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Foreign Trade

EC's Association and Preference Policy

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The EC's association and preference policy has again and again given rise to criticism by those developing countries who are not favoured as well as by the other industrial states. Sometimes, however, it seems that preferences have been overestimated. It cannot be overlooked that the importance of tariff policy in EC's development policy is diminishing.

After the association of the African states there were above all the EC's Mediterranean policy, the expansion of the preference granting area by Denmark's, Great Britain's and Ireland's joining the EC, as well as the imminent or already effective inclusion of Commonwealth States in the preferential zone, which had strengthened the suspicion of the creation of a new bloc in world trade by an "enclosure strategy" of the EC. The resulting reproaches and the consequences for economic policy are an important topic of the negotiations on occasion of the GATT round.

The EC does not challenge a certain discrimination against third developing countries, but lays stress on the benefits of the association agreements and preferential trade agreements to development policy. Although in principle there is agreement on the fact that the EC's preference policy can theoretically lead to a discrimination against third countries, the views about the real effects are heavily diverging, due to the lack of adequate empirical research. In order to debunk the discussion it was necessary to do some empirical research work on the EC's association and preferential agreements. In this context the following questions were to be analysed in particular:

□ Will empirical investigations, relative to the global development of exports as well as to the exports of preferential goods of special importance, demonstrate a trade creation for the favoured countries or a trade diversion, respectively, for the developing countries who are not favoured?

□ What implications of the effects of the association and preference policy are hitherto exist-

ing for the EC's future mode of procedure — especially with regard to the GATT round. Such a study was made by the Hamburg Institute for International Economics (HWWA)¹. This analysis had to be limited to Greece, Turkey and AAMS since only for these countries significant time series were at hand. All other agreements were signed or became effective such a short time ago that an interpretation of the effects of preferences by means of the available figures was impossible.

General Analysis of Expansion Rates

The total analysis has yielded differing results for the individual countries and products. A first impression of the effects of the association and preferential agreements was intended to be given by the global investigation of the EC's imports from the associated and non-associated states. The examination of the associated countries' shares in the EC-markets, though, yielded no more results which could be generalised than the analysis of the expansion rates. Although the discussion was limited to the states with the best conditions for verifying the theoretical effects by an investigation over a longer period, the efficiency of the preferences did not come out distinctly. A reason can be found in the numerous separate factors, which may have superimposed the effects of the preferences.

The general analysis of the expansion rates shows that between 1961 and 1971 only the Greek exports to the EC have grown faster than the Community's total imports. In spite of the preferential

¹ See Karl Fasbender, Hajo Hasenpflug, Franz-J. Jägerler, Dietrich Kobschull (project director): EWG-Zollpräferenzen und Welthandelsstruktur (EC's Tariff Preferences and World Trade Structure), Hamburg 1973.

* The Hamburg Institute for International Economics.

tion and association, respectively, Turkey and the AAMS fell short of the average. Even if one supposes that the average import value becomes distorted by the explosive growth of EC-trade, there remain few clues to the export promoting effect of the preferences.

Only for Greece whose market share increased — relative to the EC's foreign trade with developing countries — on a very low level from 1.02 p.c. to 2.06 p.c., "trade-creation-effects" caused by tariff reductions can first be supposed. However, an additional examination over the same period of the Greek export structure with reference to the different goods and regions shows clearly that the principal cause of this growth was in the rapid expansion of Greek industry and its reorientation towards the nearby receptive EC-markets rather than in the relatively small tariff preferences.

This supposition is supported by the fact that Turkish exports in spite of the tariff preferences declined between 1961 and 1970 from 1.64 p.c. to 1.53 p.c. of the EC's foreign trade. Only 1971 a slight rise to 1.70 p.c. was noticed. It is characteristic that the proportions of exports of semi-finished and finished industrial goods — in contrast to the development in Greece — remained nearly on the same low level.

The shrinking of the AAMS-share from 11.10 p.c. to 8.94 p.c. cannot be attributed to one uniform cause for the individual associated African states. The analysis, however, gives support to the hypothesis that the different countries' dependency on the export of individual products and their sales opportunities might have played the decisive role. In this connection it surprises, however, that countries which have been able to improve their EC-market shares (Ivory Coast, Togo) are dependent on their exports of certain primary commodities (coffee, cocoa) similarly to countries whose market shares have decreased (Cameroon, Madagascar). Since the development of the shares of the AAMS, Greece, and Turkey in the individual EC-states showed heavily diverging tendencies and the levels of their market shares are very different, too (high AAMS-share in France, low shares in the Federal Republic and Italy), it did seem necessary to examine the effects of preferential and association agreements in more detail for selected associates and third countries as well as for special representative commodities.

It was decisive for the selection of products that the commodities took a high share in the producer countries' foreign trade, that they had been preferentialized during a longer period, and that they were in competition with products from third countries. Thus the discussion included the fol-

lowing products as typical: Coffee, cocoa and bananas for the AAMS and tobacco for Greece and Turkey.

