

South Asia's Exports to the EEC — Obstacles and Opportunities



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and Ann Weston

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List of Abbreviations

ASEAN	—	Association of South East Asian Nations
BTN	—	Brussels Tariff Nomenclature
CAP	—	Common Agricultural Policy
CCA	—	Commercial Co-operation Agreement
CET	—	Common External Tariff
cif	—	commission insurance freight (ie including transport costs)
dc	—	developed country
EEC	—	European Economic Community
EP	—	Effective Protection
fob	—	free on board
GSP	—	Generalised System of Preferences
HSR	—	Health and Sanitary Regulations
IIFT	—	Indian Institute of Foreign Trade
JC	—	Joint Commission
JDI	—	Joint Declaration of Intent
ldc	—	developing country
LTA	—	Long Term Agreement
MFA	—	Multi-fibre Agreement
mfn	—	most favoured national
mnc	—	multinational company
msa	—	most seriously affected
MTN	—	Multilateral Trade Negotiations
NTB	—	Non-tariff Barrier
QR	—	Quantity Restriction
SITC	—	Standard International Trade Classification
ton	—	metric ton (unless otherwise stated)
UNCTAD	—	United Nations Conference on Trade and Development
VAT	—	Value-added Tax
VER	—	Voluntary Export Restraint

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1 Historical and Institutional Background

Introduction and Origins of the Study

This study of commercial relations between the European Economic Community and the four countries of South Asia, India, Pakistan, Bangladesh, and Sri Lanka is one of a succession of pieces of research by ODI on various aspects of the policy of the Community towards developing countries. The study was motivated by a belief that if the Community is to have trade and aid policies towards developing countries which are credible, and creditable, a reasonable test for these policies is that they should relate in a constructive way to four countries which between them account for 40% of the population of the developing world outside China.

This introductory chapter gives a largely descriptive account of commercial relations between the European Economic Community (EEC) and the four countries of South Asia and explains how they have developed into their present form. Subsequent chapters will seek more precisely to evaluate the access problems facing South Asian exporters to the Community in general and by product, and the extent to which commercial policy changes could assist them. An attempt is also made to place issues of market access and commercial policy in a wider economic and political context.

Scope

In defining the study we have made a series of assumptions and limitations. First and perhaps most important, we have assumed that there is genuine content and potential in a set of bilateral international commercial relationships. To some, this might seem to concede too much to the philosophy of bilateralism in trade. They believe, as do the authors, that it is mainly through multilateral trade negotiations, and general internationally enforceable rules, that the trading interests of ldc's, and others, can best be promoted. Unfortunately the reality is markedly different from the ideal, and it is within the context of the former that reforms have to be effected. This context includes bilaterally negotiated trade quotas (for access to the Community) for textiles, garments, jute products, sugar, and some lesser items. It is heavily influenced also by the misleadingly entitled Generalised System of Preferences (GSP) under which certain developed countries, such as the EEC, give preferential tariff treatment to ldc's, though in practice the operation of safeguard mechanisms make it highly discriminatory. Above all, the South Asian countries, which have experience of a long history of trade with the Community in which initially they were tied to one European colonial power, have subsequently had to adapt to a complex and discriminatory hierarchy of

Community preferences based primarily on different geographical zones of influence—other West European countries, Lomé, Mashraq, Maghreb, and so on. It is unsurprising therefore that they have sought to influence Community commercial policy through developing bilateral links of which the four South Asian Commercial Co-operation Agreements (CCAs) are the most important tangible sign.

This particular study is however concerned only with one side of the bilateral relationship and that is South Asian access to the EEC market. This is mainly because it has never been at issue that South Asia should offer formal reciprocity on tariff or non-tariff barriers (NTBs). This is not to say that India, at least, could not begin to do so. Nor does it disregard the wider issue of mutual interests—in fact Chapter 2 is partly devoted to this. A further reason is that the relationship is asymmetrical. The EEC market accounts for a far higher proportion of South Asian exports than vice versa. EEC exporters are well placed to take advantage of whatever additional foreign exchange is spent by importers in the four South Asian countries. South Asian exporters by contrast face a considerable measure of discrimination in the EEC market.

A third assumption is that it is useful to talk about South Asia as representing more than a contiguous area on the map. The common interest of the four countries derives from the Joint Declaration of Intent (JDI)¹ made at the time of UK entry by the enlarged Community, which aimed to safeguard the position of the Commonwealth Asian countries, which for all practical purposes has included Pakistan. These countries found themselves outside the framework of association under the Lomé Convention. Nor were they eligible for the special status given to Commonwealth countries in the Mediterranean. Of the Asian 'Seven Outside'², Hong Kong was excluded from the scope of the Joint Declaration of Intent. Malaysia and Singapore chose to pursue their commercial policy interests through the Association of South East Asian Nations (ASEAN).³ The four South Asian countries were thus left in a residual category whose common characteristics have been reinforced by similar CCAs with the EEC, by experience of joint negotiation over GSP, and by improving bilateral relations in the subcontinent. However the political and economic ties within South Asia are as yet very tenuous. Sri Lanka, in fact, is contemplating an alignment with ASEAN. Moreover there are great differences of interest and in bargaining power between India at one extreme and Bangladesh or Sri Lanka at the other. India is unique not only in South Asia but in the world for its combination of extreme poverty on the one hand and sophisticated industrial development on the other. It is also a substantial manufacturing exporter in its own right even in markets, like West Asia, in which it does not enjoy preferential terms. In the EEC context, its exports are so diverse that specific access problems, while in absolute terms more important than others of the subcontinent, are less constricting. Pakistan, with the beginnings of a manufacturing export base but less diversity, has found itself with perhaps the most

serious access problems of all the four countries. It faces substantial barriers on its main exports to Europe (textiles, clothing, rice), and potentially on carpets, sports goods, and tobacco. Sri Lanka and Bangladesh are almost entirely concerned with primary and semi-processed commodities at present. In the study these divergent interests will be brought out as well as the extent to which South Asian interests benefit from common treatment and joint representation to the EEC.

Fourth, we have chosen to focus mainly on EEC policy rather than on the policies of European national governments. This is justified to the extent that tariff policy is now determined at EEC level; also, anti-dumping policy, important NTBs such as agricultural levies, the terms of textile import ceilings under the Multi-Fibre Agreement, and the administration of CCAs. However in parallel with EEC-level agreements are EEC-national agreements which have the same basic principles and institutions as those at Community level,⁴ and these are arguably more important in some instances. Most NTBs remain under national control (as is discussed in detail in Chapter 5). Moreover national governments retain responsibility for wider issues of economic and foreign policy, and it is misleading to discuss EEC policy without referring to the underlying blend of European national interests which it represents. Thus of crucial importance in determining the degree of liberal access accorded to South Asian exports has been the influence of Britain on one hand and France and Italy on the other—though Germany and Denmark appear to be replacing Britain as the main protagonists of a liberal import regime.

Fifth, we have, in general, confined ourselves to trade and commercial relations knowing that this excludes such important contributory factors to economic co-operation as investment flows, aid, foreign policy, and migration, though these will be touched upon where relevant. In general, in the Community's external relations, these factors tend to reinforce each other; those groups closest in trade terms, like the Mediterranean region and the African, Caribbean, and Pacific members of Lomé, also have priority in aid, technical, and industrial co-operation. Although some progress has been made in developing a Community programme of 'non-associate' aid, magnitudes, even including food aid, are derisory. In any event the Community rejected in 1972 a proposal by India that a broad CCA covering wider issues than trade should be signed. Although the CCAs themselves, and restrictive interpretations of the area of co-operation by the participants, preclude our ranging too far, it would be wrong to discount the influence of non-economic factors on bilateral relations. They are relevant because 'as if by an invisible hand the concessions that one nation can, without threats, obtain from another are rationed; good will cashed on one issue is not available for another'.⁵ The treatment of immigrants, defence interests, aid, and textile quotas are linked, even if loosely.

Sixth, we are concerned primarily with public policy issues, though in practice most of the actors in trade are private businessmen and consumers and many barriers to trade are not susceptible to government control. There already exist private links through chambers of commerce, of which the Indo-German is perhaps the most dynamic, and bilateral friendship societies. More negatively, it is probable that the low import penetration by South Asian exporters in—say—France is due less to official obstruction than to the conservatism and lack of concentration of the French retail sector and to their own lack of enterprise. Similarly their failure to meet health and safety standards in several European countries is due more to genuinely poor quality control and carelessness than to NTBs. There are two extreme views about the role of government in ‘commercial co-operation’. One is highly *dirigiste*, as in the type of trade agreements India has with the Soviet Union and Eastern bloc. At the other extreme a government’s role could simply be that of improving information flows and reducing uncertainty (eg financing South Asian participation in trade fairs and business trips; providing investment guarantees for European foreign investment in South Asia) but working within an essentially market economy framework. Most participants in commercial co-operation negotiations have been trying to find common ground between the two extreme approaches, but this is difficult when the enthusiasm for *dirigisme* varies considerably between governments and over time. As is shown below all four South Asian governments are now more market-oriented than several years ago and this broadly corresponds to the modest expectations Community members have of the role of the Commission in day to day commerce.

Finally the fact that we focus on market access problems does presume that we give this some weight relative to supply factors: the availability of industrial capacity, inelasticity of agricultural production, labour relations, entrepreneurship, favourable exchange rates and export credit policy, shipping availability and rates. It became clear during the course of the study, however, that supply factors were almost certainly as important as access in explaining the export performance of South Asia relative to other developed and developing countries, and that the immediate gains from improved export policies were probably somewhat greater than from better market access. More detailed work carried out in the subcontinent, by the World Bank among others, supports this judgement. Substantial steps have recently been taken in all South Asian countries to make the economies more export oriented and to remove the more obvious domestic bottlenecks. Although commitment to this new approach varies, and is qualified, tentative, and possibly temporary, market access seems likely to be more of a problem in the future than supply constraints, particularly given the swing to protectionism in Europe. It also acts as one determinant of the speed at which the Asian countries reform their economy internally; those arguing for less autarchic policies can do so with more conviction if the rest of the world is doing likewise.

Historical Background

Before UK Entry to the EEC

Until Britain first applied to join the EEC in 1961, recorded expressions of interest in European integration by South Asians were few and largely hostile, though tentative interest was shown by the Indian government in 1960. British negotiations for entry precipitated the first serious consideration of the possible costs that might derive from loss of Commonwealth Preference and the new barrier of the EEC's Common External Tariff (CET) in the British market. Negotiation led to provisional agreement between the EEC and the UK that the enlarged EEC would enter into a comprehensive trade agreement with India, Pakistan, and Sri Lanka by 1966. The CET would be applied progressively on textiles and jute; it would be eliminated altogether on bulk tea, spices, and minor industrial products (eg sports goods) and partially on handloom textiles and some tropical products. UK quantity restrictions on jute imports would be phased out. Otherwise, there would be no relief from the CET. According to one estimate, acceptance on broadly these terms would have led to a short term loss (for India) equal to approximately 10% of the value of its exports to the UK followed by more favourable long term effects.⁶

The terms became largely academic when the negotiations lapsed, but the issue of access to the EEC market (without the UK) remained a live one. The EEC Council of Ministers rejected suggestions from the Commission that even in the absence of the UK, the Community should have trade agreements with the (then) three countries. The EEC put into effect agreed tariff suspension on bulk tea (though imports of tea still faced an import turnover tax and, in Germany, an additional excise duty), spices and sports equipment. Tariffs were cut on several other items in the context of the Kennedy Round of multilateral trade negotiations (MTN), but in the case of cashew nuts and whole peppers the preference margin was maintained in favour of states associated under the Yaoundé and Arusha Conventions.⁷ Germany unilaterally lifted quota restrictions on imports of jute products. There was pressure for further tariff concessions (on coir, carpets, leather, jute, ground pepper, mushrooms, prawns, tropical fruit, and juices) which went largely unheeded. Agreements were reached (with India and Pakistan) on textile and jute quotas, the former in the context of the Long Term Arrangements. India proposed over the 1967-70 period various changes which were to remain the major issues in the next few years; first, a system of preferences for ldfs incorporating tariff quotas for such sensitive items as tobacco, second, long term commercial co-operation in marketing new products and joint ventures in third countries. As far as the three other South Asian countries are concerned, there is little trace of any lobbying by them at this time.

Little progress was made and attention shifted to the final stages of the Kennedy Round in 1967 and in 1968 to the second session of the United Nations Conference on Trade and Development (UNCTAD). But changes were taking place independently which were affecting the basis of the earlier assumptions concerning UK entry. The value of Commonwealth preferences in the UK market was being eroded by the increasing share of Britain's trade with non-Commonwealth countries, including the European Free Trade Agreement (EFTA), which enjoyed tariff free preference on industrial goods, and by most favoured nation (mfn) tariff reductions under the Kennedy Round (eg on tobacco, clothing, footwear, leather, spices, and textiles). The gradual extension of protection to cotton textiles by tariffs and quotas (as for jute), even if initially with South Asian interests in mind, was a further loss. There remained however tariff preferences, albeit reduced on most products, and quota restrictions on non-Commonwealth sugar—the latter of some value to India. In the EEC market, meanwhile, the CET was being eroded by some modest tariff cuts under the Kennedy Round, but the margin of discrimination against Commonwealth Asia was widened by concessions to African states under both the association agreements.

Partly as a consequence of these changes, though possibly due more to the commodity composition of their exports and to supply constraints, the share of exports from all four South Asian countries, particularly India, fell sharply in both the UK market and the market of the six original EEC members (the EEC-6). In the EEC-6 it fell from 0.8% in 1960 to 0.4% in 1970 (from 0.4% to 0.2% in the case of India). In the UK market, access to which was relatively unrestricted, the fall was significantly worse—from 4.8% to 2.0% for all four South Asian countries (3.3% to 1.2% for India).

Not only was the deterioration of the South Asian market share greater in the UK but the slower growth of the UK economy meant that the value of preferential access to it was becoming less important. The share of Pakistani exports to the UK in total Pakistani exports fell from 17.4% in 1960 to 10.4% in 1970 but only from 16.9% to 13.2% to the EEC-6. For India the share fell from 27.6% to 11.6% for the UK and 7.7% to 6.5% for the EEC-6, while the share of exports to the UK in total Sri Lankan exports fell from 28.2% to 22.8% and to the EEC-6 from 10.2% to 9.0% over the same period. Even so these magnitudes suggest that there was still a much greater interest in the UK market; in 1970 India's exports to the UK were worth \$235m as against \$131m to the EEC-6 and Sri Lanka's were \$76m as against \$30m. By contrast, Pakistan, and later Bangladesh, had a significantly greater interest in the European market. In 1970 Pakistan's exports to the EEC-6 were worth \$95m while UK only took \$75m. In general, static trade analysis suggested a more pessimistic outlook as a result of the loss of preferential links with the UK at the time of UK entry than was really justified given the declining importance of the British market.

The Generalised System of Preferences and UK Entry

The introduction of a GSP by the EEC-6 in 1971 and another by the UK in 1972 was mainly significant for eroding further the differential access barrier for South Asia between EEC and British markets. Attention was later to shift to the relative generosity of the two systems. But, considered as a separate issue from UK entry, the introduction of a relatively liberal GSP in the UK helped to eliminate much of the remaining value of Commonwealth preferences for ldfs by extending equal treatment to competitive ldfc suppliers such as Brazil, Taiwan, and Korea. The EEC scheme, however restrictive, represented a reduction in CET on many manufactured items and a reduction in *existing* discrimination in favour of African suppliers. This was later offset, but only in part, by further concessions to a large number of countries under the Lomé Convention. It is not the purpose of this publication however to rehearse the complex origins of the GSP. This is done satisfactorily elsewhere and its contemporary relevance is discussed in Chapter 3.

South Asia got worse terms from UK entry in 1973 than were negotiated in 1962. There was no special trade agreement, no special transitional period above the five years allowed to the UK for the alignment of its tariffs to the CET and the elimination of Commonwealth preferences. GSP harmonisation took place largely on EEC rather than UK terms which entailed two specific drawbacks. First, there was very limited preferential access on agricultural items included in Chapters 1 to 24 of the Brussels Tariff Nomenclature (BTN) and none at all on products covered by the EEC's Common Agricultural Policy (CAP). Second, strict tariff quotas and country ceilings were placed on sensitive products, limiting tariff free access on 53 items of interest to ldfs, over and above items which were subject to the Long Term Arrangement (LTA) on cotton textiles, including shoes, leather and other leather products, wood products, toys, sports goods, electronic components, and simple iron and steel products. The scheme for manufactures was neatly described at the time by Richard Cooper: 'it is most generous for those products in which the developing countries are least competitive, and the most generous quotas are for those products, such as jet aircraft and advanced computers which the developing countries have little hope of exporting for many years, duties or not. In contrast, it offers little incentive, or none at all, to expand exports of those products which are currently of greatest interest to the developing countries, for such exports must pay, or expect soon to pay, the full tariff duty'.⁸

One helpful gesture to the South Asians was the JDI, which did not, however, commit the EEC very far: 'the EEC is ready, from the date of accession, to examine with these countries such problems as may arise in the field of trade with a view to seeking appropriate solutions, taking into account the effect of the generalised tariff preference scheme and the situation of other developing countries in the same geographical area'.⁹ It is now possible to review with

hind-sight, as we do in detail in Chapter 2, the extent to which in practice the GSP system of the enlarged EEC (EEC-9) has evolved in respect of coverage, preferential margins and safeguards provisions. It is however worth quoting some of the observations made at the time, of which many were negative.

'The result of British membership of the EEC, on present terms,' (ie by applying EEC-GSP terms to UK and EEC imports) 'will be to worsen the conditions on which Commonwealth Asian countries export to Britain. India stands to lose a great deal from the phasing out of remaining Commonwealth preferences in the British market. Pakistan will also lose ... By contrast Bangladesh and Sri Lanka, the majority of whose trade enters duty-free on mfn terms, have few Commonwealth preferences to lose. EEC enlargement will create new discrimination against Commonwealth Asian non-associables, which can only be partially offset by GSP access, whatever system is adopted by the enlarged Community'. (P. Tulloch)¹⁰

'On the whole we fear that India's losses in the British market are very unlikely to be balanced by gains in the rest of the EEC'. (M. Lipton and J. Firn)¹¹

'It has been demonstrated that the enlargement of the EEC would cause considerable erosion in the value of preferences accorded to developing countries, first because all of Europe would become a free trade area in manufactures, and because Britain and Denmark would adopt the EEC scheme, which is more restrictive than their own'. (M. Kreinin)¹²

'... the conclusion that such enlargement would involve a serious threat to the trade interests of less developed countries is one which is difficult to avoid'. (David Wall)¹³

Since these conclusions were drawn, EEC discrimination against non-members and non-associates has been consolidated: first, by the Lomé Convention which gives preferential tariff access to 53 African, Caribbean, and Pacific states, as well as NTB preference eg in the renegotiated and stricter Multi-Fibre Agreement (MFA); second, by preferential terms for Mediterranean, Mashraq, and Mahgreb countries and third, by the now real prospect of full EEC membership for Greece, Spain, and Portugal. Against this has to be set the progressive if limited improvement in the scope and degree of preference under the GSP.

In spite of this history, there is no discernible nostalgia amongst South Asian negotiators for the pre-entry period. Some Asian officials have expressed strongly the view that earlier studies were based on static and pessimistic assumptions that have been invalidated by subsequent developments. In

particular they point to the progressively shrinking weight of the British market in Europe and the boost which enlargement has given to German interest in the Indian subcontinent as a source of low cost imports and future industrial joint ventures. They also claim that in the context of preferences the EEC has shown willingness under pressure to make at least some meaningful concessions. The main setbacks have been over NTBs, notably on textiles, where Britain, not the former 'Six', led the protectionist demands within the EEC. In any event South Asian perceptions of the costs of UK entry have now been emphatically altered by the effects of other factors altogether more important, such as the onset of world recession, and its effects on all developed countries' attitudes to access for competing ldc goods.

EEC-South Asian Relations After UK Entry

The methods employed in practice to carry out the spirit of the JDI have been, essentially, three:

(1) GSP Liberalisation

The most important have been GSP concessions of particular interest to South Asia. The main changes have been, first, to obtain free access on almost all manufacturing items (BTN 25-99) except textiles and jute. The number of items on the non-textile sensitive list has been cut from 53 to 13. Problems for South Asia remain also for tobacco (although the tariff quota was raised in the 1977 offer), footwear, travel goods, and carpets. These still represent a major component of Pakistan's manufactured exports to the EEC but are of decreasing importance to India which has been more successful in diversifying to take advantage of the GSP. Second, concessions are being sought based on the principle of special provision under the GSP for the least developed ldc's, which as presently defined include Bangladesh, but not the other three. The EEC Council of Ministers accepted the principle in 1975 but to date the only concession offered has been the exemption of the least developed countries from the maximum country amount rule which normally applies to products subject to ceilings, such as tanned leather, textiles, and clothing. (The operation of the GSP is explained in detail in Chapter 3.) In the case of textiles and clothing this exemption has little value as imports from the least developed countries face quantity restrictions (QRs) under the MFA. (The impact of quantity controls on EEC textile imports is examined in Chapter 6.) Third, the GSP or MTN approach, where appropriate, was used to obtain concessions on tropical products. Concessions have been given for pepper, some tropical fruits and vegetables, tea bags and other items but problems still remain for some marine products, rice and some fruits and vegetables. In 1977 the four South Asian countries jointly submitted to the EEC a list of requests for improvements in the EEC's GSP of 1978. This submission reflects rather less enthusiasm for the progress being made under the GSP than several years earlier, expressing concern

with, first, the virtual absence of action resulting from the decision to give particular attention to the poorest ldc's, second, the disturbing downward trend in utilisation of GSP opportunities, and third, the continuing problems encountered by exports to the EEC of vegetables, fruits, ethnic specialities, rice, marine products, tobacco, leather and leather goods, textiles, and jute products. Furthermore they felt these disadvantages were accentuated by recent agreements between the EEC and the Maghreb and Mashraq countries.¹⁴

(2) Sectoral Agreements

The second approach has been through sectoral agreements for silk and handloom cotton fabrics, handicrafts, coir, jute, and cotton textiles (see Table 1.1). The jute and coir agreements effectively phase out tariffs but QRs remain on jute (EEC level QRs on some items, national QRs on others) and on French imports of coir mats. Textile negotiations have been conducted under the MFA; quota coverage has been considerably extended in product terms, discrimination made explicit against non-Lomé, non-EFTA suppliers, and there has been a considerable curbing of the maximum rates at which the volume of textile imports may grow.¹⁵ Sectoral agreements have not, so far, solved access problems, merely codified them.

(3) Commercial Co-operation Agreements

The EEC-India CCA¹⁶ was signed on 17th December 1973, to become effective 1st March 1974 for 5 years. The distinguishing feature was the emphasis given to the potential complementarity of the Indian and EEC economies. Both exports from the EEC to India as well as Indian exports to the EEC would be expanded on the basis of 'comparative advantage and mutual benefit' (Article 1). This marked a significant departure from the basic philosophy of the GSP under which any increase in Indian exports to the EEC was seen to involve sacrifice on the part of the EEC. The growth of EEC-Indian trade would stem from reciprocal mfn treatment (Article 2), attempts to diversify in a complementary fashion (Article 4), and co-operation in exports to other ldc's (Article 5).

The task of defining what was meant by areas of mutual interest or potential co-operation and how such co-operation would be effected, was left to the Joint Commission (JC), set up under the CCA (Article 7). The JC was required (Article 9) to study possible means of: (i) developing economic and commercial co-operation, (ii) overcoming tariff and non-tariff barriers, (iii) developing complementary trade and marketing structures, and (iv) exchanging information. Under Article 10 it was to ensure the proper functioning of any sectoral agreements. Another important element of the CCA was Article 12 which attempted to define the relationship of this agreement to pre-existing bilateral trade agreements between individual EEC members and India.¹⁷ These were to be replaced by the CCA only to the extent that their provisions were either incompatible or

Table 1.1 The Network of Trade Agreements between South Asia and the EEC

	Duration
Bangladesh-EEC	
Commercial Co-operation Agreement	1/12/1976 to 30/11/1981
Agreements on Trade in:	
— jute products	1973 to 1980
— handicrafts	1974 (unlimited)
— silk and handloom cotton fabrics	1974 (unlimited)
India-EEC	
Commercial Co-operation Agreement	1/3/1974 to 28/2/1979
Agreements on Trade in:	
— silk and handloom cotton fabrics	1968 (unlimited)
— handicrafts	1969 (unlimited)
— coir products	1969 to 1980 ^a
— jute products	1970 to 1980 ^a
— cotton textiles	1962 to 1981 ^a
Pakistan-EEC	
Commercial Co-operation Agreement	1/7/1976 to 30/6/1981
Agreements on Trade in:	
— handicrafts	1969 (unlimited)
— silk and handloom cotton fabrics	1970 (unlimited)
— cotton textiles	1962 to 1981 ^a
Sri Lanka-EEC	
Commercial Co-operation Agreement	1/12/1975 to 30/11/1981
Agreements on Trade in:	
— handicrafts	1973 (unlimited)
— silk and handloom cotton fabrics	1975 (unlimited)
— coir products	1973 to 1980 ^a
— cotton textiles	1977 to 1981

Note: ^arenewed at intervals.

identical with those of the CCA. Finally it is worth noting that although the European Commission's negotiating directive did not allow for tariff concessions, it was able to consolidate and make binding certain concessions on tea, whole pepper, cardamoms, and East India kips, which it had previously granted autonomously.

The CCAs between the EEC and Sri Lanka, Pakistan, and Bangladesh¹⁸ became effective on 1/12/75, 1/7/76, and 1/7/76 respectively, also for five years. Negotiations were closely modelled on the Indian agreement. Unlike India, however, these countries had little of the initial substantial infrastructure of bilateral agreements and private sector links, and the agreements represented therefore something more tangible. There were also certain differences, of which the most important was that the EEC sought non-discriminatory 'access' to natural resources in all three countries. Pakistan and Sri Lanka rejected this request as the EEC was not prepared to make a reciprocal guarantee on behalf of its members. Bangladesh suggested that its most abundant natural resource, labour, might enter the EEC free of restrictions—to the horror of EEC negotiators! Only Bangladesh was prepared to sign the access clause for certain sectors and then as a means of encouraging EEC private investment in its economic development. Bangladesh also promised to improve the terms on which foreign firms could invest there. The details were not however spelt out in the agreement, largely because France was against the EEC having power to negotiate in matters of economic co-operation (ie investment as opposed to trade). Thus although the Bangladesh agreement avoided any explicit reference to foreign investment the clause on access to raw materials made a gesture in that direction.

Another difference lay in the binding of tariff concessions already given by the EEC which were included in Annexes to the Agreements. Whereas Bangladesh and Sri Lanka both benefitted—Bangladesh to the extent of nine items, Sri Lanka six items—Pakistan gained not even this, despite seeking tariff cuts on cotton yarn, leather, and sports goods as well as levy cuts on rice. This resulted from Pakistan's apparent misunderstanding that the Agreements could lead to *negotiations* on tariff cuts, whereas all that was possible was ratification of earlier concessions. Otherwise, the details of the Agreements were similar to the EEC-India CCA. All set up JCs to carry out the supervision.

The extent to which the formal structures have led to substantive progress is set out in more detail in subsequent chapters. Progress is difficult to evaluate when major issues of interest, notably textiles and the GSP, have been for the most part kept out of JC sessions. The EEC-India JC has covered, in the course of six meetings, a good deal of ground including assistance for Indian export promotion (eg of engineering goods) and for an exchange of delegations of computer firms, discussions on leather tanning leading to a visit of European tanners to India (but not to any change of trade policy at either end), talks on technical problems in oilcake supply and the quality of tobacco, tea bagging, co-operation in coal and pelletised iron ore supply to Europe, and a consultant's report which sought to define thirty industries where India could boost its exports to the Community. At the last meeting agreement was reached on the establishment of an Indian Trade Centre in Brussels to be jointly financed by the Community and the Indian Government for an initial period of three years. Co-operation has also extended to joint projects in third countries. The EEC-

Pakistan JC has met once, in April 1977, as a result of which a subcommittee was set up to look into Pakistan's ability to act as a subcontractor, supplying simple engineering goods, and the possibilities of improving this by technical co-operation. Joint ventures in tanning and leather goods, fisheries and electronics were sought as well as help with tobacco processing and crustacean marketing, and a general commitment by the EEC to help with the promotion of Pakistani exports in the EEC and the establishment of a trade agency. The EEC pressed Pakistan to reduce export restrictions on hides and semi-tanned leather and refused to discuss the import of shoes. There was no communiqué and apparently sharp disagreement over textiles, rice, and leather. The first and only meeting of the EEC-Bangladesh JC covered similar ground, with Bangladesh requesting joint ventures in leather, fisheries, and forestry. In addition the Community has run a seminar in Dacca on the GSP. Sri Lanka's JC has also met once but this meeting was largely confined to a general exchange of views, which were in any event overtaken by a change of government in Sri Lanka and a subsequent change in its export policies.

In seeking an evaluation of progress made in general on EEC-South Asian relations it is necessary to consider, by contrast, progress in the EEC's treatment of other groups of ldc's.

The EEC's Hierarchy of Commercial Relations

For reasons which are rooted in the earlier, pre-UK entry, history of the EEC, the Community has developed an enthusiasm for dealing with different groups of non-members on a preferential basis. Though this offends basic GATT principles and irritates other developed countries considerably, the practice has become even more important in recent years with the signing of the Lomé Convention and a series of trade agreements with Mediterranean countries. It is possible to visualise the commercial (and other) relationships in a hierarchical form which Table 1.2 tries to convey. However there is a considerable gap between theoretical and effective access for ldc imports. For example, the United States pay full CET and enjoys no preferential status but following successive rounds of GATT negotiations tariff barriers are now negligible for almost all manufactures, in which the USA has an interest. On the other hand the most favoured ldc or Mediterranean suppliers still face access barriers on some of their exports to the EEC due to safeguard provisions; such as Botswana with beef, Spain, Portugal and Greece with textiles, citrus fruit and wine. For the countries concerned these are substantial interests. Nor do the less developed Lomé countries have the capacity to avail themselves of very liberal access for manufactures. Despite this South Asia ranks well below Lomé signatories in terms of trade and aid preferences.

Table 1.2 The Hierarchy of the EEC's External Trade Relations in 1978

Countries	Agreement	Trade Provisions
(1) EEC (Belgium, Denmark, France, Germany, Italy, Ireland, Luxembourg, the Netherlands, UK)	Treaty of Rome (1957) Treaty of Accession (1973)	Free trade in all goods. Common external tariff on imports from third countries.
(2) EFTA (Arusha, Finland, Iceland, Norway, Portugal, Sweden, Switzerland)	European Free Trade Agreement (1973 for an unlimited period)	Free trade in all manufactures.
(3) 53 African, Caribbean and Pacific countries	Lomé Convention (1975 for 5 years)	Duty free access to the EEC for all industrial and many agricultural goods, though one or two products subject to safeguard clauses. Some concessions for leviable agricultural products. QRs on bananas, beef, sugar and rum; all products are also covered by a general safeguard clause.
(4) Applicants to the EEC Greece	Association Agreement (1962) providing for full customs union by 1984	Duty free access for all industrial goods, except steel and coal, and a range of agricultural goods. Volume of cotton products not restricted under the MFA but limited by VER.
Spain	Preferential Trade Agreement (1970) working towards customs union	60% duty reductions on most industrial goods; some concessions on agricultural products. Cotton products limited by VER.
Portugal	Free Trade Agreement (1972)	Duty free access for all industrial goods (under EFTA); some concessions on agricultural products. Cotton products limited by VER.
(5) Maghreb countries (Algeria, Morocco, Tunisia)	Preferential Trade and Co-operation Agreements (1976 for an unlimited period) ^a	Duty free access to the EEC for most industrial goods. Tariff concessions on some agricultural goods.
(6) Mashraq countries (Egypt, Jordan, Lebanon, Syria)	Preferential Trade and Co-operation Agreements (1977 for an unlimited period) ^a	Duty free access to the EEC for most industrial goods. Tariff concessions on some agricultural goods. Egypt's exports of cotton products are restricted under the MFA.
(7) Other Mediterranean Countries Turkey	Association Agreements providing for full customs union with the EEC (1964 for unlimited period)	Duty free access for industrial goods except some textiles, coal, steel and petroleum products; some concessions on agricultural products. Cotton products subject to VER.

Countries	Agreement	Trade Provisions
Malta	(1971 for 5 years) ^b	From 1978 duty free access for industrial goods, some concessions on agricultural goods. Cotton products subject to VER.
Cyprus	(1973 for 4 years) ^b	70-100% duty reductions on most industrial goods; some concessions on agricultural goods. Cotton products subject to VER.
Israel	Preferential Trade and Co-operation Agreement (1975 for an unlimited period)	Duty free access for most industrial goods; substantial concessions on 85% of agricultural goods.
Yugoslavia	Non-preferential Trade Agreement (1973 for 5 years)	JC set up to promote economic and commercial co-operation. Cotton products restricted under the MFA.
(8) Other ldc's (except Taiwan)	Generalised System of Preferences ^c	Duty free access for all industrial goods—for some 180 products duty free treatment is subject to quotas. Duty reductions on nearly 300 agricultural goods, of which 3 are subject to quotas.
(9) 16 ldc's (Argentina, Brazil, Colombia, Hong Kong, India, Korea, Macao, Malaysia, Mexico, Pakistan, Peru, Philippines, Sri Lanka, Singapore, Taiwan, Thailand)	Bilateral Agreements under the MFA (1978 to 1983)	Varying restrictions on the volume of cotton products which may be exported to the EEC (restrictions to be administered by the exporting country).
(10) 27 other ldc's		Imports of cotton textiles from each country restricted to an equal volume (restrictions to be administered by the EEC).
(11) South Asia (India, Sri Lanka, Pakistan, Bangladesh)	Commercial Co-operation Agreements (1974, 1975, 1976, 1976 respectively, each for 5 years). Sectoral Agreements	Commitment to promote trade with the assistance of JCs. Promoting trade, research and development, better marketing, of a few exports to the EEC. But imports of jute and coir products face QRs.
(12) Latin America (Argentina, Brazil, Uruguay, Mexico)	Non-preferential Trade Agreements (1972, 1974, 1975, 1976 respectively for 3 to 5 years) ^b	Reciprocal liberalisation of trade and co-operation in the agricultural sector. Special provisions on beef and veal for Argentina and Uruguay.
(13) China	Non-preferential Trade Agreement (1978 for 5 years)	Reciprocal granting of mfn treatment for all products. Removal of restrictions on most EEC imports from China being considered, except textiles.

Notes: ^a subject to periodic review

^b can be extended automatically

^c this is a unilateral offer by the EEC rather than a binding agreement.

What does this mean in practice? For manufactured products (BTN 29-90) South Asia enjoys tariff free access on GSP terms for all but a small number of sensitive items. Sectoral agreements and 'voluntary' export restrictions (VERs) act as a further restriction on access for textiles, clothing, jute, and coir. Lomé countries face none of these restrictions and free access is underwritten by a binding agreement (unlike the GSP) though it is subject to safeguards. Safeguards also apply to duty free access by EFTA industrial exports and Portuguese textiles have been subject to controls. Most South Mediterranean associates enjoy free access, subject to exemptions, eg restrictions on refined petroleum products, cork and textiles. Others are working towards a customs union with the EEC (Spain, Greece, Cyprus, Malta, Turkey). Free access without qualification would follow from EEC enlargement to embrace Greece (and eventually Spain and Portugal). In general, although the GSP has been substantially liberalised, its limitations of scope, uncertainty and complexity render it inferior to the terms on which goods from almost all other countries enter the EEC except for a small number of OECD countries and the Communist bloc.

The EEC agricultural policy is very complex and varies by product as well as by country. In general South Asian countries and other GSP beneficiaries enjoy no preferential access where *CAP products* are concerned. This is not however a particularly serious matter since only a few of their products are affected (molasses, tobacco, rice, and vegetable oils) and there have been some concessions under GSP, for instance on tobacco. By contrast Lomé countries face quantitative ceilings, but not levies, on beef. They have however obtained levy reductions on certain products including rice, millets, maize, and oranges, and have duty free access (subject to safeguards) for vegetable oils, tobacco, and wine. The Mediterranean countries have less generous but tangible advantages mainly in the form of levy cuts for citrus fruits and various vegetables including tomatoes, and in the case of Spain and the Maghreb, wine and olives. In respect of *processed agricultural products* there has been some progress under the GSP with tariff reductions on fish products, processed and preserved fruit, and vegetables, but bigger concessions have been given to the Mediterranean countries while the Lomé countries have been allowed duty free access (though for processed CAP products they have still to pay some of the levy). 'A sober assessment of the Community's GSP might be that despite all the idealism that went into its creation, it has so far only operated to reduce the domestic prices for Community users of imported raw materials, without affecting any of the Community's vital interests in agricultural production or processing'.¹⁹

In the field of commercial or industrial co-operation it is perhaps too early to evaluate the EEC's recent initiatives which include the South Asian CCAs. It is claimed that the Indian Joint Commission is more active than committees arising from other EEC commercial agreements for instance with Mexico or with the Mashraq and Maghreb countries. It meets more often and formulates more substantive recommendations. However it has little or no resources

to implement its findings. An EEC centre which was to have been established to help India and other GSP beneficiaries to utilise the GSP by providing monitoring and/or market research support, has failed to get off the ground through lack of money. By comparison with the commercial co-operation framework of the Lomé Convention, over and above improved access, aid, and Stabex provisions, achievements are minor. The European Development Fund is able to lend to industrial projects in the Lomé countries (in 1976/77 such loans amounted to one third of all Lomé aid) and the European Investment Bank also lends to Lomé industries (50 mua in 1976/77—1 unit of account (ua) = \$1.2 in 1977). A Centre for Industrial Development, charged with promoting EEC-ACP industrial co-operation, has helped collect information on over 100 projects, half of which were put forward by EEC companies interested in investing in the Lomé countries. The manpower, enthusiasm, and finance, left over for non-Lomé countries are being spread increasingly thinly with existing attempts to establish informal contacts with the Andean and ASEAN states.

Finally, there are political factors. The EEC's interest in the 53 Lomé countries and the Mediterranean basin is clearly inspired by a sense that these are regions in which the Community should play an active political role and have particular influence. In addition frustration with the lack of progress in internal economic unification has recently propelled the Community into a more active foreign policy role. This explains at least part of the interest in a Euro-Arab dialogue and in better links with Comecon and China. With the South Asian countries, however, no such political interest has been aroused despite the absence of dominant interests by other powers (indeed the Indians have recently been eager to diminish the role of the Soviet Union) and the presence of two functioning parliamentary democracies (a strong theme in the EEC's Southern European policy). Certainly this is an omission, on both sides, which goes some way to explain European indifference to a more positive commercial policy towards South Asia. What the Europeans and South Asians might hope to gain from closer links will now be considered.

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3. ASEAN-EEC relations were discussed at length in the *Far Eastern Economic Review*, 21 April 1978.
4. Amongst these are long-standing Indian agreements with Britain (from 1935), West Germany (1955), and France (1959). See Dharma Kumar, *India and the European Economic Community*, London, Asia Publishing House, 1966. See also M. Lipton and J. Firn, *The Erosion of a Relationship: India and Britain since 1960*, London, OUP for the Royal Institute for International Affairs, 1976; and D. Ghai, 'The Enlargement of the EEC and Asian Commonwealth Countries', *Commonwealth Economic Papers No. 2*, Commonwealth Secretariat, London, 1973. Similar agreements exist between Pakistan and Belgium-Luxembourg (1952), West Germany (1957), and Italy (1961), and between Sri Lanka and West Germany (1955).
5. Lipton and Firn, op cit.
6. Dharma Kumar, op cit, p60. The losses would have been mainly on cotton textiles (below 20 counts), handloom cloth, jute sacking and hessian, coir mats, hand knotted carpets, East India kips, castor and linseed oil, essential oils and cashew nuts.
7. The agreements were effective from 1965 and 1971, respectively, to 1975 and gave 21 countries preferential trading status with the EEC. For further details of these relationships see: M.E. Kreinin, *Trade Relations of the EEC*, New York, Praeger, 1974; J. Pinder, 'The Community and Developing Countries: Associates and Outsiders', *Journal of Common Market Studies*, 1, 1973.
8. Richard N. Cooper, 'The European Community's System of Generalised Tariff Preferences: A Critique', *Journal of Development Studies*, July 1972, p381.
9. Joint Declaration of Intent, Treaty of Accession, op cit.
10. Tulloch, op cit, p25.
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14. Joint Submission on the GSP from the Missions of Bangladesh, India, Pakistan, and Sri Lanka to the European Communities, Brussels, 1977.
15. For further details see *The Textile Trade, Developing Countries and the Multi-Fibre Agreement*, ODI Briefing Paper, November 1976.
16. Cmnd. 5746, London, HMSO, 1974.
17. These agreements tend to have objectives and institutions similar to those of the CCAs; they are designed to promote trade and other forms of commercial co-operation, and discussion of these matters is undertaken by joint economic committees. They are usually strengthened by the existence of binational chambers of commerce linking businessmen in India to those in the EEC.
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2 The Economic Basis of EEC-South Asia Relations

Future relations between the Community countries and these four countries which between them account for a large share of the world's most extreme poverty are often portrayed, particularly by those who wish to see Europe doing more, in moralistic terms. It is quite correct, in our view, that concern for the alleviation of poverty, and for reducing differences in income and wealth should be internationalised in this way. But we doubt that the moral imperative is a strong motivation of Western governments especially in their trade policy. If relations between Europe and South Asia are to be put onto a more substantial footing it will be because mutual interests dictate that this should be so. In this chapter we seek to evaluate the extent of these mutual interests. First, we look at South Asian interests and expectations in greater trade with the EEC. Their self-interest in getting better access to the EEC might seem more obvious than the Europeans' but there are still many influential critics in the region who regard closer economic links with Western countries with great suspicion for both economic and political reasons. Second, we look at possible European interests in giving more liberal access to South Asian exports. The notion that South Asia has more to offer than an insatiable appetite for charity may be an unfamiliar one for many European policy-makers and segments of public opinion, but it is central to our argument.

Part I South Asian Export Priorities and Potential

The interest of the four countries in raising the rate of growth of their exports, and consequently, in overcoming access barriers to major markets, has quickened in recent years. Exports accounted for 8% of Indian national income in 1977/78 having increased steadily from 4.4% in 1970/71. In Sri Lanka they accounted for 20% of national income in 1976 as against 18% in 1971; in Bangladesh 6% in 1976/77 as against 5.5% in 1973/74. By contrast the importance of exports from Pakistan has been generally declining from 14% in 1972/73 to 11.5% in 1975/76 and 8.4% in 1976/77. There are several reasons for concern with export growth. The first is that attempts to raise economic growth can run up against the bottleneck of a shortage of domestic savings relative to domestic investment, which in turn results in a current account balance of payments deficit. This notion of a 'resource gap' has been crucial in much of post-war thinking in all four countries and especially in India and Pakistan but was hitherto seen mainly as a rationale for import substitution.

There is a second motive which underlies some of the enthusiasm for export led growth currently in India, and in Pakistan in the 1960s, based on observation of the apparent success of countries like Korea and Japan. According to this view, export growth is important not only to break the balance of payments

constraint but to stimulate growth directly through the export sector, by providing a new source of demand for industries which have largely exhausted import substitution possibilities. Moreover this new activity could be more labour intensive and less costly in resource terms than the final stages of import substitution. Third, there is what one might call a 'vent for surplus' approach, which gives priority to domestic availability and is not necessarily committed to 'export led growth' in the long term, but sees exports as a useful means of getting rid of excess industrial capacity or excess stocks of commodities and raw materials where these arise as a result of a mismatching of domestic supply and demand. All these three motives are essentially mercantilist in character and offer little room for the traditional neo-classical ways of looking at trade as it is seen in some Asian states, Singapore for example, in terms of the welfare gains from specialisation and the benefits of import competition. There is, however, a fourth school of thought that currently has some influence, notably in India and Sri Lanka, which is endeavouring to promote import liberalisation and a more export oriented economy, not only to overcome bottlenecks, but because of the benefits which they believe could be derived from exposure to international competition.

Although the motives have differed from country to country and over time, there has been in the last two or three years an unmistakable shift in all countries, except possibly Pakistan, towards greater export orientation. Perhaps this marks a decisive shift of direction, the end of a period in which the four Asian countries have been reacting against a colonial heritage where 'free trade' often had unpleasant connotations for those on the periphery; and they now appreciate some of the costs of a pattern of development which is too inward-looking.

(1) Exports to meet the resource gap. Perhaps the best way to assess the extent to which trade performance is a constraint on growth is to look at the actual and planned trade and current account balances. Recent estimates permit us to assess the extent to which the draft Indian Sixth Plan (1978-1983) implies a future balance of payments constraint (see Table 2.1). For the growth target of 4.7% p.a. to be met the Indian government anticipates a trade gap of \$3.2bn in 1982/83 in current prices, while the World Bank, which believes this estimate is inconsistent with savings/investment assumptions, anticipates a gap as large as \$5.8bn. Even at this level, however, the gap does not pose serious problems given the large reserves on which India can draw and the large inflow of remittances from Indian workers overseas.¹ This reflects the quite remarkable transformation in India's external position since 1975, a product of good luck (good harvests leading to reduced food imports) and good management. The most recent (August 1978) provisional figures for 1978/79, however, indicate a sharp deterioration in trade resulting in a deficit of some \$1.2bn to \$1.5bn. Even so, it could be argued that it is India's ability to absorb new investment, including imported capital goods, which is now the constraint on development, not the balance of payments. The planned real export growth, about 7%, is less than the 8.5% planned for the Fifth Plan, though broadly the rate recorded in

the 1972-77 period. In the longer run, the pressure to export in order to stave off balance of payments problems may increase, especially if Indian savings fail to meet ambitious expectations. Given the difficulties in the way of achieving high export growth in traditional items, such as tea, jute, sugar, and spices, India is looking to other sectors which have already shown promise, including clothing, handicrafts, jewellery, chemicals, marine products, and engineering goods.

