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Intereconomics

*Suggested Citation:* Hasse, Rolf (1975) : A new model with old problems?, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 10, Iss. 8, pp. 238-242, <https://doi.org/10.1007/BF02929273>

This Version is available at:

<https://hdl.handle.net/10419/139244>

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## *Stabilization Fund of Lomé*

### A New Model with Old Problems?

by Dr Rolf Hasse, Cologne \*

**The stabilization of export earnings from primary commodities within the framework of the Convention of Lomé was eulogized as a "historic event", "a gleam of common sense in this world" and an approach to a general solution. How is this agreement to be judged?**

With the aim of remedying the harmful effects of the instability of export earnings and thereby enabling the ACP states to achieve the stability, profitability and sustained growth of their economies, the Community shall implement a system for guaranteeing the stabilization of earnings from exports by the ACP states to the Community of certain products on which their economies are dependent and which are affected by fluctuations in price and/or quantity."

Thus Article 16 under "Title II: Export earnings from commodities — Chapter 1: Stabilization of export earnings" of the Convention of Lomé.<sup>1</sup> It was because of this passage in particular that the Lomé Convention between the nine EC states and 46 states in Africa, the Caribbean and the Pacific (the "ACP states") was eulogized as "a historic event", "a gleam of common sense in this world", "a new model" and "the beginning of new economic relations between industrial and non-industrial countries."<sup>2</sup>

After a more judicious appraisal it must still be said that the arrangement for the stabilization of the earnings from important primary commodities marks indeed another milestone — like the raising of the prices for oil and the outcome of the UN Conference on Raw Materials in 1974 — in the recent international discussion about basic products. For the stabilization fund is not a solitary agreement about one commodity but embraces a multitude of products at one and the same time. In comparison with it the arrangements concerning trade cooperation; industrial cooperation; financial and technical cooperation; provisions relating to establishment, services, payments and capital movements and institutions pale into in-

significance. The latter are, in part, very far-reaching and well-endowed financially<sup>3</sup> but do not eclipse the preceding association conventions.

After negotiations which had lasted from July 25, 1973 to February 1, 1975 this fourth Convention of the EC with developing countries was signed in Lomé, Togo, on February 28, 1975. It had been preceded<sup>4</sup> by

□ the first Convention of Yaounde — Yaounde I — of June 1, 1964;

□ Yaounde II, in force since January 1, 1971, with 19 associated African states and Madagascar (AASM) and — since June 30, 1973 — the island of Mauritius; and

□ the Convention of Arusha, also in force since January 1, 1971, with the three East African states of Kenya, Uganda and Tanzania.

These conventions expired on January 31, 1975. That the number of associated developing countries was increased followed from the accession of Great Britain to the EC. Great Britain had demanded for the developing countries of the Commonwealth the same benefits as had been granted to the former French colonies (AASM). Under Protocol No. 22 of the Act of Accession the Community not only undertook to put the 20 developing countries in the Commonwealth on a par with the

<sup>3</sup> 3,015 mn units of account, exclusive of the stabilization fund. The definition and conversion rate of the units of account was fixed by the Council of Ministers specifically for the Lomé Convention by decision of April 21, 1975. According to this 1 unit of account is equal to DM 0.828, £ 0.0885, ffr. 1.15, Lire 109, hfl 0.286, sfr. 3.66, dkr. 0.217, and Irish £ 0.00759. (Cf. European Communities Gazette, 18th year, No. L 104 of April 24, 1975, p. 35.)

<sup>4</sup> Cf., amongst others: A. Fernandes, Die Assoziierung der Afrikanischen Staaten und Madagaskar (AASK) mit der Europäischen Wirtschaftsgemeinschaft (EWG) und das afrikanische Streben nach wirtschaftlicher Integration (The Association of the African States and Madagascar (AASM) and the European Economic Community (EEC) and the African Aspiration for Economic Integration), Freiburg 1974; K. Fasbender, H. Hasenpflug, F.-J. Jäger, D. Kobschull, Die Auswirkungen der Assoziierungs- und Präferenzabkommen der EWG auf die Struktur des Welthandels (The Effects of the EEC Association and Preference Agreements on the Pattern of World Trade), Hamburg 1973.

