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The Future of Trade Preferences for Sugar*

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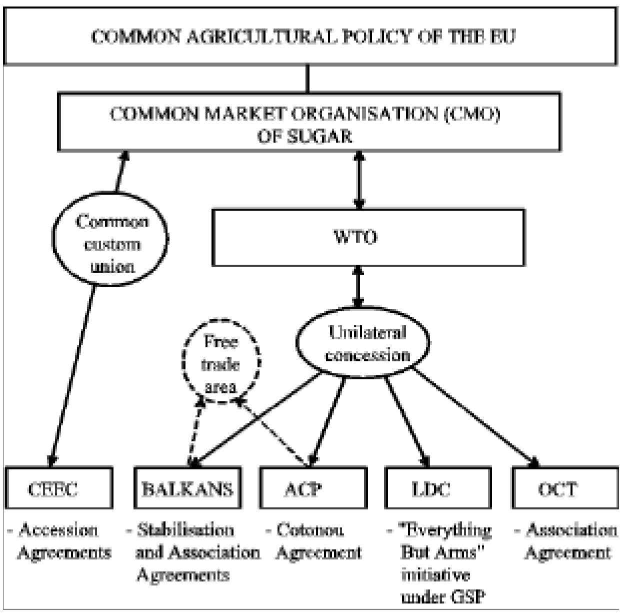
The EU is presently engaged in enlarging and negotiating or implementing a variety of trade agreements, which may be unilateral, bilateral, regional or multilateral in nature. The common market organisation (CMO) of sugar is a good example of the interactions between the different trade agreements.

The EU sugar regime and trade agreements



The reform of the EU sugar regime will affect not only the EU member states and candidates for accession, but also countries that are associated with the EU through preferential, regional and multilateral trade agreements. For several decades, the EU has supported and protected the EU sugar sector. Sugar from developing countries will not be able to enter the EU sugar market without preferential trade agreements. There are two unique features of the trade concessions in the EU sugar regime: sugar under preferential import quotas can enter the EU market duty free and the price paid for sugar equals the high EU price for sugar.

One crucial issue for the African, Caribbean and Pacific (ACP) countries is whether the EU will continue the ACP/EU Sugar Protocol after the end of the Cotonou Agreement in 2008. The Sugar Protocol explicitly states that the EU undertakes for an "indefinite period" to purchase and import, at guaranteed prices, specific quantities of cane sugar originating from the ACP countries. But the European Commission is currently examining options for reforming the sugar regime, most of which involve substantial cuts in the EU's guaranteed price. For instance, the ACP countries' income from sugar exports will be reduced by more than €200 million per year with a 25% cut in the EU sugar intervention price. The worst scenario for the ACP countries would be the abolishment of the Sugar Protocol. Those ACP countries that are dependent on this trade preference will be gravely affected. According to the Australian Bureau of Agricultural and Resource Economics (ABARE), the removal of the Sugar Protocol would be harmful for the employment prospects of poorly educated rural farm employees with possible negative social consequences in Fiji, a classic beneficiary of the Sugar Protocol. A further example is Guyana where preferential sugar contributes to 20% of its total GDP and over 50% of its agricultural production. Moreover, the sugar industry directly and indirectly employs 26,000 workers who provide a living for 150,000 people out of a total population of 750,000. Guyana's sugar industry and the livelihood of the rural poor will most probably be threatened if Guyana is faced with competition from the massive and dominant sugar industry of Brazil. Thus, the rural poor will incur the bulk of the burden of structural change. This will work against the United Nations Millennium Development Goal of reducing poverty and hunger.

It has been argued that the current preferential access to the EU market to selected developing countries is an inefficient instrument for supporting the economies of developing countries. Moreover, there is some uncertainty as to who actually reaps the benefits (quota rents). It is argued that direct aid would be a better choice or it would generally serve the developing countries better to have free access for their products to the markets of developed countries. Firstly, the choice of harming some developing countries in order to help others should be avoided. Secondly, in contrast to the "banana regime", more than 95% of the income benefits from the high EU price for sugar accrue to the developing countries while sugar traders receive less than 5% of the income benefits.[1] In comparison, it is common knowledge that a substantial part (sometimes as high as 70-80%) of direct aids for developing countries are repatriated back to the donor countries with only a minor part reaching the developing countries. The question is how much of the aid money will finally reach the rural poor who are incurring the burden of structural change. Also, although the preferential sugar system may be administratively burdensome, the transaction costs are minimal due the learning experience of several decades.[2] Finally, the theory of "survival of the fittest" will not help the least developed countries because these countries will not be able to compete with developing countries that already have the infrastructure for sugar production in place. For example, Mozambique's sugar industry had been destroyed by flood and civil unrest. The sugar industry in Mozambique is being rebuilt only after preferential market access for sugar has been given to Mozambique under the "everything but arms" trade concession. The question is how to motivate foreign direct investment into the least developed countries without the incentive of preferential market access in the developed countries.

The "everything but arms" initiative, which eliminates all duties and quotas for sugar imports from the least developed countries, is pressuring the EU to reform the EU sugar regime in order to avoid a major influx of sugar coming from the least developed countries. The lucrative EU sugar market will attract both genuine and fraudulent trade in sugar due to the high EU price for sugar compared to the world market price. The "safeguard cases" involving the Overseas Countries & Territories and Western Balkans have shown that the European Commission is willing to make use of the safeguard measures stipulated in the preferential market access agreements. The emerging question will be whether it is politically correct to impose the safeguard measures on the least developed countries, when the EU has committed itself to open its market fully to the world's poorest countries or whether the EU will protect its domestic market due to internal pressures from the sugar industry and producers. The EU will have to find a solution to this complex situation.

Reform of the EU sugar regime will not be easy. The complexities in the interaction between the different trade agreements and the politically sensitive issues that involve trade preferences for sugar will be hotly debated not only in the EU but throughout the world.

* This Policy Brief is based on ENARPRI Working Paper No. 1, *The Impact of Preferential, Regional and Multilateral Trade Agreements: A Case Study of the EU Sugar Regime*, Ellen Huan-Niemi and Jyrki Niemi, September 2003.

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[1] This information has been obtained by tracing the relevant financial transactions and interviewing top officials of EU refineries for raw sugar imports.

[2] Both the EU refineries and ACP countries have long-standing associations that manage the trade of preferential sugar.