Table 2.1 India's Balance of Payments (\$m)

	1974/5	1975/6	1976/7 ^a	1977/8 ^a	1978/9 ^b	1980/1 ^b	1982/3 ^b
Exports (fob)	4175	4665	5760	6400	7100	8150	12200
Imports (cif)	5665	6084	5950	6600	7600	10000	18000
Trade Balance	-1490	-1419	- 190	- 200	- 500	-1850	-5800
Current Account (inc. remittances)	-1271	- 855	+ 810	+1170	+1230	- 670	-3530
Reserves	1400	2200	3700	5800	8200	11300	10100

Notes: ^a estimates
^b projections

Source: World Bank

Sri Lanka is in a rather similar situation, though its economy is more precariously balanced. Like India it suffered seriously from the oil price rise of 1973, which aggravated the existing economic depression; real growth averaged 3.8% over the 1960-77 period, less than 1% per head. Good fortune, in the form of a virtual doubling of tea prices, raised export earnings by 37% in 1977 but this is unlikely to continue and official predictions are that the current account will worsen in 1978.

Table 2.2 Sri Lanka's Balance of Payments (\$m)

	1970	1974	1975	1976	1977	1978 ^a
Exports (fob)	339	511	555	556	781	805
Imports (cif)	392	701	757	640	768	1086
Trade Balance	- 53	-190	-202	- 84	+ 13	-281
Current Account	- 71	-178	-187	- 65	+ 45	-263

Note: ^a estimates

Source: World Bank

Any attempt to raise the Sri Lankan growth rate significantly above past trends is likely to result in a serious deterioration in the balance of payments given the smallness of the economy, which has resulted in the exhaustion of even moderately efficient import substitution possibilities and the need to import most capital goods and raw materials. The World Bank believes Sri Lanka can expand its growth rate of 5.5% p.a., but only if exports themselves grow at around 10%, keeping the current account imbalance at around \$200m in 1982. Since the two main exports, tea and rubber, especially the former, are unlikely to contribute much of this growth, exports of coconuts and manufactures would have to increase by over 30% in real terms.

The constraints on Sri Lanka are mild by comparison with those on Bangladesh. Not only has Bangladesh had to cope like the others with rising import costs, notably of oil, but also post-independence reconstruction. A real growth of 5.7% over the last five years has almost restored per capita incomes to the minimal 1970 levels but the balance of trade is so hopelessly in deficit that aid keeps the economy afloat. More recent estimates than those below suggest that there may have been a deficit of \$1bn in 1977/78.

Table 2.3 Bangladesh's Balance of Trade (\$m)

	1969/70	1973/4	1975/6	1976/7	1977/8 ^a	1978/9 ^b
Exports (fob)	479	339	381	421	470	560
Imports (cif)	594	958	1290	865	1360	1395
Trade Balance	-115	-619	-909	-444	-890	-835

Notes: ^a estimates
^b projections

Source: World Bank and UNCTAD

Any attempt to achieve higher growth is likely to cause the payments situation to deteriorate further despite severe import restriction, especially as there is a serious mismatch of domestic savings and investment (savings are only 2% of national income). Thus higher export growth, which means growth of jute and jute product exports plus the handful of items showing signs of successful diversification (fish products in particular, and leather), will be indispensable for more rapid development, unless a fairy godmother is going to greatly increase aid allocations.²

Paradoxically, it is Pakistan, the paragon of export led virtue in the subcontinent in the 1950s, which is now most seriously constrained by its balance of payments. Exports recovered rapidly from the secession of Bangladesh but have slumped in real terms since 1973/74. This combined with rapid import growth, in the wake of large scale public sector investment, and increased oil prices, has

precipitated a serious trade deficit, mitigated only partly by the large flow of remittances from the Middle East. It is estimated that in order for Pakistan to grow at 5.4% p.a. until 1982/83 (as against the 4.1% p.a. experienced in the period 1971/2-1976/7) exports will need to grow at 7.4% p.a. (as against -1.0% p.a. in the earlier period) even with a substantial degree of import substitution holding import growth to 1.7% p.a. (as against 3.1% p.a. previously). The latest Pakistan Five Year Plan (1978-83), to be published soon, apparently envisages 7% real growth, which makes even more ambitious demands on the export sector. This implies growth significantly above recent trends for cotton textiles and other manufactures.

Table 2.4 Pakistan's Balance of Trade (\$m)

	1972	1973	1974	1975	1976
Exports (fob)	936	1014	1047	1163	1117
Imports (cif)	1040	1902	2208	2220	2490
Trade Balance	-104	-889	-1161	-1057	-1373

Source: IMF

The constraint which the current balance of payments may impose on development in the four South Asian countries is further underlined by the low level of foreign exchange reserves; at the end of 1977 its reserves would only have bought two months of imports for Bangladesh, three months for Pakistan, five months for Sri Lanka, and a year's imports for India.

In summary, for Pakistan, Bangladesh, and possibly Sri Lanka significantly greater export growth is needed than that experienced in recent years. For India the pressures are less immediately serious but will probably emerge in the medium-term.

(2) Exports as the engine of growth. Associated with growing awareness of the importance of export growth to help break the foreign exchange constraint on development, a belief has arisen, particularly in India, that export growth is an important development objective in itself. Impressed by the experience of some Far Eastern countries, and by the apparently negative effects of the import substitution route, there are those who argue that exports can make a useful contribution to overall growth. This might seem a potentially small one when trade accounts for less than 10% of GNP but some studies³ have suggested that for every 2.5% growth in export earnings, Indian per capita incomes rose by 1%.

The main impetus behind the search for export markets for industrial products in India has been the stagnation of the internal market, a consequent under-utilisation of capacity, and lack of new investment. Industrial output has risen

less than 40% in seven years constrained by lack of demand and also by power shortages, labour unrest and, in some sectors, lack of capacity. Investment has generally stagnated, particularly in the private industrial sector, accounting for around 14% of GNP for the last decade, never surpassing the peak of 15.4% in 1966/67, while savings have risen steadily over this period from 11% to above 16% of GNP. Thus India is in the unusual position for a developing country of being unable to use its investible surplus, with a major reason being lack of demand. Capacity has been seriously underutilised in many sectors and, in the absence of export growth, could have been much worse. It was underutilisation of capacity, of over 50%, which in 1967 first pushed parts of the engineering industry into substantial exports: diesel engines, steel pipes and tubes, castings and forgings, non-ferrous sheets and circles, cables and wire rope. This explains why exports are seen as strategically important for the industrial sector. Moreover there has been considerable stimulus to employment from the ability of some export industries—garments, textiles, light engineering, and handicrafts—to provide opportunities for labour intensive techniques of production, by contrast with limited opportunities for employment in the public sector heavy industry projects which have traditionally acted as a catalyst in Indian industrial activity.

Even if it were possible to find markets for increased manufactured exports this approach is criticised by people who argue that it is absurd for a country of 600m people (but not so absurd for Sri Lanka) to be looking overseas for markets when these could be generated internally, by income redistribution or other policies which raise the purchasing power of the rural poor.⁴ But even if the will for this kind of programme were present, the means of doing so are not—at least not without significant inflation in the short run which all four South Asian governments, especially the Indian, are committed to fighting. A more far-reaching criticism along the same general lines has been made by people who argue by analogy with experience in Brazil, Korea, Taiwan, and Mexico, that a necessary condition for successful export led growth is severe labour discipline, looser control of private firms, especially multinationals which can gain easier access to developed markets and, in general, political conditions that are inconsistent with the proclaimed objectives of present day leaders in South Asia. For these reasons there are in practice serious limitations on the adoption of a fully-fledged 'export led growth' strategy.

(3) Exports as a vent for surplus. Short of an across-the-board commitment to export promotion there is an attraction in using the world market to dispose of surpluses when *bad planning, temporary excess capacity in scale sensitive industries, or changing patterns of demand, produce a mismatch of domestic supply and demand. This is particularly relevant for agricultural goods when supplies are price inelastic and demand price elastic making it difficult to maintain a stable domestic market. Under the early Five Year Plans in India trade was frequently employed in this way to dispose of surpluses of*

sugar, coal, iron and steel, while more recently exports of tea and vegetables were cut back to guarantee satisfaction of domestic demand. One disadvantage of treating exports in this 'stop-go' way is that a reputation for unreliability undermines future sales. The problem is a major one: a recent study has identified around 20% of India's exports as being of 'essential' food items (notably meat and fish, sugar, groundnuts, pepper and other spices, onions, fresh fruit and vegetables) whose diversion into exports can create (and have created) shortages in domestic markets adding to inflationary pressure and possibly dietary imbalances.⁵ Exports of coconuts, lobsters and shrimps from Sri Lanka face competition with domestic uses. In Pakistan shrimps and other foodstuffs have in the past faced export bans. There is also an indirect conflict of interests between exports and goods for domestic consumption in terms of land use, for example, in Bangladesh jute competes with rice, in Pakistan cotton with food grains. Nevertheless, there may be particular appeal in the export of goods which provide abundant employment but face a limited domestic market, for example made-up garments, handmade carpets, jute bags, semi-polished gems and jewellery.

(4) Trade as a stimulus to competition. The idea, which lies at the heart of neo-classical trade theory, that the gains from trade arise not primarily from increasing exports relative to imports but from the greater efficiency of resource use, is an unfamiliar one in South Asia. Where import liberalisation has taken place it is mainly in facilitating imports of necessary raw materials and equipment. But three of the four governments go some way to accepting the merit of greater competition from imports. In Sri Lanka for example the new government has declared its intention to 'free the economy' and liberalise imports. In India some limited steps have been taken to dismantle quantitative restrictions on imports, despite opposition mainly from competing Indian producers of capital goods and man-made fibres. Even in Bangladesh consideration is being given to relax import controls.

There are three main reasons for liberalisation. One is the wish to reduce the cost of inefficiencies which have arisen from pursuing import substitution with scant regard to resource costs. Some of these costs have fallen directly on exporters (for example, the cost of yarn and cloth to garment makers). A second, deriving from the first, is the hope that the stimulation of greater competition will be anti-inflationary (for example by reducing the cost of capital goods used in major public sector investment projects); at present many firms shielded from competition can increase profits by cutting output and raising prices. A third is the belief that exposure to international competition will help to create a better psychological climate and greater awareness for exporters, which is based on the Japanese experience of the early sixties when import liberalisation sparked off an investment boom. On the other hand voices are being raised in all countries, but especially in India, that powerful lobbies are managing to obtain substantially freer import of 'unnecessary' items, since the

present system of 'import entitlement' encourages firms to be more import-intensive than they otherwise would be. This, it is claimed, is paid for by the poor, to the extent that they carry some of the incidence of taxes which offset export subsidies, and that they pay in higher prices for the non-availability of exported mass consumption items.

To summarise, in each country there is growing awareness of the value of a dynamic export sector but also a more critical awareness than in some Far Eastern and Latin American countries of the cost of using resources for exports rather than domestic consumption and of the political costs of such a strategy if pursued too energetically.

Export Potential and Policies

It is one thing to evolve a more export oriented government philosophy, or even, like India, to produce impressive real export growth over a short period; it is another to convert this into long-term policies and performance. Projections recently made by the World Bank suggest that the South Asian countries could double their manufactured exports in 1985 above the level expected on a trend basis, if they adopted consistently more helpful export policies, with rather less scope, except in Sri Lanka, for making major gains in exports of raw material and food.

Table 2.5 Alternative Projections of Ldc Manufactured Exports: 'Existing Policies' Case (A) versus 'Better Policies' Case (B) (\$m)

	1975	1985		Annual Growth Rate (%)	
	actual	A	B	A	B
South Asia	2900	6250	11800	8.0	15.0
India	2080	4490	8430	8.0	15.0
Pakistan	590	1210	2180	7.5	14.0
Bangladesh	180	430	620	9.0	13.0
Sri Lanka	35	90	480	10.0	30.0
All ldc's	32700	94000	115000	11.1	13.4

Based on: *Prospects for Developing Countries: 1977-85*, World Bank staff study, 1976.

Two sets of projections are made (see Table 2.5). Both assume that in the next decade there will be no net change in the terms of access facing ldc exports to dc markets, since the authors believe the use of emergency safeguards will cancel out the effects of any tariff liberalisation under the Tokyo Round. In addition Case A assumes that existing policies of exporting countries will remain unchanged. Case B, the 'better policies' case, demonstrates what could happen if ldc's adopted policies as favourable to exporters as those in most East Asian countries. The

potential is clearly very large and probably greater than would accrue from improved access under present export policies. The adoption of better export policies could result in exports from India and Pakistan being nearly twice as high in 1985 as otherwise, while in the case of Sri Lanka the increase could be five-fold. It is easy to summarise in general what these 'better policies' are considered to be: exchange rate devaluation to a realistic level, liberal access for foreign investors, firm control of domestic inflation, supporting policies designed to help labour intensive industries.

Since this is a study of EEC access policy rather than South Asian export policies we shall not elaborate in detail upon either the history or the current status of the latter. But it is clear that all four countries are, with varying degrees of conviction and effectiveness, fashioning policy instruments designed to achieve higher rates of export growth than achieved over most of the post-war period. Moreover all four, with the possible exception of Bangladesh for whom the maximisation of raw jute exports is an important goal, are committed to achieve this higher growth primarily by diversification from raw materials, through more processed products and through manufacturing exports in general. The implications for the rest of the world are in general not particularly great; in aggregate South Asia currently accounts for about 9% of ldc manufacturing exports and assuming a real annual average growth rate of 8% will only account for 6.6% of ldc manufacturing exports in 1985 (see Table 2.5 above). Even if maximum policy improvements are effected—which seems unlikely—and the growth rate is 15% p.a., the South Asian share will be little more than 10%. Since the EEC should, on past trends, take about one-quarter to one-third of additional exports, the South Asians are looking to the Community to take an extra \$1bn to \$2bn (at present prices) of manufactured exports from them in eight years time plus some of the growth in exports of largely non-competing raw materials and foodstuffs. Amongst the four countries it is worth recalling that India is likely to account for about two-thirds of this increase. Given the present total level of EEC manufactured imports (\$65bn in 1976) the accommodation of this level of imports should not be a particularly tall order. But their likely concentration in sensitive categories such as clothes and cotton fabrics, leather products and the more standardised engineering items, as well as efforts to add value to raw materials currently processed in Europe (iron ore and hides) present obvious difficulties. Whether the EEC camel is likely to accept these additional straws on its sagging back will ultimately turn on its perceived self interest in South Asia and to that question we now turn.

Part II Complementarity and Mutual Interests

A major theme of the EEC-South Asian Commercial Co-operation Agreements and of the rhetoric surrounding their activities is the idea of 'complementarity' (see for example Articles 1 and 4 of the EEC-Indian CCA) and the idea, closely linked, that co-operation should be based on 'mutual benefit'. Since mutual self-interest is the criterion both sets of countries wish to use it seems appropriate to explore its implications.

At present, European perceptions of mutual interests with South Asia tend to be somewhat negative for two opposing but equally negative sets of reasons. The first, simplifying considerably, is the belief that South Asia is a 'breadbasket' or 'bottomless pit' which will repay with small gratitude and political favours, and irregular export orders, the enormous transfer of resources required to make any discernible impression on its poverty. The second, which applies mainly to India, is the fear that here is a new Japan which might well in the 1980s or 1990s present a serious trade threat. Unlike Brazil it would offer few pickings to European multinational companies and unlike Hong Kong, Taiwan, and Singapore but like Japan the 'threat' is of potentially unmanageable proportions. By contrast, the EEC's preferential treatment by aid and trade under the Lomé Convention of the Ivory Coast, Kenya, or Gabon—suppliers of non-competing raw materials, nice to foreign investors, small, politically pliable—seem to present relatively few problems. While these negative perceptions of South Asia are parodies they do contain a small element of truth; Bangladesh will be dependent on aid givers' generosity for the foreseeable future, and India does show both impressive industrial export growth and relative lack of interest in foreign investment. But this does not mean that there are not important mutual interests. These will be examined under four main headings: 'complementarity' or gains from specialisation through trade; 'reciprocity' which is used here as an umbrella term relating to the balance of gains from a trading relationship; raw material security; and factor mobility.

(1) Complementarity and Comparative Advantage: One of the central tenets of traditional international trade theory is the concept—both positive and normative—that nations do, and should, specialise through trade on the basis of 'comparative advantage'. That this is not merely a theoretical proposition is reflected in the explicit acknowledgement in the CCAs (Article 1 of the EEC-India CCA) that 'comparative advantage' and 'mutual benefit' are inextricably related. A country's comparative advantage, in its crudest form, is based on the production of goods which use its stocks of relatively abundant factors. No profound thought is required to see that in the case of the EEC and South Asia this could lead to South Asia specialising in products using large numbers of unskilled labourers (and certain kinds of skilled workers), or requiring tropical climatic conditions, while the EEC would specialise in products or processes using a high proportion of capital equipment, advanced technology and industrial skills, or requiring a temperate climate. Such a pattern of production would be in a very obvious way 'complementary' and would offer mutual benefits, manifested mainly as reduced prices for consumers but also accruing to producers from efficiency gains.

There are, however, two ways in which this form of complementarity may not coincide quite so neatly with mutual interests. The first is that in order to arrive at a complementary pattern of specialisation there may first need to be competition among producers of particular items. This leads to the so-called trade

adjustment problem. The second is that purely bilateral 'complementarity' may well lead to a more inefficient and costly solution than a multilateral one. Both of these effects can be traced with the help of customs unions theory; the first is comparable to trade 'creation', the second to trade 'diversion'. Customs union theory⁶ tells us that the economic gains of union, resulting in complementary production patterns, are likely to be greater the greater the *initial* degree of competitiveness in product composition (ie the countries should produce the same goods) and the greater the initial disparity in costs. By way of example and to simplify greatly, let us reduce trade between say India and the EEC to three commodities, tea, textiles, and capital goods. The gains from opening up trade and removing barriers arise primarily from the EEC importing more competing textiles and India importing competing capital goods. Where there is bilateral trade in non-competing tea (or, for that matter, any non-competing textiles or other goods) bilateral trade liberalisation or 'co-operation' has little to offer. It can actually be damaging if it promotes bilateral trade in non-competing products, since a better solution in almost every case would be for the importer to buy on the world market. Where South Asian suppliers can compete at world market prices such trade takes place anyway as with tea, raw jute, cotton, coconuts, natural rubber, and more recently frozen shrimps, mica, iron ore, and bauxite. Unfortunately the view is certainly widespread in the EEC that the search for 'complementarity' involves the search for precisely such non-competing items, and, conversely, the avoidance of items which can yield gains from trade 'creation' resulting in genuine complementarity. It is in this bog of misunderstanding over the meaning of 'complementarity' that commercial co-operation has so far been stuck.

The approach adopted here is to reassert the relevance of the concept of 'comparative advantage' to which the CCAs pay lipservice. The most obvious basis for trade is the growing disparity in factor endowments between the regions. This is not the place to resurrect the vast theoretical and empirical literature concerning the Heckscher-Ohlin theorem that the pattern of international trade is based on factor endowments. Nonetheless the theorem has proved an enduring guide, albeit a rough one, to patterns of specialisation. Following scepticism generated by the 'Leontieff paradox' and by the work of Minhas,⁷ recent work, notably by Lary,⁸ Fels,⁹ and Mahfuzur Rahman,¹⁰ has given the theorem persuasive support as an operational idea. These studies show that the relative factor intensities of different industries are significantly correlated between countries, and that patterns of trade (at least in industrial goods) between developed and developing countries can be explained convincingly on the basis of factor endowments. But this and other work reinforces caution. Factor endowments cannot be used as a 'coin in the slot' guide to which industries should be promoted through trade; there are frequent reversals and ambiguities.¹¹

In order to demonstrate the relevance of these results a brief test was made for two countries, the UK and India, for which recent census data are available. Twenty-six categories of industries at three-digit levels were selected (see Table 2.6). For India it was possible to rank the industries by two measures. One was by fixed capital per man employed, a clear measure of physical capital intensity, though one distorted by dubious measures of capital asset values; the other was by the value added per man (following Lary) which indirectly measures the joint contribution of physical and human capital (on the assumption that the unskilled wage rate, therefore the unskilled wage cost per man employed, will be fairly uniform and, somewhat less plausibly, that capital intensity will be reflected in annual profits per man employed). For the UK, the industries were ranked only by value added per man.

Rank correlation analysis shows there is a statistically significant relationship between the two rankings of Indian industries according to the two different measures of capital/labour intensity (Spearman's co-efficient $R = 0.65$) and between British and Indian industries ranked according to the same value added method ($R = 0.68$). There were some marked inconsistencies (which are underlined in the table), between the two Indian measures (for paints and varnishes, pottery, ceramics and china, photographic and optical instruments, musical instruments, footwear, iron and steel) and some apparent 'reversals' of factor intensity between the Indian and UK industries (for leather tanning, printing and publishing, jewellery, watches and clocks). Only in two cases did the two value added rankings differ sharply from the physical 'capital' ranking—paints and varnish, optical and photographic equipment—though in both in the opposite sense from what would have been expected on 'human capital' grounds ie precision optical equipment came out as relatively low on human capital, paints and varnish as relatively high. But it was quite clear that however measured some industries were relatively labour intensive in character—other textiles, clothing, cotton spinning and weaving, leather goods, pottery and china, and bits of the engineering industry: railroad equipment, bicycles and motorbikes. Others emerged as appropriate to the comparative advantage of countries well endowed with capital and advanced technology: petroleum refining, rubber products, miscellaneous and industrial chemicals, non-ferrous metals, cements, non-electrical machinery. Engineering goods tended in general to have a consistent medium ranking which suggests the prospects for a good deal of two way intra-industry trade in engineering goods.

This seems to indicate that for several clearly defined sectors there is scope for gains from inter-industry trade, in the form of consumer benefits, reduced input costs, and greater all-round efficiency. From the South Asia side the list of labour intensive product areas is predictable and already apparent in existing patterns of trade. It is, however, even in its own terms, far from a complete explanation of these patterns. In particular the implications that South Asian exports should be specifically *unskilled* labour intensive and its imports of

manufactures skill intensive may be too static a view. The South Asian countries certainly do not see themselves occupying a narrowly defined segment in the international division of labour, providing items requiring little skill or technology. India, and to a lesser extent, Pakistan, has acquired a large cadre of engineers and skilled industrial workers which seems to give the country a comparative advantage in various metal working industries (though it is necessary to account for the discriminatory subsidies which exist in favour of these industries). As one author points out,¹² 'Indian exports of plant in relatively simple industries like textiles, sugar processing, and cement have been common for some time now. Recent years have, however, witnessed the export of complete plants in sophisticated activities like large-scale electrical generation; complete automatic telephone exchanges; electrical transmission equipment, pharmaceutical plants' and so on. The development of advanced skills is an increasingly important factor also in the cutting and polishing of gems, watchmaking and parts of the handicraft sector.

An additional source of comparative advantage for South Asia results from the way in which many products pass through various stages of the 'product cycle'; initially goods may require a large input of capital and technical knowhow, favouring location in industrialised countries and subsequently they progress to a 'mature' phase when basic unskilled or semiskilled labour availability is a crucial factor. Electrical consumer durable goods, cars and steel production are often quoted as examples, and of these steel is now being exported by India, together with Brazil and Korea. Perhaps less well known is the fact that India is now a major manufacturer of Lambretta motorbikes as well as being a large source of spare parts for the French 'Alouette' helicopters. However, generally speaking, it is still South East (as opposed to South) Asia which is being used to take advantage of the 'maturity' of technological processes for developing new export industries.

Table 2.6 Ranking of 26 industries in India and the UK by Capital-Labour Intensity (in ascending order)

Industry	INDIA		UK
	Fixed Capital per man	Value added per man	Value added per man
Other textiles	1	2	9
Clothing	2	4	2
Leather tanning	3	7	14
Musical instruments	4	17	11
Railroad equipment	5	5	5
Cotton spinning/weaving	6	8	8
Footwear	7	19	6
Printing and publishing	7	9	17
Leather goods	9	3	1
Jewellery	10	10	20
Motorbikes and bicycles	11	11	10
Paint and varnish	12	21	22
Pottery, ceramics and china	13	1	4
Watches and clocks	14	18	3
Transport equipment	15	13	16
Metal products (machine tools, forgings etc)	16	14	13
Rubber products	17	22	19
Non-electrical machinery	18	15	15
Motor vehicles	19	16	12
Miscellaneous chemicals	20	23	23
Photo and optical equipment, precision equipment	21	6	7
Non-ferrous metals	22	25	21
Iron and steel	23	12	18
Cement	24	20	25
Industrial chemicals	25	24	24
Petroleum refining	26	26	26

Source: Government of India, *Summary Census of Manufacturing Industry (1969)*, Delhi, 1977, covers factories with power reporting 10 or more employees, 20 or more for those without; UK Business Statistics Office, *Business Monitor*, HMSO, 1975, covers firms with over 20 employees.

Problems have arisen in trade relations between South Asia and the EEC precisely because Community access barriers appear most severe in those areas of production where the South Asian countries have the most obvious comparative advantage, and therefore from which mutual gains from trade specialisation are potentially

greatest: clothing, woven cotton, textile fabrics, jute products, leather and leather goods, carpets, and in the technologically 'mature' assembly industries. There are some exceptions—polished gems and some labour-intensive engineering activities like handtool manufacture—but in general, there is a clearly observed tendency and a growing one for developed countries, not only in the Community, to resort to trade protection of their labour-intensive industries against developing country competition. Analysis of the reasons why this occurs is not within the scope of this book but the subject is being vigorously debated elsewhere.¹⁴ It appears to reflect a desire to avoid or reduce apparently avoidable adjustment costs to labour and to small immobile firms especially when concentrated in politically sensitive areas and in periods of high unemployment. But there is often also considerable exaggeration of the actual or potential costs and understatement of the gains from accepting adjustment. Given the apparently intractable nature of the 'trade adjustment' problem for politicians particularly at present in Britain and France, there is not a great deal which developing country exporters can do other than to maximise their own output performance, to exploit whatever gaps in the protective shield exist, and conceivably to develop a systematic form of retaliation against particularly disruptive protectionist countries. While it does not greatly help in the short run, it almost certainly will in the long run if developing countries seeking benefits from improved access take steps to let it be seen that they accept themselves the benefits of trade liberalisation and by doing so, ensure that European as well as South Asian producers benefit from increased competitive trade. This is at the heart of the idea of 'reciprocity': the idea that mutually beneficial trade should be seen to be two-way.

(2) Reciprocity

In terms of EEC-South Asian trade, there is no sign at present that the Community is seeking bilateral reciprocity in terms of tariffs; it formally renounced 'reverse preferences' in the context of the Lomé Convention and would be unlikely to revive the idea here. While there has been talk of a 'graduation procedure' to remove the richer and highly 'competitive' ldc's from the Community's GSP and demands that these ldc's should offer concessions on dc imports if they wish their own exports to face easier access to dc markets, the four South Asian countries are unlikely to be early candidates for such treatment. The issue of tariff reciprocity is moreover a multilateral one, and complicated by the fact that in South Asia protection against imports is mainly by quantitative restrictions. In any event India is leading moves in the sub-continent to dismantle unilaterally some of its extensive panoply of controls. Rather, what is more important to the EEC, is reciprocity in flows of purchasing power. Provided South Asians spend most of what they earn, and roughly in the same proportion on European goods as the Europeans spend on South Asian exports, there is 'reciprocity' (more or less) in the trade balance, and consequently in whatever output and employment implications stem from that trade.

This is, of course, to simplify grossly. First, the whole concept of a 'bilateral trade balance' would seem to many a ludicrous and offensive intrusion into international trade discussions. It makes an implicit assumption that mercantilist measures of welfare in trade have some merit. Wrongheaded though they may be, politicians persist nonetheless. Britain's former Secretary of State for Trade, Mr. Dell, a self-confessed mercantilist,¹⁵ was particularly exercised in 1977 by Britain's trade deficit with India—and it is important at least to see what concerns him and other policy makers. Second, even if one were to accept the theory behind bilateralism, the trade deficit can easily be misleading. Trade figures take no account of 'invisible' trade, including services, in which the EEC, especially Britain, almost certainly has a positive balance with South Asia in terms of banking, insurance and sea transport, and interest payments, royalties and profits, but a negative balance (for Britain only) in respect of immigrant remittances. Figures do not exist to indicate the orders of magnitude involved but they are certainly substantial relative to the value of trade. Only in the case of Britain, and that is doubtful, is there any probability that the overall balance of transactions might be negative.

The bilateral trade figures themselves are highly misleading in the sense that they lump together products which are substitutable for domestic production with items which are not. For example, Britain ran a £100m trade deficit with India in 1967 but four items alone in Britain's imports from India—tea, tobacco, spices and non-metal minerals (largely gemstones and mica)—which accounted for £170m by value, would have to be imported from elsewhere if not from India. Britain in fact ran a trade deficit with India for most of the colonial period. Their thinking unclouded by present notions of mercantilist trade policy, the eminently sensible men who ran the Empire almost certainly regarded a trade deficit with India as a way of consuming more without paying for it in full. To talk about 'reciprocity' in terms of the balance of trade is therefore extremely ambiguous. Finally, and from the opposite direction, EEC export figures to South Asia are considerably inflated by exports provided under tied aid (Table 2.7). In aggregate, aid flows accounted for about a quarter of EEC exports to India, Pakistan, and Sri Lanka and almost twice exports to Bangladesh in 1975, though not all was tied.

Table 2.7 EEC Aid to South Asia (\$m)

	Total EEC 9 net bilateral oda		European Commission net multilateral oda	
	1970	1975	1970	1975
Bangladesh	2.6 ^a	149.0	6.0 ^a	60.7
India	177.0	311.7	4.2	99.5
Pakistan	68.8	110.2	4.1	24.6
Sri Lanka	20.3	31.2	1.1	12.2
	<u>268.7</u>	<u>602.1</u>	<u>15.4</u>	<u>197.0</u>

Note: ^a 1971 figure.

Source: OECD, *Geographical Distribution of Financial Flows to Developing Countries*, Paris, 1977.

Table 2.8 EEC-South Asian Balance of Trade (\$m)

A 1976	Bangladesh	India	Pakistan	Sri Lanka	South Asia
UK					
Imports	36	580	66	57	739
Exports	49	408	177	36	670
Balance	+13	-172	+111	-21	-69
France					
Imports	9	193	28	13	243
Exports	13	253	66	45	377
Balance	+4	+60	+38	+32	+134
Germany					
Imports	8	271	67	21	367
Exports	25	403	166	28	622
Balance	+17	+132	+99	+7	+255
Italy					
Imports	24	133	47	18	222
Exports	1	72	77	6	156
Balance	-23	-61	+30	-12	-66
Netherlands					
Imports	8	105	19	8	140
Exports	17	86	45	8	156
Balance	+9	-19	+26	0	+16
Belgium-Luxembourg					
Imports	14	90	11	1	116
Exports	6	166	23	10	205
Balance	-8	+76	+12	+9	+89
Denmark					
Imports	2	36	9	2	49
Exports	4	10	7	2	23
Balance	+2	-26	-2	0	-26
Ireland					
Imports	-	14	3	2	19
Exports	-	1	1	1	3
Balance	-	-13	-2	-1	-16
EEC-9					
Imports	101	1422	249	122	1894
Exports	115	1399	563	136	2213
Balance	+14	-23	+314	+14	+319

B Changes from 1972 to 1976

	Bangladesh ^a	India	Pakistan	Sri Lanka ^b	South Asia
UK					
Imports	-7	+340	+14	+2	+349
Exports	-13	+126	+117	-6	+225
Balance	-6	-214	+103	-8	-125
France					
Imports	+2	+140	+12	+10	+164
Exports	+6	+207	+54	+32	+299
Balance	+4	+67	+42	+22	+135
Germany					
Imports	-2	+197	-25	+9	+229
Exports	-14	+209	-103	-5	+293
Balance	-12	+12	+78	-14	+64
Italy					
Imports	+13	+77	+13	+15	+118
Exports	-17	+36	+50	+4	+63
Balance	-30	-41	+37	-11	-55
Netherlands					
Imports	+2	+67	+9	+15	+83
Exports	+5	+43	+33	+6	+87
Balance	+3	-24	+24	+1	+4
Belgium-Luxembourg					
Imports	-5	+64	+5	+1	+65
Exports	+4	+107	+14	+7	+132
Balance	+9	-43	+9	+6	+67
Denmark					
Imports	+2	+29	+6	+2	+39
Exports	-	+6	+4	-	+10
Balance	-2	-23	-2	-2	-29
Ireland					
Imports	-	+5	+3	+1	+9
Exports	-	+1	+1	+1	+3
Balance	-	-4	-2	0	-6
EEC-9					
Imports	+4	+910	+107	+69	+1090
Exports	-30	+735	+378	+70	+1153
Balance	-34	-175	+271	+1	+63

Notes: ^a 1973 to 1976 for Bangladesh

^b 1971 to 1976 for Sri Lanka

Source: IMF/IBRD, *Direction of Trade 1970-76*, Washington, 1978.

Since the direction let alone the magnitude of these various effects cannot be estimated satisfactorily it is difficult to come to any definite conclusions, except to regard bilateral trade measures as a poor measure of welfare. For what they are worth the first part of Table 2.8 gives a breakdown of EEC-South Asia trade balances in 1976 and the second part shows how these have changed since 1972. In 1976 the EEC as a whole ran a surplus on trade with South Asia largely due to a massive surplus with Pakistan, trade with the other three balancing out more closely. In 1972 the EEC-South Asia surplus was somewhat smaller due to much lower exports to Pakistan though there was at that time a sizeable trade surplus with India which has since disappeared. Of the various EEC countries Britain in 1976 had a deficit on trade with the subcontinent, almost entirely accounted for by India, and this deficit has emerged since 1972 when Britain actually had a trade surplus with both South Asia and India. Britain also accounts for a disproportionately large slice of EEC aid to South Asia, though this is not firmly tied, and for a large share of net remittances from overseas South Asians. But these must be offset against Britain's unquantifiable though probably substantial earnings from invisible exports to the subcontinent. Italy also had a trade deficit in 1976 with all four countries, mainly because of raw material imports, but gave little aid. Germany seems to benefit, in mercantilist terms, all round. Its trade surpluses are large, consistently in excess of its aid and to these must be added fairly generous earnings from invisible transactions, notably royalties on technology agreements. France had a trade surplus of similar proportions, in contrast to 1972 when its trade with South Asia was balanced, while it gave little aid. Of the remaining EEC countries, the Netherlands and Belgium-Luxembourg had small surpluses in their trade with South Asia, while Ireland and Denmark had small deficits.

Looking to the future, rather than to the immediate past, the EEC may be worried that any rapid increase in South Asian export earnings will not be spent, but hoarded in the Japanese or South Korean manner (though even these, like the OPEC surpluses, tend to be recycled by means of foreign investment). Such concern may have been given superficial support by India's extraordinary balance of payments record in 1976 and 1977, as a result of which reserves rose to the equivalent of almost 12 months supply of imports. It is quite clear that India's foreign trade policy is now designed to reduce these reserves as rapidly as possible and this will benefit EEC exporters. Moreover, India's next Five Year Plan has been constructed on the assumption that imports will grow twice as fast in real terms as exports. There is, however, an altogether more radical and dynamic view of the situation which focuses on the potential market demand of a subcontinent of over 700m people. That such an area currently accounts for only one per cent of world trade need not imply that it will continue to be of marginal interest. If this change occurs as a result of more rapid growth and/or a move away from import substitution (as discussed above), then there is a case to be made in the short-run for EEC trade policy to be more generous and thereby facilitate the earning of foreign exchange resources which in turn will stimulate South Asian spending. In the long-run the EEC will have

built up a store of goodwill and contacts in South Asia. With just a little vision, European trade policy makers could ensure, by taking a liberal approach to access of competing South Asian products, benefits not only to these economies but to their own.

(3) Raw Material Security

Attempts to negotiate the CCAs coincided with attempts by the EEC member states to draw up a Community Raw Materials Policy. Though this issue has become less topical and no policy was ever agreed, the perception of potential conflict or complementarity of interests with ldc's over raw materials is nonetheless very real as the Community has made clear: 'if consuming countries respect minimum world prices, the producing countries must guarantee supplies'.¹⁶ Community officials expressed to us the view that one important purpose of maintaining a dialogue with the South Asians was to 'moderate' their views on commodity issues. Table 2.9 shows the position of South Asia as a supplier of raw materials to the EEC. Except for jute and tea, of which South Asia supplies over half of EEC imports, and to a lesser extent other vegetable fibres, tobacco, spices and rice, the EEC is overwhelmingly dependent on imports from outside South Asia. It is, however, necessary to spell out what the issues are since at least in the early days of discussion about raw materials policy much excitement was created by simplistic, sometimes downright silly, arguments about 'the world running out of resources', OPEC-style cartelisation of all main raw materials, the Russians getting hold of 'our' sources of supply and so on. Now that some of the excitement has subsided it is possible to look at the issues in a clearer perspective.

First, there is now little fear that producer cartels, on OPEC lines, would be viable for many other commodities. Producer associations are struggling to establish themselves for bauxite and iron ore in which India has an interest as a member of the organisation of iron ore exporters. Second, there is the political threat, of disruption of strategic materials supplies. The Community's own appraisal is that of the main South Asian raw materials only manganese and hides are subject to such risks. South Asia is in any event a marginal supplier. Third, there is the general problem of underinvestment in mining and energy leading to long-term shortages of supply. But this runs up against South Asian (and other ldc's) apprehensions, sometimes legitimate, about foreign mining and oil companies. Only India has major mineral reserves and the government shows no interest in opening up extraction to foreign investment. Bangladesh, however, might do so, if its natural gas reserves attract interest. Fourth, there is the question of processing; conflicts of interest arise over whether value added should accrue to processors in the importing or exporting countries. This is the area where South Asia and EEC have something to discuss. The South Asians are anxious, in principle, to tan their own hides, bag their tea, spin and weave their cotton, convert manganese into ferromanganese and iron ore into steel.

Table 2.9 Dependence of the European Community on Developing Countries for Supplies of Primary Commodities

Product	Total EEC imports from non-EEC sources (1975 \$m)	Imports from Idcs (% of total)	Imports from South Asia (% of total)
A Tropical Products			
Coffee	1705	98	0.5
Cocoa	900	95	0.1
Tea	343	93	54.8
Bananas	591	100	—
Spices	115	71	5.3
B Renewable industrial raw materials			
Wood (i) raw	678	66	0.3
(ii) processed roughly	2282	18	—
Hides and skins (untanned)	366	29	0.4
Rubber	572	74	2.1
Cotton	985	59	1.4
Wool	900	16	0.4
Jute	37	98	67.6
Other vegetable fibres (coir, sisal, etc)	128	89	7.3
C Non-renewable industrial raw materials			
Copper	2646	57	—
Tin	348	85	—
Iron ore	2104	51	1.6
Bauxite ore/aluminium	876	16	—
Crude fertilisers (phosphate)	894	74	—
Manganese (& Ferromanganese)	266	28	—
Tungsten	61	49	—
Refractory materials (eg mica)	212	8	2.0
D Agricultural food products			
Fresh meat	1259	19	0.1
Fish	623	28	0.5
Animal feedstuffs	1729	51	2.7
Oil seeds	2707	37	0.1
Citrus fruit	902	34	—
Sugar	1570	90	1.4
Wheat	1249	4	—
Rice	145	41	4.5
Tobacco	1064	41	7.0

— nil

Source: Eurostat, *EEC Foreign Trade Statistics (Nimexe)*, Luxembourg, 1975.

All of these aspirations conflict to some degree with those of European processors. Finally, there is the whole issue of international commodity diplomacy and the extent to which individual ldc's within the Group of 77 can be persuaded to take, in Western eyes, a more 'helpful' position on issues such as UNCTAD's Integrated Programme for Commodities. While the South Asians may find as little attraction as the Europeans in the price stabilisation proposed under the Programme, given that commodities such as tea, jute, and cotton present problems of long-term price decline rather than short-term stabilisation, they do have an interest in the proposals for arrangements other than buffer stocking and in any event are unlikely to break ranks with other ldc's.

There are perhaps three ways in which bilateral South Asia-EEC arrangements could be important. The first relates to processing. The Community has warned against recourse to unilaterally imposed solutions and export prohibitions by producers. Since this is precisely what India and Bangladesh in particular are doing in order to obtain greater value added from leather processing, the subject has provided the basis for extensive discussions in the context of the CCAs. Where suppliers are co-operative over raw material supply the Community favours technical assistance and the promotion of investment, and this could form the basis of substantial co-operation on jute with Bangladesh. Even in the case of leather, agreement could surely be reached over the release from the subcontinent of guaranteed quantities of raw or lightly tanned hides, probably decreasing gradually over time in an agreed manner, in return for Community co-operation over access (tariffs) and technical help. Second, there are cases where, even in the absence of formal access barriers, lack of knowhow may inhibit South Asian exporters (eg coal, mica) and where there is a parallel wish by European producers to negotiate long-term supply agreements. Thirdly, there is the question of foreign investment in mining and other non-renewable natural resources. This raises more general issues which are now considered.

(4) Foreign Investment and Factor Mobility

We have already observed that the CCAs (except for the EEC-Bangladesh one) do not formally incorporate foreign investment (let alone immigration) as part of their terms. This is partly for practical reasons. The Community has no jurisdiction over foreign investment where companies originating in member states are concerned. But at the same time it is not very meaningful for the Joint Commissions to discuss 'industrial co-operation' without taking it in. Moreover there is an obvious complementarity of interest, which parallels that in trade in manufactures, based on Europe's relative abundance of capital and technology and South Asia's supplies of labour. The gains from trade based on factor endowments are after all merely a mechanism for achieving the gains which would alternatively, or in addition, accrue through factor mobility. In practice they prove to be limited for political reasons (European hostility to Asian immigrants; Asian hostility to European investment) but given the potential mutual gains it may be useful to explore the possibilities.

Data on private foreign investment is somewhat fragmentary. For the UK the South Asian picture is one of virtual stagnation. Between 1962 and 1974 British overseas investment rose from £3.4bn (book value of net assets excluding oil, insurance, and banking) to £20bn. Investment in South Asia rose merely from £338m to £364m—a significant decline in real terms, while as a share of British overseas investment it fell from 10% to under 4%. Of this India accounted, in 1974, for £275m (£260m in 1962), Pakistan £44m and Bangladesh £15m (jointly £32m in 1962) and Sri Lanka £30m (£46m in 1962). These figures may represent something of an understatement, since British banking is important in the subcontinent. Lipton and Firm estimated that in 1971 the market value of all British private capital in India was around £500m, as opposed to the UK official estimate of £275m. Even if the valuations are somewhat unsatisfactory, to the extent that they rely on partial and historic cost accounting data, the sharply declining trend in terms of relative importance to the UK is clear enough. A decline has also taken place in Britain's share of India's stock of private foreign capital (from 68% in 1960 to 53% in 1968). This has continued to fall as a result of the restrictive effect of the Foreign Exchange Regulation Act, which required the reduction from 1974 of foreign companies' shares in Indian-based companies and resulted in the sale of shares in many of the larger British companies (eg the tea plantations). Germany, by contrast, represents a growing source of investment; a German consortium of banks has put up £650m to invest in India in 1978 and 1979 alone. In countries like India where foreign equity capital is not regarded with too much enthusiasm, foreign participation is measured by more discreet arrangements such as technical collaboration agreements and joint ventures (Table 2.10). These one can merely enumerate, not measure their value. Of the collaboration agreements signed in India in the 1957-75 period (a total of 4,587) 2,378 were with EEC-based companies, of which 1,119 British, 772 German, 202 French and 135 Italian. However, in every year since 1972 Indo-German agreements have outnumbered Indo-British agreements.

Table 2.10 Number of Foreign Collaboration Agreements in India

	1957/69	1970	1971	1972	1973	1974	1975	Total 1957/75
UK	811	39	55	38	53	59	54	1119
Germany	463	28	42	49	60	71	59	772
France	118	7	15	11	13	22	13	202
Italy	81	8	5	8	5	16	10	133
Netherlands	47	3	4	4	2	3	1	64
Denmark	35	1	1	1	3	4	—	45
Belgium	25	1	3	3	1	5	5	43
Total EEC ¹	1580	87	125	114	137	180	142	2378
Total ²	3008	183	244	257	265	359	271	4587
$\frac{1}{2}$ %	53	48	51	44	51	50	52	52

Source: *India and European Community*, February-April 1977 and August-October 1977.

It is Sri Lanka and Bangladesh, currently very minor recipients of overseas private investment, which are now seeking to attract it most energetically. In Bangladesh investors face no restrictions on the freedom to repatriate profits or capital, or on ownership share in any sector, or in the employment of expatriates, and five- to ten-year tax holidays are available. American companies (further assisted by an Investment Guarantee Agreement) are beginning to take advantage of these policies but there is less evidence of EEC companies doing so. Sri Lanka is a more recent convert, operating generous incentives within an investment protection and free trade zone, a five-year tax holiday, no restrictions on imported inputs, and the free transfer of capital.