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<sup>1</sup> Text: European Communities Gazette, 18th year, No. L 136 of May 28, 1975. Lomé Dossier, reprinted from "The Courier", No. 31, special issue.

<sup>2</sup> Cf. *ibid.* pp. 16/17. — The Convention in the News: Frankfurter Allgemeine, No. 28 D of February 3, 1975; Neue Zürcher Zeitung, overseas edition, No. 27 of February 3, 1975; Bulletin of the European Communities, 8th year, No. 1, 1975, pp. 6 ff.

AASM states but (in the third part of this Protocol) affirmed its willingness to consider special provisions for raw materials.<sup>5</sup>

This was the basis of the proposal by the EC Commission on April 4, 1973 to devise a mechanism for the stabilization of earnings of the ACP states from altogether seven main export products<sup>6</sup>. The Community thereby offered to create an instrument against which it had always held out previously. The attempts by France between 1964 and 1967, for instance, to create common equalization funds or a stabilization fund for bananas from AASM states had always failed.<sup>7</sup> When a satisfactory solution had apparently been worked out for the questions relating to maximum financial cost, reference period and determination of territories of origin, the EC states gave their assent to the proposal although they felt great misgivings on grounds of economic order and financial policy.

### The Stabilization Fund (STABEX)

The criteria for the selection of commodities for the stabilization of earnings and the mode of stabilization are: employment, deterioration of the terms of trade between the Community and the ACP state concerned, level of development and problems of transport (least developed, landlocked or island). Twelve major and seventeen subsidiary products – a total of 29 products – were included in the system of *individual* export earnings stabilization (Article 17), instead of the seven commodities which had been suggested by the EC Commission.<sup>8</sup> Special provisions were made concerning sugar.

The financial allocations for STABEX have been limited to 375 mn units of account<sup>9</sup>, and this sum

<sup>5</sup> "... the Community will make it its business to safeguard the interest of all the countries (AASM and Commonwealth countries in Africa, the Indian and Pacific Oceans and the Caribbean) the economy of which depends to a large extent on the export of basic products, especially sugar. The case of sugar shall be dealt with in this light and bearing in mind the importance of sugar exports to a number of these countries, more especially Commonwealth countries."

<sup>6</sup> Bananas, cotton, groundnuts and groundnut oil, cocoa, coffee, copper, sugar.

<sup>7</sup> Cf. R. Biskup, R. Clapham, J. Starbatty, *Dirigismus versus Marktwirtschaft in der EWG. Das Beispiel der europäischen Bananeneinfuhr (Dirigisme versus Market Economy in the EEC – The Example of the European Banana Imports)*, Untersuchungen des Instituts für Wirtschaftspolitik an der Universität zu Köln, Vol. 19, Cologne 1969.

<sup>8</sup> 1. Groundnut products, (a) groundnuts, shelled or not, (b) groundnut oil, (c) groundnut oilcake. 2. Cocoa products, (a) cocoa beans, (b) cocoa paste, (c) cocoa butter. 3. Coffee products, (a) raw or roasted coffee, (b) extracts, essences or concentrates of coffee. 4. Cotton products, (a) cotton, not carded or combed, (b) cotton linters. 5. Coconut products, (a) coconuts, (b) copra, (c) coconut oil, (d) coconut oilcake. 6. Palm, palm nut and kernel products, (a) palm oil, (b) palm nut and kernel oil, (c) palm nut and kernel oilcake, (d) palm nuts and kernels. 7. Raw hides, skins and leather, (a) raw hides and skins, (b) bovine cattle leather, (c) sheep and lamb skin leather, (d) goat and kid skin leather. 8. Wood products, (a) wood in the rough, (b) wood roughly squared or half-squared, but not further manufactured, (c) wood sawn lengthwise, but not further prepared. 9. Fresh bananas. 10. Tea. 11. Raw sisal. 12. Iron ore, iron ore and concentrates and roasted iron pyrites.

will be, corresponding to the duration of the Convention, divided into five annual instalments of 75 mn units of account. Provision has however been made that the instalment of any one year may be exceeded by up to 20 p.c.<sup>10</sup> and that residual amounts may be carried forward to the following years. The transfers in principle take the form of currency loans which are *free of interest* though *repayable* and paid out on application *with no strings attached*.