In order to make allowance also for processed goods whose importance for the developing countries' foreign trade might rise in the long run, with cocoa-paste, cocoa-butter, and peanut-oil, products were included into the analysis which are characteristic of the diversification policy of the countries of the Third World. The following examples are restricted to coffee and bananas.

Coffee: Diverging Developments

In the field of primary commodities it is impossible in the first impression to gain uniform consistent results concerning the effects of the EC-preferences, as the analysis of the product coffee already shows. Characteristic are the heavily diverging developments on the individual EC-submarkets. While the imports of coffee of the Federal Republic of Germany and the Netherlands have increased tenfold between 1960 and 1971 and grown much faster than imports from third countries, in Belgium and Luxemburg they decreased by 51.5 p.c. In Italy and France there were slight increases which, however, fell short of the expansion rates of the imports from third countries. Insofar a connection between the granting of preferences and the development of imports seems imaginable — though by no means conclusive — only in the cases of the Federal Republic and the Netherlands.

At first, the modificatory statement must be made that the expansion of imports from the AAMS has happened on a very low level. So the AAMS's market shares increased only to 6.6 p.c. in the Netherlands and to 12.1 p.c. in the Federal Republic. The high expansion rates have little indicative value and might probably fall off slightly in future. This opinion gets support from consumer habits. In the Federal Republic and in the Netherlands — as well as in Belgium-Luxemburg and Italy — consumers prefer Arabica-coffee of which the AAMS-states are able to deliver only very limited quantities. Only in France there is a prevailing demand for the slightly bitter Robusta-coffee which is typical for the AAMS (market share in 1971 almost 63 p.c.). In this case the traditionally close relations with the former African colonies have very probably had an overwhelming influence on consumer behaviour, while in the other EC-states a stronger expansion of demand for Latin American produce could be noticed. The fact, that a heavy expansion of imports from the AAMS did not take place, can be explained by the removal of quotas for third countries in 1964.

An additional explanatory factor for the improvement of AAMS's position in the Federal Republic and the Netherlands is the demand for instant coffee, which is comparatively strong in these countries. Since the production of instant coffee on the basis of the cheaper Robusta sorts is more profitable, there arise additional chances for the AAMS-countries' sales. In the other EC-States, however, the demand for instant coffee remained comparatively insignificant.

If it is assumed that the preferences have been important at least for the demand for Robusta for instant coffee, it must be indicated that the relief effect of the coffee-tax tends to compensate the preferential advantages (e.g. in the Federal Republic). Since coffee is taxed on a quantitative basis, the cheaper Robusta-coffee is burdened relatively heavier than the Arabica sorts. Altogether it can be stated that the granting of preferences has very probably not led to a favoured position of the AAMS and thus not to a sensible discrimination of the producer countries on any of the EC-markets.

Over-Estimate of Preferences

The poor results of the preference policy can be demonstrated most clearly by using bananas as an example. Though in this case high preferences had always been existing (20 p.c. since January 1, 1970), the AAMS' market share declined from 27 p.c. in 1963 to 13 p.c. in 1971. Causal for this development was above all the comparatively high price of the AAMS-products in connection with their inferior quality. Although meanwhile the qualitative difference could, at least partly, be eliminated through the plantation of superior sorts, there is still a much higher demand for Latin American bananas which through a wide advertisement campaign have been made branded goods.

With this it was of decisive importance that the world banana market is to a great extent dominated by international fruit-companies, which — compared to the AAMS — have a good financial standing and dispose of their own sales channels and plantations (in Latin America). They could register great success on the Italian market which had been protected until 1965. Only in France are their sales possibilities still limited by market regulations. This is why in France the AAMS have a relatively high — nearly constant — market share of roughly 33 p.c.

Apart from this, the effect of the preferences is to a considerable degree limited by the fact that the Federal Republic is granting tariff-free import quotas to third countries, which altogether are higher than the actual imports. Insofar the EC-preferences have by no means led to a discrimination of third countries.

The over-estimate of the preferences in the international discussion is indicated also with the global analysis of the counter preferences which have often been criticised. Here a discrimination of third countries conditional on the preferences can very probably be eliminated, too. As far as a shift to the loss of third countries occurred, it is to a great extent traceable to other promotional measures of the EC-states (e.g. industrialisation policy in Italy) and above all to the EC's agricultural policy.

Transferability of the Findings

From the EC's tariff preferences for the benefit of the associated states no (respectively, no sensible) discriminations have emerged for third countries. Here it was decisive above all that the margin of preference represents only one element of the price, and that the price is just one determinant of the demand for a product. The trade

Shares of Selected Export Products of the AASM, Greece and Turkey in the Quantitative Imports of the EC-countries

(In p.c.)