There is no obvious function for the CCAs or the bilateral agreements between the individual member states and South Asia in all of this, except in the field of investment protection and then only if both sides want it (and this is for EEC member governments to initiate). The South Asian governments may, however, be advised to consider that in practice it is organised capital rather than labour which generally offers the most effective protectionist opposition to competing processed imports.¹⁷ One way of diminishing that opposition is to offer the EEC companies concerned opportunities for profitable production as partners in joint ventures or under sub-contracting arrangements, for example. Some German leather companies are discussing the opportunities to be had from processing and manufacturing leather goods in India. The Joint Commission can best assist this process in a modest 'Euronet' function, bringing together potential collaborators. The real function of the Commissions is in trade policy and to this we now turn in more detail.

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3 Tariffs, Preferences, and South Asia

Introduction

The philosophy behind the GSP and its basic methods of operation have been described elsewhere and do not need elaborate repetition.¹ Nonetheless an evaluation of the EEC scheme is called for to the extent that it affects the South Asian countries and because the GSP was seen as a central instrument for implementing the Joint Declaration of Intent (as we saw in the first chapter).

It is necessary to begin with a brief description of the bare essentials of the EEC's GSP. It was initiated in July 1971, the first of 11 such schemes set up by the major OECD countries, in response to ldc demands for preferential tariff treatment, dating from the first UNCTAD conference, in 1964, which were in principle conceded by the dcs four years later at the second UNCTAD conference. The underlying theory is one of infant industry subsidisation of ldc manufactured exports and it was therefore intended to make the schemes temporary, lasting no more than a decade. The EEC, however, has committed itself already to extending its scheme beyond 1981.

The objective of each of these schemes is to facilitate access to developed countries' markets for all ldc exports of manufactures, semi-manufactures and some processed agricultural goods, through the reduction of tariffs on a preferential and non-reciprocal basis. Preferential tariff reductions can stimulate exports from ldcs in two ways: first, trade may be created by reducing the protection given to competing producers in the importing countries; and second, trade may be diverted from non-preferred sources of supply to ldcs. In practice the generosity of the schemes is limited by a reluctance, first, to extend generalised preferential access where this dilutes non-generalised preferential access arrangements (such as the EEC's Lomé Convention with the 53 ACP states) or where it is at the expense of multilateral tariff reductions, and second, to accord access at the expense of domestic producers in 'sensitive' industries. The latter has been the most pressing constraint.

The EEC scheme is characterised by a system of *a priori* limitations on the amount of ldc imports which may benefit from tariff reductions, designed to protect EEC industrial and agricultural interests. In the case of industrial products, these limitations vary according to whether the import is classified as sensitive, semi-sensitive, or non-sensitive. There are further limitations which vary according to whether the supplier is considered to be more or less competitive.

(1) Some 50 sensitive products, of which textiles and clothing, footwear, leather goods and steel are the most important, face tariff quotas. The

quota is sub-allocated among the individual EEC members on the basis of predetermined market shares, roughly corresponding to GDP: for most of the sensitive items the rates are 27.5% to Germany, 22% to the UK, 19% to France, 15% to Italy, 10.5% to Benelux, 5% to Denmark and 1% to Ireland. In the case of textiles there is a slightly different scale for Germany at 27%, Italy 14%, Benelux 10%, and Denmark 7%. When imports from GSP beneficiaries of a sensitive product reach a member state's allocated level, additional imports to that member state must normally pay full mfn duties again, though imports of that product to other member states may continue to enter at GSP rates. For a few sensitive products, however, only 70% to 80% of the Community's total quota is initially allocated between members, the rest being set aside as a 'reserve' which may be used by any member state which fills its allocated level ahead of the other member states. In effect this postpones the date at which mfn duties may be reintroduced.

(2) Semi-sensitive products face a system of tariff ceilings. These fix the amount of imports to the Community as a whole which may benefit from the GSP, with no sub-allocation of the amount between member states. It is necessary to distinguish between two groups of semi-sensitive products. For a small group (around 30) sometimes known as 'hybrid' products, withdrawal of preferential treatment once the Community ceiling is reached is automatic. For a second group, the majority of semi-sensitive items, imports, though subject to careful surveillance, may continue to receive GSP treatment until an individual member state makes a request to the European Commission that the mfn duty be reimposed on its imports. Imports to other member states may still benefit from the GSP.

(3) Non-sensitive products, numbering some 1700 tariff categories (though many are of no interest to ldc's), are also subject to tariff ceilings, but these are normally so large in relation to imports from ldc's as to have no effect. The ceilings for each product are calculated as the sum of EEC imports from all beneficiaries in a base year (the basic amount) *plus* 5% of imports from non-beneficiaries (the supplementary amount). Unlike sensitive or semi-sensitive products, however, the ceilings are not pre-calculated or published, nor are imports closely monitored, so that it is possible for imports to exceed the ceiling and still benefit from GSP. This situation arises because of the time needed for the domestic EEC producer competing with a particular import to apply to his government, which in turn has to apply to the Commission for permission to reimpose mfn duties. In principle, therefore, it seems that access for non-sensitive products is intended to be free.

(4) Finally, limitations are placed on the maximum amount of a tariff quota or ceiling which may be supplied by any one GSP beneficiary. These limits (or 'butoirs' in Community parlance) are intended to reserve

a share of the GSP benefits for the less competitive ldc's. They are normally set at 50%, though for sensitive products and the first group of semi-sensitive products they are often lower—between 20% and 30% of the tariff quota or ceiling. In addition for many sensitive products there are special butoirs for imports from specific 'super-competitive' suppliers, including South Korea, Singapore, Hong Kong, Yugoslavia, Brazil, Colombia, and Mexico. These are normally set at 10%. Once the butoirs are exceeded full mfn tariffs may be restored automatically, in the case of sensitive products and the first group of semi-sensitive products, or at the discretion of individual member states, subject to Commission approval, in other cases.

In contrast, for nearly all of the 300 or so agricultural products covered by the GSP there is no system of ceilings. Only six items face tariff quotas, with no butoirs. But all agricultural products under the GSP, like all industrial ones, are subject to a safeguard clause. Finally, it is important to be clear that duty-free access under the GSP even for non-sensitive items does not have the same status as mfn free access: the GSP is not legally binding, and any part of it can be withdrawn by the EEC unilaterally.

Development of the EEC-GSP scheme

When the GSP was introduced by the EEC in 1971 Richard Cooper described it as 'highly restrictive'. 'It is difficult to take seriously the contention of the Community that ... "it will give immediate and significant benefit to developing countries"'.² He did concede, however, that it might contribute an 'entering wedge' to force the EEC into further concessions and that it helped 'draw attention in a world of imperfect information to the possibility of exporting to Europe'.

It is perhaps a useful time to take stock of the improvements that have been made since 1971. There have been various influences at work. The first has been the accession of Britain and Denmark to the EEC. These had their own GSP schemes with less resort to *a priori* restrictions. In adapting to the EEC scheme, which was generally more restrictive (except on textiles in the UK case) they managed to force some liberalisation. Second, there has been parallel progress in the other 11 GSP schemes. It was the absence, until 1976, of an operational scheme in the United States which was probably a major factor inhibiting the EEC from taking its GSP too far ahead of that of its major trade competitor. Third, the state of the world economy has been a generally constraining factor. Each year the EEC Commission submits proposals to the Council of Ministers for changes in the GSP. These have sounded an increasingly lugubrious note: 'the import capacity of the Community is in danger of being reduced—with the exception of certain essential raw materials—to the disadvantage of the developing countries' (1974)³ ... 'the Community's capacity to provide

assistance through generalised preferences particularly in certain sectors, seems to be reaching a level which requires, if not a pause in the development of the GSP, at least an adaptation of its speed to the economic possibilities of the moment' (1975)⁴ ... 'the GSP has become an economic challenge. We now find ourselves in a period of uncertainty and recession which grows more severe year by year' (1976).⁵ Finally in 1977, the Commission dropped its earlier annual recognition that 'however serious the economic difficulties may be which the Community faces, they cannot be compared with those which the developing countries are passing through, particularly the poorest'⁶ and simply said 'For 1978 the commitments entered into will be honoured, but without the systematic substantial improvements of previous years'.⁷

In evaluating the improvements made we shall look at what have been perhaps the three main strands of policy in recent years; the first being liberalisation of *a priori* restrictions on industrial goods, the second being special provision for the poorest ldc's, and the third being the extension of the GSP to agriculture. Two further issues are explored: attempts to simplify the scheme to make it comprehensible to beneficiaries, and the development of 'rules of origin'.

General Liberalisation

Liberalisation has been achieved in part by a movement of products out of the sensitive category. In 1974 there were 51 sensitive items other than textiles or steel and now there are 13, while the number of sensitive textile products (30) has not changed. For those that remain, however, the combination of butoirs and EEC importing country quotas is a severe handicap to full utilisation of what are usually highly restrictive tariff quotas. To ease this difficulty, the Commission recommended, as early as 1971, the introduction of a reserve in the administration of the EEC's quota, but it was not accepted by the Council until 1975 and then only for some quotas; in 1978 it was extended to all tariff quota items (industrial and agricultural) excluding textiles and steel products. It should be stressed that this innovation had less to do with concern in the Council over the low utilisation rate of the GSP than concern over the fact that rigid country quotas contravene the spirit, if not the letter, of the Treaty of Rome. They do so by treating the EEC as seven markets, though in fact EEC importers or ldc exporters can try to escape the quota limitations in one member state by trans-shipment to another where the quota has not yet been reached. Even so it was only with difficulty that Ministers were persuaded not to adopt a Belgian proposal to apply rigid country shares to the Community reserve itself.

The number of semi-sensitive items has grown to over 100, mainly to accommodate items switched from the sensitive list. This represents only a modest improvement as ceilings are often still a significant obstacle to tariff-free access. There has been little change in the number of non-sensitive items, except to incorporate a few products removed from the semi-sensitive list.

A measure of the inhibiting effect of both the EEC member country quotas and the supplying country butoirs can be gained from the degree of utilisation of quotas and ceilings. There is a paradoxical situation that these are at the same time both over- and under-utilised: over-utilised by particular suppliers in particular markets, under-utilised by other suppliers, elsewhere. Thus for sensitive items tariff quota utilisation was estimated at 62% in 1974, 83% in 1975 (66% and 57% for textiles; 16% and 19.5% for steel); and for semi-sensitive (including tariff ceilings) items 74% in 1974, 55% in 1975 (after the addition of former sensitive items), 46% in both years for textiles, 57% and 9% for steel.⁸ The extent to which EEC member national quotas contribute to under-utilisation can be seen from Table 3.1. Although the only figures available are seriously dated (1972) and relate only to a few textile items, where the phenomenon was particularly marked, it is easy to see how, for each item, tariffs were re-imposed in some member countries, often early in the year, while imports into other countries had not come close to the quota limit.

Table 3.1 Utilisation of National Quotas (1972) (%)

	Germany	Benelux	France	Italy	Overall
55-09 BIIb (cotton yarn)	76	100 (June) ^a	77	97	87
55-05 BIIId (cotton yarn)	63	100 (Sept)	31	—	49
55-09 AIIa (cotton fabric)	58	68	100 (Sept)	100 (April)	81
55-09 AIIb (cotton fabric)	73	100	100 (Aug)	100 (March)	93
55-09 AIIc (cotton fabric)	45	36	100 (April)	100 (Feb)	70

Note: ^a The month indicates when the quota was finished.

Source: COM(73) 1800, 24 October 1973, p.16d-16e.

As a footnote to the discussion it is worth commenting that one of the more extraordinary characteristics of tariff quotas and ceilings is that until 1979 they have been based on the unit of account (ua), which has a fixed gold reference weight and is converted into EEC national currencies at the gold-parity rates of 1969, rather than the newer European unit of account (eua), which is a composite basket of fixed amounts of the nine members' currencies and whose value is calculated daily to take account of the variations in the market exchange rate of each of the nine's currencies. The difference is substantial. For example using the eua instead of the overvalued ua the UK would

have had tariff quotas of 60% larger, though the French quota would have remained the same. Since the UK was one of the more open EEC economies to Idc imports, at least until recently, the effect of using the Smithsonian ua has been to promote under-utilisation of GSP ceilings and quotas in general. More important, as the UK takes a higher share of South Asian imports than, say, France, the use of the ua has effectively restricted the benefits of the GSP to South Asia and other traditional UK suppliers. The introduction of the eua in the 1979 GSP scheme, by raising the UK's quota by some 60%. should therefore increase South Asian trade under the GSP.

Another way of looking at the development of the GSP is in terms of the increase in the value of ceilings of trade eligible for GSP concessions. This is how the Commission itself presents the EEC scheme.

Table 3.2 EEC Estimates of GSP Eligible Imports and Utilisation

Year	Value of total eligible imports ^a (mua)	% Increase over previous year	Utilisation ^c	Value of sensitive and semi-sensitive imports (mua) na
1971	— 500 ^b	—	44	na
1972	— 1100 ^b	120	41	na
1973	(2320) 1250 ^b	14	56	na
1974	3250	40	66	1262
1975	3680	13	50	1376
1976	4600	25	67	1346
1977	6720	20	63	2719
1978	6800	1	55	na
1979	7900 ^d	16	na	na

Notes: ^a includes both manufactures and agricultural items
^b EEC-6 only; in 1973 the EEC-9 equivalent is calculated
^c utilisation defined as actual GSP imports as % of value eligible
^d meua

Source: Various issues of 'The European Community's Scheme of Generalised Tariff Preferences (Proposals and Communications from the Commission to the Council)'

As Table 3.2 shows, the GSP eligible trade doubled in value from 3250 mua in 1974 to 6800 mua in 1978 and the 1979 offer envisages a further increase of 16% to 7900 meua. These total ceilings represent the maximum possible level of imports under the GSP for all items, sensitive, semi-, and non-sensitive. While some of the growth in ceilings is due to extended product coverage, a large part arises from the continual updating of the reference year used for the calculation of quotas and ceilings. In 1971 the reference year for both the basic and supplementary amounts was 1968. By 1978 it has changed to 1974 and 1975 respectively.

It should also be noted that the ceiling for a product may never fall below the level of the previous year. On the other hand, in certain years the increase in ceilings for some products has been limited to 50% above the level of the previous year.

The general trend in ceilings and quotas calculated in this way is quite misleading, and flattering to the EEC, for several reasons. First, the values of ceilings and quotas are substantially diminished in real terms by inflation (except for those which are fixed in volume terms as in the case of some textiles, jute, coir, sisal products, carpets, plywood, tobacco, cocoa butter, instant coffee, and canned pineapple). The EEC Commission itself acknowledges the obligation to maintain real values as well as a duty which 'runs along the lines of the Resolution on Manufactured Goods adopted at UNCTAD IV in Nairobi ... that donor countries should as far as possible initiate a tangible rise in the ceilings and tariff quotas under their generalised preference schemes'.⁹ While export prices of traded manufactures increased by 26% from 1974 to 1977, GSP eligible trade increased by 109%; in other words roughly one quarter of the increase in GSP ceilings was lost through inflation.

Second, and more important, the Community adds together two conceptually quite different measures. One is the value of ceilings on sensitive and semi-sensitive items. The lifting of the ceilings on these is a genuine concession (though the *modus operandi* of the scheme means that there will inevitably be some under-utilisation). The other is the value of ceilings on non-sensitive items. As explained above, these ceilings are largely meaningless, or 'open-ended', since they are usually non-operational¹⁰ and are invariably at a level much greater than the value of goods actually traded. This arises from the way in which ceilings are composed of two factors of which the supplementary amount is equal to 5% of the value of imports from all non-beneficiaries. Thus where the ldc market share is small the ceilings will be large relative to existing ldc exports. In fact, as Table 3.2 shows, half of the 'growth' of the GSP from 1974 to 1977 occurred in these fictional ceilings on non-sensitive items: while the total coverage of the GSP has risen by 2980 mua the value of ceilings or quotas on the sensitive and semi-sensitive items rose by 1454 mua.

Annual average growth rates in ceilings, as given in the table, are also misleading. In 1975 ceilings were increased on average by 15% but only 8% in the case of sensitive items, and 12% for semi-sensitive items, as compared with 20% for the rest. In 1976 when ceilings rose generally by 18%, textiles were kept to 5% growth. In 1977 when there was a major increase in benefits as high as 43% for industrial goods overall, due to the adoption of a new base year, growth in ceilings on textiles was held down to 5%, on steel to 6%, while shoes had no growth at all. In the 1978 offer, again with a base date advance, ceilings on textiles, shoes, steel, and plywood were not changed. Finally for 1979 it is proposed that a more recent year (1976) be used to calculate supplementary amounts, though for several products, notably footwear and steel, 'no increase

can be risked'.¹¹ This means that since 1976 ceilings and quotas on many items of importance to South Asia have been frozen.

A further downward bias arises from the two to three year old data used to calculate quotas and ceilings. This means ceilings do not allow for any recent and rapid growth in ldc imports to the EEC as may have occurred in response to earlier tariff liberalisation. Thus the scheme, as Murray suggests, 'might be called "close-ended", meaning that the GSP tariff rates apply only on a trade volume that would have occurred even in the absence of any GSP tariff incentives. Any increase in imports from the beneficiaries would face mfn duties; consequently the GSP will not contribute to any increase in developing country trade'.¹²

A somewhat more meaningful and useful measure of the value of GSP concessions is in terms of the tariff revenue lost by the Community as a consequence of the GSP. This measure takes into account both under-utilisation of quotas and the nominal character of non-sensitive ceilings. Moreover it gives a clearer measure of the true nature of GSP benefits. When ldc's are exporting sensitive and semi-sensitive items duty is payable at the margin. If the quota or ceiling is set at a level lower than the amount which would be traded anyway in the presence of tariffs, there is no incentive to ldc's to increase exports, if marginal revenue/marginal cost principles are observed. There is, however, a potential revenue gain equal in value to the preference margin multiplied by the value of goods sold duty-free under the quota or ceiling. For non-sensitive items there is also a revenue gain, either calculated as above, or the result of expanded sales at reduced prices, or a combination of the two. In terms of this revenue effect, then, an overall assessment of progress in the GSP can be made.

Using various simplifying assumptions, the Community have estimated the total revenue loss from the GSP to be 385 mva in 1978, or the equivalent of just under 6% of ldc imports eligible for GSP (Table 3.3). How the EEC produced the value assumed for average tariff incidence is unclear, but the magnitudes seem plausible. It should be remembered, however, that the revenue lost is not necessarily converted into revenue gain in the ldc's. There are many other potential beneficiaries including shippers, importers, and consumers in Europe. The amount accruing to ldc exporters will depend on their relative bargaining strength, their sophistication in pricing policy, and market organisation. These are in practice unlikely to be substantial, and the gains to ldc exporters will be considerably less than the maximum values shown here. Rather 'it is generally the importer who gets the immediate benefit from the GSP tariff cuts'.¹³

Table 3.3 EEC Estimates of the Fiscal Value of GSP Concessions

Year	Value Eligible (mua)	Utilisation (%)	Average Duty Concession (%)	Fiscal Value (mua)
1974	3250	65	8.3	178
1975	3680	50	8.5	156
1976	4600	62	9.3	287
1977	6720	55 ^a	9.1	385
1978	6800	55 ^a	8.5	318
				1324

Note: ^a estimate

Derived from same source as Table 3.2.

Special Concessions to the Poorest

In order to ensure that the benefits of the GSP reach the poorest and least industrialised ldc's the EEC has increasingly sought to make a distinction in its administration of the scheme between the more industrialised, usually middle-income ldc's, and the rest. This concern was reflected as early as March 1975 in the declaration of the Council of Ministers that improvements in the GSP 'pay particular attention to the interests of the less favoured developing countries'.¹⁴ One reason is a belief, not in itself unreasonable, that the more economically advanced ldc's should soon come to be treated on a normal mfn reciprocal basis. This conviction is strengthened by the fact that some countries (Yugoslavia, Rumania, Hong Kong, and Singapore) were admitted to the GSP largely for political reasons, as on per capita income grounds or levels of industrialisation they could not realistically claim ldc status. Another reason is the monopolisation of GSP trade by a small group of these largely middle-income countries: in 1974 as much as 72% of EEC imports under the GSP came from 10 countries, of which only India and Pakistan were among the poorer ldc's (South Korea being next up the per capita income scale). Table 3.4 shows that this monopolisation is even more extreme for certain sensitive and semi-sensitive industrial products, particularly footwear and cotton textiles.

Table 3.4 Major Users of the EEC's GSP in 1974 (by % GSP imports)

	South Korea	Hong Kong	Yugoslavia	Singapore	Brazil	Pakistan	India	Mexico	Other ^a
A Industrial goods (not textiles/steel) subject to tariff quotas									
Footwear	20	..	17	..	19	15	7	..	22
Other ind products	12	23	19	11	8	..	..	..	27
Subject to ceilings (under surveillance)									
All products	8	16	24	6	12	5	6	11	12
B Textiles subject to tariff quotas									
Cotton	7	..	..	..	..	29	21	8	35
Non-cotton	19	..	..	..	..	2	12	8	59
Subject to ceilings (under surveillance)									
Cotton	6	..	..	..	..	40	38	..	16
Non-cotton	..	..	36	..	5	16	..	..	43

Note: ^a Other countries (including Rumania)

Source: p.4 to 8, Annex II, *The European Community's Generalised Tariff Preference Scheme for 1977*, Com(76) 303 final.

This diminishes the political appeal of the scheme in the Group of 77 as a whole and amongst those in the EEC seeking to help all ldc's develop through trade. However, rather than confront the question squarely of whether some of these countries should face immediate or eventual exclusion from the scheme, the Community has introduced a series of complex and often contradictory devices for discrimination within the GSP.

First, as mentioned earlier, a system of special maximum amounts has been introduced for sensitive and semi-sensitive items to limit the share of GSP imports from a dominant supplier, defined in terms of trade performance in that category. These limitations, normally 15%, penalise Hong Kong and Yugoslavia particularly. But, critics claim, they do not actually help others; in fact the threat of attracting special maximum amounts may be a disincentive to new producers. In few cases where the special maximum amount ceiling is enforced, is the overall quota ever reached by other suppliers. Thus, if one ldc is a dominant supplier, the special country amount is a way of freezing part of the ceiling, as no one else can use it and it is not transferable to other items or to subsequent years. Second, in 1977 imports of all semi-sensitive and non-sensitive items from countries classified by the UN as 'least developed' were exempted from the butoir rule. This would certainly be a valuable concession were the 'least developed' ldc's not so defined as to exclude India, Pakistan and

even Sri Lanka, which are classed instead as 'most seriously affected' (msa); of the four South Asian countries only Bangladesh is included. As a consequence no ldc with any measurable industrial capacity can exploit the concessionary benefits. Third, for 28 textile items, the global ceiling is divided into two parts, 30% for all ldcs of over \$300 per capita income (in 1972) which are supplying at least 6% of EEC imports of an item, with no butoir; 70% for all other ldcs, with a 50% butoir. The textile régime is, however, further complicated by MFA restrictions.¹⁵ All poor countries including msas can benefit from these adjustments of the GSP for textiles, but given the restrictiveness of the overall tariff quotas and of the MFA inhibiting trade expansion, the concessions are of negligible utility. Finally, in 1978, the Commission proposed that no least developed country should have to pay duty on semi-sensitive or non-sensitive items, even when EEC ceilings for these products have been reached. In addition, changes in the administration of textile products are planned for 1979, favouring the least developed countries particularly.

The confusion produced by these attempts to discriminate between ldcs is visible in Table 3.5. This shows the value of dutiable exports from different ldcs to the EEC covered by the GSP (column 5), the share of their GSP eligible trade restricted by quotas or ceilings (column 7), and the share of all dutiable imports which enter without restrictions under the GSP (column 8). As one would expect, some of the more advanced and richer ldcs achieve relatively little unrestricted access under the GSP, notably Hong Kong, Brazil, Argentina, and Algeria. Some of the poorer and/or less industrialised do well on this measure, such as the Philippines, Peru, and Malaysia. However, there are some remarkable anomalies. The richest country (in per capita terms) in the sample, Singapore, has a high share (38%) of its dutiable exports benefiting from unrestricted GSP treatment. The least generous treatment is accorded to one of the poorest, Egypt, with Colombia, Pakistan, and Thailand also doing badly. India is another of those less favourably treated. A rank correlation test between these figures (column 8) and per capita income (column 1) gave a negative result ($R = -0.245$, $N = 19$); the restrictions on GSP use therefore appear to be relatively more severe for the poorest ldcs, quite the reverse of what one could reasonably expect.

To sum up, attempts by the EEC to discriminate between various groups of ldcs appear to have some justification, but there are serious problems. A per capita income criterion is the most straightforward, but it is arbitrary and possibly ambiguous. In practice it is also unacceptable to producer interests in the EEC which are afraid of competition from certain low income ldcs, notably India.

Table 3.5 Benefits of the EEC's GSP by Country (ranked by per capita income)

	(1) 1976 GNP per capita (\$)	(2) Total exports to EEC-9 ^a (\$m)	(3) Mfn exports (non-GSP) (\$m)	(4) % of which duty- free	(5) Total GSP eligible exports (\$m)	(6) GSP sensitive/ semi- sensitive (\$m)	(7) (6) as % of (5)	(8) GSP non- sensitive as % of all dutiabale exports to EEC ^b	(9) Difference in ranking [(1) - (8)]
India	150	546.1	353.6	60	188.5	91.7	49	29.1	- 8
Pakistan ^c	170	220.8	138.9	68	80.9	65.5	81	10.2	- 12
Sri Lanka ^d	250	91.8	71.3	26	20.4	0.8	4	26.8	- 7
Egypt	280	156.0	122.1	78	20.8	20.7	100	0	- 15
Thailand	380	171.1	155.7	43	14.4	4.2	29	9.8	- 10
Philippines	410	176.1	134.1	97	41.9	5.3	13	79.7	+ 4
Colombia	640	215.2	197.6	18	17.5	10.3	59	3.9	- 11
Korea	670	125.6	16.7	26	108.7	87.8	81	9.4	- 8
Cuba	710	56.2	44.4	24	11.8	0.1	1	25.7	- 2
Peru	800	307.7	206.3	93	101.1	0.4	0	87.1	+ 9
Malaysia	860	411.0	232.8	92	86.6	8.2	9	69.7	+ 8
Algeria	990	853.7	799.3	93	53.6	13.8	26	36.3	+ 4
Chile	1050	401.4	389.6	98	11.3	0.3	3	57.6	+ 9
Lebanon	1070 ^e	98.4	76.8	94	21.2	8.1	38	50.7	+ 8
Mexico	1090	148.5	86.5	63	59.2	12.8	22	50.9	+ 10
Brazil	1140	1488.7	1266.7	52	218.5	49.1	22	20.5	+ 4
Argentina	1550	1057.8	934.8	18	121.7	5.7	5	13.1	+ 4
Hong Kong	1610 ^e	922.1	629.3	5	225.8	154.9	67	8.0	+ 1
Singapore	2700	189.0	112.2	42	75.2	21.7	29	38.2	+ 12

Notes: ^a 1975 trade flows

^b The percentage is derived from (5)-(6) divided by [(5) plus (3) times 100 - (4)%]

^c Pakistan figures include Bangladesh exports to the EEC-9

^d and Maldives

^e 1974 figures

Source: Compiled from UNCTAD Research Memorandum No. 57, 1976.

A criterion based on trade performance by product, however, is highly complex and penalises any form of product specialisation. An overall performance criterion is more manageable but would mean preferences for high income but inefficient producers of manufactures, such as Venezuela or Saudi Arabia, and not for some of the poorest ldcs (India and Pakistan). These doubts combine to make one question the whole notion of such discrimination. It is highly debatable whether poor and/or non-industrialised countries benefit from discrimination against those somewhat more advanced. And if the latter are so far along the road as no longer to be 'developing countries' then perhaps they should no longer be in the GSP scheme. On the other hand, it is possible that whatever discriminatory devices are used, there can be no developmental bias in the GSP as long as textile imports from the poorer ldcs are subject to restricted dutiable access. Textile products

(clothing especially) are invariably the first step in manufactured export-led growth for ldc's trying to develop labour-intensive exports for trade, yet the EEC régime penalises them for it. This tangle will have to be sorted out when the scheme is redrafted in 1980. So far attempts at piecemeal reform have complicated the situation without significantly improving it.

The GSP and Agriculture

Another way in which the EEC has attempted to help the poorer and smaller ldc's has been in the extension of the GSP coverage of agricultural items, since these ldc's are more likely to be interested in adding value by processing their agricultural products or in eliminating duties on non-processed items, than establishing an entirely new industrial base. Accordingly the number of agricultural items covered by the scheme has been increased in stages from only a few in 1971, valued at some 45,000 ua, to 311 items in 1978, valued at 1,300 mua. Over one-fifth of the GSP eligible trade, therefore, is now in agricultural goods. At the same time there have been gradual increases in the tariff cuts. But it is tempting to overstate the value of these changes. Most of the tariff cuts have been modest—only 25% of the 311 items have had complete elimination of duties, and 60% of the remainder have had cuts of under 50%. Several of the most important processed agricultural items in the EEC GSP, such as cocoa butter, soluble coffee and preserved pineapples face tariff quotas. There has also been little progress under the GSP on items about which EEC members are sensitive,¹⁶ notably CAP items, and in other cases such as coffee, cocoa, and some spices, ACP countries have resisted the extension of GSP preferences, though not always successfully. It is in any event questionable whether GSP concessions rather than mfn tariff cuts are the appropriate vehicle for stimulating trade in those agricultural products for which there are usually no dc competitors. In fact, in its mfn tropical products offer made at the Geneva MTN in 1977, the EEC promised concessions on coffee and cocoa, as well as binding concessions already made on tea in bags and packets.

Administrative Complexity

As a result of this desire to discriminate in favour of certain groups of ldc's in addition to the need to make concessions to producer interests in Europe, the GSP is growing extremely complex. Complexity is in itself a barrier to trade especially when ldc producers and exporters are small, disorganised and unable to respond quickly to take advantage of changes in detailed regulations. One problem arises because inexperienced exporters are not familiar with the precise product specification of the EEC tariff code and conditions governing preferential margins, and as a result suffer loss through incorrect pricing. For example some years ago one South Asian exporter sold a substantial volume of shrimps to an importer in one EEC country on the assumption (and assurance) that the product was covered by GSP. Customs officials declared that the shrimps

did not qualify for the 11-12% preferential margin, which is available on two types of shrimps, and the full mfn duty had to be paid. The importer sued the exporter for the losses incurred. (In fact this story had a happy ending—the customs officials were eventually proved wrong—but the case illustrates the risks.) Product mis-specification is not merely a question of exporter error. Producers in Europe can easily take advantage of any ambiguity to initiate a complaint, for a semi-sensitive item for example, based on a level of aggregation appropriate to their own interests.

Where tariff quotas are concerned the risks for exporters are even greater and the potential gain less. Considerable experience is usually required, as well as established contacts in Europe and warehousing, to get imports in under the tariff quota before its expiry at the beginning of the year, and to exploit market information on under-utilised quotas to arrange rapid trans-shipment. There is a long time lag before exporting countries receive notice that a particular quota has been exhausted. Exporters who price their goods on the assumption that no duty will be paid, stand to lose heavily should they have to pay duty, hence few do, and the importer pockets the duty reductions, if any, as a windfall gain. Thus the importer is the main beneficiary of the GSP. He may subsequently choose to place more orders in Idcs as a result of these gains, but if they are unpredictable this is less likely. European governments have, of course, the discretion to choose which importers benefit and different governments operate on different principles. One system—as in Benelux—is a 'first come, first served' or 'greyhound' principle, which encourages 'racing' in imports. This has the merit of simplicity, but favours big, well organised importing concerns with warehousing facilities, who will in turn tend to prefer to co-ordinate their activities with larger and closer suppliers. A second system, used by the French, is by prior allocation of tariff quotas to importers. This gets around the defects of the first system but creates others, notably under-utilisation, unless there are provisions built in for rapid return of unused quotas, and a strengthening of the bargaining position of importers (who cannot lose money in the absence of uncertainty) relative to exporters. In France there is a further problem that many tariff quotas are deliberately channelled to competing French producers who may wish to 'sterilise' them. Britain runs a more flexible and sophisticated hybrid system. For some thirty products whose tariff quotas are likely to be exhausted within the first few days of the year a 'banding' system is operated: all imports registered at customs by, say, 2 pm on 4 January each year share the quota. For example if the value of imports registered is twice the value of the quota then they are given only half the GSP tariff reduction. (Imports after this date must pay the full mfn duty.) For the remaining products the tariff quota is allocated on a 'first come, first served' basis. In fact, this summary is to simplify considerably since in 1978 all sensitive items come under a 20% Community reserve system, and further allocations can take place, using this reserve, once the tariff quota utilised reaches the 80% limit.

The cumulative effect of the tendency to greater complexity and frequent changes in the rules, is uncertainty. This effectively undermines one of the main aims of the GSP, to give an incentive not just to casual exports, but to new investment in export capacity. Because of the complexities involved in country quotas, ceilings, butoirs, etc there has been pressure on the EEC to introduce a comprehensive system of information pooling so that exporters know where they stand with regard to utilisation of quotas and ceilings and can therefore switch markets or products to take advantage of unutilised quotas. The EEC promised an information centre in Brussels two years ago, but the Council of Ministers vetoed expenditure when it was proposed in 1976 and there is no sign of agreement yet. Hostility to the centre was based in part on British objections (which were raised in the European Parliament) that the centre would not be democratically accountable for its expenditure, and on the wish of the French to restrict the scope of the centre to the ACP states. The French point reflects disagreement over whether the centre should be promotional or for information (in the latter case the ACP states would have no interest). Consequently, it seems unlikely that anything will be operational before 1980 when the GSP in its current form expires.

Rules of Origin¹⁸

In order to prevent the GSP provisions leading to 'paper-processing' or the re-export by multinational companies of products with little local value added (originating either in industrialised countries, or other ldc's restrained under quotas) all GSP systems have rules of origins. The EEC specifies three conditions:

(1) Processing: exporters are required to establish that the product has a minimum degree of domestic processing. This is not an issue which is in general particularly relevant for two of the four South Asian exporters. In India and Pakistan the domestic economy is sufficiently sophisticated to provide most domestic inputs. But, both there and in Sri Lanka, Export Processing Zones are being set up which encourage the use of imported inputs and the issue could become important. The EEC defines the minimum degree of processing in terms of a 'process' criterion, unless it is wholly produced locally in which case the problem does not arise—though proof must still be offered. Under this criterion, processing is defined in terms of the extent of the change in tariff headings of the contributing inputs as they become output. Since this measure is often ambiguous, long lists of exemptions have been drawn up to specify processes which satisfy the criterion but are not acceptable (list A) and others which do not but are acceptable (list B). These lists are very long and as a consequence are extremely difficult to administer. Capricious definitions also make for further problems. Murray quotes the case of transistor radios and plastic manufactures, where EEC rules of origin effectively require ldc's to have their own industries for making transistors and plastic materials. Not surprisingly, few (except India) do.

There is, however, one qualifying factor which weakens the restrictive impact of the GSP rules of origin. This is the provision for 'cumulative origin' under which other ldc inputs can be calculated as domestic. The EEC has permitted this for ASEAN, the Andean Group and the Central American Common Market. No South Asian country benefits in this way and there is a case for them to press for all inter-ldc trade to be treated as 'cumulative'. Certainly intra-South Asian trade could be. Another qualification which the EEC could introduce, following the example of the German and Dutch 'offshore assembly provisions', would be duty-free treatment for products assembled in ldcs from EEC inputs or components, regardless of the degree of value-added in the ldcs. Finger has shown that such provisions could be an effective means of encouraging 'a labour-rich country to perform the parts of the production process in which it has comparative advantage'.¹⁹ The advantage of these rules of origin can, however, be problematical, especially if each GSP scheme has its own. For an ldc to ensure that an export qualifies for each GSP scheme, separate production lines for each market may be necessary. If this is indeed the outcome, then it would represent a very strong criticism of the whole GSP apparatus.

(2) Documentary evidence: as proof that the above requirements have been met, certificates of origin are required, officially certified by an acknowledged agency. Official certification is no longer a problem in most cases, once the certificate has been presented. It is the preparation of the certificate which makes for difficulties, given the complexities described above, and this can cause delay and loss of money to the importer or exporter. This is a particular problem when the export industry is itself an assembly operation of a variety of inputs each with different degrees of processing.

(3) Consignment: goods must be sent directly, not through another state. Since none of the four South Asian states is landlocked, this does not present immediate problems. But it does impose lack of flexibility in terms of re-routing, to take advantage of rapid market shifts. There is also considerable difficulty for exports which have to be directed to a non-beneficiary country for final stage operations. For example, Afghan carpets which have to be washed in special Swiss factories do not qualify for GSP.

Although the rules of origin present problems, and could be improved, it is easy to understand why they exist. The GSP would be quickly discredited if it were used to encourage the packaging of Japanese exports by ldc merchant houses. The main complaint which ldcs make is that different developed countries have different schemes each immensely complex. Since the EEC's is the most used it has the least reason for changing, but for countries like New Zealand and Finland to have separate and quite different rules is absurd.

The GSP and South Asia

What emerges from the above is that 'GSP schemes of the EEC have been consistently improving in favour of the developing countries though the pace of improvements is altogether rather slow'.²⁰ Of more direct relevance here, is the way in which these changes have directly impinged on the four South Asian countries, in particular India and Pakistan which have a high volume of dutiable items, proportionately very large for Pakistan (81%). As Table 3.6 shows a high percentage of their dutiable trade, though covered by the GSP is sensitive or semi-sensitive and so restricted by tariff quotas and ceilings; 61% in the case of Pakistan and 19% in India's, while Sri Lanka and Bangladesh have virtually none.

Table 3.6 Tariff Treatment of South Asian Exports to the EEC^a

	Sri Lanka		Bangladesh		India		Pakistan	
	mua	%	mua	%	mua	%	mua	%
Non-dutiable	67.7	74	24.0	51	440.9	63	36.2	19
Dutiable, of which:	23.6	35	23.4	29	254.9	37	152.1	81
total GSP-covered	22.9	34	12.5	26	223.4	32	130.6	69
GSP sensitive	0.9	1	—	—	101.4	15	100.7	53
GSP semi-sensitive	1.5	2	—	—	26.3	4	14.9	8
Sample total	91.3	100	47.4	100	695.8	100	188.3	100
(Total Exports)	(98.4)		(51.7)		(728.2)		(209.0)	

Note: ^a sample composed of four digit NIMEXE over 1 mua only, exported in 1975, using 1977 tariffs.

Source: EEC, NIMEXE Import Statistics, 1975 and EEC, *Practical Guide to the Use of the European Committees' Scheme of Generalised Tariff Preferences*, Brussels, 1977.

A rough indication of the importance of the GSP to South Asia was obtained by calculating the fiscal gain from 1975 trade flows, the last year for which data exist (see Table 3.7). The rationale and assumptions behind the use of this measure are discussed in more detail below, but essentially it measures the customs duty forgone by the EEC on a given set of trade flows, and therefore the fiscal gain to South Asian exports if all of the benefit is passed back. Some problems were encountered in making this calculation, notably in terms of estimating how much of 'sensitive' or 'ceiling' items entered duty free. Where possible, use was made of maximum exporting country amounts, or butoirs. There were two (unavoidable) deficiencies in this method. First it over-stated the fiscal gain since EEC member country national quotas, rather than the Community-level butoirs, act as the real constraints. Where import patterns do not correspond with the distribution of member country quotas, substantial duty could be paid in some countries even though the overall Community butoir has not been reached. Second, it understates the fiscal gain when, as sometimes seems to be the case, the butoir is not in practice triggered when it should be; for example, this has

happened with imports of tobacco from India, carpets, women's outer wear and bedlinen from Pakistan. In the case of textile products this could be because some items recorded together in the trade statistics enter, separately, under the handloom products tariff quota.

Table 3.7 Static Value of Preferences (1975, mua)

	Sri Lanka	Bangladesh	Pakistan	India
Total exports to EEC	91.3	47.4	188.3	695.8
Dutiable items	23.6	23.4	152.1	254.9
Static Value of Preferences				
— on all items	1.0	2.2	14.3	17.1
— on sensitive or semi-sensitive items	0.17	—	13.3 (of which 10.0 for carpets)	9.4 (of which 5.4 for tobacco)
— on quantity restricted items	—	2.1 (jute products)	0.5	4.4 (of which 3.0 for jute products)
Value of Preferences				
as % of dutiable exports	4.2	9.4	9.4	6.7
as % of total exports	1.1	4.6	7.6	2.5

Source: as per Table 3.6.

Looked at in this way (Table 3.7) the GSP in 1975 was worth roughly 14 mua to Pakistan and 17 mua to India. Proportionately this was worth more to Pakistan but almost all its benefit accrued to sensitive items, which means that the trade stimulating effect is substantially diminished by tariffs at the margin. Handwoven carpets accounted for 10 mua, over two thirds of the total. India's gains accrued rather more to non-sensitive items. Tobacco attracts most of the benefit, followed by jute products. Bangladesh has, with Pakistan, the highest fiscal gain in relation to dutiable exports, but almost all is for jute products which are quantity restricted and therefore unable to benefit from trade stimulation. Of the total fiscal gain to South Asia of about 35 mua only a minority in practice seems likely to be passed back to the exporter rather than absorbed by intermediaries.

Table 3.8 National Quota Shares and Imports from South Asia in 1975

	Imports allowed under GSP Quota	(tonnes)		Imports from India	Share of EEC quota	(percentage)		
		Actual Imports from all ldcs	Imports from Pakistan			Share of EEC imports from ldcs	Share of EEC imports from Pakistan	Share of EEC imports from India
58.01 ex A Carpets (<350 knots/m of warp)								
Germany	765.45	8283	26	2600	27	74	8	77
France	538.65	409	4	39	19	4	2	1
Italy	396.90	64	17	6	15	1	5	0
Benelux	283.50	612	20	269	10	6	3	8
UK	623.70	1494	291	421	22	14	81	13
Ireland	28.35	na	na	na	1	na	na	na
Denmark	198.45	59	3	30	7	1	1	1
Total	2835.00	10921	361	3365	100	100	100	100
62.02 Cotton and other bedlinen^a (India hits EEC butoir)								
Germany	15.66	9552	208	1958	27	57	26	44
France	11.02	343	20	104	19	2	2	2
Italy	8.02	251	180	64	14	1	22	1
Benelux	5.80	1223	109	379	10	—	13	9
UK	12.76	4878	257	1444	22	29	32	33
Ireland	0.58	46	0	1	1	0	0	0
Denmark	4.06	740	37	470	7	4	5	11
Total	57.90	17033	811	4420	100	100	100	100
42.02 B Travel Goods								
	(000 ua)							
Germany	2708	30416	—	331	27.5	52	—	20
France	1871	4886	—	118	19	9	—	7
Italy	1477	896	—	56	15	2	—	3
Benelux	1034	7286	—	182	10.5	13	—	10
UK	2166	11627	—	895	22	20	—	55
Ireland	99	220	—	6	1	0	—	0
Denmark	492	2059	—	42	5	4	—	3
Total	9847	57390	—	1630	100	101	—	98
55.09 A II Unbleached cotton fabric (85-115cm wide)								
			Pakistan & India				Pakistan & India	
Germany	325.89	8953	502		27	29	4	
France	229.33	3924	883		19	13	7	
Italy	168.98	3455	340		14	10	3	
Benelux	120.70	2056	308		10	7	3	
UK	265.54	12636	10055		22	41	81	
Ireland	12.07	na	na		1	na	na	
Denmark	84.49	61	22		7	0	2	
Total	1207.00	31085	12110		100	100	100	

Note: ^a GSP quotas for cotton and other bedlinen are separate but as quota for other bedlinen is very small—and imports from South Asia of other bedlinen are also small—they are considered together here.

Source: As per Table 3.5.

Improvements have been registered in recent years; as regards items which are affected by ceilings or quotas, there has been a small improvement in two directions. The first was the switching of some items in 1974 and 1975 from the sensitive to semi-sensitive list. Of products of interest to South Asia, however, only leather gloves and imitation jewellery were switched and neither are important products, except gloves to Pakistan. The second has been the increase in quotas and ceilings though, as we have seen, these have lagged considerably behind the expansion of non-sensitive ceilings. In 1976 for about half their sensitive items (other footwear, some cotton yarn, some cotton fabric, women's cotton outer wear, carpets and bedlinen) India and Pakistan hit the butoir for the EEC as a whole. The restrictiveness is in practice much more severe since the real constraint is the EEC member allocation of the tariff quota. For the UK the quota share was exhausted for two-thirds of its imports of sensitive items from all ldc's and for over half of these in the first few days of the year. This effectively penalises countries, like South Asia, with traditional links with the UK.

As an illustration of the restrictiveness or otherwise of EEC member country quotas, four 'sensitive' products of interest to South Asia were chosen for detailed analysis (Table 3.8); carpets (<350 knots/m of warp), bedlinen, travel goods, and cotton fabric. It is worth noting that in every case except Indian carpets South Asian exports are much more heavily skewed to the UK market than is the distribution of EEC quotas amongst the nine members. Thus exports from South Asia have mfn duties reimposed on them earlier than those from most ldc's. Indian carpets, however, were largely exported to Germany, in fact Indian carpets to Germany exceeded Germany's national quota in 1975. Exports to the EEC as a whole hit the butoir as early as February 1975 and for the rest of the year Indian carpets had to pay the full duty, although the national quotas of three members (France, Italy, and Denmark) remained unused. This illustrates how butoirs, which were in theory introduced to prevent certain ldc's over-utilising the GSP, in practice result in under-utilisation of GSP quotas. The system works somewhat better in the case of bedlinen: both Indian and Pakistani suppliers hit the butoir, but at the same time all nine country quotas were rapidly exhausted. In the case of travel goods, India paid duties at an earlier stage of the year as a result of overall ldc imports reaching national quota limits, but Italy's share remained largely unused. The same was true of cotton fabrics, where butoirs were triggered too, but Denmark's share was never fully used.