The conditions governing the drawing and repayment of STABEX currency loans are rather complicated. All exports (fob) of the product groups to the Community ("inclusive of the inward processing arrangements made there in order to be processed") qualify, but a right to compensatory transfers arises only when during the year preceding the year of application, earnings from the export of the product or products to all destinations represented at least 7.5 p.c. of the ACP state's total earnings from merchandise export (Article 17 para 2). For sisal this "dependence threshold" has been fixed at 5 p.c. and for the 34 least developed, landlocked and island ACP states at only 2.5 p.c. (Article 24)<sup>11</sup>. The dependence threshold is thus extremely low. Furthermore, it has been stipulated that an ACP state may apply for compensatory transfers only when its actual earnings from exports of individual commodities to the Community, considered separately, have for the whole of a calendar year been at least 7 p.c. below the reference level. For the 34 ACP states this "fluctuation level" is, according to Article 24, as low as 2.5 p.c. The reference level is the average of the export earnings (quantity and price) during the four years *preceding* the year of application; it is thus calculated anew for each year.

The currency loans must be paid back in the five years following the disbursement if the unit value of the exports is higher than the reference unit value and the quantity actually exported to the Community is at least equal to the reference quantity (Article 21 para 3).

This asymmetry between the calculation of the reference level (quantity multiplied by unit value) and that of the sums to be repaid (in which quantity and unit value are not treated alike) may be illustrated by the following example:

Reference level: The value of reference is 10,000 – quantity 100, unit value 100.

<sup>9</sup> Cf. footnote 3. On June 20, 1975 the resources of STABEX amounted to DM 1,142 mn or £ 215.13 mn. European Communities Gazette, 18th year, No. C 140 of June 21, 1975, p. 1.

<sup>10</sup> The maximum amount STABEX can disburse in one year is thus: 75 mn units of account + 15 mn units of account = 90 mn units of account.

<sup>11</sup> All ACP states except Cameroon, Ivory Coast, Ghana, Equatorial Guinea, Guyana, Kenya, Liberia, Malagasy, Nigeria, Senegal, Sierra Leone and Zaïre.

Case 1: The actual receipts are 8,000 – quantity 80, unit value 100: The ACP state is entitled to ask for a transfer of 2,000.<sup>12</sup>

Case 2: The actual receipts are 11,000 – quantity 100, unit value 110: In this case the actual unit value is higher than the reference unit value. The ACP state must pay back 1,000.

Case 3: The actual receipts are 14,000 – quantity 140, unit value 100: The ACP state is not required to repay anything because the actual unit value does not exceed the reference unit value.

STABEX does not bear the features of a solidarity fund, but it is a simple credit fund. Repayments are made by ACP states only within the limits of the transfers received.

There are several *discretionary* clauses which tend to *cushion* these clear-cut provisions:

□ By decision of the Council of Ministers<sup>13</sup> the list of products may be enlarged after twelve months already. In a statement on Article 17 the EC states merely affirmed that they were on

grounds of principle refusing to include more mineral products in the list.

□ In special cases<sup>14</sup> the stabilization system can be applied to *all* exports of the products concerned irrespective of the country of destination.

□ The 24 less developed ACP states (Article 48) are entirely exempt from the obligation to pay back transfers which they have received. The other states are only exempt if the level of their export earnings is such as not to allow full or partial repayment and the Council of Ministers cancels the obligation to make repayment.