Product	FRG		France		Italy		Netherlands		Belg./Lux.		EC-countries	
	1960	1971	1960	1971	1960	1971	1960	1971	1960	1971	1960	1971
Raw coffee	1.8	12.1	70.1	62.9	22.2	15.1	1.0	6.5	22.6	11.0	29.1	25.5
Raw cocoa	14.5	57.1	85.0	82.5	13.0	31.1	34.2	59.3	24.3	56.2	33.9	60.7
Cocoa-paste, Cocoa-butter	—	19.3	68.7	96.2	0.9	74.9	0.1	11.6	—	1.7	19.3	41.1
Bananas	0.2	—	30.0	33.0	91.0	17.0	—	—	26.0	—	20.0	13.0
Peanut-oil	—	1.4	95.4	72.0	—	24.1	—	1.4	—	— ³	65.3	40.7
Raw tobacco	¹ 18.6	13.8	14.2	6.8	29.4	7.4	1.6	1.9	6.8	4.4	12.6	9.0
	² 6.2	10.3	6.1	10.2	20.2	2.8	0.6	1.7	2.4	6.0	4.9	8.0

¹ Greece. ² Turkey. ³ 1970: 11.9 p.c.

Source: Derived from Statistical Office of the European Communities, Foreign Trade, Analytical Tables, Import, different volumes.

diversions, which have been discovered, can virtually be attributed to factors like consumer habits, qualitative requirements, fluctuations of harvests, traditional relations between exporting and importing countries, market power of the importers, or the removal of quantitative restrictions. Another essential, though hardly quantifiable, determinant might have been the Community's development aid. As far as the association is connected with a favoured treatment of the countries concerned relating to the grant of development aid, and special measures are taken for the direct sales promotion of the preferential goods, development aid can become a decisive factor. As yet, however — regarding for example the projects of the European Development Fund — such an orientation of development policy can at the most be registered with cocoa.

The criteria for the selection of the analysed goods guarantee a highly representative exploration. Thus its results seem transferable to other commodities, with which — due to a different customs clearance — diversion effects may have emerged, as well as to other association and preferential agreements. With slight modifications this might also apply to processed agricultural products² and to semi-processed and processed industrial goods. It must be considered, though, that in cases of almost homogeneous export goods, which are subject to a severe price competition between associated and non-associated countries, a considerable margin of preference may well have some influence on the competitive position. For that raw cocoa can be regarded as a typical example.

Introduction of the Preferential System

If, however, the preferences — like they usually do — apply to more differentiated goods and the margins of preference are low, then they miss their real aim — the creation of competitive advantages of the associated states vis-à-vis the third countries. Thus, the removal of this one-sided preferential treatment in favour of a general grant of preferences to all developing countries would in most cases bring no decisive deteriorations for the associates. On the other hand, the European Community would have the political advantage of being no longer exposed to corresponding reproaches.

The introduction of a general preferential system is also suggested by the following points:

☐ Zero-tariffs have already been introduced for important exports of the preferential states (e.g. caoutchouc, cotton, sisal, tea, tin, cobalt, copper, calcium phosphates, skins and furs).

☐ After the expansion of the preferential area by the joining of the Commonwealth countries, the hitherto associated states will have to share their one-sided preferences with a higher number of competitors.

☐ General tariff reductions can be expected as results of the GATT round.

☐ The EC-members have engaged themselves to extend their general preferential system.

All these points might result in a further decreasing importance of the preferentialisation in the framework of the EC-association policy³. Consequently they suggest the introduction of general preferences.

Coordination of Policies Necessary

With regard to the diminishing importance of tariff policy in the framework of development policy the European Community should lend greater weight to measures in the field of financial and technical cooperation, especially support for diversification and marketing as well as guarantees for export incomes. These measures, which have been mentioned in the memorandum of April 1973, would enable the carrying-through of a more purposive development policy free of disputes relating to commercial policy.

The heavier concentration on measures in the field of financial and technical aid, however, should urge the member-states' governments to conceive a common European development policy. Additionally, efforts should be made to provide for a coordination of regional, agricultural and development policy, because measures in the framework of the European regional and agricultural policy can substantially contribute to development aid if they promote structural changes and let the less competitive sectors have subsidies only for a transitional period. This would reduce the need of import restrictions as the labour-intensive industries, which are dominating in the developing countries, as well as the processing and non-processing agricultural economy belong to the branches of business which in the industrial countries benefit from the highest protection.

² An exception are agricultural products which are competing with products of the Community. In these cases substantial advantages could be granted to the associated states by reductions of price-adjustment levies and/or the removal of quantitative restrictions.

³ See Kommission der Europäischen Gemeinschaften (Commission of the EC), Memorandum der Kommission an den Rat über die künftigen Beziehungen zwischen der Gemeinschaft, den gegenwärtigen AASM sowie den im Protokoll Nr. 22 der Beitrittsakte genannten Ländern in Afrika, im Karibischen Raum, im Indischen Ozean und im Pazifischen Ozean (Memorandum of the Commission to the Council about the future relations between the Community, the present AASM and those countries in Africa, the Caribbean, the Indian and the Pacific Ocean mentioned in protocol No. 22 of the enrollment), Luxemburg, March 4, 1973, p. 15.