As far as semi-sensitive items are concerned, only in one case in 1976 was the EEC ceiling not exceeded (gloves). For half of the items India hit the butoir before the ceiling was reached and so these had to pay full duties before imports from other ldc's.

Certain products have been given special concessions. Of these, two are overwhelmingly important in GSP terms, given the volumes currently traded and the height of the tariff. On *carpets*, an important item with a very high mfn tariff of

24%, the butoir for carpets of under 500 knots per metre of warp was raised in 1977 to 1892 tonnes of which 1325 tonnes applies to the EEC-6. 780 tonnes was the limit in 1972 for the EEC-6, when it applied to carpets of under 350 knots per square metre. There was to be a further widening of the butoir to 1988 tonnes in 1978. This level of restriction is still a tariff barrier. Pakistan exported in 1975, 2233 tonnes under the new category, and India 3900 tonnes. Thus in 1977 the butoir was exceeded by each country on 1975 trade figures and the total tariff quota by them both together (Iran also exports in competition). Up to and including 1976 only India was affected by the tariff quota since its products were heavily concentrated in the cheaper range covered by the then quota. The widening of the product definition has made the quota less restrictive for India, but has for the first time brought Pakistan under the threat of tariffs, as previously its carpets, which are fine (ie finer than 350 knots per metre of warp), were free from quotas altogether. Since European factory-made carpets can hardly compete with the superior qualities of these hand-made carpets the rationale behind this adjustment of quotas is difficult to understand. The effect is to limit the value of the GSP concessions, in trade expansion terms, for South Asia as a whole.

Clearer benefits have occurred from the liberalisation of access for tobacco. For the cheaper variety of unmanufactured flue-cured Virginia type tobacco the tariff quota is fixed at 60,000 tonnes pa (1977 and 1978) and within this tobacco enters at a reduced duty (7% with a maximum of 45 ua per 100 kg as against the mfn rate of 14% with a maximum of 45 ua per 100 kg). The mfn duty has also been cut, from 23% to 14% since 1972. Before 1974 tobacco was not admitted to the GSP system and the initial tariff quota was a mere 20,000 tonnes, so the improvements are obvious. South Asian exports under this heading were 30,000 tonnes in 1975 and since there is no butoir, most of this can expect to enter duty-free. However, there are important qualifications to this concession. There is competition from other GSP suppliers of the 590,000 tonnes (approximately) imported altogether. 45% approximately were from GSP sources including Brazil, Mozambique, South Korea, Mexico, Argentina, and Thailand. Further, the existing sales of South Asian tobacco are heavily skewed to the UK market. Although the UK has a specially high quota share (58%) this barely covers imports from South Asia alone. Finally the specific duty which can replace the ad valorem duty on low value imports means the duty paid may be well above 7%. (The implications of these various qualifications are considered separately in a paper on South Asian exports of tobacco to the EEC, available from ODI upon request.)

On agricultural items generally, a whole series of duty concessions have been made, largely designed to help the South Asian members of the Commonwealth. Helpful reductions have been obtained for pepper and other spices, castor oil, coconut oil, shrimps, frogs' legs, mangoes, dal, gram, and nuts.²¹ Some are, however, miserly to the point of worthlessness, such as the reduction from 6%

to 5% on mangoes and 8% to 6% on castor oil. Nor has there been any encroachment on CAP products such as rice and molasses. More technical problems have arisen in the South Asian drive for extensive product category subdivision for exotic specialities. In many cases, the tariffs are not protective, since there is no substitute. Tariffs serve in these cases as special taxes on Asians (in Britain) and patrons of Asian restaurants. One amusing but typical case is that of Indian papadums or 'papad', which were classed together in the customs tariff nomenclature with Italian pasta (lasagne, spaghetti, etc). The Italians were reluctant to concede tariff-free access, and it required special tasting sessions to establish that papadums were no substitute for pasta. Even when the case was conceded on culinary grounds, there were still bureaucratic objections to splitting an already specialised tariff group—'X'ing the X's, in Community parlance. Victory was eventually gained. 'Papads' now enter free under a special heading. Similar concessions were obtained for coriander and cumin seeds (which otherwise paid duty of 11% to protect EEC badian seed growers), pawpaws, tamarinds, guavas (otherwise dutiable at 5%, as mangoes), chickpeas, and okra. Not all of course are solely of interest to South Asia.

Finally, there have been specific concessions on jute and coir. Jute and coir product tariffs have now been eliminated; the UK continued to give duty-free access under the first set of agreements between India and Bangladesh and the EEC, while the remaining EEC duties were cut substantially. The tariffs have now been removed. However, both products still face quantity controls. The effect of these is considered in greater detail in a paper available upon request from ODI.

Methodology for Evaluating GSP changes Affecting South Asia

Exercise I — Static Value of Preferences

One specific question which we shall try to answer is whether the modifications in the GSP since 1973 have compensated South Asia for the loss of preferential access in the UK market, both in the form of higher duties (in some cases) and in the loss of Commonwealth Preferences. The answer should help us to understand whether the JDI has in practice been honoured, or whether more remains to be done, over and above the case for more easy access to the EEC for Asia on other economic or developmental grounds.

The methodology followed in the first estimation, as in Tulloch's earlier study *The Seven Outside*, is to evaluate the static value of preferences as the fiscal cost to the donor. This is simply done for one year (1975) by multiplying the value of South Asian trade by the tariff preference margin. There are several implied assumptions in using this method. First, it assumes an efficiently functioning market economy and one in which the preferred supplier is a price taker. This assumption may be invalid if, for example, South Asian suppliers

have a substantial share of the market (as they do for jute, and some spices). They may moreover, even as small suppliers, choose to reduce prices below the market price to expand their market share, rather than retain the extra profit arriving from tariff preference.

This point underlines the second general assumption which we are making which is that dynamic consequences of tariff preferences are ignored. Not only are the static values weighted by the existing trade structure rather than the trend changes in it, but the effects of changing preferences on trade flows are ignored. If price elasticities of import demand are high as they are for most manufactured goods in the long run, this would have the effect of understating considerably the gains from preferences. For this reason, some writers disregard static analysis entirely. However, we believe this is mistaken. For sensitive and semi-sensitive items which account for the majority of present EEC trade with South Asia, and also for quantity restricted items (textiles and jute), dynamic factors are less relevant. Because full duty is payable at the margin there is little or no incentive to expand production for export. Some exporters may use these profits to subsidise marginal exports but there is no reason to assume that they all behave in this way. For the remainder, non-sensitive, items we are concerned in this exercise only with *improvements* in the GSP scheme since UK entry. Since no major manufacturing items have been added to the non-sensitive list, nor any significant further reductions made in GSP duty, there is no great distortion by ignoring them. There have been tariff cuts, unbounded by ceilings, on agricultural items mostly processed and semi-processed. But for agricultural items generally, elasticities of supply and demand are low, and for very few items have tariff cuts exceeded 5%, which is normally regarded as minimal to evoke much producer or consumer response. Thus the dynamic consequences of adjustments in the preference scheme since 1973 must be regarded as rather small. The use of static value analysis, or fiscal transfer effect, seems therefore to have theoretical merit as well as the virtue of simplicity, at least for this limited purpose.

Another simplification we make is that tariff changes are analysed in terms which are identical to those of an mfn tariff reduction applied in a non-discriminatory manner. This measures, as well as the maximum potential fiscal transfer, the potential trade creation gains for those products which are not restricted by ceilings. It ignores the discriminatory aspect of preferences which indicate the potential for trade diversion (again, depending upon the relevant elasticities). This is a factor in the loss of Commonwealth Preference as well as in the GSP.

A final assumption and perhaps the most questionable one is that the fiscal value of the preferences is transferred to the exporter. Such is the substantial share of shippers', importers', wholesalers' and retailers' margins (up to 500% of Asian fob prices in some cases) that inevitably a substantial part of the

preference value will be 'lost' here. For this reason, we probably exaggerate considerably the gains or losses, especially from the adjustment of ceilings on sensitive items where exporters are at a particularly acute disadvantage in benefitting from short term and complex administrative changes.

We consider two elements: first the effect on South Asian suppliers of changes in the UK market and, second, in the EEC. As far as the latter is concerned we assume that all improvements in GSP terms since 1972 can be credited to the effects of UK entry and the JDI. This is a somewhat generous assumption since improvements in ceilings would probably have occurred anyway given the EEC's general commitment to offset inflationary erosion. Specifically we calculate for sensitive items the maximum possible benefit which a specific country could obtain, which is the full utilisation of the butoir. We compare the value of the butoir in 1972 and 1977 (or 1978 where possible) using 1975 import values (the latest available in the NIMEXE series). The comparison for the EEC-6 is made by allocating to them a share of the butoir based on their national share of the EEC quota, which is 72% (70% for textiles). By making this calculation we are inflating the gains, since we are ignoring the effect of the restrictiveness of the individual national country quota allocations in the EEC-6 (even with a Community reserve), and we are disregarding the fact that because of competing suppliers the butoir was not reached by South Asian suppliers in all cases. Thus the figure represents a maximum rather than an actual improvement in the value of the GSP for sensitive items. For semi-sensitive items we have a difficult problem in that the butoirs within the ceilings are sometimes substantially higher than the amount imported. This applies to leather gloves (formerly sensitive), medical instruments and sports goods (formerly non-sensitive). In the first of these cases the 'gain' in GSP terms is measured by the preference margin multiplied by the difference between the 1972 EEC-6 butoir and the amount actually imported in 1975. In the other two cases where there has been some retrogression, but to a level where very few if any imports are dutiable (the ceiling for sports equipment was reached in mid-December 1976) no gain or loss is assessed. Finally there are those items whose status has not changed since 1972: non-sensitive items bearing reduced or zero duty. It could be argued that in one sense the South Asians have 'gained' to the extent that they can export larger quantities to the EEC-6 under increased 'ceilings'. To include this, however, would be to stretch to nonsensical limits the concept of improvement, when *de facto* free access had already been conceded before UK entry and the JDI. For illustration only, the total fiscal value of GSP preferences on sensitive and semi-sensitive items is calculated for South Asian exports to the EEC-6 which represents both improvements and original concessions. However, the distinction needs to be made clearly between improvements and original concessions.

The losses or gains in the UK market are more easily calculated. For those few items not included in the original UK GSP scheme, where Commonwealth Preferences were relevant, the static value is calculated (Commonwealth

Preferences in fact expired on 1st January 1978). It is of course possible that even in the absence of UK entry Commonwealth Preferences might have disappeared gradually by incorporation in the UK GSP or through mfn concessions, but there is no evidence that the UK was contemplating this for products of particular interest to South Asia, especially tobacco and cotton garments. A second effect to calculate is that which follows from alignment to the EEC's CET and GSP. In some cases this has involved South Asian exporters paying duty even with the GSP in the UK market, notably on tobacco, shrimps, rice, and leather. In other cases, notably cotton textiles, there is a liberalising influence from duty-free entry (up to the UK country share of the quota for sensitive items) when previously duty was paid.

Results

It is perhaps useful to compare our results with those of the Tulloch study.

Table 3.9 Summary of Annual Fiscal Gains and Losses from UK Adoption of the EEC GSP: Tulloch Study (1972 scheme; 1970 import figures) (\$m)

	India	Pakistan	Bangladesh	Sri Lanka	All South Asia
Agricultural exports to UK (BTN 0-24)	161	10	—	81	252
Industrial exports to UK (BTN 25-29)	<u>90</u>	<u>30</u>	—	<u>6</u>	<u>126</u>
	<u>251</u>	<u>40</u>		<u>87</u>	<u>378</u>
Static value of Commonwealth Preference losses on:					
— Agricultural exports	-10.5	-1.2	-0.3	-0.3	-12.3
— Industrial exports	<u>-2.0</u>	<u>-0.4</u>	<u>-0.1</u>	<u>—</u>	<u>-2.5</u>
Total	<u>-12.5</u>	<u>-1.6</u>	<u>-0.4</u>	<u>-0.3</u>	<u>-14.8</u>
Static value of GSP gains/losses	-0.69	-0.10	—	-0.27	-1.06
From adoption by UK of EEC GSP	<u>+1.80</u>	<u>+0.76</u>	—	<u>—</u>	<u>+2.56</u>
	<u>+1.11</u>	<u>+0.86</u>		<u>-0.27</u>	<u>+1.50</u>
Overall	-11.39	-0.74	-0.4	-0.57	-13.3

Source: Compiled from Tulloch, *The Seven Outside*, op cit.

The Tulloch study found that overwhelmingly the largest element in the static gain and loss calculation was the loss of Commonwealth Preferences. This was particularly large for India, although only a few products were affected, as they were important Indian exports: the loss from tobacco was \$7.4m, oil cakes \$2m,

and leather \$0.9m. In addition there was a loss from the adoption of the CET on agricultural items which had duty-free access to the UK. On the other hand, the South Asian suppliers would benefit under the EEC rules from some duty-free access, up to tariff quotas and ceilings, not permitted in the UK. This benefit appears, however, to have been over-estimated by taking the overall butoir, rather than the more limited quota shares of the major South Asian markets, as representing the maximum gain. Taking all the above factors into consideration Tulloch estimated a net loss to South Asia equivalent to 1% of Sri Lanka's earnings from exports to the UK, 2% of Pakistan's, and 4.5% of India's.

Our own recalculations (shown in Table 3.10) for the 1975 import values and the 1977 scheme, taking into account improved access to the EEC, suggest a somewhat more positive conclusion. The gains from improved EEC access have more than compensated for losses in the UK market for Pakistan, Sri Lanka, and Bangladesh; though the net gain varies considerably (equivalent to 1.5% of Pakistan's earnings of exports to the UK in 1975, 0.5% of Sri Lanka's and 6% of Bangladesh's), and not all of it may be passed back. For India there is still a significant net loss of broadly the same magnitude, 2.5% of India's exports to the UK. The reason, again, is the heavy weighting given in a fiscal calculation to the loss of Commonwealth Preferences on tobacco and also on some manufactures, notably women's outer wear, of which UK imports from India have increased in the last three years. The gains from EEC duty reductions are also concentrated heavily on one or two items. In the case of Pakistan 2.8 mua out of the total gain from liberalisation of 4.5 mua is attributable to the raising of the carpet quota: while half of India's gain of 3.9 mua is also attributable to the adjustment in the quota as well as more liberal treatment of tobacco in the EEC.

To conclude, tariff adjustments in the EEC-9 since UK entry, have largely compensated three of the four South Asian countries for the 'fiscal' loss of Commonwealth Preferences, and even show a net gain, albeit small. However, we would not make too much of this. The gain is in 'fiscal terms' not in stimulated trade. And it owes as much to the contracting importance of the UK market as to EEC GSP liberalisation. Ironically, given its net fiscal loss, India is perhaps the most pleased of the four South Asian countries about the general effect of the EEC's GSP in assisting the growth of its export industries. These benefits derive from concessions given before UK entry as part of the original GSP (in both the UK and EEC). To this we now turn.

Exercise II – Trade Flow Study

One obvious criticism of a static approach is that, even when there are formal limits to duty-free access, there are dynamic benefits arising from greater confidence and experience in dealing with increasing liberalised markets. Moreover, much of the growth in trade can occur in small, non-traditional categories excluded from our product coverage. This might suggest that, considered over time, the gains or losses from trade preference changes might be substantially larger

than indicated by static values alone. Any attempt to estimate, *ex post*, the wider gains and losses in this case founders on the lack of time series information. British accession to the Community took effect in 1973 and Commonwealth Preferences have been phased out over the 1973-78 period. The EEC GSP became effective only from July 1971. The latest date for which adequate trade data are available is 1975. Thus there is (at best) a three year time series to evaluate 'before/after' effects on an *ex post* basis.

Table 3.10 Annual Gains and Losses from UK Entry to the EEC ('000 ua) (1977 GSP, 1975 trade flows)

PAKISTAN	Loss of Commonwealth Preferences	Adoption of CET by UK	Liberalisation of EEC GSP or mfn rate reduction	Sum
A GSP non-sensitive items				
Shrimps	-26	-15	+13	-28
Other crustaceans	-3	-26	+292	+263
Dried mushrooms	—	—	+43	+43
Fish flour	—	—	+36	+36
Sheep leather	—	—	+37	+37
Others	—	—	+ 4	+ 4
B Non-GSP items				
Long grain rice (CAP item)	-320	-512	—	-832
Molasses (CAP item)	—	-424	—	-424
Light oil	—	+246	—	+246
Linseed oilcakes	-126	—	—	-126
Tanned cow leather	-13	—	—	-13
C GSP sensitive items				
Tobacco	-1740	-406	+367	-1701
Leather gloves	—	—	+245	+245
Cotton yarn	-2	+8	+123	+129
Cotton fabrics	-442	+355	+290	+103
Carpets	—	—	+2816	+2816
Women's undergarments	-57	—	+173	+116
Women's outer wear	-137	+35	+116	+4
Men's/boys' undergarments	-7	+61	+104	+158
Bedlinen	-120	+89	+36	+5
Cotton sacks				+28
Footwear				+183
Sports equipment			-150 ^a	-210
Total	-2993	-589	+4545	+963

BANGLADESH	Loss of Commonwealth Preferences	Adoption of CET by UK	Liberalisation of EEC GSP or mfn rate reduction	Sum
A GSP non-sensitive items				
Frogs' legs	-	-	+22	+22
Other offal	-	-	+16	+16
Shrimps	-60	-4	+22	-42
Jute products	-	-	+1152	+1152
B Non-GSP items				
Freshwater fish	-10	-	+8	-2
Semi-tanned cow kips	-5	-	-	-5
Total	-75	-4	+1220	+1141

SRI LANKA

A GSP non-sensitive items				
Coconuts	-	-	+222	+222
Coconut oil	-29	-5	+117	+83
Tea extracts	-	-	+11	+11
Essential oils	-	-	+11	+11
Light oil	-56	-	-	-56
B Non-GSP items				
Raw cocoa	-	-	+5	+5
Freshwater fish	-10	-1	+8	-3
Tea	-	-	+157	+157
Light oil (other)	-	-	+214	+214
Calves' skins	-36	-	-	-36
C GSP sensitive items				
Tobacco	-276	-64	-	-340
Total	-407	-70	+745	+268

INDIA	Loss of Commonwealth Preferences	Adoption of CET by UK	Liberalisation of EEC GSP or mfn rate reduction	Sum
A GSP non sensitive items				
Frogs' legs	—	—	+94	+94
Shrimps	-12	-19	+43	+12
Other crustaceans	-58	-54	+89	-23
Okra	-18	—	—	-18
Mangoes	-287	-29	—	-316
Pepper	—	-9	+240	+231
Castor oil	-156	-94	+11	-239
Vegetable oils	—	-376	—	-376
Saddlery	—	—	+33	+33
Electrical equipment	—	+3	—	+3
Dump trucks	—	+39	—	+39
Car parts & engines etc	—	+29	—	+29
Jute products & jute mats	—	—	+160	+160
B Non-GSP items				
Walnuts	-69	-55	—	-124
Coffee	-6	-40	+111	+65
Ginger/paprika	—	-53	—	-53
Rice	-166	-266	—	-432
Groundnut & oil seed	-465	—	—	-465
Vegetable products (saps etc)	-44	-16	—	-60
Linseed/castor oil	-153	-77	—	-230
Oilcakes	-448	—	—	-448
Cow kips	-192	—	—	-192
Radio receivers	-1	-21	—	-22
Imitation jewellery	—	-91	—	-91
C GSP sensitive items				
Footwear	—	—	+168	+168
Cotton fabric	-163	+220	+264	+221
Silk shawls	-181	—	—	-181
Carpets	—	—	+1202	+1202
Women's undergarments	-16	—	+210	+194
Women's outer wear	-2077	+83	+262	-1732
Men's/boys' underwear	-97	+80	+255	+238
Bedlinen	-676	-108	+105	-679
Embroidery/lace	-161	—	—	-161
Tobacco	-6809	-1589	+1112	-7286
	-12255	-2443	+4359	-10339

Source: as per Table 3.5.

Some insight might be gained from looking at overall growth figures for exports from South Asia to the EEC-6 and the UK. Indian exports to the EEC-6, for example, rose 23.3% in the period 1970-75 as against 4.6% in the period 1965-70 and 1.6% in 1955-65, and this could be regarded as an indication of improved market access under the GSP. It might, however, suggest one of two other things. The first is an increased market for all imports to the EEC, as a result either of improved access, or a general increase in EEC aggregate demand. This could be isolated by measuring India's share of EEC imports. There seems to have been an improvement in the Indian position, although its share of EEC-6 imports fell from 0.7% in 1955 to 0.4% in 1960, 0.3% in 1965 and 0.2% in 1970, it stabilised thereafter at 0.2%. The second possibility could be that the rise in India's exports to the EEC reflects better export performance generally by the Indians. Indian exports overall grew by 16.3% in the 1970-75 period, as against 1.1% in 1965-70 and 4% in 1955-65. This gives two possible competing hypotheses to explain better Indian performance in the EEC-6 market. If it were possible to separate the influences of general Indian export trends and general EEC import trends one might, for a given time period, be able to identify a residual which could indicate special market factors at work.

We try to do this for the period between 1971 and 1975 by comparing the effect of changing preferential arrangements in the UK and two of the EEC-6 markets (France and Germany). Since overall exports include a substantial amount of primary commodities, whose changes in value reflect price rather than quantity variations, and are anyway scarcely affected by preferences, we looked first at manufactures alone, excluding uncut gems and other unworked metals and minerals. Data problems were serious, especially in obtaining accurate 1975 data, and in combining Pakistan and Bangladesh data. In any event, a comparison of changes between two years is not particularly satisfactory, though the 1971-74 period was used for a cross-check. So the results must be regarded as approximations. Following studies by Young²² and McQueen²³ (who did not, however, separate manufactures) we calculated first, the ratio (r_1) of South Asian export growth to France, Germany, and the UK relative to the growth of the rest of the world's exports to France, Germany, and the UK. Second, we calculated the ratio (r_2) of South Asian export growth to the rest of the world relative to the rest of the world's total export growth. If r_1 is greater than r_2 this is *prima facie* evidence of a positive preferential effect, whether as a result of trade creation or diversion; and vice versa. In order to correct for obvious misinterpretation we separated from the manufactured goods category items subject to quantitative restrictions (mainly textiles and clothing). Finally, in order to test for any time trend influences we calculated r_1 and r_2 for the 1968-71 period as a base for comparison. McQueen carried out regression and time trend analysis to correct these influences but this seemed in the South Asian context, unnecessarily elaborate given the crudity of the data.

Two simple tests should establish *prima facie* evidence of a strong 'preference effect' in the period 1971-75 (or 1971-74)

- (a) $r_1 > r_2$ for France and Germany; $r_2 > r_1$ for the UK
 (b) $(r_1 - r_2)$ 1971-75 $>$ $(r_1 - r_2)$ 1968-71 for France and Germany;
 $(r_1 - r_2)$ 1971-75 $<$ $(r_1 - r_2)$ 1968-71 for Britain.

Table 3.11 summarises the results, which are not conclusive, but give support to the hypothesis of a positive preference effect especially for test (a) for manufactures as a whole. Of eighteen tests of (a) there were only two failures both by negligible amounts. Both France and Germany's manufactured imports from India and Pakistan/Bangladesh increased in the period 1971-75 and 1971-74 at a rate well above the growth of their total manufactured imports and the growth of South Asian manufactured exports. In the case of Britain the effect was predictably negative for Pakistan/Bangladesh exports. But Indian exports seemed unaffected one way or the other. If quantity restricted (QR) items are excluded, the picture is also broadly consistent with the hypotheses, the more so for Indian exports to the UK, except that there is no evidence of any influence on Indian exports to France. The upsurge of Indian garments exports between 1971 and 1975 influenced the overall figures for Anglo-Indian trade significantly. If a time trend is considered, however, the picture is confusing. A positive preference factor would seem to have been operating already for South Asian exports to France and Germany in this pre-GSP period, excepting only Franco-Pakistan trade in non-QR items, and a negative factor for Indian trade to the UK. Of the 24 possible tests of (b), the tests failed 10 times. This suggests that the trade preference factor is not mechanically related to tariff changes but to a whole set of expectations about future trade opportunities. Thus the German 'preference' for Indian and Pakistan/Bangladesh goods, which the statistics show, reflects a growing interest by South Asian and German businessmen in mutual trade which actually preceded the GSP.

Too much should not be made of this exercise. Trade flows are small, and random occurrences could weigh heavily—as the sudden change in fashion which affected Indian handloom cloth garments in Europe in 1974/75. Breaking the analysis down to commodity level (as in Table 3.11) exposes us even more to the danger of generalisations based on very small trade flows, but gives a more detailed picture of what is happening. It indicates for the 1971-74 period 'above normal' growth in trade flows to Germany from India of chemicals, carpets, engineering goods, leather, clothes, and textiles, to France of clothes and chemicals, to Germany from Pakistan/Bangladesh of carpets, leather, textiles, and clothes, and to France of shoes, leather, and carpets. But many of these tendencies were already apparent before 1971, certainly for Indian clothing exports to both countries and leather and chemical exports to Germany. With regard to imports into the UK, the 1971-74 period represented a steady 'below normal' trend for everything except clothes and shoes, continuing broadly the pre-1971 patterns of trade flows.

To conclude, both exercises to evaluate the effect of GSP changes have been retrospective. They suggest that UK entry to the EEC has not had the damaging effect on South Asian trade feared at the time of UK accession. We now turn to more forward-looking work, in an examination of the residual tariff and non-tariff barriers to access in the enlarged EEC.

Table 3.11 Trade Flow Indices^a

	India exports of manufactures ^b				Pakistan/Bangladesh exports of manufactures ^b													
	1968-71		1971-74		1971-75		1968-71		1971-74		1971-75							
	I ₁	I ₂	I ₁ ²	I ₁ ²	I ₁	I ₂	I ₁ ²	I ₁ ²	I ₁	I ₂	I ₁ ²	I ₁ ²						
All manufactures																		
UK	-0.20	0.65	-0.85	0.69	0.60	0.09	-0.44	0.50	-0.94	0.80	0.22	0.58	0.41	0.90	-0.49	0.20	0.74	-0.54
France	0.77	0.65	0.12	1.13	0.60	0.53	1.24	0.50	0.74	0.33	0.22	0.11	2.33	0.90	1.43	1.97	0.74	1.23
Germany	1.08	0.65	0.43	1.37	0.60	0.77	1.45	0.50	0.95	1.75	0.22	1.53	2.37	0.90	1.47	1.81	0.74	1.07
Excluding clothing, textiles, jute																		
UK	0.26	0.24	0.02	0.44	0.69	-0.25	0.47	0.76	-0.29	0.26	0.09	0.17	0.41	1.28	-0.87	0.28	1.18	-0.90
France	0.85	0.24	0.61	0.68	0.69	-0.01	0.86	0.76	0.10	0	0.09	-0.09	1.94	1.28	0.66	1.69	1.18	0.51
Germany	1.81	0.24	1.57	1.11	0.69	0.42	1.22	0.76	0.46	1.41	0.09	1.32	2.14	1.28	0.86	2.50	1.18	1.32

Notes: ^a derivations explained in text. Sri Lanka not considered because of smallness of trade flows.

^b Manufactures = SITC 5 to 8 (inclusive) less SITC 68.

Trade Flow Indices by Product ($r_1 - r_2$)

SITC Categories (<i>Tariff restricted</i>)	India						Pakistan/Bangladesh					
	UK		France		Germany		UK		France		Germany	
	1971-4	1971-5	1971-4	1971-5	1971-4	1971-5	1971-4	1971-5	1971-4	1971-5	1971-4	1971-5
Chemicals	+0.04	-0.02	+0.95	+0.56	+0.30	+0.61	-	-0.75	-	-	-	-
Carpets	-1.08	-0.25	+0.60	-	+2.03	+2.50	-1.84	-2.10	+4.10	+7.20	+2.00	-
Leather	-0.09	-0.26	-0.28	-0.48	+5.48	+4.96	-1.40	-1.70	+0.78	+0.10	-	+3.10
Engineering goods	-0.60	0	+0.23	-0.04	+1.41	+0.18	-1.50	-0.52	-	-	-	-
Shoes	+0.05	-0.47	+1.43	+3.20	-	-	+0.71	+1.25	+2.60	+0.30	-0.12	+0.63
Sports goods	-3.70	-4.00	-	-	+1.90	+1.80	-2.30	-1.25	-	-	-0.54	-0.42
<i>(Quantity restricted)</i>												
Cotton yarn	+0.05	+0.44	-	-	-	-	-0.30	-	-	-	-	-
Cotton cloth	-1.06	-0.71	-0.47	-0.04	+1.01	-0.67	-0.69	-0.50	-	-0.71	-	-2.10
Jute products	+1.59	-	+1.21	-	-1.05	-	+0.67	-	-	-	-	-
Clothing	+1.70	+0.75	+2.96	+3.93	+1.10	+1.44	+0.89	-1.35	-0.66	-0.58	+2.30	+1.64

References

1. The best sources are Tracy Murray, *Trade Preferences for Developing Countries*, London, Macmillan, 1977 and Peter Tulloch, *The Politics of Preferences*, London, Croom Helm/ODI, 1975. For a detailed review of the EEC scheme, see Antonino Pitrone, *EEC GSP Scheme*, Rome, Editrice Commercio Estero, 1977.
2. R.N. Cooper, 'The European Community's System of Generalised Tariff Preferences: A Critique', *Journal of Development Studies*, July 1972, p.384.
3. EEC Commission paper COM (74) 950, 19 June 1974, p.2.
4. COM (75) 280, 11 June 1975, p.2.
5. COM (76) 303, 30 June 1976, p.1.
6. Ibid, p.2.
7. COM (77) 330, 29 July 1976, p.2.
8. COM (76) 303, *op cit*, p.4.
9. Ibid, p3-4.
10. See Pitrone, *op cit*, p.26.
11. COM (78) 470 final.
12. Murray, *op cit*, p.67.
13. Hugh Cubillos, 'Using GSP: Advice to Exporters', *International Trade Forum*, Oct-Dec 1977.
14. COM (75) 280 final, *op cit*, Annex.
15. Pitrone, *op cit*, Ch.4.
16. One interesting case is dried garlic. Attempts to include it have foundered on the politically impossible problem that one of President Giscard d'Estaing's supporters in an important constituency in the South of France owns a farm and plant producing this item.
17. Much of this section draws upon H. Cubillos, *op cit*, and A. Pitrone, *op cit*, together with the authors' personal experiences of exporters' and importers' difficulties.
18. The best summary of the issues is contained in Tracy Murray, *op cit*, Ch.6.

19. J.M. Finger, 'Tariff Provisions for Offshore Assembly and the Exports of Developing Countries', *Economic Journal*, June 1975, p.369.
20. V.R. Panchamukhi, *Effectiveness and Scope for the GSP*, Trade Development Authority, India, 1978.
21. A consideration of the implications for the structure of production and trade of tariff changes on agricultural items also raises the possibility that reductions of duty on goods which are inputs to a processing industry raises the effective protection of domestic production. This matter is dealt with in more detail in the next chapter.
22. Charles Young, 'Association with the EEC: Economic Aspects of the Trade Relationship', *Journal of Common Market Studies*, 1972.
23. M. McQueen, in A. Shlaim and G. Yannapoulos (eds.), *The EEC and the Mediterranean Countries*, Cambridge, CUP, 1976.

4 The Importance of Residual Tariffs as an Access Barrier for South Asian Exports to the EEC

Introduction

The main effect of GSP liberalisation has been to reduce tariff barriers on ldc exports to the EEC of manufactures and some agricultural products. Since most other South Asian items enter duty-free as raw materials, it is reasonable to assume that *in general* tariffs are not a significant access barrier. The purpose of this chapter is fourfold. The first is to test the hypothesis and to examine those products where it does not hold true. The second objective is to evaluate the extent to which tariffs with a preferential element perform a function in discriminating between alternative suppliers. South Asia 'gains' from this trade 'diversion' from GSP but 'loses' from the more generous preferences given to Lomé, EFTA, and Mediterranean competitors. The way in which these conflicting influences are resolved at product level is a matter of interest. Third, for some items, consideration of nominal, rather than effective, protection disguises the barrier which tariff escalation represents to raw material processing by exporters. Thus, reduction of duties on both inputs and final output may leave effective protection unchanged. An attempt is made to investigate this. Finally, there is a review of the negotiating strategy being pursued by the South Asian governments in respect of tariff issues, and an assessment of some of the implications of further tariff liberalisation on products of interest to South Asia, both manufactured and agricultural.

Potential for Further Trade Liberalisation

Our first exercise was to estimate the overall significance of the common external tariff as an access barrier for South Asian exporters, taking into account existing concessions. The method employed is that based upon existing trade values and what we know about price elasticities of import demand in the consuming markets. There are however, some basic problems with this approach which should be spelt out:

- (1) The analysis is demand based. But long-term supply constraints such as a shortage of manufacturing capacity or agricultural land may act to diminish the trade achieved by stimulation of demand achieved through tariff cuts.
- (2) Existing trade values in themselves reflect the tariff structure. High tariff items will tend to be under-represented in the existing weighting, or not present at all. Thus gains from tariff liberalisation on these items will be understated.

(3) There are some cases, notably textiles, jute and CAP items (eg rice) where non-tariff barriers, such as quotas, voluntary export restraints (VERs), or levies are the effective restraint on trade expansion. In these cases the tariff performs little function as an access barrier, which raises the interesting issue of why the Community clings to it. Tariff liberalisation would not noticeably stimulate trade in these products whatever its other benefits.

(4) The effects of tariff escalation are ignored. Cuts in nominal tariffs on finished or intermediate goods may over- or understate changes in the effective protection of processing.

(5) The use of disaggregated price elasticities of demand for imports raises a whole set of issues. In general the first three factors discussed above lead to a downward bias in elasticities derived econometrically from past trade flows, the last to an upward bias. A recent compendium of econometric research revealed, even for what it called 'long run elasticities', large disparities in the estimates for each product, depending upon the importing country and time period chosen.¹ In this case we have the special problem that the degree of substitutability between South Asian imports and European products, eg carpets, may be rather less than between all imports and European products from which elasticities were derived. For the purpose of this study, we use crude long-run estimates of -2.5 for the price elasticity of demand for imported manufactures, -1.5 for semi-manufactures and -1.0 for foodstuffs. This broadly corresponds with estimates derived from the above source and used in current major projection analyses (eg the recently published Brookings' analysis of Tokyo Round effects²). But the figures should be treated with caution. One recent major study, for Britain, used a long-run price elasticity of demand of -8.0 for manufactured imports in general³, and another, analysing the effects of the Kennedy Round, obtained a figure of -3.5 for the tariff elasticity of ldc imports to the EEC (-10.0 to -12.0 in the USA and Japan).⁴ The most recent estimates by the World Bank for agricultural items confirm that a range of 0 to -1.0 is usual, but there were two significant exceptions for EEC imports: -2.7 for tobacco, and -4.5 for rice.⁵ This conforms to common-sense prediction since there are closely competing European producers for these products, whereas for most raw materials and foodstuffs, import elasticities are determined mainly by the price elasticity of demand for the product itself.

(6) The reduction in tariffs is assumed to result in trade creation only. If the liberalisation were to be achieved from mfn cuts on all items, then South Asian imports and European products, eg carpets, may be rather liberalisation were achieved through GSP, there would be an additional trade diversion gain. For the moment we disregard this factor on the

grounds that trade diversion effects of preferences are likely to be small relative to those from trade creation, but we return to it later.

(7) A final problem arises with items classified as sensitive under GSP. Part of South Asia's exports of these items enter the EEC duty-free, up to the tariff quota or country butoir, whichever is exceeded first. The theory of the effects of tariff ceilings and tariff quotas has been set out elsewhere and the trade stimulating effect of preferential margins has been analysed in terms of a 'kinked supply curve';⁶ if a ceiling is interposed the supply curve becomes discontinuous and the price indeterminate within this discontinuity. Since we do not know what the equilibrium levels of trade actually would be it is extremely difficult to devise a practical measure of the extent to which GSP tariff quotas replacing mfn tariffs have been trade liberalising or not. For the sake of simplicity we assume that existing tariff quotas are very low in relation to actual amounts traded, and that no trade stimulation will have already taken place; therefore tariff elimination would be equivalent in its effects to elimination of tariffs on the whole amount currently traded.

Table 4.1 Static Value of Residual Tariffs (mua)

	Sri Lanka	Bangladesh	India	Pakistan
Food				
(a) Tobacco	—	—	2.51	0.52
(b) Other CAP items	—	—	0.93	3.57
(c) Other food	0.30	0.06	1.33	0.22
Industrial semi-manufactures				
(a) Textiles (MFA)	—	—	1.86	4.49
(b) Other	—	0.56	0.90	0.63
Manufactures				
(a) Textile products and clothing (MFA)	—	—	10.80	0.60
(b) Other (including carpets)	—	—	4.90	2.20
Total static value	0.30	0.62	23.23	12.23
Weighted residual tariff (%)	0.3	1.3	3.2	7.0
Weighted mfn tariff (%)	1.4	5.9	4.8	12.1

Note: excludes duties on jute, made tariff free in 1978.

Source: based on EEC, *NIMEXE* import statistics, 1975; EEC, *Practical Guide*, op cit; and EEC, OJ NoL289, 14 November 1977.

Knowing the static value of the residual tariffs, it is possible to work out the average weighted tariff faced by South Asian exports to the EEC after GSP tariff reductions (average weighted tariff = static value of residual tariffs ÷ total value of exports). Comparing this with the average weighted mfn tariff which, in the absence of the GSP, they would have to pay, it appears that the GSP has so far cleared about half the tariff access barriers facing both India and Pakistan (slightly more in the case of Pakistan). Sri Lanka and Bangladesh have fared even better—their mfn tariff has been reduced by 3/4 to 4/5, leaving very little to remove.

Estimates of the additional annual trade resulting in the long term (ie by 1982/3) from complete tariff liberalisation are given in the following table. For food imports a price elasticity of demand of - 1.0 is used, - 2.7 for tobacco, - 1.5 for semi-manufactures, and - 3.0 for manufactures.

Table 4.2 Long Term Annual Trade Creation from Complete Tariff Liberalisation (mua, 1975 prices)

Dutiable; not quantity restricted items	Sri Lanka	Bangladesh	India	Pakistan	Total
Food and tobacco	0.15	0.03	7.40	4.00	11.60
Semi-manufactures	—	0.82	1.35	0.95	3.15
Manufactures	—	—	14.70	6.60	21.30
Total	0.15	0.85	23.45	11.55	36.00
Dutiable; quantity restricted items (largely textiles & clothing)	—	—	35	8.5	43.5

Source: as per Table 4.1.

The total annual gain would, excluding textile items, very roughly be equivalent to 3.5% of current (1975) South Asian exports to the EEC; 6% for Pakistan, 3% for India, 1% for Bangladesh and virtually nothing for Sri Lanka. It is worth remembering that almost half the Indian gain is for carpets. If Indian claims are right that their carpets do not compete with European producers, then the elasticity factor, -2.5 to -3.5, is almost certainly too high. On the other hand the gains to Sri Lanka and Bangladesh are almost certainly under-estimated, given the very low starting base. Even if we doubled the elasticities to allow for downward bias, the magnitudes are clearly very small by comparison with the growth expected (to 1985) on the basis of an unchanged trend (a doubling) or on the basis of improved export policies (a possible quadrupling). It is also small by comparison with the likely gain from NTB liberalisation on textiles and clothing alone; and even less than the gains from complete tariff liberalisation on textiles (which of course would be ineffective without NTB liberalisation also).

If the impact of complete tariff liberalisation is small for South Asia it is quite negligible for the EEC. A very crude attempt may be made to express the cost to the EEC in terms of employment. We take the marginal productivity in those European sectors affected by South Asian competition as represented by the average productivity of the least efficient industry, clothing, in one of the less efficient European member states, Britain, where average output per man is around 10,000 ua. On this basis the total number of workers displaced in the EEC as a result of complete tariff liberalisation for all South Asian imports is at most 3,250, and only after a period of years. Even if we triple the figure to allow for a possible underestimate of demand elasticities and indirect effects, we still have under 10,000. And this is almost certainly an overstatement; productivity will rise anyway in the affected industries, thereby reducing the number of workers which can be hurt by imports, while expenditure of additional foreign exchange by South Asia will have a positive effect on EEC employment. This is a very small straw on a very large camel's back. It could be argued that these costs would have to be generalised to all mfn or GSP suppliers. But that would be a matter of political choice. If the Community were so minded it could confine tariff-free access provisions to South Asia by extending Lomé trade provisions to them or by declaring that all msas are tariff exempt under GSP.

In practice tariff issues boil down to specific product disagreements (see Table 4.3). For items worth over 1 mua in 1975, and excluding textiles, India faces duties of over 5% on crustaceans, ground pepper, tobacco, various vegetable oils (castor, linseed), several types of leather, and carpets; Pakistan, on crustaceans, tobacco, oils, leather, footwear, sports equipment, rice, and molasses (in addition to levies); Bangladesh, on leather; Sri Lanka on tobacco and solid coconut oil. In addition it should be remembered that the nominal tariff rate may well underestimate effective protection and that existing tariff concessions under GSP are both unbound and, with the system of ceilings, unpredictable.

Tariff Discrimination

Reduction of the nominal tariff facing all exporters to the EEC would have the effect of 'creating' trade in the sense used in customs union theory. Preferential tariff reductions, however, have a trade diverting as well as a trade creating effect. For the EEC, the complexity of preferential arrangements, both within the EEC, and with EFTA, the Mediterranean, Lomé, and GSP countries, makes it difficult to assess for a particular supplier the direction—let alone the magnitude—of trade diversion arising from preferences. We shall not attempt to assess quantitatively the potential gain (or loss) from trade diversion resulting from preferential tariff changes. This is partly because the methodology is difficult (it hinges on measures of elasticity of substitution) and because we suspect that it is small relative to the already small potential trade creation benefits. Baldwin and Murray estimated the trade diversion benefits of GSP to be as little as 10% of the trade creation

benefits.⁷ Even if the elasticities of substitution between imports are two to three times those between LDC imports and EEC products the magnitudes in general are small. We confine ourselves therefore to looking at the direction of tariff discrimination under the existing structure.

This is done by attempting to measure trade discrimination following Tinbergen.⁸ The first step is to try to construct what—for want of a better phrase—we can call a ‘functional tariff’, the average import duty paid on a particular category of imports into the EEC, taking into account the different tariff structures facing different exporters. Unfortunately data on duties paid is not available, so one has to approach the question indirectly by weighting the relative importance of various suppliers. For example, suppose an item carries an mfn rate of 20% and a GSP rate of 10%. ACP and EFTA imports enter individual EEC states duty free. Overall EEC imports consist of 20% from EFTA, 40% from ACP, 15% from GSP sources, and 25% from other mfn sources. The average ad valorem duty paid on all imports, or the ‘functional tariff’, will be 6.5%. The difference between the ‘functional tariff’ and the rate paid by GSP exporters (10%), -3.5%, gives us a measure of trade discrimination. One could also look at discrimination in terms of the effect of the CET in diverting trade from extra- to intra-EEC sources. Suppose, on the above example, intra-EEC imports equalled extra-EEC imports in value, then the ‘functional tariff’ for individual EEC members would be 3.25% and the tariff discrimination between GSP and EEC suppliers would be -6.75%. Using this approach one can obtain some measure of the overall discriminatory effect of the EEC’s tariff system on South Asia.

There are certain problems however. First, the origin of imports reflects tariff preferences and thus gives undue weighting to low duty sources of supply (according to the degree of substitutability with imports from other suppliers). The effect of this is to deflate the ‘functional tariff’. Second, practical problems are involved in the classification of Mediterranean goods (which were treated as comparable to GSP though in some cases treatment was more generous), agricultural imports from EFTA (which were assumed to carry mfn duties), Comecon imports (which were assumed to carry mfn duties too, though Rumania pays GSP and others above-mfn rates). Fortunately none of these categories was particularly large. Third, a more serious problem is caused by ceilings and quotas. It is impossible to make any intelligent guess at the ‘functional tariff’ paid by GSP suppliers of sensitive and semi-sensitive GSP items, given uncertainty over how much actually pays duty and the extent of discrimination as between various GSP suppliers. We assume therefore that in the case of garments, textiles and non-leather footwear the tariff quota has no trade stimulating effects, and in the case of tobacco that it is not fully used. Knotted carpets is a difficult case since almost all imports are from GSP sources and in practice discrimination has existed against some GSP sources (India) and in favour of others (Pakistan).

The following table gives estimates of tariff discrimination facing imports from South Asia and other GSP beneficiaries. A positive sign indicates discrimination in favour of these countries.

