concluding Remarks

In this paper we build a single-country multi-sector CGE model of Uganda to demonstrate the possible outcomes of East Africa customs union. To see the different effect of the East Africa customs union three scenarios were considered, two cases of partial tariff reduction and total tariff removal, allowing for fixed and flexible deficit and mobile labour among sectors. Specifically, our counterfactual analyses adopted three scenarios of progressive tariff reduction of 25, 33, and total removal (100 per cent). This arrangement allows us to see the impact of tariff reduction in the medium term on the Ugandan economy. Static CGE models are always medium term, not short-run as is sometimes believed.

The results in this paper indicate that the customs union reduction of tariff rates has only had a small effect on the macro-economic variable of Uganda of less than 0.2 per cent growth in real GDP and less than 3 per cent in exports and imports, less than 0.2 of absorption, 2.1 per cent of net income tax and 2 and 3 per cent for exports and imports respectively. The removal of tariffs has mixed results on the industrial sector as some industries gained and others lost. There is reduction in the welfare of the poorest households (1st, 2nd, and 3rd quintiles) while the welfare of the 25 per cent of the richest rural and urban households (4th quintile) improved.

The main policy implications of the study are as follows. First, intra-regional trade should be promoted. Tariff reduction alone under the customs union would not generate high intra-regional trade without extra measures. While the EAC customs union would generate more trade among the member countries, Kenya's manufacturing sector remains far advanced than other member countries and may spell doom for Uganda in the short and medium terms. Before the complete removal of tariffs on goods from Kenya, Uganda's domestic industries need to be competitive enough if the country is to benefit.

Second, Uganda needs to be cautious in implementing liberalisation policy. In fact, it should be done in a piecemeal manner. Synchronisation of various trade reform programmes is essential. For instance, to consider the removal of tariffs under the Economic Partnership Agreement (EPAs) on goods from the European Union (EU), while at the same time implementing a common external tariff on all goods imported outside the customs union are conflicting goals.

Third, liberalisation should be carried in tandem with fiscal reforms. Uganda needs to identify alternative sources of tax revenues if she is to reduce the level of fiscal deficit.

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