Elements which tend to *stiffen* STABEX are, in addition to the ceiling on allocations, the following two provisions:

□ An application for compensatory transfers is not admissible if it appears on examination that the fall in earnings from exports to the Community of the products in question is the result of a trade policy measure of the ACP state concerned adversely affecting exports to the Community in particular (Article 19 para 4a).

□ Consultations will be held between the EC-Commission and the applicant ACP state if significant changes are noticed in the latter's exports in order to determine whether these changes may have an effect on the amount of the transfer and if so to what extent.

### Benefits and Problems

The dependence of the ACP states upon the products covered by the Convention is in many cases very great but there are considerable differences (cf. Table 1). The importance of trade with the nine member countries of the EC for the ACP states is shown by the figures for 1970: The Community was their most important trading partner, purchasing 54 p.c. of the exports and supplying 44 p.c. of the imports (for Africa alone the figures were 60 and 55 p.c., respectively). The stabilization of the export earnings may be expected to secure some of the mentioned objectives for the ACP states: enhanced stability, maintained import capacity, steady growth, a more equitable balance of payments, avoidance of a further deterioration of the rates of exchange, of withdrawals of capital and of interference with trade and capital movements.

<sup>12</sup> Attainment of the "fluctuation level" (a deviation from the "reference level" by 7 or 2.5 p.c., respectively) is only one condition which has to be fulfilled to justify a payment. It emerges from the agreement that the compensatory transfer amounts to 100 p.c. of the difference between actual earnings and reference level.

<sup>13</sup> A new institution. It consists of the members of the EC Council of Ministers, the EC Commission and one representative of each of the Governments of the ACP states.

<sup>14</sup> According to a statement on Article 17 para 4 this regulation at present concerns Burundi, Ethiopia, Guinea-Bissau, Ruanda and Swaziland.

Table 1

### Shares of STABEX-Products in Total Exports of Some ACP States 1973

Botswana	leather and hides (9 %)
Burundi	coffee (86 %), cotton (3 %), leather and hides (6 %)
Cameroon	cocoa (23 %), coffee (26 %), timber (12 %)
Central African Republic	coffee (23 %), timber (21 %), cotton (18 %)
Chad	cotton (69 %)
Congo People's Republic	timber (42 %)
Dahomey	palm products (34 %)
Ethiopia	coffee (38 %), leather and hides (13 %)
Fiji	coconut oil (5 %)
Gabon	timber (32 %)
Gambia	groundnuts, incl. oil and cattle-cake (94 %)
Ghana	cocoa (61 %), timber (19 %)
Ivory Coast	cocoa (15 %), coffee (23 %), timber (29 %)
Jamaica	bananas (4 %)
Kenya	coffee (22 %), tea (11 %)
Liberia	iron ore (71 %)
Madagascar	coffee (30 %), sisal (3 %)
Malawi	tea (17 %), groundnuts (7 %)
Mali	cotton (39 %), groundnuts (7 %)
Mauritania	iron ore (73 %)
Niger	groundnuts (15 %), groundnuts oil (9 %)
Rwanda	coffee (61 %), raw hides (4 %)
Senegal	groundnuts and groundnuts oil (35 %)
Sierra Leone	iron ore (10 %), palm kernel oil (5 %)
Somalia	bananas (26 %), copra (45 %)
Sudan	cotton (56 %), groundnuts (9 %)
Swaziland	cotton (3 %)
Tanzania	coffee (19 %), cotton (13 %), sisal (9 %)
Togo	cocoa beans (26 %), coffee (13 %)
Tonga	copra (50 %)
Uganda	coffee (66 %), cotton (15 %), tea (5 %)
Upper Volta	groundnuts and groundnuts oil (8 %), cotton (22 %)
Western Samoa	cocoa (28 %)

Taken from: Lomé Dossier, op. cit., p. 28.