Table 4.3 Tariff Discrimination on Items of Importance to South Asia (%)

Product	mfn rate	GSP rate	'Functional tariff' for extra-EEC imports	Degree of tariff discrimination (extra-EEC imports only)	Degree of tariff discrimination (including intra-EEC trade)
A Non-GSP dutiable					
Walnuts	8	—	8.0	0	-4.0
Coffee	5	—	2.3	-2.7	-2.7
Linseed oil	5	—	5.0	0	-2.7
Industrial oil	7	—	6.5	-0.5	-3.5
Tanned cow leather	8	—	6.7	-1.3	-3.7
Tanned sheep leather	3	—	2.7	-0.3	-2.5
Tanned goat leather	3.5	—	2.6	-0.9	-0.9
B GSP Non-sensitive					
Frogs' legs	10	0	4.2	+4.2	+4.2
Shrimps	12	6	4.8	-1.2	-2.4
Okra	16	0	0	0	0
Mangoes	6	5	2.7	-2.3	-2.7
Whole pepper	10	5	4.0	-1.0	-1.0
Castor oil	8	6	6.0	0	-0.5
Vegetable oils	17	11	9.5	-1.5	-10.0
Other crustaceans	20	6	9.5	+3.5	0
Dyestuffs	12 ^a	0	2.5	+2.5	+0.9
Resin acids	5	0	3.3	+3.3	+3.1
Saddlery	9	0	2.9	+2.9	+1.6
Lamps etc	7	0	3.1	+3.1	+2.1
Mica	5 ^a	0	1.0	+1.0	+0.3
Iron products	7 ^a	0	3.1	+3.1	+1.6
Domestic goods	7 ^a	0	2.8	+2.8	+1.5
Handtools	6 ^a	0	2.2	+2.2	+1.2
Metal objects	6.5 ^a	0	2.9	+2.9	+0.7
Engines & pumps	6.5 ^a	0	4.2	+4.2	+1.4
Electrical equipment	10.5 ^a	0	6.2	+6.2	+2.4
Transport equipment	13.5 ^a	0	8.9	+8.9	+1.5
Jute-woven & sacks	20	0	1.5	+1.5	-0.5
Silk scarves	16	0	10.0	+10.0	+3.2
C GSP Sensitive (low tariff quotas)					
Cotton yarn	7	7	7.0	0	-2.0
Cotton fabrics	14	14	13.0	-1.0	-5.5

Product	mfn rate	GSP rate	'Functional tariff' for extra-EEC imports	Degree of tariff discrimination (extra-EEC imports only)	Degree of tariff discrimination (including intra-EEC trade)
Bed linen	19	19 (0 for Pakistan)	19.0	0	-7.0
Garments (most relevant categories)	17	17	16.5	-0.5	-8.5
Non-leather footwear	8	8	6.5	-1.5	-6.1
	20	20	16.2	-3.8	-15.2
D GSP Sensitive (high tariff quotas)					
Knotted carpets	24	? (0 for Pakistan, high for India)	?	0 (for GSP as whole)	-1.0
Tobacco (main categories)	23	7 (almost all)	13.0	+6	+6.0

Note: ^a indicates average of several rates.

Source: as per Table 4.1.

The table shows that, discounting intra-EEC trade, there is a considerable preference margin in favour of South Asian engineering goods and minimal discrimination against the main sensitive items, despite high GSP duties, since most extra-EEC imports come from GSP sources. Even for the products for which Lomé suppliers enjoy preferences (coffee, vegetable oils, various fruits and nuts) negative discrimination is scarcely significant. Using these results it is possible to work out, by calculating the weighted average of the items listed, the overall tariff preference enjoyed by South Asian exporters over the average (non-GSP) extra-EEC supplier of the same products. For India this is almost zero—the positive trade diversion effect of the GSP is cancelled out by the negative effect of special preferences to Lomé and EFTA; -0.4% for Pakistan; +0.7% for Bangladesh; and +0.6% for Sri Lanka. This suggests that complete tariff elimination would neither add to nor subtract from South Asian export flows to the EEC which arise from trade diversion. On the other hand, if intra-EEC trade is also considered, there is much more evidence of negative discrimination against South Asian products. In total the weighted rate of tariff discrimination is -1.35% for India, -2.40% for Pakistan,

-0.15% for Sri Lanka and -0.42% for Bangladesh. This implies that across-the-board multilateral tariff cuts would more than compensate for what is lost through the removal of preference margins, by displacing intra-EEC trade.

Tariff Escalation and Effective Protection

There is one important sense in which nominal tariff barriers may understate the degree of protection, and in which the value of GSP concessions may therefore be understated. It is therefore necessary to look at the 'effective protection' given to raw material processing. Effective protection (EP) measures the extent to which value-added at domestic prices is greater, as a result of tariffs or non-tariff intervention, than it would have been under free trade. Effective protection can be expressed, following the above definition, as:

$$EP = \frac{V_d - V_w}{V_w} \quad \text{where } V_d \text{ is the value-added at domestic prices and } V_w \text{ the value-added at world prices.}$$

The concept can be applied to the tariff barriers facing South Asian exports. As can clearly be seen for each of the thirteen cases illustrated in Table 4.4 there is evidence of tariff escalation from low (usually zero) rated raw materials up to the final product. The resulting rate of effective protection will depend on the importance of raw material costs in the final output, and on the precise progression of the tariff at each stage of processing. In several cases where the value-added content in final output is low, there is a very high rate of effective protection, notably in the refining and processing of coconut oil and groundnut oil, rice milling and the manufacture of cigarettes. There are cases where a high duty on an intermediate input can reduce the rate of effective protection to a negative figure (chocolate), to below the nominal level (jute sacks), or to a level little higher than the nominal rate (leather, clothing).

What is the effect of the GSP? There are several particularly striking cases where the GSP has removed a large measure of effective protection for ldc suppliers, notably steel products, jute sacks, and coir matting. In the former case the effective protection is now almost certainly negative (as a result of minor inputs being dutiable). But in the case of jute and coir the gain is illusory since quantity restrictions act as an effective barrier.

Table 4.4 Tariff Escalation and EEC Effective Tariff Protection on Items of Interest to South Asia

	Nominal Tariff		Effective Tariff	
	mfn	GSP	mfn	GSP
A Not Quantity Restricted				
coconut (copra)	2.5	0	—	—
coconut oil for industrial use (crude)	5	2.5	—	—
coconut oil (crude)	10	7	85.4	77
coconut oil (refined)	15	13	186.3	233
leather (simply tanned)	0	—	—	—
leather (tanned)				
sheep	3	0	9.2	—
goat	3.5	0	10.7	—
bovine	8	0	24.4	—
leather shoes	8	0	na	na
leather gloves	10.5-13	0	na	na
rice	12 (+L)	—	—	—
milled rice	16 (+L)	—	70.3 (+L)	—
			105.9	
rice flakes	23 (+L)	—	—	—
groundnut	0	—	—	—
groundnut oil (crude)	10	—	92.5	—
groundnut oil (refined)	15	—	179.5	—
tobacco	14-23	7	—	—
cigarettes	90	87	150	150-164
iron ore	0	—	—	—
steel ingots	4	—	1.1	—
engineering goods	5-10	0	19.5	0 or negative
cocoa	5.4 ^a	—	—	—
cocoa paste	15	11)		
cocoa butter	12	8)	76	na
chocolate	12-27	10	-7	na
	(+ads)	(+ads)		
cocoa powder	10	3		

	Nominal Tariff		Effective Tariff	
	mfn	GSP	mfn	GSP
wool (greasy)	0	0	na	na
carpets	24	0	na	na
<hr/>				
silk (raw)	5	0		
silk yarn	7	0	na	na
silk scarves	16	0	na	na
<hr/>				
fresh mangoes	6	5		
mango jam	30 (+ads)	12 (+L)	na	na
tinned mangoes	22 (+ads)	8 (+L)	na	na
mango juice	21 (+ads)	10	na	na
<hr/>				
B Quantity Restricted			(tariff only)	
jute	0	—	—	—
jute yarn	8	0	na	na
woven jute	15-22	0	57.8	0 or negative
jute sacks	15-20	0	14.0	0 or negative
jute mats	20	0	na	na
<hr/>				
cotton (raw)	0	—	—	—
cotton yarn	4-8	0	22.8	(indeterminate)
cotton fabric	13-15	0	29.7	"
clothes	17	0	21.4	"
<hr/>				
coir fibre	0	—	—	—
coir yarn	0	0	na	na
coir mats	23	0	na	0 or negative

Notes: ^a prior to 1977 offer of reduction to 3%.
 ads = additional duty on sugar.
 L = levy.

Sources of effective protection co-efficients: UNCTAD, *The Kennedy Round: Estimated Effects on Trade Barriers*, TD/G/Rev. 1, 1969, and *Measures to Expand Processing of Primary Commodities in Developing Countries*, TD/B/C/197. Also A.J. Yeats, 'Effective Protection in the EEC, Japan and the US', *Quarterly Review of Economics and Business*, Summer 1974.

Another consequence of the GSP is that even when nominal duties are reduced, at all levels of processing, this can have the result of retaining the level of effective protection or even increasing it, if input duties are reduced faster than output duties. One case which illustrates this well is coconut oil processing. Sri Lanka

currently exports large quantities (worth some 30 mua) of coconuts and coconut products to the EEC each year; half of that amount (by value) is raw coconut for refining as well as eating unprocessed, about one quarter is in semi-processed form (coir fibre, charcoal), and only one sixth is refined oil. As can be seen from the calculations in Table 4.5, the widening of the degree of escalation following GSP reductions, albeit by a few percentage points, increases the degree of effective protection of refining from 200% to 233%.

Table 4.5 Effective Rates of Tariff Protection facing Sri Lankan Coconut Oil Exports to the EEC (\$)^a

	Value of Exports to EEC including duty	duty	Value excluding duty	% rate of duty
A Crude solid coconut oil				
(i) mfn				
input: coconut (copra)	1.025	0.025	1.000	2.5
output: crude solid oil	<u>1.210</u>	0.110	<u>1.100</u>	10.0
value added	<u>0.185</u>		<u>0.100</u>	
EP = 85%				
(ii) GSP				
input: coconut (copra)	1	0	1.000	0
output: crude solid oil	<u>1.177</u>	0.077	<u>1.100</u>	7
value added	<u>0.177</u>		<u>0.100</u>	
EP = 77%				
B Refined coconut oil				
(i) mfn				
input: crude oil	1.100	0.100	1.000	10
output: refined oil	<u>1.181</u>	0.150	<u>1.027</u>	15
value added	<u>0.081</u>		<u>0.027</u>	
EP = 200%				
(ii) GSP				
input: crude oil	1.070	0.070	1.000	7
output: refined oil	<u>1.160</u>	0.133	<u>1.027</u>	13
value added	<u>0.090</u>		<u>0.027</u>	
EP = 233%				

Note: ^a The calculations are made on the basis of exports of coconuts (in case I) and crude oil (in case II) worth \$1, excluding duty.

Even these estimates give only a very partial picture of the significance of tariff escalation. One crucially important development in recent years is the extension of virtually duty-free access to Lomé countries and, on many items, to the Mediterranean. Thus high effective protection has the function not only of assisting European processors, but also of stimulating processing in the Lomé and Mediterranean regions.

There are however two factors working to offset tariff escalation. The first is the export subsidisation of processing by the exporter. Export duties on unprocessed output by the exporter are equivalent to a tariff in the importing country; export subsidies to a negative tariff. This has been an important factor in attempts to encourage Asian exports of processed leather and tea (in packets/bags).

A second factor is transportation and insurance costs incurred differentially on goods at different stages of processing. If these costs are lower on the final product this will tend to diminish effective protection in the importing country. There is only very indirect evidence of the importance of this factor, as much as can be gleaned from comparing cif and fob values for the same trade flows. Using this approach, work by Yeats on US imports from developing countries, gives some indication of the relative magnitudes. As Table 4.6 shows, it appears that the shipping costs are higher (in ad valorem terms) for processed products than for primary; this will strengthen the bias against South Asian processed exports caused by tariff escalation.

**Table 4.6 Escalation of Transport and Insurance Costs with Processing:
% Increase in cif over fob Values**

		Primary products	Final products	Ad valorem escalation
Vegetables	All countries	4.3	14.9	+10.6
	India	15.9	23.2	+ 7.3
Fish products	All	6.8	5.6	- 1.2
	India	12.6	12.7	+ 0.1
Leather	All	3.9	9.1	+ 5.2
	India	10.1	21.1	+11.0
Rubber	All	9.9	15.6	+ 5.7
	India	10.2	35.0	+24.8
Wool	All	8.9	9.6	+ 0.7
	India	9.6	13.9	+ 4.3
Cotton	All	4.3	8.5	+ 4.2
	India	4.6	8.0	+ 3.4
Jute	All	41.2	11.9	-29.3
	India	36.0	20.0	-16.0
	Bangladesh	34.2	19.3	-14.9
Groundnuts	All	14.7	2.9	-11.8
Copra	All	6.2	2.7	- 3.5

Source: A.J. Yeats: 'Do International Transportation Costs Increase with Fabrication? Some Empirical Evidence', *Oxford Economic Papers*, November 1977, p465-6.

Tariff Negotiation Issues

There are essentially two approaches open to the South Asians in negotiating tariff issues with the EEC. One is through discussions on the GSP, the other through the multilateral trade negotiations (MTN). A third possibility is through special bilateral sectoral agreements, as has occurred with jute and coir, but this is likely to be of importance only when the South Asians are dominant suppliers, and where there are both NTBs and tariffs to be negotiated. Given the general commitment by dcs to help ldc through the MTN as well as through the GSP, there is a choice as to which would be the best approach for South Asia, both in general and for particular products. The South Asians have two sets of competing interests:

- (1) The first is in enlarging or preserving preferential margins through the GSP. Clearly the preference margin is only worth preserving to the extent that there is competition, potential or actual, from mfn suppliers.

(2) The second is in the reduction of mfn tariffs generally, where these act not only as a barrier to access but provide protection to other preferential suppliers—Lomé, the Mediterranean and EFTA.

Other things being equal there are obvious advantages in obtaining improvements in mfn access rather than in GSP access. In particular the benefits would be more certain than those obtainable under the GSP (see Chapter 3)—even for GSP items which are currently not sensitive, ceilings are a potential threat, while the GSP itself is not permanent.

The net aggregate effect of mfn tariff cuts on ldc trade is unclear without a detailed knowledge of the preferential tariff margins on particular items, volumes traded and elasticities of supply, demand, and substitution for each product. This information is simply not available. Attempts have been made, notably by Baldwin and Murray,⁹ to assess *in general* the benefits of seeking a deep mfn cut as opposed to the maintenance of preferential margins. They made various assumptions, of which the most important was that imports from ldc beneficiaries are imperfect substitutes for imports from dcs. They calculated that under a 50% mfn tariff reduction ldc would benefit in annual trade flows to the EEC to the tune of \$45m from the absence of value limits on imports eligible for tariff cuts, offset by \$9m loss in preference margins. Textiles and shoes were excluded from the analysis. This study has, however, been criticised on two main grounds.¹⁰ First, it is claimed that Baldwin and Murray underestimated the elasticity of substitution between different imports; empirical evidence suggests that this is usually two to three times the extent of substitution with domestic products. Even if this were the case, however, mfn liberalisation would still have a net positive effect on ldc exports. Second, and more seriously, it is argued that while the analysis may be true in general, it is not necessarily true for particular products and particular countries, and so ldc would be best advised to opt for a selective product-by-product approach, seeking to preserve margins where relevant and improving GSP treatment of sensitive items. This may be overoptimistic given the present condition of the world economy.

We have endeavoured to relate these arguments to specific items of importance to South Asia. In crude aggregate terms we showed earlier that the net discriminatory effect of preferences was very small, suggesting that across-the-board mfn tariff cuts would also be neutral in this sense. Therefore in general a mfn approach is preferred. The results are considered here in detail.

Manufactures

A very crude test is employed to measure the potential for trade diversion should the GSP-mfn tariff margin be reduced (see Table 4.7). If less than 20% of imports to the EEC from all non-EEC sources paid mfn duty, the preference margin is treated as of negligible importance (column I) and, if over 40%, it is allowed

considerable importance (column II). Where 20-40% of the imports paid duty the importance of the margin is considered to be indeterminate (column III); and if the product was quantity restricted the margin is regarded as irrelevant (column IV). On this basis, less than 55 mua, or 10% by value, of South Asian manufactured exports to the EEC in 1975 are found to have important tariff margins to preserve. Most of these are engineering goods, which can hardly escape mfn cuts if there is progress under the Tokyo Round; moreover the preference margins (6-10%) are small by comparison with current export subsidies, especially on Indian engineering exports. Of the major non-engineering items only sports goods and leather garments had margins sufficiently large (at 13.5% and 9.5% respectively) to suggest that they might suffer from trade diversion, although this might be less so at a disaggregated level. The tariff margin of 8-20% may also be important for footwear; but the fact that only 20-40% of EEC imports pay duty, and that there are severe limits on the amount of footwear imports which can benefit from the GSP, make this less likely.

Manufactured imports worth nearly 150 mua, or 30% of all EEC manufactured imports from South Asia, faced quantity restrictions such that little trade diversion (or trade creation) could be achieved by preferences. But there would be a loss if mfn rates were cut as the fiscal transfer under the GSP (p62) would be correspondingly lower.

Where trade is monopolised by GSP suppliers (column I), as in the import of knotted carpets, mfn cuts would not make any difference in terms of trade diversion to South Asian exports. There are only a few items, such as tanned goat leather and industrial oils, which would benefit from GSP rather than mfn treatment. But in practice either would bring trade creation gains—though these would be marginal as the tariffs involved are small (3.5% and 7% respectively).

Taking all things into consideration the threat of the erosion of GSP preference margins for manufactures as a result of the MTN does not appear a very serious one for South Asia. But to the extent that South Asia finds it more productive to pursue demands under the GSP, the following are the most important:

(1) *Reclassification of carpets*; both in terms of the value of trade, the employment potential in South Asia, and the severity of the tariff barrier, knotted carpets, hand woven from wool and goat hair, constitute the most important item. The South Asians have jointly asked that the relevant categories (ie carpets with less than 500 knots per metre of warp) currently treated as sensitive, be moved into the same semi-sensitive category as carpets of above 500 knots per metre of warp and given more generous Community ceilings. They argue that there is no effective substitution with European machine-made carpets. As it happens the present method of protection, under national tariff quotas, largely restricts imports to Germany which is not seeking protection. On the other hand this system provides the threatened Belgian industry with a safe export market. If the threat to Belgian or other European interests were felt to be intolerable, for reasons presently obscure, their position could be safeguarded in large part by exempting msas from the tariff ceiling, while leaving it in place for the major supplier (Iran). Certainly, this is one product where restrictions on GSP use appear most damaging and unjustified.

(2) *More generous treatment of sensitive items notably shoes* (by redefining EEC national quotas, or by enlarging butoirs). Footwear (notably from Pakistan) has been particularly badly affected by the freezing of tariff quota limits in recent years. South Asian suppliers are minor in relation to Far Eastern producers and concentrated in particular areas, eg gym shoes, not central to the survival of the European industry. Yet tariffs for the items concerned, mainly in the BTN category 64-02B (shoes with non-leather uppers), are very high (20%) at the margin. And recently these have had to be paid by Pakistani imports from May each year. Again, the ideal solution would be a substantial raising of global tariff quotas and butoirs. But if this is impossible, an attempt to get exemption for msas would present few problems either for the industry or for competing exporters.

(3) *Larger ceilings for semi-sensitive items, notably sports goods*; the latter is the other main non-textile item affected, particularly for Pakistan, by ceiling limitations. Pakistan is one of the main suppliers of certain, somewhat specialised items (footballs, tennis rackets). Tanned goat and sheep leather is also restricted, though the issues surrounding leather processing are more complex and the tariffs are small. (A paper on South Asian exports of leather and leather products to the EEC is available from ODI upon request.)

(4) *Changes in the import régime governing textiles and clothing*; many of these items are affected by sensitive product status. However tariff issues are subsidiary for textiles. Given quantity control under the MFA, there is little or no scope for trade creation or diversion except for a few items, eg embroidery, cotton sacks, and for items in which little at present is traded, notably for Pakistan and the two small suppliers. It is still useful to obtain tariff concessions for the fiscal benefit, and to help raise *total* European textile demand, especially for cottons. But there is little purpose in spending a great deal of negotiating time and diplomatic goodwill on something which cannot stimulate trade. It would probably benefit the South Asians to give up textile GSP entirely on MFA products in return for fiscal compensation or concessions on quantities. But more attention should be focused on the behaviour of the European lobbies, which have managed to persuade EEC governments to double-insure them against competition, at extra cost to consumers and to end users of fabrics, for no gain in terms of European employment.

Agriculture

The somewhat complex picture is set out in Table 4.8 The EEC has already made an offer of tariff reductions on certain tropical products under the MTN. It helps South Asia by cutting the Lomé preference margin on coffee and cocoa but is otherwise largely worthless, as many of the mfn reductions are to a level *above* that conceded already under the GSP. The following are the main residual problem areas:

- (1) *Tobacco*: this is overwhelmingly the most important item. The significant margin dictates a GSP approach. The main objectives are therefore first, a substantial raising of the tariff quota (100,000 tons has been suggested, from 60,000 tons) and second, a reduction in the 7% GSP rate. Clearly there will be opposition from competing Lomé and EEC suppliers, but all four countries of South Asia have a strong case based on their own competitiveness and on the potential for rural employment in their extremely poor economies.
- (2) *Other CAP items*: rice, sugar and their products (rice extract, molasses, canned fruit) are currently outside the GSP. In each case the main barrier is the variable levy, but in addition there are tariffs, and tariff liberalisation could stimulate trade. The chances of improvement are not particularly bright, but given the magnitude of the tariffs, and the trade flows, notably from Pakistan, the gains are potentially large.
- (3) *Spices*: concessions have already been obtained for most items but, except for cloves and ground pepper (neither of which is currently exported in any quantity from South Asia), they still face a 'nuisance' tariff of only 5% or less. The GSP has been the main avenue for achieving

Table 4.8 Tariffs Remaining on Agricultural Items of Interest to South Asia

Tariff Heading	Product	I	P	B	SL	GSP rate %	mfn rate %	Extra-EEC Imports ('000 ua)	% mfn pay- ing	% GSP pay- ing	% Lomé	Preferred Tariff Concessions	Affected Interests
A Non-GSP items													
07-01 III	Onions and garlic*	-*	-	-	-	-	12	38533	73	27	-	1. GSP 2. mfn	Holland/other EEC Spain/other Mediterranean
07-01 T	(Aubergines* (Others*	-*	-	-*	-	-	16	15444	36	74	-	1. GSP 2. mfn	Italy, Spain/ Mediterranean
07-04 A and B IV	Dried onions and garlic	-*	-	-*	-	-	16	12855	52	48	-	1. split category 2. GSP or mfn 1. GSP 2. mfn	None for most sub-items Holland/other EEC
08-05 B	Walnuts*	738*	-*	-	-	-	8	3067	76	24	-	1. GSP 2. mfn	France mainly Lomé
09-01 A	Coffee	-	-	-	-	-	7(5)	1253661	-	67	33	1. mfn	
12-03 EI	Vegetable seeds*	114*	-	-*	-	-	10	8195	81	19	-	1. split category 2. mfn	Holland?
18-01 ex 20-02 H	Cocoa Beans* Vegetables prepared (not in vinegar) achar	-	-	-	-	-	3	53098	-	16	84	1. mfn	Lomé (Ghana)
10-06 B II ex III 17-03	Basmati rice* Molasses	1162*	3204*	-	-	-	16	31585	61	37	2	1. CAP levy removal 2. GSP 3. mfn	Italy mainly
23-02 AI	Maize and rice extract	971*	4699*	-*	-	-	65	87289	17	80	3	1. CAP levy removal 2. mfn 3. GSP	France/Holland
		2683	612	-	-	-	21	107029	19	68	13	1. CAP levy removal 2. mfn 3. GSP	Germany, Indonesia
B GSP items													
(i) Fish products													
03-03 AII	Lobsters*	-*	-*	-	-*	8	10-20	4827	94	6	-	1. split. 2. GSP (protect margin)	UK mainly
03-03 AIVc	Shrimps	913*	479*	963*	-*	7	18	54857	38	31	32	1. GSP (protect margin)	Holland, Lomé

Tariff Heading	Product	I	P	B	SL	GSP rate %	mfn rate %	Extra EEC Imports ('000 ua)	% mfn pay- ing	% GSP pay- ing	% Lomé Concessions	Preferred Tariff Concessions	Affected Interests
16-04 GII	Sardines	--*	--	--	--	10	20	41918	58	42	--	1. split. 2. GSP (protect margin)	Spain, Portugal, Morocco
16-05 exB	Other Crustaceans	1663	2524	--*	--	6	20	58808	47	52	1	1.GSP (protect margin)	Holland
(ii) Spices													
09-04 AIIb	Pepper (whole)	2019*	--	--	--*	5	17(10)	31449	2	84	14	1. mfn 2. GSP (protect margin)	Madagascar
B ex II	Pepper (ground)	*	*	--	*	7	12.5	7261	98.5	--	1.5	1. mfn 2. GSP	EEC processors, Spain
09-06A	Cinnamon (ground)*	--	--	--	--*	5	13(10)	53	--	--	--	(1. GSP (protect margin)	EEC processors
B	(other)*	--	--	--	--*	4	10(8)	2407	36	58	6	(2. mfn (below 4-5%)	Madagascar
09-07	Cloves*	--	--	--	--*	12	15	4287	0	25	75	1. mfn (below 12)	Tanzania/ Madagascar
09-08 BIII	Cardamom (ground)	149	--	--	*	5	5(0)	864	0	77	23	1. mfn (conceded in Tokyo Round)	Tanzania
09-08 AII	Nutmeg (whole)* (ground)*	--	--	--	--*	2	15(10)	6106	0	100	--	(1.mfn to 0 2.GSP to 0 (Tokyo Round con- sessions meaningless	None apparent Holland?
09-10 D	Ginger	408	--	--*	--	0	10(0)	2615	23	49	28	1.mfn 2.GSP	West Indies
E	Turmeric (fenugreek)*	579*	--	--	--*	0	10(0)	839	4	96	--	1.mfn 2.GSP	Morocco
FIIa	Others (curry (powder)	783*	--	--	--*	0	2(0)	907	11	89	--	1. mfn 2. GSP	UK processors
(iii) Vegetable Oils													
15-07 CII	Castor oil*	2097*	--	--	--	6	8	9628	1	99	--	1. mfn 2. GSP	EEC processors (Holland/FRG)
DIIa3)	Coconut Oil*	--	--	--	--	2.5	5	21670	1	91	9	1. mfn 2. GSP	EEC processors (Holland/FRG)
DIIb2)	Linseed oil	3068	--	--	--	7	10	14359	2	85	13	1. mfn 2. GSP	EEC processors (Holland/FRG)
DIIa3)						2.5	5	27421	31	69	--	1. GSP (protect margin)	EEC processors (Holland/FRG)

Tariff Heading	Product	I	P (000 ua)	B	SL	GSP rate %	mfn rate %	Extra- EEC Imports (000 ua)	% mfn pay- ing	% GSP pay- ing	% Lomé Concessions	Preferred Tariff Concessions	Affected Interests
(iv) Others													
08-01 ex H	Mangoes	590*	-	-*	-	5	6	2541	3	53	44	1. mfn	Lomé none
07-04 BIV	Dried mushroom/other	-	-	-*	-	8	16	14789	62	34	4	1. split category	
20-06 BIIa5aa	Tinned Pineapple*	-	-	-*	-*	12-15	23	5758	33	36	31	1. CAP levy removal 2. GSP	Lomé/Martinique
20-06 BIIa8	Other fruit (mangoes)	145*	-	-*	-	8-12	22/3	12359	79	21	-	1. CAP levy removal 2. GSP	EEC sugar producers and EEC canning industries
(v) Tobacco													
24-01 AI	Tobacco (VFC)	14247	-	-	921	7	14	202837	68	30	12	1. GSP (preserve margins)	Italy
AI	Tobacco (VFC)	3680	-	-	-	7	14	28643	26	40	34		France
B	Tobacco (VFC)	32315	7393	-	-	7	23	111191	33	58	9		Lomé

KEY: * = item of special importance, for which concessions have been requested by one or all of the South Asian countries

- = negligible

() = tariff concession offered by the EEC in the Tokyo Round

L = levy

VFC = Virginia flue cured

Source: as per Table 4.1.

these improvements, as mfn concessions so far have been either nugatory or have diminished the value of the preference margin (eg cinnamon). The remaining tariff liberalisation will not be easy since there are important Lomé interests (Tanzania was overridden on cardamoms but Madagascar, a large exporter of pepper appears to have rather more muscle), and some European processing interests, which have tried to maintain the margin of effective protection—eg on ground cinnamon and nutmeg.

(4) *Vegetable oils*: nominal GSP tariffs are now low, but effective protection of processing is formidable. Unless the MTN can produce big cuts, GSP is the preferred approach. There are few competing interests outside Europe.

(5) *Marine products*: here the South Asians have an important preference margin, though the GSP tariff is in most cases still fairly high. There is competition in the main product area (shrimps and prawns) with EEC fishermen, though this is weakened by the considerable differences in taste and size between the EEC and the South Asian products. (See the paper on marine products available from ODI upon request.)

(6) *Fruit and vegetables*: given the considerable diversity of products involved, several of South Asia's interests could be met by redefinition of product categories, eg 'other fresh vegetables' which includes curry leaves and other Asian specialities. In some cases, such as dried garlic, there is still a high protective tariff designed to protect what appear to be minor interests in Europe.

GSP Reforms

We have sketched out in a piecemeal way the kind of products for which GSP improvements are a priority for South Asia, and where the preservation of GSP margins is important. However, the whole of the EEC's GSP is due to be renegotiated in the 1980-81 period and a few broader observations should be made. In general we are somewhat sceptical about some of the claims made for the GSP'. We certainly do not share the view sometimes held that the GSP provisions have stimulated South Asian exports to the EEC tremendously. They have probably promoted Indian and Pakistani trade modestly, or at least helped to offset their losses of trade from UK entry to the EEC, particularly in non-sensitive categories such as engineering goods. Sri Lanka and Bangladesh currently get virtually nothing out of the scheme, but they may benefit more in the next decade as they develop a manufacturing export capability. On the whole it would seem that the scheme is worth trying to preserve and enlarge. There are four main issues.

(1) Sensitive Products

We have already described how for most sensitive items the GSP works to award an unpredictable and windfall fiscal benefit to importers, while providing little stimulation to trade. Some ideas have been suggested for improving this situation and it is worth quoting them in full, since they are relevant to each of the four countries.¹²

'(a) Setting up Indian importing houses to import sensitive and semi-sensitive items only, so that GSP concessions accrue to Indian interests representing exports, so that the benefits of the concessions can be used to improve their competitive position, either by reducing prices to the European consumers, investing more in promotion, or improving the exporters' profitability.

(b) Modifying the GSP system to offer no tariff concessions on sensitive items, but to pay the equivalent of the tariff concessions which would have been earned into a fund administered by the appropriate EPC (Export Promotion Council) which can only be used for trade promotion within the Community, and so to stimulate demand or to reduce prices.

(c) Modifying the GSP system so that instead of allowing the whole concession on a limited tariff quota, a proportionate concession is offered on all Community imports, the proportion being calculated so that the same lump sum of tariff concessions is offered in each case, eg if in 1977, the quota is 1,000 units at \$100 each and the tariff concession is 10% and 2,000 units are imported, the total tariff concession is still 10% of \$100,000 equals \$10,000. This represents 5% of the total imports for that year, and this could be the concessional rate of duty applied to all imports in the *following* year. This would at least ensure that the EEC importer would know in advance what concessional duty might apply and he could set his pricing policy accordingly, thus benefiting the EEC consumer with lower prices and the exporter with higher volumes—the objective of the GSP scheme.'

The first of these points seems eminently sensible but does not require the cooperation of the EEC. We would suggest that it might help the South Asians to be taken seriously, as a group as well as achieve economies of scale especially in the smaller EEC markets, if they set up import houses jointly. The second and third points present alternative approaches. The second treats the GSP as producing no more than a fiscal transfer rather than its declared objectives. This approach would be ideally suited to textiles where there is no potential for stimulating trade; simple tariff abolition for countries and products affected by MFA restraints would result only in a transfer of revenue. As EEC interests may not allow this to happen, a fall-back position is to scrap the GSP entirely and seek fiscal compensation for duty paid on all quantity restrained textile

imports. Since the EEC would be unlikely to encourage the use of this for trade promotion of textiles, the sums involved—around 12-15 mva annually for India, half of that for Pakistan—would probably be an untied aid transfer. Whether this would be additional to existing aid is critical in determining the merits of this approach. The third suggestion would benefit products such as footwear and sports equipment from Pakistan and carpets from India, which currently meet tariffs half-way through the year, and replacing this system with reduced tariffs would add to certainty and stimulate trade. It would also do away with the cumbersome, confining, and largely unnecessary system of EEC national quotas. It would not, however, dispense with the need to treat the two most important items, tobacco and carpets, separately. The latter presents more of an issue of tariff category classification and should cease to be regarded as sensitive, while the main priority for tobacco is to raise the tariff quota.

(2) Margins on non-sensitive items

We have already explained how tariff cuts in the MTN will entail costs in respect of the substantial volume of trade which the GSP diverts to Idcs. But it would almost certainly be counter productive and ineffective to seek to obstruct MTN cuts. Alternatively Idcs, including the South Asians could seek compensation for loss of preference margins primarily through deeper than average mfn tariff cuts on products of interest to them not currently covered by the GSP (eg tanned leather and some agricultural products) and special concessions on special items (notably carpets and tobacco).

(3) Graduation procedures

With the GSP moving into a second decade, there are legitimate questions being raised in Europe as to why some of the more advanced and industrialised developing countries should be included. These countries present a particular problem for South Asian exporters, not so much because of 'crowding out' under tariff ceilings (it is difficult in fact to find examples where South Asian exporters hit ceilings or quotas without themselves being major suppliers; electrical components and cutlery are the only obvious cases), but because they provide a good excuse for the Community to resist further concessions in general under GSP. The present system of graduation which discriminates on the basis of performance in particular product categories hits poor industrialised countries like India and Pakistan particularly hard. It is possible that the obviously more developed countries could be excluded from the next phase of GSP, eg, Yugoslavia, Hong Kong, Singapore, South Korea, Brazil, but it is unlikely for political reasons. In this case (or even, in any event) the best solution for South Asia would be an extension of completely tariff-free access to all msas. This could be done following a general declaration, or in practice by exempting msas from butoir limitations. We have already shown that this would be of negligible consequence to the EEC in output and employment terms—a case which needs to be forcefully publicised.

(4) Rules of origin

Although there are administrative difficulties, there is no evidence that GSP rules of origin are currently a major barrier for the South Asians, but they could become so for Sri Lanka and Bangladesh, which lack the industrial base to supply most inputs domestically. The more obvious reforms likely to be useful are a reduction of the requirement of local value-added from 50% to 30%, and the re-definition of 'cumulative origin' to allow for trade between the four countries, as with ASEAN and CACM, or ideally to allow for all inter-lc trade; at the very least inputs purchased from the EEC should be given originating status.

Conclusions

This chapter has endeavoured to bring out the significance of tariffs as a barrier to trade. Very crudely, we estimate that tariff concessions already achieved under the GSP represent just under half of the static value of the weighted mfn tariff for India and Pakistan, and significantly more for Bangladesh and Sri Lanka. Our judgement is that, while they are worth negotiating, further tariff concessions are not only likely to be modest in their effect, but also minor by comparison with non-tariff barriers, to which we turn in the next chapter. Broadly speaking we do not expect that the benefits of complete trade liberalisation in respect of products of interest to South Asia would yield greater than the equivalent of 5% to 10% of current exports to the EEC for the potentially largest beneficiary, Pakistan, and 3% to 6% for the subcontinent as a whole. But for individual products the benefits are obviously greater. Moreover if we consider effective as well as nominal protection, particularly of agricultural processed items, there are further gains. But it is the very modesty of the costs to Europe which make a South Asian demand for tariff-free access for msas essentially realistic and reasonable.

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9. R. Baldwin and T. Murray, *ibid*.
10. J. Ahmad, 'Tokyo Rounds of Trade Negotiations and the Generalised System of Preferences', *Economic Journal*, June 1978.
11. This view is expressed with reference to India in a report carried out for the India-EEC Joint Commission on *Joint-Project Planning* by A.S. Consultants Multinational Ltd. in 1977, p324.
12. *Ibid*, p324-5.

5 Non-Tariff Barriers

It is often argued that while import duties are a hindrance to the growth of ldc trade, other, non-tariff, barriers (NTBs) are perhaps more important.¹ Successful rounds of GATT negotiations have resulted in the reduction of import duties, but these may in turn have been replaced by NTBs. In the current Tokyo Round a special group on NTBs has therefore been set up to establish rules on their use. Similarly, under the four CCAs between the subcontinent and the EEC, the Joint Committees are required

‘to study and devise ways and means of overcoming trade barriers and in particular existing non-tariff and quasi-tariff barriers in the various sectors of trade, taking into account the relevant work undertaken in this field by the international organisations concerned.’²

This chapter therefore addresses the subject of NTBs and attempts to show how far they are a problem for South Asian exports to the EEC. The first part deals with definitions and surveys existing empirical work on the general use of NTBs by the EEC. This is followed by a more detailed examination of the specific NTBs faced by South Asian exports to the EEC and a set of proposals for dealing with them. Finally, there is a brief review of how NTBs are being treated at the international level and the implications for their treatment by the Joint Committees.

NTBs in the Community

There is no universally accepted definition of an NTB. At one extreme, NTBs have been widely defined as ‘all private and governmental policies and practices (other than tariffs) that serve to restrict or distort the volume, commodity composition, or direction of international trade’³ or ‘any act of intervention in the economic process by which foreigners are consciously discriminated against’.⁴ But using either of these definitions means that any change in government (or private) policy in an importing country which affects an exporter of goods to that country, would be classified as an NTB, even though its primary impact was outside the sphere of trade. GATT and UNCTAD have both adopted a more pragmatic approach to the problem. UNCTAD has identified a list of government measures which may be considered NTBs insofar as they are intended to have an impact on trade, either by quantitative restraint or by increasing the costs and prices of foreign goods on the domestic market.⁵ GATT has constructed and is steadily updating an inventory of NTBs based on some 800 complaints received since 1968 from members whose exports to other member countries have been affected. These complaints have been divided into five major types of NTBs:⁶

- (1) state trading, government monopoly practices

- (2) customs and administration procedures;
- (3) standards (health, sanitary, labelling etc);
- (4) import restrictions, licensing, export restraints;
- (5) charges on imports (internal taxes, levies etc).

None of these methods is wholly satisfactory. First, the UNCTAD and GATT inventories focus on government policy and practice. This may be most relevant to inter-governmental negotiations, as in the Joint Committee meetings. But activities of the private sector, which are ultimately controlled by governments, may also discriminate against foreign trade. An example may be the barriers to tea being processed in South Asia before export, put up by the tea multinationals. Second, the GATT data are based on officially registered complaints. It has been argued that in addition to these 'visible' NTBs there may well be instances of NTBs which do not get recorded. For example many importers, when clearing their goods through customs, experience delays which often result in spoilage. The term NTBs will be used in this chapter to include any EEC government policies which fit into the five categories used by GATT. Reference will also be made to other government policies and practices of the private sector in the EEC which are said to restrict imports, including freight rates and other 'invisible' NTBs.

Even when a number of NTBs, sufficient to be representative of the access difficulties, have been identified, there remains the problem of evaluation. Various writers have suggested that the GATT-UNCTAD material can be used to calculate the 'incidence' of NTBs. This has been defined as (1) the percentage of a country's total exports facing one or more NTBs on import to another country, and (2) the number of NTBs imposed on exports of a particular product. But an NTB may affect different countries in different ways; South Asia may be less able than more advanced Idcs such as Taiwan to meet rigorous technical standards on electric consumer goods. Similarly a product may be affected by different NTBs in different ways; it is difficult to say how far the imposition of a health regulation on potato imports already restricted by a QR will strengthen the barrier facing these imports. One study⁷ has shown that there is no correlation between the frequency of NTBs facing products and the differential between domestic and international prices. Finally, some account must be taken of the possibility that there are NTBs which simply prevent any trade at all. With these qualifications in mind existing studies can be used to assess:

- (1) how far the EEC countries use NTBs against imports from all countries, especially Idcs;
- (2) how far the use of NTBs varies within the EEC;
- (3) which are the most common NTBs facing South Asian exports to the EEC (and elsewhere);

- (4) which products are most affected, and
- (5) whether certain NTBs are directed specifically at South Asian exports to the EEC.

A series of interviews with importers in four EEC members: UK, Germany, France, and the Netherlands, was carried out to collect supplementary information on 'invisible' NTBs and also to obtain alternative, though unquestionably less objective, assessments of the barriers posed by NTBs.

In principle the EEC now forms a single customs union. The transitional period during which the nine member states set about harmonising their external tariffs and customs codes ended on 1 July 1977 and producers throughout the world were offered the world's largest market. But in practice many differences still exist between individual members' trade policies. First, although customs codes and the common external tariff have been established, it is still possible for these codes to be interpreted and applied differently under the different legal systems, until the customs procedures are simplified and harmonised. Second, without economic and monetary union and concomitant fiscal harmonisation, the flow of goods within the customs union will have to be controlled at each frontier, to allow for the imposition of countervailing excise duties. Third, there remains the fact that each member has a different set of laws largely designed to protect the consumer, including health and sanitary regulations (HSR) and laws on labelling. As long as these vary between states there will be technical barriers to trade within the EEC.

The implications of these differences are twofold. First, the South Asian exporters do not face one large market but nine markets with differing access barriers. And second, the Joint Committees, set up under the CCAs, may not be the appropriate bodies to deal with those access problems which vary within the EEC.

However, some work has been done on NTBs at the EEC level. This is examined first. The evidence on NTBs in each member state is considered in a later section.

Table 5.1 Value of Exports to the EEC Affected by NTBs^a (\$m)

Country	Total Exports	Exports Affected by:				Exports Affected by NTBs as %	
		QRs ^b	Licensing	HSR ^c	Levies	Total	of Total Exports
Sri Lanka ^d	91.8	0.1	0.1	0	0.2	0.4	1
Pakistan ^e	220.8	3.7	8.3	0.5	2.7	11.5	5
India	546.1	11.5	16.1	2.4	7.1	37.1	7
Brazil	1488.7	7.5	8.8	133.7	128.3	278.3	19
Thailand	171.1	2.5	0.6	0.1	82.3	85.5	50

Notes: ^a The data refer to EEC imports cif in 1972 and the assumption is made that all trade in a tariff line for which there was a reported NTB is in fact subject to the restraint. When an NTB is applied by one or more (but not all) of the member states the trade values have been approximated by using weights.

^b Quantity restrictions

^c Health and Sanitary Regulations

^d Sri Lanka includes Maldives

^e Pakistan includes Bangladesh

Source: UNCTAD Research Division, *Summary of Trade Barriers and Preferences Facing Individual Developing Countries in Major Developed Markets*, Research Memorandum No 57, 10 May 1976.

From Table 5.1 it appears that the EEC's NTB policies do not pose serious problems for South Asia. Once duties had been paid, 94% of EEC imports from South Asia could enter the EEC market freely—whereas nearly one-fifth of Brazilian exports faced barriers of some sort. It is interesting to note that the share of exports affected was higher for India than for Pakistan or Sri Lanka. As Indian exports contain a high proportion of manufactured goods this may suggest that NTBs in the EEC affected manufactured goods in particular. But in the case of Thailand, whose exports to the EEC are largely agricultural, the share of exports affected by NTBs was as high as 50%. Relative to other dc's the EEC policy on NTBs seemed moderate as far as the South Asians are concerned. The same piece of work shows that in the US the share of South Asian exports facing NTBs was 19%—three times higher than in the EEC. On the other hand only 7% of Thailand's exports to the US faced NTBs. Other work, by Ingo Walter⁸ in 1971, produced similar conclusions. He found that in 1968 only 3.9% of ldc imports to the EEC were covered by NTBs, a slightly higher share than the 3.0% of all extra-EEC imports to the EEC. His work also examined the incidence of NTBs by product, showing that while in the EEC NTBs were not a problem at the aggregate level, they affected certain products seriously. In particular, most imports to the EEC of processed foods, beverages, and tobacco faced NTBs whereas imports to the US of processed foods were NTB-free. These comparisons must be treated carefully, however, for the reasons stated above, until it can be shown that the impact of \$1 worth of goods facing HSR, the major NTB in the US, is equal to \$1 worth of goods facing licensing,

quotas or levies in the EEC or, alternatively, that the impact of \$1 worth of goods facing NTBs is the same for an Indian exporter as for a Thai. In addition it is necessary to remember that these data refer to conditions prior to British entry to the EEC and prior to the 1977 renegotiation of the Multi-Fibre Agreement.

Table 5.1 also suggests that of the various NTBs used by the EEC, licensing and QRs were more important for India and Pakistan-Bangladesh, while for Sri Lanka variable levies posed greater problems. Later work by the US Tariff Commission in 1974⁹ shows that of all ldc complaints to GATT on the subject of trade with dcs, 40% were made with reference to QRs, 34% to non-tariff charges, and about 11% to customs procedures. Standards were responsible for only 5% of complaints. Further information on the most prevalent sorts of NTBs in use in the EEC is available as a result of the multilateral trade negotiations. A GATT document, *The Consolidated List of Requests for Concessions* (MTN/TP/W11 Rev.2) on tropical products is useful; despite the concentration on one range of products it covers both primary and processed goods, eg jute manufactures and tanned leather. The table below shows the number of products for which requests for tariff and non-tariff concessions were made by each of the South Asian countries to the EEC-9 (as a whole) and gives a breakdown of the type of NTB concessions requested.

Table 5.2 Concessions Requested at GATT (by number of products)

	Tariffs	NTBs	of which — types:				
			(1)	(2)	(3)	(4)	(5)
Bangladesh	47	24	2	—	7	13	2
India	42	26	—	—	9	15	2
Pakistan	25	22	1	2	6	9	4
Sri Lanka	23	16	—	—	1	4	11
	137	88	3	2	23	41	19

- Notes:*
- (1) state trading, government monopoly practices
 - (2) customs and administration procedures
 - (3) standards (health, labelling etc)
 - (4) import restrictions, licensing, export restraints
 - (5) charges on imports (other than tariffs)

Source: GATT, Multilateral Trade Negotiations, 'Tropical Products' group Request Lists, 1975.

