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European Trading Arrangements in Fruits and Vegetables

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Abstract

The European Union (EU) participates in regional and preferential trading arrangements more than any other country or region. Over 70 percent of EU fruit and vegetable imports are from countries benefiting from preferential treatment for some portion of that trade. The most valuable preferences are accorded the 42 least developed countries, while 77 former colonies of EU countries also receive important preferences. The EU's many preferential agreements create a mosaic of tariffs, quotas, and other import restrictions that vary considerably among products and among preferred partners which makes analysis impossibly complex. These agreements are an integral part of the management of EU imports by the Common Agricultural Policy. Exports from countries without preferences, including the United States, are at a disadvantage in EU markets.

Keywords: European Union, fruits, vegetables, preferential agreements, trade, managing imports.

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Introduction

The European Union (EU) is the world's largest importer of fruits and vegetables. The EU has been a principal participant in global multilateral trade negotiations, but it also has participated in regional trade agreements and other nonglobal preferential trading arrangements more than other countries. Only the United States and nine other countries—China, Taiwan, Japan, South Korea, Singapore, Hong Kong, Australia, New Zealand, and Canada—face exclusively most-favored-nation (MFN) treatment for access to EU markets, which puts them at a disadvantage to the EU's trading partners with preferential agreements.

MFN treatment is the foremost principle of the General Agreement on Tariffs and Trade (GATT). It requires members to accord to all other members the lowest tariffs and best trading conditions provided to any country. Implicitly, the MFN principle requires that all trading arrangements be global, with imports from all members treated equally. However, the GATT also provides for two exceptions to the MFN principle. The first provides for free trade agreements (FTA) that establish bilateral free trade without any barriers on substantially all the trade among the FTA members (Burfisher et al., 1998.) FTAs of the EU generally provide for free trade in nonagricultural goods, but many sensitive EU agricultural products are excluded altogether, or EU agricultural imports are limited by tariff-rate quotas or minimum import price requirements.

Since the 1970s, a second exemption from MFN obligations has been provided for a Generalized System of Preferences (GSP), allowing developed countries to provide trade preferences for developing countries, including special measures for the least developed countries. GSP preferences differ from FTAs because they are nonreciprocal and nonbinding. The EU receives no advantages for its exports to GSP countries. The GSP also does not involve free trade for many products but rather provides selective tariff reductions. The United States also operates a GSP for imports from developing countries.

All nonglobal trading arrangements must conform to GATT requirements for FTAs or those for the GSP, or three-fourths of the members of the World Trade Organization must consent to a special waiver. Preferential trading arrangements provide lower tariffs and other more favorable terms for imports of some agricultural products from preferred trading partners. There are numerous EU trading arrangements, including bilateral FTAs with individual countries and broader agreements encompassing numerous trading partners. The EU's many preferential agreements create a mosaic of tariffs, quotas, and other import restrictions that vary considerably among agricultural products and among preferred partners. All EU preferential agreements disadvantage U.S. exports because U.S. exports face higher tariffs and more restrictive requirements than preferred EU partners. FTAs also provide advantages to EU exports in the markets of the EU's preferred partners.

EU preferential trading agreements are an integral part of the management of fruit and vegetable imports by the Common Agricultural Policy (CAP). For fruits and vegetables produced in significant quantities within the EU, the CAP maintains relatively high prices by controlling the quantity and pricing of imports. For many products, the CAP establishes minimum import price requirements or restricts imports through quotas associated with the various preferential trading arrangements. Relatively low tariffs often are applied within quotas or for imports observing minimum import price requirements. Applied tariffs, quota amounts, and minimum import price requirements are varied seasonally to provide the most protection for EU producers during their peak production seasons. Ultimately, the capacity to maintain EU internal prices relies upon the imposition of very high MFN tariffs if quotas are exceeded or if minimum import price requirements are not met (Burfisher et al., 1998).