Nevertheless one must not make the mistake of disregarding or underrating the problems which are inherent in this kind of earnings stabilization. A *beneficial* and novel feature of the arrangement is that the prices of primary commodities are not fixed directly but determined by the market. STABEX resembles the British system of deficiency payments, albeit on a world scale, in that compensatory transfers are made only for the difference between the reference level and the lower level of actual export earnings.

*Problematic* features of the arrangement are that

□ the stabilization of earnings may tend to solidify the economic structure of the ACP states and to delay or impede the diversification of the export pattern at the right time;

□ there is reason to fear that the resources of STABEX will not be adequate for the attainment of

**Table 2**

**Model Calculation on Prices, Price Developments, In- and Outpayments of STABEX from 1975 to 1979 for Raw Cocoa**

	Model 1	Model 2	Model 3
Price 1971	228.85		
" 1972	263.75		
" 1973	526.07		
" 1974	897.11		
Reference level 1975	47,894	47,894	47,894
Price 1975	360.00	380.00	452.75 <sup>1</sup>
Transfer (+) / repayment (—)	+ 11,894	+ 9,894	+ 2,619
Reference level 1976	51,173	51,673	54,147
Price 1976	340.00	420.00	452.75
Transfer (+) / repayment (—)	+ 17,173	+ 9,673	+ 8,872
Reference level 1977	48,786	55,579	58,217
Price 1977	320.00	480.00	452.75
Transfer (+) / repayment (—)	+ 16,780	+ 7,579	+ 12,942
Reference level 1978	47,928	54,428	56,384
Price 1978	300.00	510.00 <sup>2</sup>	452.75
Transfer (+) / repayment (—)	+ 17,928	+ 3,428	+ 11,109
Reference level 1979	33,300	44,750	45,275
Price 1979	295.00	550.00	452.75
Transfer (+) / repayment (—)	+ 3,500	— 10,250	± 0

<sup>1</sup> Price multiplied by assumed sales volume of 100 units = actual earnings of 45,275. Since these earnings amount to 94.5 p.c. of the reference level, the ACP states can only claim transfer payments according to Article 24 (fluctuation level 2.5 p.c.).

<sup>2</sup> As with 1; the actual earnings reach 93.7 p.c. of the reference level.

Notes: The prices from 1975 to 1979 reflect hypothetical figures.

Model 1: Gradually declining cocoa prices.

Model 2: First declining, then again vigorously and continuously rising cocoa prices.

Model 3: Constant price on a high level (as of June 21, 1975).

Reference level: It is assumed that the sales volume is to be constantly 100 units. This is a favourable assumption, 1. because higher quantitative sales raise the reference level and thus payments still further; 2. because anyway only the unit value counts for the calculation of repayments.

Source: Monthly Price £/t, Ghana Cocoa in London. From 1971 to 1974 real prices. Cf. Federal Statistical Office, International Monthly Figures, May 1975, p. 52.

the desired objectives. If the ceiling should have to be raised on political grounds, the cost to the EC states would be greater than anticipated. This thesis is based on the following reflections:

(a) The reference level of the average of the four preceding years will for some time to come be very high because the commodity boom of 1973/74 will still form part of the reference period. As a result almost all states will apply for transfer payments for all the listed products and the ceiling will be punctured. Moreover, it is to be expected that for some time no repayments will be made (cf. Model calculation in Table 2). From this example it is clearly to be deduced that in the event of a gradual decline and stabilization of the world market price at a high average level it must be expected that payments will be made only to ACP states (Models 1 and 3), and, even if after the current depression in the commodity markets is over, prices were to rise sharply, repayments would at the earliest fall due when the years 1973 and 1974 have been left behind in the reference level calculations (Model 2). Until 1978 the disbursements will on balance exceed any repayments, with the result that STABEX will suffer a severe financial strain, and probably a penetration of the ceiling, in the first five years. Results similar to those shown in the model must be expected for most other raw materials because they experienced similarly strong price rises in 1973/74. The example of cocoa is in this respect typical.