Various studies of NTBs have been carried out which enable us to rank the import régimes of the EEC members, according to their degree of severity and in particular by the extent of their discrimination against ldc. Table 5.3 summarises the results of the most recent of these studies and ranks the Nine on the basis of these results.

Table 5.3 The Use of NTBs in the Nine Member States—various indicators

	No. of NTBs used against ldc imports	No. of NTBs used against ldc imports	No. of NTBs used against all imports	Import Régimes ranked in order of severity (1 = high, 8 = low)		
	1972 (1)	1974 (2)	1974 (3)	(1)	(2)	(3)
France	140	141	476	1	1	1
Germany	54	70	310	2	2	3
Italy	38	46	411	3	3	2
Belgium-Luxembourg)	27)	25)	270)	5)	7)	4
Netherlands)			267)			5
UK	19	36	214	7	5	6
Denmark	29	38	142	4	4	7
Ireland	21	35	68	6	6	8

- Sources: 1. UNCTAD, Third Session, Santiago de Chile, volume II, p148.
 2. quoted in IIFT, *Non-Tariff Barriers to International Trade*, 1975, p118, original study by UNCTAD, TD/B/C.2/11/Rev 1, 1974.
 3. World Bank, Annex E, Trade Liberalisation Study, 1977, based on US Tariff Commission, *Trade Barriers*, 1974, Ch VII, p167.

Once again it is necessary to emphasise the problem of evaluating the impact of NTBs (whether having a large volume of imports affected by one NTB is a greater barrier than having a small volume affected by many NTBs). But the table can be used to make one or two comments. Most striking is the fact that France offered the least accessible market for all imports and, compared with the other EEC members, its treatment of ldc imports was particularly restrictive. In 1974, it used more than twice as many NTBs against ldc imports than any other EEC country. It is also interesting to note that Germany, reputedly a country in favour of free trade, had the most restricted market after France while the UK and the Netherlands were considerably more open to ldc imports. Finally, the table allows some comment on the use of NTBs over time. This increased for six of the nine countries, but only in the case of the UK did the increase appear significant—with the number of NTBs used against ldc imports nearly doubling within two years.

An analysis of the submissions to the GATT *Inventory of NTBs* (1968) produces a slightly different picture. Of the 20 complaints made by Pakistan and India (none were received from Sri Lanka, while Bangladesh did not exist at the time), the most (8) were against Italy, with 4 against France and 2 each against Germany, Holland, Belgium-Luxembourg, and the UK. The results of the more recent studies mentioned above, however, are borne out by the more general observations made by the Indian Institute of Foreign Trade (IIFT) and by our own interviews with importers in four EEC countries.

The IIFT has produced two reports on NTBs with specific reference to Indian exports to the EEC,¹⁰ written in 1975 and 1977. These present the problem of NTBs by country of destination as well as by commodity. From these reports it appears that certain EEC members, in particular France, Italy, and Germany, though theoretically following liberal commercial policies, in practice make extensive use of NTBs. In France a wide range of goods, if not actually banned, require special import certificates, while in Italy many imports of tropical products including coffee beans face internal taxes. In Germany there are said to be many restrictions on imports, especially QRs. On the other hand the UK, Belgium-Luxembourg, and the Netherlands appear relatively free.

Interviews with importers of South Asian goods in the UK, France, Germany, and the Netherlands confirmed these findings but with a few reservations. First, certain formalities exist which to the novice may resemble NTBs but once experienced may be considered routine trading procedures. Thus access to the French or German markets, which are new to the Indian exporter, may appear more difficult than access to the more familiar UK market, but this is not sufficient to justify claims by the exporter or the IIFT, that NTBs are at work. Second, the IIFT reports include NTBs on a wide variety of imports such as tulip bulbs which may not be considered important export products for India—and this distorts the picture. Third, even if the IIFT comments were generally true in 1976, the treatment of imports is rapidly changing throughout the EEC. With growing unemployment in all nine countries, partly due to the falling domestic demand but also to the rise in imports, there are increasing pressures for controlling markets through the use of NTBs, such as QRs, countervailing duties, and customs delays. This is true not only for France but also for the UK, as became apparent in the recent MFA negotiations. The following section considers in greater detail how specific NTBs have affected South Asian imports to different EEC markets and the extent to which the situation is deteriorating.

EEC Barriers to South Asian Imports

(1) QRs and Surveillance Licensing

The NTBs which have been given the most prominence in the discussions of the Joint Committees, as well as at GATT, are those which explicitly restrict the volume of certain imports either at the port of entry (QRs) or at the port of export (VERs). This may be because they operate in a fairly simple manner and so the cost to the exporter can be easily worked out, for example, by comparing the growth in quotas for product to the growth of exports of that product to other, non-restricted markets. More important in the EEC-South Asian case, is the fact that the South Asian exports affected include textiles, clothing, jute, and coir products which together account for over 20% of all South Asian exports to the EEC. The next chapter, Chapter 6, deals with the impact of these restrictions and in particular the way in which they are administered. (The

arrangements covering imports of jute are examined separately in an Appendix available upon request from ODI.)

In the short term it is feared that this narrow product coverage will be extended further, probably on a bilateral basis as with the MFA, to include imports such as steel products, leather shoes, and even certain engineering goods for which EEC producers are currently seeking 'sensitive' status, similar to that of the textile industry. While these goods do not yet figure largely in the basket of South Asian exports they are beginning to form part of the growth industries in the Indian export sector. Any extension of the use of QRs seems likely therefore to damage the growth of Indian exports in particular.

The problem of QRs does not end here. Other QRs exist which are often overlooked precisely because they have prevented the development of export capacity in South Asia. For example both India and Bangladesh would export potatoes to the UK but for the fact that there is a ban in the UK on all imports of potatoes (except new potatoes). In 1976 this regulation was eased allowing imports to offset domestic shortages and both countries sent shipments. (In fact delays were experienced in the import licensing procedures with the result that several shipments deteriorated and were refused entry on health grounds!) The following year there was a glut of potatoes on the British market and the ban on imports was reimposed. Such uncertainty over access helps to explain why particular South Asian exports to the EEC have not been developed, and why particular QRs have been understated.

Other member states also continue to have national QRs on certain imports which may enter freely elsewhere in the EEC. In addition to the direct effect this has on trade, the ambiguity it creates for an exporter considering the EEC market is a problem. For example Bangladesh in its submissions to GATT has claimed that France restricts the volume of imported dried vegetables and canned pineapple, while India has experienced restrictions on French imports of coffee and Virginia flue-cured tobacco. There is no evidence however to support these claims; the contents of the GATT lists are themselves subject to negotiation. It is likely that there has been a confusion here between directly restricting QRs (ie QRs in the conventional sense) and other forms of NTB, such as discretionary licensing or tariff quotas, which interfere with the import mechanism and as a result indirectly affect the volume of imports. This confusion may be deliberate to the extent that QRs are taken more seriously in international negotiations. Alternatively it may be the inadvertent result of misleading academic work which considers other NTBs ranging from discriminatory government procurement to tariff quotas and import licenses as QRs 'in the sense that they quantitatively restrict imports'.¹¹

Under the Common Market regulations, an EEC import licence (other than an open general licence) is necessary for certain imports—such as rice and sugar¹²—to keep a check on the size of imports. This licence entitles the holder to

import a stated amount of goods within a certain period. It is issued upon payment of a deposit, and if the goods are not imported within this period, the importer loses his deposit.¹³ In addition to the market organisations of the European Communities there are still similar organisations at the national level which control the licensing of several imports, such as ethyl alcohol, mangoes in brine, preserved vegetables, and nuts. For example, in France all imports of vegetable oil must be cleared by the Société Interprofessionnelle des Oléagineux, an organisation of vegetable oil processing companies. In Germany, import licences for certain agricultural products must be obtained from the Federal Office for Food and Forestry. In some cases the licensing may be for statistical purposes only and so automatic, in others it may be discretionary, depending on the quality of the import or even the volume. This sort of system is open to abuse; frequently delays may be experienced in receiving licences, or their validity may be so short as to render them useless. While the overall effect may be to reduce the volume of imports, this may not have been the primary intention and so it seems best to keep the problems of surveillance licensing distinct from those of QRs. In particular it is extremely difficult to evaluate the effect of this NTB, given its uncertain nature. But two points can be made. First, the volume of South Asian trade likely to be affected is small, as licences (EEC and national) are only necessary for a few, relatively unimportant products, though whether or not the number of licences necessary has decreased with the formation of the EEC is a moot point. Second, while licences may have a shortrun negative impact on imports the net effect may be positive as their use allows a country to keep its trade régime fairly flexible; administrative delays in the allocation of licences can be set in action and then stopped with greater ease than QRs, which may have to pass through the legislative machinery.

(2) Levies

The second most important NTBs for South Asia are levies, which raise the price of some South Asian imports to the EEC. In fact one study has found that for food, grains, beverages, and tobacco, nearly all the differential between French and world prices is explained by levies (the remainder being due to transportation charges).¹⁴ Under the EEC's Common Agricultural Policy certain agricultural imports including rice and sugar,¹⁵ and their first-stage products, face a system of variable levies in addition to the normal customs tariffs. This ensures that the price of imported rice, for example, is kept to the level of the target support price for rice produced within the EEC. The importer is charged the difference between the lowest cif price offered on world markets and the target price, less a small amount to cover the cost of transporting the rice from the port of entry to its final market (normally known as the threshold price). All exporters to the EEC face these levies though in the case of the ACP states (and the countries applying for EEC membership) they are cut by up to 50%. The target price for most products is set once a year at a meeting of the nine countries' agricultural ministers. The levies, however, vary on average once a week, but sometimes more frequently, to follow changes in world prices.

In addition to the uncertainty inherent in such a system,¹⁶ there are two major worries for the South Asian exporters of these products. First, where other competing exporters (such as the USA in the case of long grain rice) have much lower prices—and it is on the basis of these lower prices that the levies are fixed—South Asian basmati rice has to pay a higher levy than is justified by the relationship of its price level to that of EEC grown rice. For instance, if basmati rice is \$700/1000 kg cif London and USA long grain milled rice is \$500, and if the intervention price is \$800, then (assuming the US price is the lowest world price) basmati rice will cost \$1000/1000 kg (pre-duty) (while USA rice will only be \$800) instead of \$800/1000 kg if it were being treated separately. On the other hand, the ad valorem rate equivalent of the levy is lower for basmati than for USA rice on this basis, which may stimulate South Asian exports. In order to offset the high price caused by the levy, importers are said to mix basmati rice with inferior qualities of rice. While this may increase sales in the short run, it also spoils the reputation of basmati rice, and so threatens future sales prospects.

Second, where the major source of competition is EEC domestic production and processing, levies provide the EEC producer and processor with a higher degree of protection over and above the tariff. The higher the EEC target price is above the world level, the higher the ad valorem tariff equivalent of the variable levy. Often this may be well above the mfn tariff on these goods. In the case of rice, as can be seen from the following table, the levy has in certain years provided up to 10 times as much protection as the nominal tariff.

Tariff 5.4 Tariffs and Levies on Rice Imports

Product	tariff (%)	tariff equivalent of levy (%)		
		1970 ^a	1972 ^b	1977 ^c
husked, long grain rice	12	34.5	107	37
bleached, milled long grain rice	16	n.a.	186	33

Notes: n.a. — not available.

^a G. Simpson and A. Yeats, *op cit*, p104.

^b World Bank, *Annex E*, p20.

^c own calculations—based on levies in March 1978.

The restrictive effect of levies operates on nearly all agricultural imports. In 1970 only in the case of sugar and its products (SITC 06) was the incidence of the levies less than that of tariffs.¹⁷ As far as South Asia is concerned the major agricultural exports which are affected by levies, other than rice, are honey and molasses, rice products such as cakes or bran, and products such as mango jam or canned mangoes, where a levy is charged on the sugar content. Sugar exports would also normally face levies but India is included in the EEC's sugar protocol

with the ACP states, and this allows 20,000 tonnes of sugar from India to be imported to the EEC free of levies. As exports do not exceed this level, levies have not had to be paid. To sum up, in 1975 the only significant South Asian exports affected by levies were: for Pakistan, rice (worth 3.2 mua) and molasses (worth 4.7 mua), for India, rice (1.7 mua) and rice bran (2.7 mua)—or less than 0.5% of India's exports to the EEC, and 3% of Pakistan's. Sri Lanka and Bangladesh were unaffected. However, these figures underestimate the cost of the CAP to South Asian exporters as they do not account for exports which may have occurred in the absence of the CAP, such as mango jam.

Of greater importance is the fact that levies rise with the degree of processing, as can be seen in the following table.

Table 5.5 Levies on Rice at Different Stages of Processing (1st March 1978)

Type of long grain rice	(ua/tonne)	
	Levies on South Asian imports	Levies on ACP imports
paddy	71.5	32.8
husked	89.4	41.7
semi-milled	203.0	91.7
wholly milled	217.6	98.6

Source: *Official Journal of the European Community*, 2nd March 1978.

The effective rate of protection on wholly milled rice from this system of increasing levies was calculated at 73% in 1970 as compared with effective protection of 32% from escalating tariffs. Similarly, effective protection from levies on a wide range of agricultural products averaged 134% or nearly two and a half times the effective tariff rate.¹⁸ Competing ACP exporters, such as Madagascar, also face a bias against their processed agricultural exports, though the level of effective protection which they face is much lower. However, the importance of this differential treatment in the case of rice is limited, as the ACP states are only small rice exporters. The US and Argentina, which are major suppliers to the EEC, compete with the South Asians on equal terms. But the protection of the EEC milling industry has made basmati rice, which is exported from Pakistan and India wholly milled, a lot more expensive to the final consumer than the American long grain rice which is imported in the husk and processed within the EEC.

The chances of the EEC eliminating this particular NTB to South Asian exports are slim. Levies are an important element of the CAP; in addition to the protection of domestic agriculture and processing interests, they provide a substantial source of revenue—estimated at 1686 mua in 1978 or the equivalent of 14% of EEC revenue in that year.¹⁹ It is therefore unlikely that the EEC will consider

seriously two alternative suggestions put forward by the South Asians: first, that the EEC treat basmati rice as a *special product which is not directly substitutable for the rice grown in the EEC, and which is of interest only to the Asian community resident in the EEC*; or second, that the revenue collected by the EEC be transferred to the South Asian governments, to compensate for lower export earnings. Nonetheless the case for selective treatment of the South Asians—at little cost to the EEC—is a strong one.

(3) Internal Taxes: Value Added Tax and Excise Duties

Within the EEC each member state has a system of indirect taxation, which presents South Asian exports with NTBs similar to levies in that they raise the price of exports above their cif, duty paid, level. However, the problems are not entirely the same. First, the levels of excise duties and value added tax (VAT) vary between members. This means that goods have to be stopped at the frontiers between different EEC states and countervailing duties imposed. Second, unlike levies, excise duties and VAT do not distinguish between goods imported into the EEC and those locally produced. Some products facing indirect taxes, such as tea and coffee, are wholly imported, however, and consequently it can be argued that such taxes are discriminating against imports by reducing the demand for them.

Under the Treaty of Rome²⁰ the European Commission is responsible for aligning these different rates (unlike direct taxation for which there is no provision in the Treaty). But as they form key components of sectoral policies, such as in agriculture, at the national level, harmonisation of indirect taxes will in turn depend on how far these national policies can be harmonised. In the case of VAT the need for a common policy is underlined by the fact that eventually the budget of the European Communities is to be financed by a percentage of each member's VAT revenue. Various directives have been issued but with little result. After 1967 all six states adopted the VAT system, but from 1969 to 1974 no action was taken to align the various rates, as the Council was unable to reach a decision on any of the proposals on tax harmonisation put to it by the Commission. The latest (Sixth) directive on VAT merely provides for a harmonised basis of assessment rather than for harmonised rates. In the meantime, rates vary by as much as 12% in the case of necessities and 24% in the case of luxuries, as shown in Table 5.6. Generally food items are subject to lower rates (0-12%) and manufactured goods to higher rates (5-33 1/3%).

Table 5.6 Rates of VAT in 1978 (as a % of prices before VAT)

Country	Standard rate	Reduced rate ^a	Increased rate
Belgium	16	6	25
Denmark	20.25	—	—
France	17.6	7	33 1/3
Ireland	20	0 or 10	35 or 40
Italy	14	1, 3, 6, 9 and 12	18 or 35
Luxembourg	10	2 or 5	—
Netherlands	18	4	16 or 17.5 ^b
Germany	12	6	—

Notes: ^a Foodstuffs and other essential goods

^b Supplementary rate for private cars according to value.

Source: 'Three Part Guide to the European Communities', *Trade and Industry*, 1 December 1978.

Proposals for common excise duties have been put forward by the Commission for tobacco, beer, wine, spirits, and mineral oils, of which only tobacco is of much concern to the South Asians. Progress has been very limited in this case. In 1972, there were two duty systems in the original six member states. Five countries had a wholly ad valorem duty on the retail price of cigarettes, while Germany, the sixth, had a specific duty per cigarette. In the UK, the structure was different again, with a specific duty charged on the weight of leaf tobacco entering a cigarette factory. Under the first stage of harmonisation (from 1972 to 1975 and then postponed to mid-1978) the duty was to be changed until it was raised on the end-product, consisting of both a proportional (ad valorem) and a specific tax in the case of cigarettes. Under the second stage (from 1/7/1978 to the end of 1980) the specific element falls to between 5% and 55% of total taxation on each cigarette. The final form of the tax is still uncertain, but it is likely to contain a high element of ad valorem tax, which will be to the benefit of exporters of cheap tobacco, such as India, as it will reduce the demand of American-type cigarette manufacturers for more expensive American tobacco. On the other hand it has been argued²¹ that a predominantly ad valorem system would allow French and Italian cigarettes to be sold more cheaply than the higher quality American-type cigarettes, thereby reducing the overall market for Indian tobacco. Together the excise duty and VAT on cigarettes constitute a major restraint on the EEC market for South Asian tobacco. On average they account for 71% of the retail price of cigarettes, as shown in the following table. (In fact the total duty equivalent of the VAT, excise, and import, duties on unmanufactured tobacco is nearer 3000%.)²²

Table 5.7 Incidence of Excise Duty and VAT on a Pack of Cigarettes in 1976 (as a % of the Retail Price)

Country	Excise Duty	VAT	Total
Belgium	61.5	5.7	62.2
Denmark	71.0	13.0	84.0
France	69.3	6.1	75.4
Germany	62.5	9.9	72.4
Ireland	63.6	6.4	70.0
Italy	60.3	15.3	75.6
Luxembourg	59.2	2.0	61.2
Netherlands	55.1	12.3	67.4
UK	60.3	3.2	63.5
Average	62.5	8.2	70.7

Source: IIFT, *Implications of NTBs to India's Exports in EEC Countries and Japan*, p47.

For some products such as tea and coffee, there are still no proposals on harmonisation for the Council to consider. This may be for two reasons. First, domestic production is small, and so there is little question of unfair competition between EEC producers, which has been the major driving force behind harmonisation in other areas. Second, only a few members have duties. These seem to be strong arguments for exporters affected by such instances to lobby the Commission themselves in an attempt to get the duty or tax removed. This has been done in the case of tea, which faces a substantial consumption tax in Germany of DM415 per 100 kg,²³ roughly equivalent to an ad valorem tax of 130% in 1976.²⁴ It is true that as the price of tea rose in 1976 the incidence of this tax fell but it is now returning to its original level. How far the demand for tea has been affected by the tax is subject to some debate. Using a price elasticity of demand of -0.73,²⁵ it seems that the abolition of the consumption tax in 1976 could have resulted in a rise in German tea imports from all sources of some 95%. But it is necessary to consider the consumption of coffee which also carries a consumption tax. At DM360 per 100 kg (for unroasted, undecaffeinated coffee) this is not only lower in absolute terms than the tax on tea but particularly in ad valorem terms, at roughly 50%.²⁶ Moreover, Germany is traditionally a coffee drinking nation. These factors suggest that the prospects for increasing tea consumption in Germany are poor and will remain so until the tax on tea is removed. Such action is unlikely to be favoured by the German government which argues that if the tax on tea were removed it would have to apply the same treatment to coffee, with the net effect of only a marginal increase in the consumption of tea.

Other South Asian exports also face excise duties of which the most important is sugar. This carries a duty in France, Germany, Belgium and the Netherlands

ranging from DM6 per 1000 kg to Bfrs60 per 100 kg. But this has not constituted a major NTB to sugar imports as it represents only a very low ad valorem duty.

(4) Health, Sanitary and Labelling Regulations

A major set of NTBs exists in the laws designed primarily to protect the EEC consumer, including health and sanitary regulations (HSR), technical standards, and laws on labelling. There are several reasons why these should be considered as part of the general category of NTBs. First, to the extent that they are more severe than consumer laws in other markets, they raise the cost of exporting from South Asia to the EEC above the cost of exporting elsewhere. A certain ingredient may have to be replaced or new machinery used to bring the product up to EEC standards. Where such modification of the production process is not possible, export to the EEC may be absolutely restricted. Second, certain laws differ within the EEC, thereby fragmenting the market and so preventing the South Asian exporter from taking advantage of economies of scale. Additionally there are many standards set by non-governmental organisations such as the British Standards Institute which have assumed a quasi-legal status—certainly products with the stamp of ‘approval’ are able to fetch higher prices and larger sales than those without. Third, these laws and standards are constantly being modified, increasing the uncertainty of the exporter as to whether his goods will find their way to a market.

Examples of HSR to which frequent reference is made by South Asian exporters, or their commercial representatives in the EEC, include rules on the pesticide residue in tobacco, the aflatoxin content of groundnuts and coconut, the bacteriological count in shellfish and the lead content of paint used on children’s toys. The need to control poisons is accepted by both exporters and importers; they are not seeking differential HSR treatment for their products (as they are in the case of other NTBs). But certain measures could be taken by the EEC which would reduce the impact of this NTB on South Asian exports while maintaining the wellbeing of EEC consumers.

In the case of tobacco, stricter laws in Germany, in particular, mean tobacco growers will have to switch to new pesticides or simply face lower yields. Proposals have been put forward to the Indo-EEC JC for technical assistance, to be funded by the EEC, which could reduce the costs involved in such a change. At the same time there are moves within the EEC to rationalise the different laws on pesticide content.

The situation with aflatoxin is slightly more complicated. Aflatoxin is a fungal poison arising when a crop is harvested in humid conditions, which is common to all oilseeds but especially groundnuts. Rules on the maximum permissible amount vary within the EEC. In Germany and the Netherlands, it is one part per thousand, while in the UK and France there are no legal limits, although codes of practice have been set up by traders.²⁷ In Belgium and Italy, according

to one source,²⁸ the level has been set so low that no Indian imports are possible. Furthermore, it is argued that the standards are unnecessarily restrictive. Groundnuts from India are normally imported in the form of oilcake to feed cattle. But the oilcake is first mixed with other ingredients to form a compound feed and this process lowers the levels of toxicity. Indian exporters feel therefore that the HSR should distinguish between groundnut cake to be used as primary feed and their groundnut cake which is used in compound feeds, with a higher level of aflatoxin being permissible in the latter. One way of making this distinction would be for the importer to sign a guarantee on the use to be made of the oilcake.

In the case of processed foods for human consumption, the main problem is the cost of inspection (and the associated delay) to see the goods meet the EEC or national standards. A recent report on Indian marine exports²⁹ found that few UK importers were aware of the Export Inspection Agency in Cochin, India, which can issue bacteriological certificates for exports. Instead goods are tested by sampling procedures either by the UK customs or by the importers themselves. Interviews with importers suggested that many factors including the poor refrigeration facilities on ships justify the double checking of seafood imports. A more serious matter arises when, as in the Netherlands and the UK, the government health authorities prefer to inspect the factory in the exporting country, than to sample each batch of imports. The UK insists that officers from the Ministry of Agriculture visit meat processing plants overseas before they can export their output to the UK.³⁰ Prior to independence, both India and Pakistan exported sausage casings to the UK and they are currently exporting them to France and Germany. But as no visits by UK officers have yet been paid to Indian or Pakistani slaughterhouses since independence, neither country is able to sell casings to the UK. This problem could be solved simply by the Indian and Pakistani governments offering to finance the necessary visits but they do not feel it necessary that the UK authorities should question the standards of the slaughterhouses in the first place when they are acceptable to two other EEC members.³¹ An alternative solution would be for funds to be made available out of the EEC aid budget.

Technical standards, though often not legally binding, present similar problems. In order to obtain a certificate of approval from one of the standards institutes which maintain a virtual monopoly in their markets, an exporter (to Germany) may have to pay £1,000 and as standards are changing constantly frequent tests may be necessary. While the sums involved may not seem large the delays associated with tests constitute a significant NTB. In some cases exporters may even have to alter their production process so that their products conform to the new standard. For example, in Germany the Technical Standards Institute recently declared that the burr which is formed when a steel pipe is electroresistantly welded is not 'allowed' with the result that India could no longer sell this sort of pipe in Germany.³² To overcome this barrier the Germans, under their

technical aid programme, are giving ldc nationals training in German standards. The government is also contributing to the cost of technical tests. In addition, standards institutes could be set up or strengthened in exporting countries, but it will take some time before they earn the confidence of EEC importers and consumers. Standards institutes could also eliminate a problem which has emerged recently, namely the participation of many companies in the export of engineering goods. This is said to have lowered the standard of Indian exports and so undermined the image of Indian engineering goods abroad which larger companies like Kirloskar had taken so long to build up. Alternatively, South Asian exporters could concentrate on particular markets such as the do-it-yourself sector, where standards for all but the most expensive products are less exacting than in the original equipment manufactures sector.³³ Finally, production under a technical collaboration agreement with a company based in the EEC may help in getting the standards of an export approved, provided the collaboration agreement included no restrictive export clauses.

Common EEC rules on how goods should be labelled, and what information the labels should show, are in the process of harmonisation. Already the Council has adopted directives on the labelling of dangerous substances. However, it is unlikely that all of the Commission's recommendations on common labelling rules will be made binding. For example, the Commission has recommended that the nominal content of a good should appear on its label, while in the UK it is still the minimal content which is legally required. But in principle the rules on contents of labels are the same and should pose no difficulty. One problem which has been experienced by South Asian exporters who have traditionally dealt with the UK but who are now trying to break into other EEC markets is the requirement that labels must be in the local language. This presents an immediate cost but one which can be dealt with easily by technical assistance either from the exporting government or from the EEC.

A more serious barrier lies in the restrictions placed on the use of certain terms to describe the contents of a can. One example, causing the Indians some worry, concerns the name 'sardine' which is normally reserved for *sardina pilchardus* (produced by Spain and Portugal) or 'X' sardines where X is the name of a country, a geographical area, or the species or common name of the species. In the UK the law requires that only *sardina pilchardus* may be labelled 'sardine'. This means that fish which British Fish Cannery of Fraserburgh, Scotland, market elsewhere as 'Scottish sardines' must be sold in the UK as 'sild'. Similarly the Indian oil-sardine would have to be labelled 'sardinella', a name that it is feared is both unknown and sounds too close to salmonella to stimulate sales.³⁴ However, this NTB may not be the constraining factor on sardine exports to the EEC. A large Dutch importer of seafoods argued that even where Indian sardines could be sold as such, they still did not sell well. In addition to the usual problems of unreliable suppliers and contaminated supplies, the price of Indian sardines was 50% higher (fob) than the price of Norwegian sardines.

Furthermore, some Indian sardines were packed in groundnut oil whereas the European consumer preferred them in soya bean or olive oil.

(5) State Trading and Public Procurement Policies

Barriers to South Asian exports are also said to arise in the area of state trading and public procurement. There is no uniformity of these policies in the EEC as yet, although alignment is likely in the near future. At a hearing in 1976 at the European Court of Justice a judge ruled that

‘national rules or practices which result in imports being channelled in such a way that only certain traders can effect these imports, whereas others are prevented from doing so, constitute a quantity restriction’.³⁵

This ruling went on to indicate that any state trading will be allowed only in exceptional circumstances, as is the case for QRs. But what effect it will have on the South Asian exports concerned, both actually—tobacco—and potentially—ethyl alcohol, matches, and newsprint—is not clear. In particular it is argued that state tobacco agencies in France (SEITA) and Italy (Monital³⁶) have caused low tobacco imports from Pakistan and India. However, there may be other explanations for this poor performance, such as high prices, low quality or slow delivery, relative to other suppliers. The South Asian case holds true only if other imports have been affected in the same way.³⁷ Even so, SEITA spokesmen may claim it is the French consumers’ preference for French tobacco rather than SEITA’s own purchasing policies which determine the volume of Pakistani or Indian tobacco imports.

As for public procurement, no EEC government, nor any of its agencies, has a written policy of buying only from national industries. Certainly there are no rules explicitly against purchasing South Asian goods. Examples are often quoted to prove that there is no discrimination in favour of goods nationally produced; for instance, the Dutch state purchasing agency has bought goods in other European countries and also Japan. In France, Renault, a state concern, has used some profile parts (spares) and aluminium lining imported from India, while British Leyland uses some Indian cranks. It is even argued that increasingly tight budgets have induced some Dutch public organisations to import wherever imported goods are cheaper. However these may well be exceptions to more general policies of buying domestic, especially in times of economic recession. Rules or conditions may exist, written or not, which, though not discriminating *a priori* against imports (or even South Asian imports), may simply be too difficult or costly for the producer outside the EEC to satisfy. For example, it is said³⁸ that in the Netherlands a representative of the state purchasing agency must be able to examine the place of production before making any purchase. This means that South Asian goods must be highly competitive before the agency would consider the cost of an inspection trip. Similarly in Germany, to

be considered a potential supplier to the Federal Post, Railways and Army, any producer—whether German or foreign—must be on an ‘approved’ list of suppliers, in addition to being able to meet the specifications of the goods required.³⁹ To be ‘approved’ a supplying factory must have been inspected by a representative of the agency. Most of the suppliers registered therefore are German, with some in the rest of the EEC and none in South Asia. As a result few tenders are in fact made globally. Another constraint is the length of notice for the tender, which may be as little as twenty days. Even where such rules can be shown to have discriminated against imports it is more difficult to prove that they were intended to do so. In particular they may be justified as insurance against the government placing large contracts with unreliable suppliers.

There is some doubt about the importance of this NTB, both in terms of the volume of goods publicly purchased and in terms of South Asia’s capacity to supply these particular goods. In Germany the volume of state traded goods or government purchases may be less than in the UK or France where there are many state industries. In the UK the fact that the steel industry and most outlets are nationalised is said to make sales of Indian castings, for example, more difficult than in France, Germany, or Italy, where the industry is only semi-nationalised.⁴⁰ In these countries the market is less concentrated both on the supply and the demand sides, so that India has even managed to sell steel products to the French Railways. In the UK, however, more marketing is necessary to sell Indian products in those areas not covered by the British Steel Corporation, such as textile machinery or handtools, where the buyers tend to be small.

There are many other products which the South Asians could supply competitively to the EEC government procurement agencies, ranging from engineering goods to jute door mats and military textiles and clothing. Various means of overcoming this NTB which are currently being discussed at the Geneva trade talks should be considered, therefore, at the Joint Committee meetings. These include technical assistance in improving the dissemination of information on tenders and in bringing factories up to the required EEC standards; assistance in financing the visits of EEC inspectors and in the construction of warehouses in the EEC to improve delivery performance; and more lenient conditions such as longer tender periods. Alternatively, where such assistance is not forthcoming, it has been suggested that one way of circumventing restrictive policies would be for South Asian companies to do contract work for EEC companies. Or, the South Asian governments could encourage EEC companies to set up subsidiaries in South Asia, as this would help to insure that their output was of the quality appropriate for sale to EEC state purchasing agencies.

(6) ‘Invisible’ NTBs

In addition to the five categories already discussed, which have been formally recognised as NTBs by GATT, there are many other instances that are commonly classified as NTBs. The term NTB is being used increasingly whenever a product

faces a problem at any stage of the export-import process. While this serves to broaden the understanding of barriers facing Idc imports beyond the narrow GATT perspective, there is a danger that giving the term such generality will render it meaningless and at the same time diminish the chances of negotiations on NTBs being constructive. For example, taste has occasionally been raised as an NTB on the grounds that it fragments the EEC.⁴¹ It is argued that as Germans are more conscious of quality than the British, they prefer shirts made in Germany to the cheaper Indian cheesecloth imports which are so popular in the UK. Similarly, the French prefer the larger Senegalese prawn to the Indian prawn. This may be true. But in the context of EEC-South Asian commercial relations it is more useful to confine the discussion of NTBs to problems over which the EEC governments may exert some influence. Four particular problems exist which merit examination: first, discriminatory shipping rates, second the uncertainty generated by EEC law, third, the friction experienced in customs procedures and fourth, the structure of the markets for various South Asian products.

(a) Shipping

There are four major types of sea freight available to South Asian exporters: (i) 'tramp' ships, chartered for single or multiple voyages at openly negotiated rates, (ii) 'conference' liners, which provide a regular and scheduled service at rates fixed under the operation of a market sharing agreement, (iii) Russian ships which undercut conference lines by 20-25%, and (iv) state-owned or privately-owned South Asian ships which form their own conference. Most of the Indian, Pakistani, and Bangladesh exports are carried by the India-Pakistan-Bangladesh and UK-Continent Shipping Conference, while in the case of Sri Lanka, over one-third of exports to the EEC are carried by the state-owned Ceylon Shipping Corporation and the rest by conference lines, though in recent years there has been increasing use of tramp ships and other non-conference lines.⁴² The development of independent South Asian conferences is still in its early stages and so they are unable to offer a real alternative to the other three types of freight.

There are two major grounds for complaint: first, the freight rates charged by the major conference lines are high, and second, the services provided are irregular. These problems combine to restrict the growth of South Asian exports to the EEC. Recent work by Yeats and others has shown that freight rates on imports often provide domestic producers with greater protection than tariffs. Figures are not available for the EEC, but in the case of Indian exports to the US, the average *ad valorem* tariff was 7.5% while the *ad valorem* transport cost was 13.6%.⁴³ The structure of freight rates is also thought to be biased against processed goods, offering even higher rates of effective protection to domestic producers. Yeats found that the average 'transportation factor' (ie the *ad valorem* incidence of transportation costs) increased with the stage of processing; for Indian exports to the US the average transportation factor on primary goods was 16.8%, on intermediate goods 21.5%, and on final goods 28.2%.⁴⁴

(See also Table 4.6 in Chapter 4.) While some commodities may be bulkier when processed than when raw, there is evidence to suggest that conference lines use higher rates on processed goods to subsidise shipments of primary products.⁴⁵ From South Asia to the EEC, conference rates are higher per cubic metre on processed goods: 32% higher on cotton shirts than on cotton yarn, 12% in the case of jute sacks (jute yarn), and 48% for instant tea (bulk tea).⁴⁶

Conference freight rates have been steadily rising. From 1974 to 1977 the basic freight rates on cargo carried from India to the UK rose by roughly 27%, to levels well above those charged by the Russians. As freight rates are highly complex, it is difficult to establish how far these rates reflect the weak bargaining power of South Asian exporters, which are fairly insignificant beside large exporters like Singapore, rather than real costs. Only a part of liner operational costs is attributable directly to the products carried (known as the basic service rate). In addition, freight rates are based on many factors, including a currency adjustment factor, a bunker surcharge, an equipment handling charge, and a port congestion surcharge, with allowances being made for full containers or pallets, and a rebate for a long term contract with the conference. Certainly other conference rates have been rising at similar rates. Where there is a differential—as in the case of shellac which costs twice as much to ship from Calcutta to Europe as from Bangkok⁴⁷—this is less likely to be the result of deliberate discrimination against South Asian exports than the result of surcharges necessary to cover problems arising in South Asia such as port congestion, half empty cargoes, dirty goods, or the lack of container facilities. For example, in 1977 several unloading points in the port of Colombo were blocked as a result of labour disputes which caused delays in the clearing of goods. Fourteen ships had to wait beyond the scheduled period to unload and demurrage charges became payable. Similarly in September 1977 a 15% congestion surcharge was imposed on Bombay cargo to cover the berthing delays of 20 days on average. A recent report by the UN on the India-Pakistan-Bangladesh conference concludes that the increases in rates charged do not bear any relation to price increases in these countries.⁴⁸

These factors—in particular delay and low volume of trade—may also explain the infrequent stops made by ships in South Asia, and their preference for business with the Far Eastern ports. In 1977 a major shipping line, which had carried as much as 49% of Sri Lankan exports to the UK in 1976, decided to strengthen its container services to the Far East and this meant cutting back the sailings from Sri Lanka to one every six weeks.⁴⁹ Clearly there must be some trade-off between frequency and freight rates. But the South Asians argue that even when conference rates are fixed the service tends to decline.

Importers emphasise the major shipping problem as being the bottlenecks in South Asian ports.⁵⁰ Many, in fast turnover trades such as clothing, prefer to rely instead on air freight despite the even higher costs. According to one study⁵¹ India doubled its share (in volume) of German imports of leather footballs to

27% from 1972 to 1974 by switching to air freight. This both removed the cost of expensive warehousing in Germany and ensured rapid as well as regular delivery to importers. Sea-freight rates *per se* did not seem a major disincentive to import from South Asia. But to the extent that they do present a barrier to exports, this could be minimised with improvements in port facilities and increased South Asian shipping capacity.

(b) Regulations

The uncertainty and risk involved in importing goods from South Asia have been made worse by the multiplicity of regulations affecting EEC trade. The sheer volume of EEC regulations, ever increasing, can work against the interests of South Asian exporters. For example, a West German food wholesaler would prefer to buy processed foods from German manufacturers, who are familiar with both German and EEC regulations, than from Indian markets. This problem will begin to disappear when laws within the EEC are harmonised. But even then EEC rules will change, following the tendency in dcs for consumer standards to continue to rise. This situation could be solved with the establishment of an EEC-based trade information centre, one of its tasks being to ensure that ldc exporters are aware of changes in regulations affecting their particular exports. But to date such a centre has not met with the support of all EEC members.

(c) Customs Procedures

The general handling of imports by customs authorities has been another subject of complaint by South Asian exporters. It is claimed that administrative friction is often used to restrict imports. Documentation procedures may be extended so that 'goods spend weeks if not months getting customs clearance. It not only serves as a neat unofficial protectionist device but also deters potential importers who don't want their stock and cash tied up for long periods on ... quaysides'.⁵² In France in 1977 some importers of Pakistani cotton yarn experienced 8 to 12 weeks delay between the presentation of their import declaration forms and invoices and the receipt of surveillance licences necessary to clear their goods.⁵³ Such delays affect the export of low cost items, where profit margins depend on high rates of turnover, with particular severity. Delays may even result in the total loss of a shipment where the good is perishable. It has been suggested that the French authorities follow a discriminatory policy of delaying imports of South Asian seafoods but not those from ACP states. But it is tempting to overstate the argument. A large French importer of seafoods felt that this may have been an attempt by the exporter to pass on the blame for goods being spoilt before reaching the importer. There are many other explanations possible for the low volume of French imports of seafoods from South Asia, relative to imports from ACP countries, such as historical trading links, taste or supply problems.⁵⁴ He also pointed out that other exporters, notably the Malaysians, have made the same claims about import delays, but in their case they claimed preference was given to South Asian seafoods! Importers

have also noted that customs delays may be the result of exporters sending the wrong documents and of the time taken by banks in the importing country to deliver the documents to the importer. For example a French importer of footballs from Pakistan, who prefers to use air freight than sea, which takes three to four months, must wait up to a fortnight when his goods arrive in France before receiving from his bank the import documents necessary to clear his goods through customs. (This is one of the drawbacks of payment by Letter of Credit which is often insisted upon by South Asian exporters.)

Customs authorities' interpretations of the EEC import regulations may also differ within the EEC. One particular problem which has arisen is the classification of goods. Some EEC countries classify a good on the basis of which constituent is dominant by weight, others on whichever constituent pays the highest rate, and others on whichever constituent determines the nature of the product. Goods which are handmade present special difficulties. The distinction between these goods and those which are machine-made is important, as the EEC gives duty-free treatment for some imports of handicrafts or handmade goods (in BTN Chapters 42 to 97) from countries including Bangladesh, Sri Lanka, Pakistan, and India, up to a quota of 1,200,000 ua for each tariff heading or subheading. In order for their goods to qualify, importers must produce a certificate of manufacture issued by the relevant authorities in the exporting countries, which states that the goods have been handmade. The customs authorities must also accept the goods as having been handmade and it is here that a problem arises, as there is no official EEC definition of handicrafts.⁵⁵ In the UK the definition is fairly flexible. Even where a good has been produced partly by machine and partly by hand it will be accepted as a handicraft, provided its essential character is derived from its handmade characteristics. In other countries, however, if a machine has been used to sew on the buttons of a lady's shirt, it is no longer given artisan status, and the full duty of 17% is payable. Similar problems arise in the definition of handloom cloth, which also has a duty-free quota. But in this case the cloth can be tested scientifically. To avoid the uncertainty created by the variety of possible interpretations, the EEC should adopt a particular definition of 'handmade', preferably the one used by the UK authorities. Alternatively the EEC could copy the US practice of listing certain 'traditional' products which are given duty-free status regardless of how they are now made.

(d) Market Structure

A final problem often mentioned is the way a few companies dominate the markets for certain South Asian imports. For instance, they may buy a large share of imports. This weakens the bargaining strength of South Asian exporters in price negotiations and tends to depress the unit value of exports. As one study points out, 'the extent of importer concentration can be an important determinant of the terms of trade and more particularly of the degree to which developing countries realise gains from the generalised system of preferences'.⁵⁶

On the other hand, it has been argued that the emergence of multinational buying groups may offer more profitable export opportunities for ldc's to the extent they cut out the middlemen in the import distribution system.⁵⁷ Even so the preference of these groups to buy in bulk can be shown to work against the interests of the small exporter. For instance John Lewis, a large importer of readymade garments and textiles, has readily admitted that it will only buy from large Indian exporters as the smaller companies are unable to supply large volumes of goods of consistent quality with a fixed time schedule.

Unfortunately it was not possible in the context of this study to examine the concentration of importers in EEC-South Asian trade in any depth. But interviews with importers provided one or two examples where imports are becoming more concentrated. In Germany, France and, to a lesser extent, the Netherlands, it appears there is a growing tendency for small specialist importers of one product to join together in organising a trade fair at which they place joint orders for imports, thereby ensuring lower prices. Alternatively, they may appoint firms to import on their collective behalf.⁵⁸ In the German sportsgoods trade there are five firms which act as importers and wholesalers for the specialised retailers who account for 85% of sales in Germany (the balance being made up by the mail order and department stores⁵⁹). On the other hand, in the UK most firms importing sportsgoods are small; the major department stores deal directly only in the cheaper, quick turnover items, preferring to use specialised importers for the more expensive goods.⁶⁰ It would be dangerous to make any generalisations on the basis of these few examples, and even more difficult to suggest their implications for EEC-South Asian trade. Two options exist to soften the problem of concentration, such as it is. First, South Asian exporters could form themselves into export houses or co-operatives, thereby strengthening their position vis-à-vis importers. But this strategy has obvious limits. A second possibility is to bypass importers altogether and sell to the retailers through importing agents appointed by the South Asian exporters. But only large exporters will be able to justify this cost.

Another illustration of how market concentration may be a problem for South Asian exports is the control of retail markets by a few domestic manufacturers. Whereas concentration in the import trade affects the unit value of some South Asian exports, concentration in the retail trade tends to restrict the total volume of some South Asian exports. The most commonly quoted example is that of the UK tea market. A recent report by the Price Commission showed that

'four major blenders account for about 85% of UK tea sales and two of them for over half. This is a highly concentrated trade. Advertising and other promotional expenditure has firmly established the brand names of the leading blenders. With the demand for tea in the UK little changed it is difficult for new businesses to set up as blenders and none has done so for many years.'⁶¹

Such concentration exists in most of the nine member countries and has prevented Indian and Sri Lankan companies from developing a market in the EEC for their processed tea. Their sales have had to be restricted to high quality tea bags and packets, sold via Tea Centres with heavy promotion costs.

This particular problem has been discussed at Joint Committee meetings. One solution which has been suggested, and which has been tried out recently in the case of processed tea, is for the South Asian exporter to organise joint promotion efforts with European retailers. The Indian Tea Board's European office arranged sales of Indian tea in retail packs, blended and packaged in India, from special stands in large department stores in Germany, Holland, Belgium, and Denmark. But even this type of exercise has costs of which South Asian exporters will have to bear the larger part until EEC retailers can be assured of an adequate return on sales. Whether or not market concentration in general should be considered by the Joint Committees, as an NTB or otherwise, is questionable. In many cases the impact on South Asian exports to the EEC will be difficult to prove. But when such proof can be found, as in the case of tea, it seems there are two things which the JCs can do usefully. They can create a forum for discussion between the affected EEC and South Asian interests. If this fails to produce agreement, they can provide financial or technical assistance to the marketing operations of the South Asian exporter. Ultimately, however, this remains a problem more appropriate for a Monopolies Commission.

NTBs in the Future

While the question of NTBs is being handled on an *ad hoc* basis at the Joint Committee meetings, international negotiations are under way in the GATT Tokyo Round which aim to tackle NTBs systematically. Two steps have been taken. First, an inventory (mentioned above) has been drawn up to identify what constitutes a NTB. Second, in late 1976 five subgroups (on Government Procurement, Technical Barriers to Trade, Customs Matters, Quantitative Restrictions, and Subsidies and Countervailing Duties) were set up to draft Codes of Conduct on the use of these NTBs. To date, however, little progress has been made. One problem has been the request by developing countries for special and differential treatment. For instance, one concession which has been suggested is a special effort by developed countries, possibly under a technical assistance programme, to supply developing countries with information on dc government purchases. This request was opposed in principle by the EEC as a whole which was prepared to give preferential treatment only on a case-by-case basis rather than to all ldc's. In 1976, when many developed countries introduced safeguard measures restricting imports, in no case were developing countries given special treatment. Another problem has been whether or not to include agricultural products in the deliberations of the NTB subgroups, given the difficulties which agriculture has caused in discussions on tariffs. A lot of time was wasted in the Tokyo Round before it was suggested that NTBs

on agriculture should be dealt with by the group on Agriculture and not by the five NTB subgroups. Finally, a difficulty which has emerged recently is a drift in the Tokyo Round towards increasingly bilateral negotiating techniques. There is a general feeling that if any of the South Asian countries wants to obtain concessions on NTBs from the EEC it would be better to deal directly with the EEC rather than to negotiate in an international forum.

For these reasons NTBs will continue to feature largely in Joint Committee agendas. Even the establishment of codes under GATT, when it occurs, will not pre-empt NTBs from Joint Committee discussions. In some cases, such as government procurement, there is no doubt that the codes will help, by clarifying what treatment South Asian imports to the EEC should be given. But it is likely that with the growing protectionism in the EEC there will be renewed instances of 'invisible' NTBs which demand consideration. While it is possible to overstate the importance of NTBs it seems likely that they will be a continuing problem in EEC-South Asian commercial relations.

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6 Quantity Controls Textiles

Introduction

The introduction by the EEC of a revised system of textile import restraints in 1978 effectively means that import growth in volume terms for the next five years (to end-1982) will be confined for most items of importance to South Asia to the range 0.25% to 4% pa. Non-tariff restriction¹ of textiles however is not new, and as far as these countries are concerned, it has long been the most severe non-tariff barrier in the EEC. It therefore merits special treatment.

The share of cotton and man-made fibre, textiles, and clothing in the total exports of the four countries, varies from around 25% of all exports (Pakistan) and 15% (India) to a mere 2% for Sri Lanka and virtually nil for Bangladesh. Since these figures represent levels of export after restraint in the main consuming markets, and exclude important items, such as wool-based carpets, as well as jute products, the actual and potential importance of textiles for Pakistan and India is clearly understated. The EEC is the largest market taken as a whole for South Asian textile exports, accounting for one third of India's cotton textile exports (60% for garments). The figures for Pakistan are similar.

The South Asian countries have also come to be seen by European producers as a threat to their interests. India is regarded as one of the five 'dominant' ldc suppliers and faces specific ceilings on the level and growth of exports to the EEC of 14 items accounting for over 90% of the country's non-jute textile exports. Nonetheless, India accounted for only 7% of dc textile imports from ldcs in 1975, as against Hong Kong's 34% and Korea's 25%. Pakistan and Sri Lanka are amongst the 20 countries also singled out for specific restrictions (on 9 and 5 categories respectively), accounting for almost all of their textile exports to the EEC.

This chapter endeavours to explain in detail the nature of these access barriers and the possible implications for the EEC and the South Asian exporters of lowering or maintaining them. It focuses on those items restrained under the Multi-Fibre Agreement (MFA)—cotton textiles and garments mainly of cotton but also of synthetics and mixtures. Woollen textile items not subject to MFA restraints are omitted, as are jute products.

Textile Exports and the Economies of South Asia.

Before discussing trade patterns, it is useful to describe very briefly the role which the textile industry plays in the four economies and the importance of external trade to them. The differences are perhaps more obvious than the similarities. The most obvious contrast is in the scale of the industries. The Indian one is vast, employing some 10 million people, mostly handloom weavers, but

with 800,000 in the organised mill (non-clothing) sector. By contrast, the Sri Lankan industry employs only some 25,000, even after a rapid mushrooming of export oriented garment factories. India's yarn spinning capacity of 19.8m spindles is virtually the same as that of the USA, Japan or China. Pakistan's 3m spindle capacity ranks a little behind that of France; its cotton textile and garment industry employs about 500,000 people in total.

A second basic difference is in the degree of export orientation of the industry. Bangladesh is not a cotton textile exporter and is unlikely to become one in the foreseeable future. Its former Pakistani-owned mills have a mere tenth of Pakistan's own capacity and are unable to meet local needs. Sri Lanka has begun to export garments, but on a small scale using imported fabrics, and only achieved a positive trade balance in 1976/77. Pakistan, by contrast, has been, since the mid 1960s, a net exporter and now exports 60% of its textile production (28% of cotton yarn output, 81% of cotton piece goods, in 1975). India was, up to independence and for a while after, the leading ldc cotton textile exporter but thereafter industrial strategy was inward looking and reinforced by restrictions on cotton textile imports in its main markets. A loss in international competitiveness as well as an increase in clothing exports caused India's textile export performance to decline to a point where in 1975 only 1% of yarn output was exported and 9% of mill-made cotton piece goods (including handloom piece goods the figure is lower). But in absolute terms India is still much the largest exporter in South Asia.

There are also important similarities between the four countries. One is the dominance of cotton over synthetics, though there is a trend towards the latter. In India for example the volume of cotton cloth currently produced is about five times greater than that from man-made fibres or blends; in 1975 it was ten times greater. This partly reflects the preference of the very poor for the cheaper, even if of poorer quality, cotton material, partly the local availability, in India and Pakistan, of cotton, and partly also, in the case of India, heavy import duties on synthetic fibres—though these have recently been cut.

Another important feature of both the Pakistani and Indian industry is the importance of the non-organised, non-factory sector. This is overwhelmingly the case for clothing manufacture. A recent Pakistani survey found that '90% of garments units are in the small scale sector ... usually equipped with 4 to 10 sewing machines and 1 or 2 electric irons'.² The Pakistani mill sector is more mechanised than the Indian, but in both countries there is a substantial contribution to production made by handloom fabric weavers, and intermediate sized power-loom weavers. In India there are incentives for the non-mill sector and a special obligation on it to supply a quantity of cloth (known as 'controlled cloth') at controlled loss-making prices. These measures have helped raise the share of non-mill production to 55% of the total (or 57% of domestic consumption), as against 38% in 1961 and 21% in 1951. Handlooms alone accounted for

30% of cloth output in 1976 and this share is expected to rise, as the Janata government wishes to reserve all production of domestically marketed cloth for the small scale sector. So, by implication, the mills will have to close or export all their output.

The third similarity is the state of crisis which currently grips the textile industry of all four countries, with production virtually stagnating. The export oriented industries of India, Pakistan, and Sri Lanka have been badly affected by Western protectionism and the fall in world demand in 1977, and now run considerably below capacity. In Pakistan's case this is aggravated by capacity originally installed to supply Bangladesh. The main problem however is not only the decline in external demand but also in the domestic market. Indians now consume, per capita, 19% less textile material than they did a decade ago.³

In Pakistan and India home and foreign demand deficiency has been compounded by numerous other problems: low labour productivity (on average 1/3 of European levels), labour unrest and increases in labour costs, erratic power supplies, ancient and inefficient machinery. In India there were added difficulties with the controlled cloth obligation (which is a form of price control), credit squeezes and cotton shortages. These have since been eased with the ending of the cloth obligation (replaced in October 1978 by a 10% levy on textile mills), increased credit and permission to import cotton. There is however no sign of an end to the 'prolonged agony' of the industry.⁴

The attractions of textile exports for South Asia can be listed as follows:

(1) Employment benefits from a generally labour intensive industry, overwhelmingly so for garments. It is possible to compare the importance of garment exports for employment in South Asia with the importance of the industry to employment in Europe, on the basis of calculations derived from average coefficients. In India it has been estimated that on average annual clothing exports of Rs50,000 (fob) provide employment for perhaps 16 people, 6 assembling the garments, 6 weaving the handloom fabric, and another 4 in ancillary and finishing trades. On the basis of these figures, current garment exports provide, directly and indirectly, 750,000 jobs in India (less than one tenth of all employment in the small scale textile sector, but over half of that derived from garment manufacture). Rs50,000 of clothing exports correlates in cif terms with roughly Rs75,000 (ie £5,000) of imports in Europe. From UK import statistics relating to the main clothing items which India exports—this represents approximately 0.4 ton of goods. The EEC has itself tried to produce employment equivalents of import tonnages, with the following results: every ton of clothing produced leads to the creation of 0.16 jobs in yarn spinning, 0.3 in fabrics, and 1.2 in clothing; 1.66 altogether.⁵ Thus 0.66 jobs would be displaced by 0.4 ton of Indian imports; one job in Europe

therefore is roughly equivalent, for the same product, to 20 to 24 in India. This is of course greatly over-simplified, and makes no attempt to separate margins from averages, or to disaggregate. In practice successful Indian exporters probably use rather more machinery to labour than the average, and unsuccessful European competitors rather less than average. But even if the ratio were 10 to 1, clothing manufacture would still have a much larger effect on employment in South Asia than in Europe, and there can be few other lines so labour intensive which are also internationally competitive.

(2) Foreign exchange earnings. Table 6.1 illustrates the earnings India and Pakistan derive from their positive trade balances in textiles and clothing and compares these with other major exporters' earnings. The trade balance needs, however, to be set against the need for imports of fibres, machinery and dyes; though India is generally self-sufficient and Pakistan is largely so for fabrics. Table 6.2 shows that textiles account for over three quarters of Pakistan's total manufactured exports and for half of India's.

Table 6.1 Net Trade in Textiles and Clothing (\$m)

	Textiles		Clothing		Total	
	1970	1975	1970	1975	1970	1975
EEC	+1445	+1658	+141	-2060	1586	-402
USA	-832	+391	-1042	-2130	-1874	-1739
Japan	+1521	+2150	+371	-208	+1892	+1942
Switzerland	+90	+247	-160	-431	-70	-184
India	+451	+610 ^a	+36	+163 ^a	+487	+773 ^a
Pakistan	+310	+330	+5	+31	+315	+361
Hong Kong	-222	-374	+653	+1929	+431	+1555
Singapore	-211	-244	+3	+56	-208	-188
Korea	-43	+395	+213	+1144	+170	+1539

Note: ^a 1974 figures.

Source: GATT, Com/Tex/W35, Add 1, 1976.

Table 6.2 Share of Textiles and Clothing in Exports of Manufactures

	1970	1974	1975
All dcs	7	6	5
Ldcs	28	27	26
of which:			
Pakistan	77	65	73
Egypt	70	71	na
Turkey	56	67	na
India	47	49	na
Hong Kong	47	52	56
Korea	46	38	44
Singapore	20	11	11
Yugoslavia	16	10	12

Note: Developing Countries include in addition to those mentioned Spain, Israel, Rumania, but exclude non-MFA members (eg Taiwan).

Source: GATT, Com Tex W/35, 1976.

(3) Capacity utilisation. This is a crucial problem for India which faces a widening gap between production and consumption, as indicated by the following projections recently made for woven cloth production.

Table 6.3 Availability of Indian Cotton Cloth (m metres)

	Home Consumption	Production	Surplus for Export	Actual exports
1970 (actual)	7300	7849	549	446
1974 (actual)	8555	8284	- 271	420
1976	8334	9443	1109	581
1977 (provisional)	na	9114	na	na
1978 (projected)	9660	10900	1240	na
1982-83 (plan projection)	12200	13500	1300	—

Source: compiled from a variety of sources.

But the problem is substantially more serious for Pakistan. Recent estimates indicate that domestic consumption of cloth in 1980 may be around 1120m yds as against 2450m yds projected capacity (of which 400m are currently being added in new investment by the more competitive mills). This implies exports of 1330m yds, to utilise capacity fully as against 545m actually exported in 1975/76. Similarly for yarn

Table 6.4 Imports of Textile Products into the EEC-9 (\$m)

Origin		Woven		Cotton		Clothing		Non-		Knitted	
		Textiles	Cotton	of	fabrics	of	which	knitted	outerwear	knitted	underwear
		which	which	which	which	which	which	which	which	which	which
All extra-EEC	1970	1152	106	260	742	302	88	162	79		
	1972	1809	189	386	1472	654	200	315	166		
	1973	2567	279	540	2212	1015	319	438	252		
	1974	3258	439	776	2866	1344	419	496	354		
	1975	3228	348	753	3518	1672	477	664	431		
Developing Countries ^a	1970	514	95	150	474	171	73	122	54		
	1972	895	171	192	1051	434	176	242	132		
	1973	1378	257	292	1643	713	280	348	206		
	1974	1707	400	394	2160	966	370	392	294		
	1975	1655	316	351	2708	1229	427	532	364		
India	1970	50	8	25	12	2	1	-	-		
	1972	64	6	27	17	11	3	-	-		
	1973	105	5	58	38	25	6	2	2		
	1974	128	12	64	70	39	17	3	5		
	1975	88	3	26	71	42	19	1	3		
Pakistan	1970	32	3	21	1	-	-	-	-		
	1972	48	9	21	2	1	-	-	1		
	1973	74	16	25	5	3	1	1	-		
	1974	119	28	42	11	5	1	1	1		
	1975	110	15	37	8	3	2	-	3		
Sri Lanka	1970	-	-	-	-	-	-	-	-		
	1972	-	-	-	0.1	-	-	-	-		
	1973	0.1	-	-	0.2	-	-	-	-		
	1974	0.2	-	0.1	0.6	0.3	0.3	-	-		
	1975	0.1	-	0.2	0.2	0.1	0.1	-	-		

Note: ^a Developing countries include Spain, Portugal, Greece, Turkey, Yugoslavia.

Source: OECD, Trade Statistics, Series C, 1970 to 1975.

production, capacity seems likely to rise in 1980 to 1200m lb as against home demand of 650m lb. The excess of 550m lb is over twice the level actually exported in 1976. In both cases, significant export increases are implied in present plans for expansion.

In addition to these benefits it must be remembered that exports have resource costs; notably that cotton production has an opportunity cost in terms of food foregone. Furthermore once the existing excess capacity is fully used, additional exports will have an opportunity cost in terms of domestic consumption foregone, while in order to achieve better export performance, investment to replace inefficient machinery will be needed.⁶ But exports would need to more than double, in India's case, before hitting a capacity problem.

EEC-South Asia Textile Trade

The broad outlines of trade in textiles and clothing can be gauged from Tables 6.5 and 6.6. *India* has been a consistent net exporter to the EEC-6 and Britain. Through the 1960s and early 1970s, despite import restrictions in these countries, the trade surplus grew dramatically as clothing exports began to make a major impact. The value of EEC exports to India was only 2% of its imports from India in the early 1970s. In terms of volumes the imbalance is even more marked as a result of the very low average unit value of Indian exports to the EEC (about half the average unit value of ldc exports to the EEC).

Of the individual EEC markets for Indian exports it can be seen from Table 6.6 that the UK predominates. More recently however there has been a rapid growth of exports to Germany, especially in 1976 and 1977.

The *Pakistani* trade balance with the Community is virtually identical to India's for textiles, rather smaller for clothing. This is remarkable: until the late 1960s Pakistan ran a trade deficit on textiles with the Community, while clothing trade was negligible. In the early 1960s Pakistan was struggling to establish a textile industry based on import substitution. Its excursion into net exporting is quite recent and growth has been rapid, both in textiles and, more recently, clothing. Pakistan's share of textile imports from all sources to the Community and the UK increased continuously until British entry, but stagnated thereafter, reflecting supply constraints. *Sri Lanka's* present trade balance in clothing items with the Community is impossible to assess; most of the growth of its exports occurred in late 1976 and 1977 for which data are not available. Its total clothing exports were worth around \$10m in 1976 and imports about half that.

It is possible to relate these trends in EEC-South Asian trade to the more general development of South Asian textile exports. Indian export performance until 1970 has been meticulously analysed elsewhere, notably by Deepak Nayyar, in attempts to explain why India, though the first major developing country textile exporter in the 1950s, persistently lagged behind other ldc's in the 1960s.⁷ The

Table 6.5 Balance of Trade in Textiles and Clothing (\$m)

	EEC-India				EEC-Pakistan				Total Balance						
	Textiles		Clothing		Textiles		Clothing								
	Exports to India	Imports from India	Exports to India	Imports from India	Exports to Pakistan	Imports from Pakistan	Exports to Pakistan	Imports from Pakistan							
EEC-6	1963	7.4	31.6	-24.2	0.1	0.3	-0.2	-24.4	3.4	2.7	+0.7	-	0.1	-0.1	+0.6
	1966	5.4	30.6	-25.2	0.1	0.3	-0.2	-25.4	8.3	4.6	+3.7	-	0.1	-0.1	+3.6
	1969	1.4	29.8	-28.4	-	6.1	-6.1	-34.5	3.0	19.2	-16.2	0.1	0.2	-0.1	-16.3
	1972	2.0	40.6	-38.6	0.1	9.3	-9.2	-47.8	3.9	31.1	-27.2	0.2	0.3	-0.1	-27.3
EEC-9	1973	3.8	131.6	-127.8	0.1	38.5	-38.4	-166.2	10.4	77.2	-66.8	0.2	10.5	-10.3	-77.1
	1974	3.0	127.2	-124.2	0.2	57.3	-57.1	-181.3	13.9	99.5	-85.6	0.3	14.4	-14.1	-99.7
	1975	4.0	93.1	-89.1	0.2	58.9	-58.7	-147.8	6.1	87.9	-81.8	0.4	9.5	-9.1	-90.9

Note: Pakistan includes Bangladesh before 1972.

Source: Comitextil.

Table 6.6 Markets for Indian Textile Exports in 1975 ('000\$)

SITC	Cotton yarn 651-3 and 4	Cotton cloth 652-2	Clothing 842 to 844	of which:								
				World	EEC-9	UK	Germany	Italy	France	Nether-lands	Belgium Luxembourg	Denmark
				11,015	2,152	1,474	210	-	-	-	388	-
				160,343	29,163	21,172	1,422	1,491	3,900	311	-	-
				146,616	45,576	15,973	11,022	5,720	6,739	4,440	627	1,209

Source: as per Table 6.5.

volume of its yarn and cloth exports increased by only 2% between 1960 and 1970 (89 to 91m kg) while Pakistan's almost tripled from 49.5 to 135.4m kg. The data available so far on the early 1970s, suggest that the growth of Indian exports continues to lag in value terms but more significantly, the growth of exports is slowing down at an even faster rate. However two supplementary points are worth noting. The first is improvement in India recently, culminating in a remarkable performance in 1976, when the value of textile and clothing exports doubled in one year from Rs2636m to Rs5130m. This was partly due to a boom in demand in Europe for cheesecloth and other 'ethnic' garments in the hot summer of 1976. Demand fell away in 1977 when there were also restrictions to contend with, but it was significant that India had the capacity to meet the demand for garments and at the same time to double its exports of piece goods. The fact that this growth was not a 'one-year wonder' can be explained by the consistent ability of the textiles and clothing industries to exceed targets since 1974, by 32% in 1974/5, by 26% in 1975/6 and 41% in 1976/7.

The second is that for both countries there has been a rapid and sustained growth in clothing exports, going back several years. These are however heavily concentrated in one or two items, mainly shirts and dresses using handloom fabric, and knitted shirts from Pakistan. Moreover, the growth of garments exports should not be interpreted as a straightforward move to higher value added textile products. Among fabric exports the movement is in the opposite direction. Grey cloth constituted 64% of 1976 exports, compared with 52% in 1975. The continuing inability of the mills to supply adequately designed high quality fabrics explains this deficiency. Pakistan has benefited like India from rapid export growth in garments, but this is still at a low level and fails to compensate for the performance of the mills, which has been poor, even by comparison with other ldc's like Egypt which are also primarily in the business of exporting cotton cloth rather than synthetics. This expansion of clothing exports should not be allowed to disguise the fact that both countries are relatively small scale exporters of this category by comparison with Hong Kong or South Korea. India for example has less than 1½% of the world garment export market and little more than 4% of ldc's exports to dcs.

The remainder of this chapter is primarily concerned with market access constraints on export growth which recent history suggests are a major problem.

The EEC's Textile and Clothing Restrictions

The renegotiated quotas for access to the EEC market agreed at the end of 1977 under the current MFA by the three South Asian exporters, ie excluding Bangladesh, and 18 other ldc's (including Yugoslavia) are perhaps the most comprehensively severe that they have ever faced in Europe. Since similar, if generally less restrictive, arrangements have been worked out for other OECD markets,

Table 6.7 Exports of Textile Products (\$m)

	Textiles		Clothing		Textiles and Clothing		Increase 1970/75 (%)
	1970	1975	1970	1975	1970	1975	
India	461	597	36	195	497	792	59.4
Pakistan	320	392	5	41	325	433	25.8
Hong Kong	275	594	699	2102	974	2696	176.8
Korea	85	649	214	1148	299	1797	501.0
Taiwan	184	649	199	890	383	1539	301.8
Brazil	32	271	3	102	35	373	965.7
Egypt	136	228	10	69	146	297	103.4
Mexico	27	200 ^a	9	42 ^a	36	242 ^a	572.2 ^b
Thailand	9	95 ^a	1	45 ^a	10	140 ^a	1300.0 ^b
EEC	2713	5063	947	1979	3660	7042	92.4
Japan	1745	2923	462	332	2207	3255	47.5
USA	603	1625	227	421	830	2046	146.5
Poland	91	253	130	448	221	701	217.2
Czechoslovakia	97	257	77	245	174	502	188.5
Portugal	161	312	80	219	241	531	120.3

Notes: ^a 1974 figures^b 1970/1974 increase.Source: Comitextil, *Bulletin*, various issues.

they effectively ensure that there will be very little growth in textile and clothing exports in the next five years for almost every item in which the three countries have developed a trading advantage. The EEC policy is the most crucial since it is, for historical reasons as well as market size, the largest market for South Asian exports.

The new arrangements represent a turning point in that there is no longer any attempt to pretend that the restraints are intended to aid restructuring in Europe or to make provision for a gradual regulated increase in the ldc market share. Rather the permitted growth rates, which are virtually zero for imports of 'sensitive items', are designed to prevent any further import of precisely those items in which the EEC has least comparative advantage.

The 1977 renegotiation can only be understood properly in its historical context, as the latest in a series of attempts to regulate the textile imports from ldc to rich country markets.

(1) The Pre-MFA Period

As can be seen from Table 6.8 the share of developing countries' imports in total imports and in total consumption is extremely variable between different dc markets and this reflects different historical experience in textile import policy. Most European countries have a long history of textile restrictions. Moreover European integration contributed to a rapidly growing intra-community trade in textiles. This differentiated the EEC in the 1950s from the more open economies, Britain, the USA, and Scandinavia, which accepted largely unrestricted imports. The share of domestic consumption met by ldc imports of cotton textiles was around 5% in the EEC (9% for the highest, Germany, and 1% for France) against 36% for Britain and 23% for Sweden. Since then, first the United States, and more recently Britain, have sought to limit ldc access to their markets, while there has been limited liberalisation by the EEC. Following restrictions imposed by the USA and, in 1959, the 'voluntary' restrictions on Commonwealth Asian cotton textile exports to UK, an international agreement—the Long Term Agreement (LTA)—was evolved under GATT for cotton products which, with extensions, lasted from 1962 to 1973. It tried to reconcile two objectives: in the words of the Agreement to 'secure (for developing countries) a substantial increase in their export earnings from textile products and to provide scope for a greater share for them in world trade' ... and 'avoidance of disruptive effects in individual markets and on individual lines of production'. Subject to a minimum annual growth rate for imports of 5%, import controls could be imposed or export restrictions agreed, for particular products from particular sources under bilateral agreements.

The main effects of the 1962-73 period for ldc, and especially South Asia were, first, somewhat better access to the EEC-6. However both Germany and Italy resorted to additional controls, under 'safeguard' clauses. Further, Indian and

Table 6.8 Comparative Import Performance: Textiles and Clothing of Cotton and Manmade Fibre (\$m)

	1970			1975		
	Total	ldcs	per capita share of ldc imports in total imports (\$)	Total	ldcs	per capita share of ldc imports in total imports (\$)
EEC	495.0	10.5	1.05	1161.0	129.2	12.70
France	561.0	32.2	0.64	1717.0	287.1	5.42
Germany	1590.0	238.7	4.02	4770.0	1267.2	20.40
Italy	343.6	59.5	1.11	615.3	151.0	2.70
Netherlands	772.5	47.8	3.67	1596.0	380.9	27.90
Denmark	235.2	21.5	4.30	345.0	98.4	19.40
UK	719.0	233.1	4.18	1887.3	757.0	13.40
Sweden	446.0	65.0	8.08	776.0	228.0	27.80
Japan	159.4	83.0	0.80	793.0	410.1	3.72
USA	1763.1	762.9	3.73	2831.0	2092.0	9.80

Source: Estimated from OECD trade statistics.

Pakistani exports suffered from an EEC agreement under which grey cloth imported from the EEC could not be processed and re-exported to the EEC. The second trend was growing protection of the UK market with a global quota permitting 1% pa textile import growth (after 1966) as well as specific Indian and Hong Kong 'voluntary' quotas. After 1969 an even more severe system of import restrictions came into effect. However Pakistan managed to increase its share of the global quota and for India the UK quota did 'not appear to have been the operative constraint towards the end of the decade'.⁸ Indeed there seems to be plenty of evidence that India's main concern was to preserve its quota as a protection against more competitive developing countries and from synthetics.⁹ Pakistan on the other hand regarded any impediment as having a harmful effect. Despite complaints, however, the exporters almost certainly regarded the situation as more acceptable than the most likely alternative of anarchic bilateral controls.

(2) The 1974 MFA

The first Multi-Fibre Agreement was negotiated multilaterally in 1974 under GATT auspices (though it went against the general principles of GATT). It tried, like the LTA, to reconcile the interests of dc domestic producers with the gradual expansion by ldc of their share in dc markets. Liberalisation was stated to be the basic principle of the MFA but essentially it was a bargain struck over restricted but guaranteed access. In general the new Agreement had several features more attractive to India and Pakistan¹⁰ than the old. The multi-fibre character of the agreement meant that cotton product exporters would no longer be competing with uncontrolled synthetic product suppliers. The 6% pa permitted growth in the volume of ldc imports under each of the bilateral agreements represented an improvement in some markets, and was considered too high by European producers. Finally, a Textile Surveillance Board (TSB) was set up, to oversee the implementation of the MFA and to review the new restraints multilaterally. Its findings however were not to be legally binding.

Within the general framework of the MFA, bilateral agreements were negotiated between individual suppliers and importers, the latter being represented in the case of the nine member states by the EEC. India and Pakistan were in 1975 the first ldc's to reach such agreements. In addition to the positive features mentioned above there were certain drawbacks to the agreements, some of which only became apparent later.

First, there was a higher degree of specification of product restraint than under the LTA. Initially for Pakistan three and for India four categories were singled out for restraint (though these lists were later extended), whereas before they had been given the freedom to diversify within a global 'cotton textile' ceiling. While this had the effect of limiting diversification it was justified, particularly by the Germans, on the grounds that it cut the protective element in the MFA: protection would be confined precisely to those products where disturbance was concentrated and not aggregated into bigger global categories.¹¹

Second, built into the EEC bilateral agreements were 'burden-sharing' arrangements designed to ensure that each importing country took a fairer share and so a fairer 'burden' of imports of each product. Shares were allocated on the basis of GNP and this had the effect of redistributing a greater share of EEC textile imports away from Britain. This was essentially an internal EEC matter, but the effect of national as well as Community quotas was to restrict the possible effective utilisation of the Community quota.

The safeguard procedures presented the most serious problem. Under Article 3 of the MFA when an importing country suffered 'disruption' it could ask for consultations with the exporter and, if agreement was not reached within 60 days, it could impose restrictions for twelve months—in the EEC, these could be either at national or Community level. Market 'disruption', as in many trade safeguard clauses, was vaguely defined and based upon the existence or the threat 'of serious damage' measured by 'a sharp and substantial or imminent (measurable) increase' in imports or prices 'substantially below' those of goods of comparable quality marketed in the importing country. In the case of the EEC-India agreement, the EEC undertook not to use Article 3, but to 'consult' on matters of friction. Within several months of the bilateral agreement being signed these 'consultations' led to self-limiting agreements ('voluntary export restraints') for four more products: T-shirts (to the UK), terry towelling (France), men's cotton shirts (UK), and cotton handkerchiefs (UK).

However the real difficulties arose in 1977. Under the bilateral agreements handloom cloth products had been exempted from controls altogether provided they were certificated as such by the Indian authorities. In 1976/77 large numbers of men's shirts, blouses and skirts arrived in Europe as 'handloom' products, some of whose cloth had clearly been produced on power looms and whose designation was aimed at bypassing the EEC import restrictions on mill-made items. As Indian sources acknowledged ... 'dishonest fair weather exporters palmed off powerloom garments as handlooms'.¹² The Community sought in discussions to have this abuse stopped, but it became clear that there were differences with the Indian government over what actually constituted handlooms.¹³ Apart from abuse, and negligent licensing procedures, there were genuine difficulties in identification. Within the 'cottage industry' sector there is inevitably some use of power driven equipment, though most cases involve limited amounts of machinery in primitive, non-factory, work-shops not easily distinguished from pure rural industries. A mission of Community experts led by Commissioner Haverkamp declared itself unable to accept that there could be a fool-proof system of checking at source or even at the point of disembarkation, reflecting both genuine bafflement on technical grounds and cynicism about Indian commitment to surveillance.

In April 1977 the EEC imposed quotas on Indian and Pakistani handloom garments as well as mill-made items (by incorporating both under the same quota). This move was made partly to preempt unilateral action by the UK government.

The dispute centred on shirts, skirts and blouses, and ended with the Indian government taking the EEC to the TSB arguing that:

- (a) handloom products were exempted from access restrictions under the bilateral agreement, and so the EEC was in breach of this agreement.
- (b) the overall quota for blouses and skirts was too low given its great importance for employment in the Indian cottage and small-scale sectors. Given that the quota had already been exceeded by April the potential level of Indian exports to the EEC for the year was far greater than that represented by the quota. Indeed capacity had already been installed and cloth bought for larger exports.
- (c) quota management should be left to India. Import quota management in Britain and France had led to serious disruption and delay, possibly deliberate.

The TSB upheld the complaint stating that the EEC's policy was 'illogical and illegal' but the Community ignored the recommendation. Its official spokesman (Mr. Tran van Thinh) commented:

'no doubt India has a very strong legal position. But for the Community it is not a legal situation. It is an unusual and non-rational situation arising out of the unemployment situation currently prevailing in the member countries of the EEC. The situation is likely to continue for another four to five years'.

The restrictions remained in force and were subsequently renewed in the re-negotiated MFA. In addition, similar action was taken against imports of dresses and some categories of shirts not hitherto restricted from the mill sector, as Indian dress exports to the EEC had risen from 1m in 1975 to 6.7m in the first nine months of 1976.

In general, implementation of the MFA left a lot to be desired from the viewpoint of ldc's; dc's had taken unilateral action to restrict imports from ldc's, without consultation or compensation, and there had been little effective multi-lateral surveillance.

(3) The 1978 MFA

It was clear in the early part of 1977 that the EEC, notably the French and British, was heading for renegotiation of the MFA, due to expire on 31 December, and was firmly committed to more restrictive conditions. The use of safeguard restrictions, on shirts for example, illustrated both the drift of EEC opinion in a period of recession and the weak bargaining position of the ldc's. Voting in the Council of Ministers on precautionary restrictive measures in August 1977 showed only Germany and Denmark opposed to this trend. The renegotiation was to take place at two levels: one in Geneva on the basic agreement with all parties to the MFA; and the other in Brussels, in the case of

the EEC, on the parameters for the bilateral agreements which would be operated under a new MFA. The latter was to prove the decisive forum; indeed the EEC made it clear that if it could not get prior agreement on detailed ceilings there it would not renew the MFA but resort to bilateral quotas alone. Of the Community's conditions for MFA renewal, the most central was the stabilisation of all imports, with a reduction in the rate of growth of imports for sensitive products. Special provision would be made for the 'poorest' developing countries. Initially Hong Kong, Singapore, South Korea, and Macao were identified as dominant suppliers whose exports would therefore be most severely restricted. But in the negotiations which followed India was also defined as a dominant supplier despite its being one of the poorest ldc's while Pakistan and Sri Lanka were treated very firmly.

In September the guidelines were fleshed out to a precise negotiating mandate for the bilateral agreements, including minimal 'rates of penetration' (defined as the share of imports in EEC consumption) for eight sensitive products at between 1 and 2%, 6% for non-sensitive items and 4% for an intermediate group. Once imports reached these rates their growth would be severely limited. Since the base for calculating 1978 growth was to be 1976 import figures a further element of restriction would be built in. The other major objective apart from a reduction in import growth was to be the introduction of global quotas to deal with 'cumulative disruption' resulting from the influence of numerous small, rapidly growing suppliers, including those from Lomé countries. However the EEC's concept of 'global' was somewhat restricted—it excluded the United States and other dc's such as Japan.

The central issue for the Community negotiators was the alleged role played by ldc imports in aggravating the effects of recession in an already declining industry. At one extreme, textile lobbyists claimed that the 400,000 jobs lost in the European textile and clothing industry between 1973 and 1976 was overwhelmingly the fault of 'low cost' imports. But as the Commission pointed out in its submission to the Council of Ministers it would be wrong to attribute the loss of employment entirely to increased imports. Substantial improvements in productivity have also contributed. Between 1972 and 1974, 130,000 jobs were lost in textiles, despite the fact that yarn and cloth output both remained at substantially the same level. Furthermore, 1975 was a recession year and some jobs would certainly have been lost without any increase in imports.¹⁴ An attempt to separate these relative effects for the UK suggests that between 1970 and 1975 jobs displaced by ldc textile imports (not for this purpose including EEC candidate members or Comecon) accounted for between 20% and 40%, depending on the statistical source used, of jobs displaced by productivity improvements.¹⁵ The proportion was much less for yarns and fabrics. Three other points should be noted. First, the main pressure for tougher restrictions came from France and Britain, not from Germany, although in absolute and relative terms it suffered by far the most serious decline in textile employment

in the 1973-76 period. Second, the nadir of the trade cycle had passed in 1975. Indices of textile and clothing production, especially in France and Italy, were moving upward in late 1976 and 1977, sometimes sharply, despite competition from imports. Third, the UK balance of trade in textiles improved sharply in 1977 under the ceilings of the former MFA falling to -£6m (clothing -£168m) from -£136m (clothing -£271m) in 1976. It was the alarming 1976 figure which helped convert doubters (the UK Treasury for example) to the tough approach. Unfortunately the 1977 figures were published too late to affect the negotiating positions.

Apart from arguments based on temporary difficulties in Europe, others were used by the Commission which in effect repudiated the concept of comparative advantage in trade. Mr. Jenkins, in his presentation of the Commission's view on April 26 1977, suggested that the Community should try to evolve a long term policy 'to make it possible to take investment decisions without the fear of continual modifications in conditions of competition', and to resist the 'natural advantage' of certain countries notably in the clothing sector characterised by 'extreme labour intensity, little rationalisation and low technology'. Moreover the textile industry could not 'be cut down below a minimum level of production'. The rationale for this view of the world was never elaborated, nor what this 'minimum' level should be in particular sub-sectors of the industry. Nor were the employment implications of trying to counter 'natural advantage' by 'an important effort on the technological level' ever spelt out.

In this argument the crucial role was undoubtedly played by the British, both because Britain had effectively changed sides since joining the EEC in 1973, and because, in employment terms, it had the largest industry in Europe. It acted together with France, to fight off more liberal arguments—to the effect that the MFA be preserved in its existing form—from Germany and the smaller countries and, outside the EEC, from the USA. The reasons for the British shift are many and no doubt have a good deal to do with personalities at an official industry and political level but two factors stand out: first, a loss of confidence in the British economy's ability to adjust its industrial structure and the consequent emergence of a conservative industrial policy; second, the effective lobbying of the manmade fibre multinationals, ICI and Courtaulds, who were in deep trouble on the fibres front and anxious to secure their downstream, clothing, outlets. They appeared to succeed in welding the very disparate clothing industry together and in presenting a joint case with the unions.

At the end of 1977, and after a fierce struggle for more liberal terms, India and Pakistan followed Sri Lanka in signing a bilateral agreement with the EEC, which incorporated specific quantitative limits. They implicitly accepted the situation recognising the dangers should the textile trade degenerate to unregulated warfare. In their final form the revised agreements have several features all of which add to their restrictiveness: as the British minister chiefly responsible

was frank enough to admit 'the new MFA is an historic turning point in the fortunes of the British textile industry'¹⁶ and the Community negotiator observed, 'all this amounts to a degree of protection going far beyond anything the clothing and textile industries have enjoyed in the past. For almost all our negotiating objectives were achieved'.¹⁷ The most significant of these features are:

(a) The overall rate of import growth has been reduced by fixing negligible growth levels—between as little as 0.5% and 4% pa—for the eight super-sensitive or Group I items: cotton yarn (0.5%), woven cotton fabrics (0.5%); woven synthetic fabrics (2.5%); knitted underwear (shirts and T-shirts) (4%); knitted outerwear (jerseys and pullovers) (3%); trousers (3.5%); ladies' knitted or woven shirts and blouses (1.5%); men's knitted or woven shirts (1%). These account for 70%, by volume, of UK 'low cost' imports (50% for the EEC) and a significantly higher percentage of UK imports (and EEC imports) from the subcontinent. For Group II, another significant lot of 23 items, accounting for 18% of UK imports, growth is held at 4% on average. From the subcontinent the items involved are dresses, coats, knitted pyjamas, woven women's underwear, bedlinen, and cotton towelling. For the four other Groups there are no predetermined limits but a mechanism has been set up which if 'triggered' ensures the introduction of controls and the overall average annual growth of imports in these Groups may not exceed 6%. In the meantime items in these categories will require export certification only.

(b) The scope for exporters to diversify into unrestricted categories is greatly reduced by the proliferation of restrained items from the previous 60 to 127 (and a similar near-doubling of the number of South Asian items affected, of which some are still quite trivial, such as manmade fabrics). The mechanism adopted is a 'trigger clause' system. It will be two or three years before the effectiveness of this system is quite clear. But on paper it means the following. For Group I products restraint is automatically imposed on existing suppliers once they supply more than 0.5% of EEC imports and for new suppliers, more than 0.2%. For Group II products, the limit is 1 to 1.5% of imports, and for the other Groups, 3 to 5%. The true purpose of these trigger clauses is revealed by the fact that the UK government has asked a leading textile company, Courtaulds, to carry out the monitoring on its behalf, using its greater expertise, its computer facilities, and, doubtless, its stronger self-interest. Further, the mechanism for introducing controls under the trigger clauses is to be tightened. If the exporter does not co-operate 'voluntarily', prompt action can be taken unilaterally with effect retrospectively from the date of complaint. The trigger mechanism is regarded with particular resentment by the exporters. It represents a new departure from the earlier MFA in that no evidence of market disruption or damage need be offered. What the EEC refused to accept was the heavy cost which this system would

impose on small suppliers, like Sri Lanka, whose interests had been specifically recognised under the 1974 MFA and who need high export growth rates in order to develop viable scale economies; some 50-100% pa in the case of Sri Lanka.¹⁸

(c) Base levels for 1978 quotas have been fixed at 1976 trade levels for the most sensitive items from Hong Kong, South Korea, and Taiwan. India and Pakistan seem not to have been too seriously damaged by this manipulation of base levels—it is the only real concession they have obtained—but other suppliers have. Table 6.9 demonstrates the relationship between 1977 and 1978 quota levels on textile imports from South Asia and the major ldc suppliers. It shows there have been significant cuts for Hong Kong and South Korea on important clothing items.

Table 6.9 EEC Quotas on Textile Imports of Interest to South Asia

No.	Item	Major Exporting Countries and South Asia	Permitted Annual Growth (to 1982)	1978 quota (under new MFA)	1977 quota (under old MFA)
GROUP I					
1.	Cotton Yarn	India		9,000 tons	limit in UK and Ireland only
		Pakistan		7,000	no limit
		Brazil	0.5%	26,900	28,100 tons
2.	Woven Fabrics of Cotton	India		40,000 tons	40,000 tons
		Pakistan	0.5%	20,000	20,500
		Brazil		16,500	18,450
		Hong Kong (plus manmade fabrics)		23,000	17,850
4.	Knitted Shirts and T-shirts	India		6.72m units	limit in UK and France only
		Pakistan		6.32m	UK limit only
		Sri Lanka	4.0%	1m	no limit
		Hong Kong		23m	24.5m units
		South Korea		10m	10m
5.	Knitted Jerseys and Outer Garments	Pakistan		6.3m units	no limit
		Sri Lanka	3.0%	0.7m	no limit
		Hong Kong		25.3m	32.3m units
		South Korea		24.7m	27.1m
6.	Men's and Women's Trousers	Sri Lanka	3.5%	1.6m units	no limit
		Hong Kong		50.4m	54.9m units
7.	Women's and Girls' Blouses and Shirts (not knitted)	India		28m units	24.5m units
		Pakistan		2.67m	no limit
		Sri Lanka	1.5%	2.75m	no limit
		Hong Kong		30m	25m
		South Korea		8.3m	7.4m

No.	Item	Major Exporting Countries and South Asia	Permitted Annual Growth (to 1982)	1978 quota (under new MFA)	1977 quota (under old MFA)
8.	Men's and Boys' Shirts	India Pakistan Sri Lanka Hong Kong South Korea	1.0%	24.5m units 2.4m 3.1m 48.1m 28.0m	19.4m units no limit no limit 65.1m 31.8m
GROUP II					
9.	Cotton Towelling	India Pakistan Brazil	5.0%	3,600 tons 870 3,400 (plus 2,100 for No. 20)	UK limit only no limit 6,400 tons
15b	Women's Raincoats	India Hong Kong South Korea	4.0%	0.67m units 6.0m 4.0m	no limit 2.7m units 4.3m (including boys')
19.	Handkerchiefs and Woven Fabrics	India Hong Kong South Korea	4.0%	64.0m units 68.9m 18.0m	52.1m units na na
20.	Household Linens	India Pakistan	4.0%	10,505 tons 870	8,540 tons 2,000
24.	Men's Pyjamas and Nightwear	Pakistan	5.0%	0.133m units	no limit
26.	Women's and Girls' Dresses	India Hong Kong	2.5%	6.5m units 7.9m	) India 13.2m units) (including shirts)) Hong Kong 13.2m
27.	Skirts	India Hong Kong	2.5%	4.3m units 7.0m units	
29.	Women's Suits	India Hong Kong	5.0%	0.39m units 2.0m	no limit no limit
30b	Women's Under Garments (excluding Nightwear)	India Hong Kong	5.0%	1.6m units 7.8m (plus 5.6m for men)	no limit 13.5m units

Source: EEC Commission documents.

(d) There has been a considerable reduction in flexibility. For example, underused 1977 quotas cannot be carried over into 1978, nor can exporters transfer unused quotas from one product category to another. Under Article 7 of the original India-EEC Agreement a complex set of flexibility provisions permitted transfers of quotas between categories, carryovers, borrowing from a subsequent year, and adding up to 20% of ceilings (15% for women's shirts and blouses). These have been tightened up for the 1977-1982 period. In addition the burden sharing formula, which divides

quotas between EEC members, operates as before but more restrictively, so that when an importing country share has been exceeded it can introduce import controls unilaterally even when the Community has not fixed an overall quota ceiling for that item.

(e) Countries not subject to bilateral agreements are still counted within global quotas and are subject to the trigger clause. This would affect Bangladesh if it ever develops an export capability. (It also affects potential supplier countries associated to the EEC under the Lomé Convention if these are used for transshipment or become suppliers in their own right.)

(f) The main guarantee of the effectiveness of the new controls will be a more elaborate system of surveillance. This will be reinforced by a system of double-checking. Exporters will have to obtain (from their governments) an export licence and certificate of origin for products subject to specific quotas. These documents will then be used by importers to obtain import licences. The earlier agreements also had a double-checking procedure but for a much smaller number of items.

(g) Handloom shirts, skirts, blouses, and dresses continue to face quotas in the absence of any means of distinction from mill-made items (though other items will be exempted if properly certified, presumably as long as import growth remains slow). The Indian government may well try to use the composite quotas to increase exports of mill-made, higher cost items, reserving a greater share of handloom products for the home market.

The effects of the renegotiated agreements on the subcontinent depend in part on the degree of flexibility of the exporters in boosting supplies of less sensitive items. We suspect that this is low and if it were higher, the EEC would move quickly to cut out the 'threat', using its trigger mechanism. The outcome will also depend on the prospects for economic growth generally in the EEC, since more dynamic growth might well lead to less rigid enforcement of the trigger clause. As it stands at present, however, the renegotiated MFA must be counted as one of the most successful actions ever carried out by the protectionist lobby, and by the textile industry in particular. Not only have exporters lost a lot of ground on textiles and clothing, but they have accepted a substantial *de facto* revision of the whole concept of protection by safeguards, with the introduction of the notion that high 'import penetration' rather than 'injury' is a justifiable basis for differential rates of permitted access. 'Import penetration' is a highly dubious concept. It depends on an arbitrary level of product subdivision, and in this case on an arbitrary choice of countries to which the measure should be applied. Its most obvious flaw, however, is that it takes no account of exports from the importing country.

The formula used to incorporate this and other innovations was expressed in a form of words agreed between the main exporter and importer countries at the GATT Textile Committee in July 1977 which provides for 'jointly agreed

reasonable departures' from the MFA. The Community agreed that these 'reasonable departures' 'would be temporary and the EEC shall return in the shortest possible time to the framework of the MFA'. The exporters clearly fear that now that the precedent has been created it will be used by others, such as the USA and Scandinavia, and in future MFA negotiations in 1981 and after. Moreover, the Community has made it clear that the TSB is 'an organ of conciliation' and 'to be distinguished from arbitral or judicial bodies'.¹⁹ Further it has said that it will not accept any action by the TSB which calls into question the bilateral agreements. On the other hand the EEC has undertaken not to use Article 19 of GATT again, as it did in 1977, breaking the terms of the MFA.