(b) The possibility of trade being rerouted through ACP states cannot be ruled out entirely, especially if the reference level is very high.

(c) The ACP states could increase their outputs and offer larger quantities. If in that case the price were to fall away (price elasticity larger than 1), compensatory transfers would be required owing to the declining price ("minimum price effect").

(d) Difficulties would also arise if STABEX — as has been suggested<sup>15</sup> — were to be financed by a trade levy similar to that under the cocoa agreement (quasi-duty effects).

(e) The special arrangement for the 24 less developed ACP states and the tendencies indicated here make it unlikely that repayments would be made. The revolving loan principle of STABEX would thus be negated.

### The Provisions for Sugar

In the provisions for sugar the EC has gone a step further. It has undertaken to absorb an amount of cane sugar equivalent to 1.28 mn tons of white sugar annually for an indefinite period at

<sup>15</sup> Cf. Die Welt, No. 93 of April 22, 1975, p. 9.

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a price not lower than the intervention price. The ACP states have undertaken to supply such a quantity. To the extent of the purchase guarantee the imported sugar is treated like the domestic product for which the benefits of the Sugar Market Order can be claimed. For the first 18 months of the agreement the EC has accepted a higher guaranteed price: 2,553 units of account per metric ton for cane sugar and 3,172 units for white sugar.<sup>16</sup> The guarantee price will be negotiated afresh each year; it will be between the standard price and the intervention price.

The EC successfully resisted the demand that the price of sugar should be stabilized at the excessive price of 1974. Great difficulties are however to be expected. The world market price of sugar has fallen away rapidly (January 3, 1975: £ 455 per ton; June 1975: £ 135 per ton<sup>17</sup> and is now once more below the EC intervention price of £ 155 per ton.<sup>18</sup> This makes the supply of sugar to EC countries an attractive proposition for the ACP states.

The financial burden on the EC will be the heavier the further the differential between the low world market price and the higher intervention price widens and the less successful are the efforts to keep the self-supply ratio in the EC below 100 p.c. Without allowing for the extension of the acreage under sugar, H. Bujard<sup>18</sup> expects for 1975/76 already a white sugar production of 9.8 mn tons as compared with a demand of 10.3 mn tons. This corresponds to a self-supply ratio of 95.1 p.c. If allowance is made for a small increase in the sugar acreage in response to the 15. p.c. rise of the market order prices for the farming year of 1975/76 decided upon in February 1975, the self-supply ratio may be put at close to 100 p.c. The ACP sugar would in this eventuality have to be bought in and "dumped" in the world market with the assistance of subsidies, which would depress the world market price or keep it down to its low level. With a self-supply ratio of 100 p.c. the financial burden on the EC of taking up the ACP sugar (cane sugar to the equivalent of 1.28 mn metric tons of white sugar)<sup>19</sup> would be £ 198.4 mn, i.e. — at an exchange rate of £ 1 = DM 5.15 — DM 1,022 mn.

<sup>16</sup> On June 20, 1975, this corresponded to £ 146.46 per metric ton of cane sugar and £ 181.97 per metric ton of white sugar.

<sup>17</sup> Cf. Die Welt, No. 10 of January 13, 1975, and No. 149 of July 1, 1975.

<sup>18</sup> The sugar prices were raised by 15 p.c. in February 1975: the standard price from 278.80 to 320.50 units of account and the intervention price from 264.80 to 304.50 units of account per ton of white sugar. The unit of account has been equal to £ 0.509741 since and the intervention price is thus £ 155.22. Cf. Bulletin of the European Communities, 8th year, 1975, No. 2, p. 40, and No. 3, p. 42.

<sup>19</sup> This figure is based on the quantities mentioned in the Lomé Convention: Article 3 of Protocol No. 3 concerning ACP sugar — 1,221,500 metric tons — and Appendix XXI (Sugar originating in Belize, St. Kitts-Nevis-Anguilla and Surinam) — 58,200 metric tons. The small quantity which India may supply has been left out of account.