Are there any redeeming features? Some South Asian officials have been remarkably optimistic, for example: 'as a result of the efforts of the Minister, Sri Lanka was able to conclude an Agreement ... very satisfactory for the Island's textile industry ... The quotas have greatly fortified its future'!!²⁰ How the Sri Lankan government can reconcile this observation with restrictions to under 5m items for the main market of an export industry with capacity closer to 20m units is impossible to comprehend. India has been appeased by fixing quotas to make it the biggest textile (not clothing) supplier to the EEC, supplanting Hong Kong. The relatively high base levels for quotas (for India, and to a lesser extent Pakistan) at least mean that for sensitive items there is no actual cut in import levels and, after the rapid growth of 1976, this could be regarded as a consolation. There now seems little hope, however, of India reaching its export target of Rs7.5bn (circa \$1bn) for garments in 1983. But there is scope for increasing the unit value of exports within the quotas, since these now effectively guarantee a market share, as well as prevent expansion of it. This could be done by improving quality or even by exporters using their control over quotas to obtain better prices from importers. What happened in 1976 was a hectic expansion based on cut-throat competition amongst Indian exporters, resulting in very narrow profit margins and lower quality. With restraint, Indian government regulation, and some cartelisation amongst the exporters, prices could be raised substantially to be passed back in higher wages, profits and prices for handloom cloth. Early efforts in 1978 to operate an export licensing system to this end were, however, proving difficult to implement, resulting in a pile up of stocks and the danger of non-utilisation of EEC quotas.

There is a recognition also that the export structure achieved under the limited restraints of the earlier LTA and MFA is lopsided, with far too much reliance on a handful of products (shirts, blouses, skirts) and a narrow fabric base, heavily dependent on current fashion. The most severe restraints now are on cloth and yarn, low unit value products which India and Pakistan will ultimately want to remove from their export structure, though both countries suffer excess capacity now and need export outlets. Within the inevitable restrictions of trigger mechanisms, both countries are eager to expand their exports to the

EEC of synthetic and blended fabrics, workmen's and defence clothing. In addition it is worth remembering that the concept of guaranteed growth, however low, insulates exporters from the highly cyclical character of the textile market. But this is to search for a silver lining in the cloud. There is no evidence so far that exporters have the bargaining power or organisation to turn the terms of trade in this way. The benefits described above are conjectural and have to be set beside the definite elimination of substantial real growth in a crucial market.

The Administration of VERs and QRs

The mechanism for textile trade regulation is currently a hybrid combination of 'voluntary' export restrictions (VERs) and import quotas. Under this system the exporter country organises the market by issuing export licences according to its own criteria but up to ceilings agreed with, usually imposed by, the importing country. Export licences are then used by the importer for obtaining an import licence. Over the last twenty years the EEC textile trade has had various administrative régimes, depending on the product and situation, between total reliance on unilateral import controls (eg France in 1977) and completely voluntary restraints. The hybrid, or double-check, arrangement now seems firmly established. But the experience of various types will now be analysed.

The major difference between QRs and VERs lies in their relative effectiveness, the latter being less draconian. VERs depend on a system of export licensing generally less strictly enforced, less comprehensive, more easily evaded (by transshipment for example) and more flexible than import controls (QRs). In the case of textiles, part of the aim behind the tough negotiating position of the EEC has been to remove this asymmetry. The other major difference is in terms of distributional effects. Under QRs importers should be able to capture the scarcity premium. 'On the other hand, under quotas allocated to exporting countries or under VERs, even when the VERs are reinforced by QRs in the importing country, the exporting country organises the market and should be able to gain a predominant share of (the surplus)'.²¹ Exporting firms, which lose a volume of trade from restraint, can compensate themselves by being able to charge higher prices. An example of a deliberate attempt to use VERs to the advantage of the exporter country is a system of minimum prices supported by an export licensing system which involves giving licences to applicants with the highest sale price. The favourable manipulation of the terms of trade may also take the form of collusion between exporter and importer, collaborating on the invoicing of import/export prices to avoid taxation and exchange regulations.

Apart from the general issues of principle there are a good many practical problems in quota administration. The first relates to ensuring full quota utilisation. Import restricting governments have no incentive to do this. Under a full QR system, as operated in France in 1977, import licences may even be issued

to manufacturers competing with imports whose only interest is to destroy them. Under a mixed QR/VER system, however, a precondition for obtaining an import licence is an export licence which leaves some discretion with the exporting government. At the export end there is no problem of motivation, rather one of efficiency. The system used in India in 1978 of allocating licences to exporters with the highest prices was extremely disorderly: buying procedures were disrupted as importers did not know at what price to bid in order to secure contracts. A further problem was that Indian exports of cloth in particular became more expensive (some 5 to 7%) than those from Pakistan, which did not allocate export licences in the same way, and so many Indian exporters had to wait until Pakistan had used up its EEC quota to receive orders from EEC importers. Finally, speculators used fake contracts showing artificially high prices to corner the supply of licences and by the end of the year a number remained unused though there were still bona fide exporters seeking permission to export. In recognition of these problems the Indian government introduced in 1979 a new system: some licences will be allocated on the basis of ready goods, some on the basis of firm contracts, and the remainder on the basis of highest price. Furthermore exporters will face penalties if they fail to use their licences within a certain period. A second set of practical problems is the time period between request for an import licence and its issue. Importing governments wishing to be difficult can prolong this procedure at the end of the year to ensure non-fulfilment of quotas. Our contacts in Germany and France said that they frequently experienced three-month delays. One minor advance under the revised MFA is that importers have been set a time limit of six weeks to utilise quotas. If not used by the end of this period the licences are allocated to other importers.

A third set of difficulties arises when there is a substantial discrepancy between the volumes licensed to exporters and to importers, for example by the exporter government trying to exceed its quota. In practice this problem has occurred more frequently when, due to emergency action in mid year, as may increasingly happen under the trigger clause, export goods are licensed, paid for and despatched but unable to obtain import licences as the quota has expired. This occurred in 1977 when shirts and T-shirts were subject to emergency action. The British and Germans took a liberal view in cases where letters of credit had been entered into, but the French required the goods to be held in bond until the next year, when fashion had changed, and importers lost heavily.

Fourth, where quantity import controls are imposed without voluntary restraints (as can happen under the MFA when export licensing has been disorganised—as with Pakistan in 1978) then the importing country government has to devise a system of allocating licences amongst importers to replace the system under VERs where the importers are selected by the exporters. Essentially, there are two methods. One is the first come—first served principle. The second is based on historic market shares, as happened recently with shirts in the UK. This has

the advantages over the first of predictability, of permitting greater planning, of fairness, and of avoiding the costs of queueing. Disadvantages are the administrative effort, therefore delays, required to compute shares, the tendency to contribute to trade in licences (which is not always stabilising) when some importers have no need for them and others are short, and finally the exclusion of new importers.

Fifth, there is abundant scope for varying interpretation of different product categories, which will be compounded now that 127 categories are involved. West German customs are regarded as particularly liberal in accepting the exporters' own classification. The French by contrast are reported to use a good deal of discretion to reclassify in a restrictive sense. This kind of issue presents itself when for example the quota for ladies' shirts is exhausted and exporters sew buttons on the 'wrong' side to get them under the men's category, though clearly they are designed for female body sizes. Similarly the quota on skirts has been circumvented by adding a simple waistcoat and calling the outfit a 'suit'. The major problem has arisen over handlooms as already described. Various customs authorities differed in their interpretation, before a blanket quota was imposed; the UK for example accepted machine sewn buttons or embroidery but not France or Italy. Customs authorities have also varied in their enthusiasm for enforcing the Community requirement for handloom/handicraft certificates, in five languages (presumably eight after enlargement)! Documentation, generally, is a prolific source of misunderstanding and delay (since rejected applications have to go through the procedure again).

In almost every respect the new MFA will make administrative difficulties worse, because of the proliferation of restrained categories, because of uncertainties inherent in the trigger mechanism and also because, in addition to other requirements, exporters are now required to produce a certificate of origin to prevent trans-shipment.

Finally there is the connection, or lack of it, between VER/QR policy and the GSP, which results in a parallel and duplicate system of certificates and approvals. As we explained in Chapter 3 the GSP on textiles is for most items of no benefit since, if a product is under QRs, tariff reductions cannot be used for expanding export volume, though the possibility of windfall gains and occasionally cheaper prices might attract importers to buy from Idcs in the few cases when QRs or VERs are underused. Also the tariff quotas for many items are so trivially small that they are often exhausted within a few hours of the new year, which is a possible small bonus for importers but of no real significance for exporters since the importer has, in a climate of uncertainty, to fix his contracts to include duty. In general, tariff quotas for products under restraint are a totally unnecessary bureaucratic obstruction which contradict the basic understanding behind VERs that the exporters, however restrained, should at least be able to obtain maximum unit value. The sole reason for

retaining tariffs for such products is psychological; producers fear that tariff removal will open the door to liberalisation and stimulate consumer awareness of the existence of 'cheap' imports.

A Way Forward?

The prospects for an improvement in the access of South Asian textile products to the EEC market are dim, at least in the short-term. Over the next few years South Asian and other producers are likely to be fighting a rearguard action to protect their already diminished access against promiscuous and restrictive use of the trigger clause on currently less sensitive items, and to utilise their quotas in the face of newly imposed bureaucratic impediments at both ends. Even the next renegotiation of the MFA seems a depressing prospect, since the European industry now has the trade tied up, and there are few if any precedents for spontaneous unilateral liberalisation. Moreover, the whole thrust of the 1977 renegotiation was to create a framework of long-term security for the European industry, to facilitate new investment, not painless euthanasia. This was underlined by the exceptionally severe restraints placed on items such as mass produced men's shirts for which under no foreseeable circumstances will the European industry be able to develop technologies to compete with Idcs. In these circumstances it is easy, but facile, to counsel despair and suggest that little or nothing can be done. After all, for Pakistan and India, clothing and textiles still account for over half of manufactured exports, and clothing exports represent one of the few areas where manufacturing exports promise really major employment gains. Moreover, unlike Korea, Singapore and Hong Kong, South Asian wages and factor endowments indicate that clothing is one area where comparative advantage is not changing to the subcontinent's disadvantage.

The first, rather obvious tactic is to seek to work within the MFA to exploit quotas to the full, to maximise unit value within them through quality improvement and discipline amongst producers, and to develop whatever unrestrained lines of production offer possibilities. Further, the countries should keep textiles and clothing firmly at the top of the agenda in all talks with the Community members on economic co-operation or other matters. This might not always be immediately productive, but might ultimately produce some raising of quotas, if pushed hard enough.

The second approach is much bolder: in effect to offer the Community a reciprocal deal on textiles. At present India and Pakistan maintain rigid protection of both their cotton and synthetic fibre, yarn, fabric, and textile machinery sectors, in none of which they have an obvious comparative advantage. It is at least possible that they could offer better access for European exporters in these areas in return for better access for Indian/Pakistani clothing exporters in the EEC. India is in a particularly good position to try this. It is attempting to liberalise imports generally, but has so far not dared to risk the wrath of its own

competing producers in sensitive areas like textile machinery. Its adjustment problems in these areas could be presented as comparable to those of European producers facing Indian competition. At present, liberalisation proceeds by putting products on Open General Licence and there is no reason why procurements of imports should be made in Europe. But the licensing system is such that European suppliers could be favoured if it were in India's or Pakistan's interest. Such a bilateral deal would normally go against the 'non-discrimination' rules of GATT and would therefore risk the retaliation of those trading partners who found themselves excluded from it. In the case of textiles, however, where international trade has degenerated, even if formally remaining under GATT rules, into a series of bilateral agreements dictated mainly by political interest, this type of arrangement may be one way for Pakistan and India to maximise their export earnings from textiles. It could not be narrowly reciprocal since the scope for Indian, let alone Pakistani, textile imports is not great, and much of its imports are in any event aid financed. But it would be a significant gesture which would go some way to meet the interests of the European producers, especially the man-made fibre producers who, despite their multinational character, see little self-interest at present in accommodating trade with third world producers.

Third, there should perhaps be some consideration of relating textiles to wider issues of North-South bargaining. There is a striking contrast between the LDC Group of 77's energetic attempts to launch commodity agreements, from which Pakistan and India as net raw material importers have little to gain (and possibly something to lose, if the agreements are more successfully price raising for their raw material imports than exports), and an apparent lack of interest in issues of market access for products such as textiles. The particular interests of these two countries (and even Sri Lanka if its exports continue to diversify) might lie in concerted action with countries like Germany which appear to share their priorities. It is not clear that North-South bargaining will produce much, if anything, but the textile exporters and consumers sensitive to consumer interests need at least to ensure that their current 'losses' in this field are not forgotten in any 'trade off' that does materialise.

Fourth, there may be scope for concerted action with other textile exporters to try to turn the terms of trade and co-ordinate tactics. Hitherto the South Asians have tried to distance themselves from the Far Eastern producers, feeling that the sympathy which they earn as 'the poorest', in the OECD world, is of some tangible advantage; in the 1977 renegotiations, India in particular was able to obtain slightly better terms. This may however be an illusory gain, and the treatment of Sri Lanka suggests that sentiment plays small part in EEC thinking. In these circumstances, and faced with the effective elimination of much of the potential for price competition under a régime of fixed quotas, there may be scope for a concerted effort to raise prices of restrained categories in parallel through an association of textile exporters. More ambitiously, the countries

concerned, the South Asian, ASEAN and Far Eastern groupings, plus Brazil and Egypt, could consider exploiting jointly their one major bargaining counter which is (collectively) an extremely large market for Western goods. For example they could use big public sector contracts to discriminate in favour of EEC countries, or others, pursuing a helpful line on textile access, and working together to back up individual members which find themselves as a result in conflict. This may seem at present somewhat unreal, but even the fact of contingency planning being made would give pause for thought in Europe. More modestly, there is a great deal of scope for such an association working on concerted lobbying and publicity in the EEC, in preparation for what will almost certainly be a succession of difficult negotiations in the 1980s. In the last rounds the exporters' case and, indeed, the European consumers' case, went largely by default, except as special pleading by individual Idcs. There is need now to prepare the political ground for a campaign to make protection limited in time, and to phase out restrictions gradually. The main thrust of this campaign would be to establish a coalition with consumer interests. As Table 6.10 shows the inflation in costs in Europe as a result of protection is prodigious (though price disparities may well disguise quality differences).

Finally there may be scope for Idcs, including the South Asians, to consolidate their position in European markets by having nationals or government organisations acquiring a part—or whole—ownership share in the clothing importing and retail business in Europe. It is likely that the value added here is greater than in the production process itself. Although India is beginning to consider small foreign investments, this is a more productive approach for countries like Singapore, or possible Singapore and the South Asians working together. Having an interest in distribution would also help in lobbying where exporters, having to act at arm's length and representing no local interest, are at a disadvantage.

On the EEC side it is important not to lose sight of the possible role of the Community in restructuring as well as protecting a problem industry—in the manner of steel or shipbuilding. The original Commission submission to the Council stressed the need for the Community to make use of the social fund for retraining and the Community Research Programme for developing new technologies and new products.

Although it is necessary to refer to the total magnitude of the EEC 'adjustment problem', for textiles, the kind of changes which the four South Asian countries might reasonably expect to obtain would have a very small effect on EEC employment. Suppose, for example, that the EEC could be persuaded to allow special dispensation for the msas (the four South Asians plus Egypt are the only ones concerned in current textile arrangements) to the effect that they were to be allowed to retain 6% annual permitted growth in the seven highly sensitive categories. This is still not particularly generous to the small suppliers, notably Sri Lanka, and it also fails to tackle the issues of restrictive definition of skirts

Table 6.10 Implicit Protection

SITC		A. Excess of EEC price over Indian cif(%)	B. ditto over Pakistan	C. ditto over lowest cost ldc supplier	D. ditto over lowest EEC price
651.3	Unbleached yarn — per kg	49	58	78 (Spain)	24
652.13	Bleached Cotton Fabric — per kg	97	133	(Pakistan)	40
659.90	Linen — per kg	142	105	(India)	117
842.11	Men's outerwear — per kg	170	—	(India)	82
	— per piece	388	—	—	172
841.12	Women's outerwear (dress/skirts) — per kg	88	—	120 (Hong Kong)	19
841.13	Men's under garments — per kg	124	156	(Pakistan)	92
	— per piece	208	217	(Pakistan)	200
841.14	Women's under garments — per kg	418	—	(India)	412
	— per piece	422	—	(India)	418
841.21	Handkerchiefs — per kg	171	—	(India)	na
841.43	Knitted under garments — per kg	19	55	(Pakistan)	5
841.44	Knitted outerwear — per kg	49	162	(Pakistan)	18

Note: The 'EEC price' was obtained from five digit SITC categories as being the average price of EEC products traded within the EEC (column A). The 'lowest EEC price' was obtained from the average price of the lowest cost EEC supplier (column D).

Source: OECD, Trade Statistics, series C, 1975.

and dresses made largely if not exclusively of handloom fabric and by handicraft methods. But it is a minimal gesture which the Community could make to the msas in recognition of the fact that their relatively unsophisticated, non-factory, clothing producers are likely to be unable to diversify from 'sensitive' items. Acceptance of a 6% growth rate for categories 3-8 under the Community agreement would mean (by 1982) an additional import from South Asia of 1.7m T-shirts, 135,000 knitted jerseys (from Pakistan alone), 160,000 women's trousers (Sri Lanka), 4m women's skirts and 3.6m men's shirts. Converting to tonnages at the agreed rate, this is an extra annual 1,800 tonnes of clothes by 1982 (India 1,380, Pakistan 240, Sri Lanka 180). Using the Community's own estimates of current job equivalents,²² this is roughly equal to (directly and indirectly) a loss of 3,000 jobs spread through the Community.

The position for textile fabrics is a little more serious. A 6% growth rate would entail approximately 10,000 tons more from India by 1982, and 5,000 tons from Pakistan. Using the Community's own estimate of 1,000 tons of fabric requiring the employment of on average 460 persons, the static (current) job equivalent of the additional imports from South Asia is 7,000. 10,000 jobs lost suddenly in a concentrated locality could represent a human tragedy. But spread over five years and through the whole EEC, the figure pales to total insignificance by comparison with the likely turnover of labour, or those likely to be displaced by technical innovation. There would, of course, be gains, which are not calculated, in terms of additional European export orders from the subcontinent. The other side of the coin is the likely gain in employment in the subcontinent, remembering that with the current rural and small scale technologies labour productivity in clothing is inferior to average European levels by 20 or 25 to 1, perhaps 5 or 6 to 1 in the mills. Thus a very modest package of adjustments to the growth levels under the MFA still leaving comprehensive and, by comparison with other product areas, severe controls, could be worth 100,000 jobs to the subcontinent while causing little by way of an adjustment problem in Europe.

References

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3. In 1964 per capita consumption was 16.85m metres of which 15.22m was of cotton and in 1976 this had fallen to 13.73m (11.36m cotton).
4. 'Continuing Crisis in Textiles', *Commerce*, Bombay, 24 December 1977.
5. European Commission working paper, *Une Presentation Simplifiée du Problème de Textiles*, Annex II.

6. An Indian Institute of Foreign Trade Study has stated that the garments industry had (in 1977) a capacity of Rs7.4bn production, output of Rs4.4bn, and exports of Rs2.4bn. There is of course a requirement for capital investment even in such a labour intensive industry (currently installed investment being estimated at Rs570m).
7. Deepak Nayyar, *India's Exports and Export Policies in the 1960s*, op cit.
8. Ibid, p81.
9. M. Lipton and J. Firn, *The Erosion of a Relationship*, op cit, p58.
10. For a good summary see C. Wadhwa and V. Mote, *International Trade in Textiles, with Special Reference to South Asia*, Trade Policy Research Centre (mimeo), 1977.
11. See H.H. Taake and D. Weiss, *The World Textile Arrangement*, (GDI) Berlin, 1974.
12. Letter to *Economic Times*, Bombay, August 14 1977, p4.
13. Under Article 4 of the EEC-India bilateral agreement handloom products were defined as '1. Cotton handloom fabrics actually woven on a loom for which the motive power is provided entirely by the operator. 2. Goods made up by the cottage industry from such cotton handloom fabrics. 3. Traditional handicraft textile products, cut, sewn, or otherwise fabricated by hand in cottages which are units of the cottage industry'.
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21. 'On the Non-Equivalence of Import Quotas and "Voluntary" Export Restraints' in C. Fred Bergsten (ed), *Towards a New World Trade Policy: the Maidenhead Papers*, Lexington Books, 1975, p165.
22. COMITEXTIL, Bulletin 78/2, p12.

7 Conclusions and Future Prospects

The authors have become increasingly conscious, working through the subject, of the dangers of an over simple approach to commercial policy issues between the EEC and South Asia. South Asian exports are often subject to a double or triple 'bind'. Tariff liberalisation may simply lead to the substitution of non-tariff barriers whose ad valorem tariff equivalent is greater than the original tariff. But then the elimination of the non-tariff access barriers could reveal fundamental inadequacies in supply or marketing. To attack the problem on one level only is likely to be unproductive. In terms of relative priority, tariffs were shown to be of modest importance overall and significant only for a small number of items. We estimated that complete tariff elimination in all dutiable items except textiles could raise South Asian annual earnings of exports to the EEC by approximately 3.5% over a period of several years with very little of this accruing to Bangladesh and Sri Lanka. But like all studies based on static analysis our findings may be too conservative. There is, in any case, no doubt that tariffs are potentially a significant barrier to the export of important products such as shoes, carpets, and tobacco, all of which are 'sensitive' in the GSP scheme. NTBs are, almost certainly, much more important as a deterrent to trade. This is mainly because of the effect of quantity restraints on the export of cotton textiles, garments, and jute. These are not only important exports to South Asia, and India and Pakistan in particular, but the tariff equivalent of the restraints is exceptionally high. It is however extremely difficult to put a figure on the magnitude of NTB restrictions. Some of these barriers are not intentionally trade restricting and probably justified (eg health checks); others are non-discriminatory (eg government procurement preference for home industries, excise duties on tea and tobacco); some imagined NTBs are the product of simple inexperience or carelessness on the part of exporters. It is difficult to enumerate NTBs let alone to quantify their effect on trade.

Even if tariff barriers and NTBs could be stripped away, supply problems remain. Our study has been demand based but we are well aware of the magnitude of the difficulties involved in these countries taking advantage of market opportunities. One estimate, by the World Bank, is that South Asia would double its manufactured exports, currently about a quarter of all exports from the region, by 1985, if it adopted a package of improved export policies.

But this is not an argument for playing down the access issue. Access and supply are closely related. The four South Asian countries are currently moving towards policies which favour greater export growth, especially Bangladesh and Sri Lanka, while India's export policies and performance have already been transformed since the 1960s. But the effectiveness of these policies depends heavily on confidence, notably on the willingness of domestic and foreign entrepreneurs to

commit themselves to investment in export capacity, and on the ability of the South Asian governments to sustain a consensus amongst their own decision makers. An outburst of EEC protectionism along MFA lines, or conversely a firm move to liberalisation, could have a decisive effect on confidence at the present stage. It may be that because of this confidence factor we have ourselves underestimated the value of qualified advances already made on access, notably under the GSP, even though these are not binding. In addition, access barriers and their liberalisation tend to be subject to a 'domino effect' in the main OECD markets. For obvious reasons, importing countries do not like to give trade concessions to third countries which are not matched by those of trade rivals. Conversely protectionist measures are quickly emulated. For example, following the recent EEC textile renegotiations the hitherto liberal Scandinavians demanded terms comparable to the EEC. As the world's main trading bloc, the EEC sets the tone not only for the rest of Europe but in part for the USA, Australasia and Japan. Finally, our general observations obscure the importance of access barriers for particular products of great importance to the economies covered. In the case of clothing, jute products, processed leather and tobacco, South Asian exports face significant barriers. All of these provide opportunities for labour intensive techniques of production, generating employment far in excess of comparable industries in Europe. In extreme cases, such as garments, perhaps twenty or more workers are employed in South Asia to produce the same tonnage as one worker in Europe.

South Asian National and Regional Interests

We have hitherto treated the South Asian countries as a group. It is easy to visualise the benefits which could flow from a better understanding in the sub-continent over trade policy: a less fragmented and more coherent approach to jute marketing by India and Bangladesh, and to tea by India and Sri Lanka, greater intra-regional trade flows, as well as the effect of all this on reducing dangerous and costly political divisions. The collaboration of South Asian diplomats and politicians in Brussels notably over GSP is a small but very useful step in that direction. It also has specific tactical advantages in dealing with the EEC. A smaller country such as Sri Lanka might otherwise have attracted little attention. For India (like Nigeria in the ACP group) there is political kudos to be derived from using its influence on behalf of smaller neighbours, and the practical advantage that for almost every product in which it has an interest one or other of the remaining three countries can give support. For Pakistan, whose access problems are most intractable (textiles and CAP products dominating), and which would achieve little or nothing in isolation, there may also be advantages in solidarity. Collaboration could be taken much further: by working together in the promotion of trade with the EEC; common use of warehousing and importing facilities to take advantage of the GSP; producing goods together which they could ask the EEC to treat as having common 'origin' under the GSP rules of origin; closer co-ordination of the work of the

Joint Commissions (eg, dealing with jute, leather, and marine products sub-regionally rather than nationally).¹ Nor is there any reason why co-operation should stop at these four countries. Smaller Asian countries, Afghanistan and Burma, for example, have negligible status, dealing in isolation with the EEC. The efforts of the South Asian and ASEAN countries could also be co-ordinated more closely.

There are of course political constraints, possibly overriding, which will cut across these efforts. And there are specific national interests which need to be spelt out.

Bangladesh has one major access problem and dispute with the EEC concerning *jute*. We believe that research has now removed any serious credibility in the case for continued protection of the European jute industry. The European jute industry no longer exists as such having adjusted, almost completely, to the production of polypropylene substitutes, where this is economic. Although this substitution has not helped the European jute work-force it has provided an alternative future for the firms which employed them. To remove all remaining access barriers would—at worse—displace half of the remaining EEC jute processing production, which is expected on present trends to provide jobs for no more than 3,000 to 4,000 in the whole of the EEC in 1980. For Bangladesh which exports raw jute as well as products, the issue of EEC protection of processing is less clear than for India, though differences could be exaggerated since protection of jute processing in Europe has hastened substitution by synthetics, diminishing the market for raw jute also. Amongst other products which still face tariff barriers, Bangladesh is interested in expanding existing exports of tanned goat and bovine *leather* (not in the GSP), and *fish and shrimps* (tariff reduced under the GSP). Potential exports include *paper*, some *fruit* and *vegetables*, *woollen carpets* and *cotton textiles* all of which are dutiable or face NTBs. But, for Bangladesh, supply problems are very severe for all of these actual or potential exports most of which require new investment, technical advice, assistance with management, and more regular raw material supplies. In terms of bargaining with the EEC for better access, aid, or technical help, Bangladesh has two advantages over the other South Asians. First, it is the only one classified as 'least developed'. Second, it has already given the Community what the latter wants by way of reciprocal concessions—generous treatment of foreign investment and written agreement on certain forms of 'raw material access'.

Sri Lanka has ambitious plans to diversify its exports, but most actual or potential exports are non-dutiable and not affected by NTBs. Exceptions are *coconut oil* for which, despite GSP tariff cuts, effective protection of European refining has remained unchanged, *tobacco* (a sensitive GSP product), *marine products* (tariffs cut under the GSP) and several items which have benefited from tariff cuts under the GSP or MTN, but still face a preferential tariff handicap against Lomé suppliers, notably *cocoa beans* and *cinnamon*. Tariffs exist on potential

exports also, notably *spices*—nutmeg and pepper (both reduced under the GSP), *fruit juice*, *tinned fruit* and *footwear*. But the real problem is *garments* where, as a small but rapidly expanding supplier, it was dealt with harshly under the 1977 MFA renegotiations. A priority is to get its 'sensitive' quotas raised to something corresponding more closely to its existing capacity. Like Bangladesh it needs capital and technical help to set up new export capacity, and has already taken significant steps to reform its own trade and foreign investment policies.

Pakistan is seriously affected by EEC access barriers, notably on *textiles* and *clothing* but especially millmade *cotton fabrics*. Since this is perhaps the most sensitive of a highly sensitive category of imports few concessions can be expected, and Pakistan might do better to concentrate on asking the EEC to liberalise its imports of *garments* which, as in India, are a major source of rural employment. Nor are there good prospects for removing tariff and levy barriers on *molasses*, *basmati rice* and *rice extracts*, though there is still a strong case for tariff liberalisation especially of the massive molasses tariff (65%) and of the tariff on basmati rice, which has a specialised demand. Other priorities for Pakistan are zero tariffs on *fish products* and *leather*, increasing the tariff quota on *tobacco*, and more generous treatment under the GSP of its exports of sensitive items, such as *sports goods* and non-leather *footwear*. Finally, there is now a threat of high tariffs on its hand-made *carpets*, where the issue is more one of unfortunate classification of its specialities than the general principle of carpet tariffs. Pakistan has perhaps the most difficult problem in negotiating better access. Its main arguments in seeking special consideration are the serious balance of payments position which it shares with other msas, and its large trade deficit with the EEC.

India has a somewhat longer shopping list, but somewhat larger bargaining resources to secure it. In terms of priorities the major barriers are QRs on *clothing* and *textiles*, notably on the former. This is partly a question of ceilings and permitted growth rates, partly a question of the classification of handloom products. Next in importance is the need for increasing the tariff quota and reducing the GSP tariff on tobacco and increasing the tariff quota or reducing the high CET on knotted hand-made *carpets* which are probably wrongly classified. Other important and hitherto unresolved access issues for India are QRs on *jute products*, duties on tanned *leather*, duties on various vegetable oils notably *castor oil*, health regulations on *oilcake*, GSP duties on *fish products* and *crustaceans*, the same problems as Pakistan with CAP products, notably *maize* and *rice extracts*, duties on various *spices*, *fruits* and *vegetables* (eg *pepper*, *mangoes*, *walnuts*) and more generous treatment under GSP of various manufactured items such as *sports goods* and some *electrical items* and *cutlery*. India's claim for generous treatment stems primarily from its status, like the others, as a msa. The benefits which would accrue to large numbers of unskilled workers, many rural, from liberalisation of access for garments, carpets, tobacco, and leather is fully consistent with the type of development strategy western

countries are encouraging ldc's to adopt. It also commands attention for political reasons. India's geopolitical importance and its attraction to western democracies are compelling but it has been unable (at least in the last two years and perhaps for no fault of its own) to translate expressions of goodwill into specific and hard concessions in key issues. This is despite a large order for Harrier jets and other indications that India has a great deal to offer Western businessmen and governments. Apart from the general reluctance of the EEC countries to concede anything in trade terms in the present economic climate, specific reasons include India's satisfactory trade position (now deteriorating), its substantial trade surplus with Britain, and its uncompromising stand in areas where the Community is looking for signs of reciprocity (raw material supplies or access for foreign investment).

Future Relationships

One general consideration facing all four countries is the extent to which they can secure advantages beyond those obtaining from general goodwill, by seeking to bargain away what they themselves have to offer by way of their own market access. As mentioned in Chapter 6 in the case of textiles this could be on a bilateral basis, but the argument applies more generally. For example India could improve access to its market for dc leather tanning and shoemaking machinery in return for concessions on Indian tanned leather and shoes. Regular supplies of raw materials and access to foreign investment could also be guaranteed. We have also heard, but this has yet to be confirmed, that India and Pakistan have secured concessions in principle at the MTN on one or two items (eg sports goods) in return for modest reciprocal offers. An increasing number of writers have sought to present North-South relations as a bargain or 'game' in which the South can strengthen its hand by acknowledging the merit of 'reciprocity'.² This would also correspond to present EEC official thinking. However South Asians might still be sceptical; there is no evidence so far that Bangladesh has benefited much from concessions already made in the terms of its formal co-operation agreement, or Hong Kong and Singapore from the unrestricted access which they offer (though admittedly these concessions were not made as part of any bargain). Another illuminating experience was the recent set of EEC negotiations with Australia, a country which can offer the Community rather more (and hurt it more) than the South Asian countries by the restriction of raw material supplies, notably of uranium, reciprocal trade measures and investment opportunities. Attempts by Australia to link these issues with its demands for better access for its agricultural exports to the EEC seem to have failed. Two lessons might be learned from that experience. One was the excessive dependence of Commonwealth countries on British patronage in the EEC. Britain's influence in the EEC on most matters which do not currently affect the interests of its own producers seems weak, and moreover it is going through a highly protectionist phase. The Indians have begun to acquire German allies but unless the South Asian countries acquire powerful friends in France, Italy,

and Belgium, they will continue to be frustrated. A second lesson is that the Community is probably incapable, for institutional reasons, of making the pragmatic trade-offs required (eg uranium guarantees against access for mutton, access for capital goods against access for shirts, flexible treatment of German investors under Indian foreign exchange rules against access for tobacco). Such understandings are perhaps only possible if they are consistent with a written set of rules and obligations such as those of a structured and formal arrangement such as the Lomé Convention. This raises the issue of what kind of institutional arrangement the South Asians can reasonably expect in future.

Lomé Extension?

Most of South Asia's access difficulties would be simply resolved if the trade provisions of Lomé were to be extended to them. The disabilities flowing from its exclusion are now becoming more obvious: the GSP has lost its dynamism and the CCAs are proving devoid of real content. Is there a case for accommodating the South Asians in a renegotiated Convention?

In the first place, it is extremely unlikely that India would wish to be part of a Lomé type of arrangement, and none of the four countries have in fact applied to join. Even if they did, strong objections would be raised to all except possibly Sri Lanka. The first objection from Lomé members would be that the populous Asian countries would swallow up large chunks of the modest Lomé aid budget (3.5bn ua over four years including Stabex contributions (350 mua) and aid to overseas territories (160 mua)). If existing levels of aid per capita were to be maintained another 9.5bn ua p.a. would have to be found. The second would be to question the logic of admitting four poor South Asian countries while excluding others in Asia (eg Burma), in Latin America (eg Honduras, Haiti) and elsewhere (North Yemen). The fact that Lomé's present membership has little logic is now obscured by force of precedent. Finally, there is the fear that the Indians in particular, with an economy so much larger and more sophisticated than those of existing members, would simply monopolise the trade advantages of the group.

But the problem remains. If the Lomé Convention is to perform the function originally intended, of a laboratory within which the Community can test its third world policies before implementing them globally, it will have to show signs of passing beyond the experimental phase, if not at this renegotiation then at the next. Some kind of bridging arrangement is required.

Special EEC Package for Low Income msas

The Community should, we believe, offer a special package of trade and aid measures to span the period of Lomé II, covering those of the poorer ldc's, not only in South Asia, currently excluded from it. We have deliberately suggested

that the emphasis of the package should be on access rather than aid provisions. We have done so because in the long run a deeper economic relationship between the two groups of countries is only likely to emerge from an awareness of mutual self-interest. This is more likely to be generated through two-way trade than from an aid relationship. Also the governments of the four countries concerned naturally prefer to earn their way in the world without strings when the capacity exists for them to do so. This is most evident in the case of India, which has difficulty at present in absorbing the aid which it is offered and which has an explicit target of independence from aid. It is, perhaps, least true for Bangladesh.

(1) The centre piece of the policy—which we might call the Colombo Convention—would be parity in terms of access with Lomé countries for manufactures and processed foodstuffs. In tariff terms this would mean lifting ceilings and tariff quota limitations under the GSP from Colombo products and reducing duties on currently dutiable items: tobacco, fish products etc. The Community might feel that this grossly compromised their 'sensitive' industries. If so, tariff ceilings and quotas on middle income suppliers might be adjusted accordingly. But the limited volume of competitive trade which would be generated scarcely seems to justify this. For QR items, notably textiles and clothing, we expect that the Community would insist on retaining ceilings (as with Lomé sugar and rum). But in principle Colombo countries would be treated more generously in terms of quota levels and growth rates even within existing global quotas for super-sensitive items.

(2) On aid, the Community has now conceded the principle of aid to non-associates going beyond food aid. The sums are still of miserly proportions (20 mua in 1976, 45 mua in 1977, 70 mua in 1978). But it would be reasonable to expect that Lomé countries would look askance at a substantial increase of this aid, if the South Asian countries were also to share their trade preferences. A formula which might get over this would be to allocate an overwhelming proportion of non-associate aid to 'least developed' Idcs within the Colombo group, ie, Bangladesh in South Asia. India and Pakistan should be sophisticated enough to realise that they would not lose much, since EDF aid is transferred in large part from national aid budgets, and that trade concessions are more important, even if of modest value, since they would be permanent and represent free foreign exchange.

(3) It is unlikely that Stabex would be extended to South Asia. It is an idea which the Community is trying to propagate in the belief that compensatory finance is a superior device for dealing with commodity market instability than buffer stocks. But so far the Community is not willing to back its ideas with more money.

(4) The industrial co-operation provisions of Lomé, which amount to a combination of technical assistance and 'broking' for foreign investment

could easily be generalised to a larger group. The objective is, primarily, to facilitate foreign investment by European companies. The Community might, therefore, wish to tie eligibility for use of the Centre for Industrial Development to Lomé, and other, countries which give investment guarantees. Sri Lanka and Bangladesh would probably wish to take advantage of such terms. Of more value to those countries, however, would be the long promised trade centre to help them pick their way through the various rules, regulations, and NTBs in the field of standards, certification, and customs valuation, and to help them with information to maximise gains from the GSP and other access provisions. Eligibility for this special package of measures could be drawn from (1) countries satisfying a low income criterion (taking the current World Bank level of less than \$265 annual per capita income in 1975) and/or (2) msas. As Table 7.1 shows the groupings substantially overlap except that the former includes Indonesia but not the latter, while the latter includes Egypt but not the former. Political considerations would dictate a wide or narrow definition of eligibility and also the position of the five (more or less) Communist states. There would be pressure from the more conservative Community members and interest groups to restrict such an offer to the 'least developed' non-associates, a definition so limited as to be of negligible value.

Table 7.1 Non-Lomé Idcs—Classification of the Poorest Countries

(1) Poorest (under \$265 annual per capita income)		(2) Msas as under (1) less	Indonesia (and Timor)
Afghanistan*	Laos		Bhutan
Bangladesh*	Maldives*		Maldives
Bhutan*	Nepal*		Vietnam
Burma	Pakistan		
Cambodia	Sri Lanka	plus	Egypt
Haiti*	Vietnam		El Salvador
India	N. Yemen*		Guatemala
Indonesia (and Timor)	S. Yemen*		Honduras

Note: Asterisk indicates 'least developed' status.

The most serious criticism of such a package approach is that it further fragments the international trading system, moving away from general rules applicable to all countries, or at least all Idcs. That would be a valid criticism but one which ignores the present reality of Lomé, Mediterranean arrangements, and the labyrinthine complexity of the EEC's GSP. If the Community is to cling to these discriminatory arrangements, as it seems, wrong-headedly in our view, determined to do, there is a strong case for getting it to establish clear, equitable and developmentally sound criteria

of eligibility. Nor is there much prospect that the MTNs are likely to produce much of value to the poorest developing countries. They will benefit indirectly from tariff cuts, but the tropical products' offer has so far been derisory and they, like other ldc's, are threatened by the new, more selective, safeguard clause likely to emerge. This increases the attraction of trying to make progress with the EEC bilaterally.

Ad hoc Adaptation

If inertia or opposition rule out a bold approach to the problems of the low income non-associates they will have to make do with minor adaptations of existing arrangements. The two most important are the GSP and the MFA. We have already explained in Chapter 3 and Chapter 6 how we would like to see these improved. The most immediate priority however relates to the CCAs which are to be renegotiated soon, beginning in 1979 with the EEC-India CCA, followed in 1980 by the EEC-Sri Lanka CCA, and in 1981 the EEC-Pakistan and EEC-Bangladesh CCAs. It is worth recalling the kind of objectives which were envisaged, when the CCAs were being drafted, by two writers committed to a meaningful Indo-EEC agreement:³

- (1) Initially, targets for total levels of India-EEC trade should be set, aiming at a balanced expansion with eased access to markets on both sides. A suitable target, given the low initial levels of trade and the size and prospects of the Indian and EEC economies, would be a tripling of the real 1973 value of trade in both directions by 1980.
- (2) Within these overall targets, the products in which Indian exports to the Community and EEC exports to India should grow most rapidly should be identified as closely as possible on the basis of market demand and economic complementarity.
- (3) Firms and workers which "lose" as a result of the creation of new trade should receive grants to adapt to new lines of production, along with other measures of "adjustment assistance" undertaken in both India and the EEC; this might be partly financed by domestic taxes on goods falling into the liberalised categories.
- (4) Some aid funds should be devoted to helping India to set up the new capacity required to meet the expected EEC requirements under (2) above and, where necessary, to assisting Indian firms (public and private) and Industrial research and marketing organisations with the problems of marketing, delivery, and other aspects of expanding sales to the EEC market.'

Of these various tasks the Indian agreement has tackled (2), through a report by a team of consultants (A.S. Consultants Multinational Inc.), although Community commitment to its defined areas of 'economic complementarity' is not yet clear.

The other three points have as yet been scarcely considered. Nor have any of the four been seriously tackled under the other South Asian CCAs. Let us consider these various possible roles:

(1) *Trade targets*: the initial reaction of most businessmen to such an approach would probably be negative. They would argue that planning of trade within specified ceilings smacks of bureaucratic control, could be restrictive rather than expansionary, and generally suggests a form of East European barter alien to EEC practice and current intellectual fashion in South Asia. However purely indicative targets for the nine EEC states both as a whole and individually could be useful as a benchmark of performance. They would also oblige Community members to make clear in what areas trade expansion would be welcomed rather than restricted. And they would force the South Asians, especially India, to think in terms of 'reciprocity' in market access, both in aggregate flows and specific sectors such as textiles. Such an approach could, in sensible hands, be practically useful rather than dogmatically *dirigiste*.

(2) *'Complementarity'*: the problem here is threefold. First the Community has to be persuaded to accept a concept of complementarity which is somewhat more sophisticated than the raw materials versus manufactures form of 'complementarity' which it finds most appealing. Second, it needs to recognise the dynamic nature of comparative advantage. South Asians would not wish and would not be welcome to concentrate exclusively on exporting products in competition with dying traditional industries. Third, the Community has to develop a common line on exports. European governments have been assiduous in defining 'sensitive' import competing sectors to be protected; less positive in defining export promotion areas in trade with ldc's.

(3) *Adjustment assistance*: few current books on trade are complete without reference to the need for adjustment assistance as an alternative to protection.⁴ Yet with the possible exception of Holland, inactivity by EEC governments on trade adjustment has been almost total. One reason for this is, no doubt, confusion over what government intervention should be trying to accomplish; to slow down or speed up industrial change; to restructure existing industrial activities to make them more competitive, or to run them down; to tackle adjustment in all its aspects through, for example, general policies designed to raise labour mobility or to concentrate specifically on trade policies. There is certainly no argument for making the subject a matter for bilateral discussion. There might have been in the case of jute ten years ago but that adjustment is now virtually complete (without benefitting South Asia). Even so, some form of alternative or parallel measures to tariffs and import controls are needed to cater for producers whose interests are affected by trade-induced changes.

In order to spell out the maximum possible damage to the EEC which might result from extending to South Asia the trade provisions of the package described above, we can put together various estimates made in earlier chapters of jobs threatened over a four to five year period both directly and in supplier industries.

Table 7.2 Effect of Changes in EEC Trade Policy towards South Asia on EEC Employment

Policy Change	Jobs Displaced
Complete tariff elimination (excluding textiles)	2,000 to 6,000
Jute quota elimination	2,000 to 3,000
Restoration of growth of sensitive textile ceilings	
to 6%: a) fabrics	10,000
b) garments	3,000
	<hr/> 17,000 to 22,000 <hr/>

These figures represent maximum rather than minimum figures though they exclude the effects of tariff liberalisation on tobacco and rice. Positive 'feedback' from South Asian spending on EEC is also ignored. Taken in aggregate the jobs likely to be lost are negligible in relation to other factors affecting EEC employment over this period. But for policy makers whose business it is to rearrange, delicately, the separate straws on the EEC camel's back, this may be less important than the fact that no adjustment problem at all would result from a minor manipulation of quotas or tariff ceilings facing other middle income or more developed suppliers.

(4) *Funding*: at present the work of the CCAs is frustrated by negligible funding. Use of non-associate aid for technological research on problems of quality and supply and for trade promotion would give them rather more substance. The mooted trade promotion centre for India and, if it ever materialises, the GSP information centre would help to overcome many marketing difficulties, to the extent that public policy can help at all. When Prime Minister Desai visited Brussels one matter discussed was the extension of the EEC-India CCA to cover 'industrial co-operation', presumably a reference to co-operation over industrial matters not relating to trade. But the crux of that issue is India's policy towards private foreign investment.

Conclusion

Arising from discussion on the CCAs, we have tried to resist the temptation to make elaborate and costly recommendations. The CCAs are moderately useful and could be more so. However they have so far done little to expedite improved access and the Community at least would not view them as having that function. There is a danger that the South Asian countries could be side-tracked into devoting too much time and effort to 'negotiating' the workings of formal agreements which have little substance. There are on the other hand many in Europe who could easily be persuaded that it is not only right, but in the Community's economic and political interests, that a generous across-the-board arrangement should be made on trade and related issues for four of the world's poorest countries, which are, as it happens, generally well disposed to Europe and, relative to most others, well run. The possible negative effects on industrial adjustment are very small. If the Community cannot appease the lobbies concerned, it is probably better that this should be widely proclaimed rather than obscured in well meaning, but vacuous, chatter by ministers, officials, and academics about the need for more 'co-operation' and 'complementarity'.

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