The combination of minimum import price requirements and the management of EU imports by quotas arranged in preferential trading agreements have led to a system in which trade generally is managed by state agencies in the exporting countries to assure that EU minimum import price requirements are met. These agencies also may secure leverage in negotiations with the EU for quota allocations and with the small group of EU importing companies for specific contracts and sales. Because of the minimum import price requirements, price competition is minimal, with most competition based on quality at relatively fixed prices.

In the end, the EU import regime for fruits and vegetables centers on prices for EU fruit and vegetable producers. The EU is generally deficit in most fruits and vegetables at those desired prices. The EU, therefore, imports fruits and vegetables as necessary to meet EU demand at desired price levels. EU import needs vary by season but tend to remain quite stable because of established tastes and multiple supply sources.

The Generalized System of Preferences (GSP)

The EU's basic GSP provides reduced import tariffs on selected products to 142 developing countries. Relatively wealthy developing countries and those that dominate trade in particular products are not eligible for GSP preferences. China, Hong Kong, the Republic of Korea, and Singapore now face MFN tariffs exclusively. Thailand, Mexico, and Chile are no longer eligible for GSP preferences for fresh fruits and vegetables.

The current GSP program, implemented at the beginning of 2002, will continue to the end of 2004. Products identified as "sensitive" are accorded a reduction in *ad valorem* tariffs of 3½ percentage points below the MFN tariff rate. Specific tariffs are reduced by 30 percent. In some cases, minimum duties were required, assuring that an *ad valorem* duty amounted to at least some minimum specific amount or a specific duty amounts to at least some minimum percentage. Those minimum duty requirements are now eliminated. Non-sensitive products remain duty-free. For products having *ad valorem* and specific tariffs, reductions are for *ad valorem* tariffs only, sometimes leaving significant specific tariffs in place. No quotas are imposed for products having GSP tariff reductions.

Many important fruits and vegetables and processed products are identified as sensitive rather than non-sensitive. Among vegetables, these products include onions, cauliflower, cabbage, celery, carrots, cucumbers, peas, artichokes, mushrooms, new potatoes, asparagus, eggplant, sweet peppers, celery, spinach, and peas. Among fruits, the sensitive products include apples, pears, grapes, melons, and strawberries. Among nuts, sensitive products include almonds, hazelnuts, and chestnuts. Tomatoes, cucumbers, bananas, and pecans are not covered by the GSP and receive no preferences.

African, Caribbean, and Pacific (ACP) Countries

The Cotonou Agreement of 2000, successor to the Lomé conventions, continues the provision of preferences to 77 former African, Caribbean, and Pacific (ACP) colonies. Since provisions of the Cotonou agreement are essentially identical to those of the previous Lomé convention, no change in trade is anticipated because most trade is operated under quotas. The ACP arrangement, although non-reciprocal, is not based on GSP provisions but is operated under a special WTO waiver.

Tariff reductions provided the ACP countries outside of quotas by the EU are generally larger than those provided by the EU's GSP. ACP tariff reductions are provided for many products not covered by the GSP, including many vegetables and some fruits. Some ACP tariff reductions are considerably larger than those provided by the EU's basic GSP, but they generally are provided only within quotas. Minimum import price requirements also must be observed. As with the basic GSP, ACP reductions generally are for *ad valorem* tariffs only, often leaving specific tariffs in effect.

Historically, a special protocol provided for EU imports of bananas from ACP countries. That arrangement was contested in the WTO. The EU's banana import regime favored EU banana distributors over distributors from other countries and former ACP colonies over other developing countries. The WTO dispute panel found the banana import quotas for former colonies to be discriminatory and inconsistent with WTO rules. Following the WTO panel finding, the EU requested a waiver and received approval by the necessary three-fourths of WTO members to operate the ACP arrangements (including a revised banana regime) for an interim period. During this period, the EU implemented a tariff-only system for banana imports and renegotiated EU trading arrangements with ACP countries. The EU intends to negotiate new reciprocal FTAs with the ACP countries by 2008 to comply with WTO rules.

The Least Developed Countries (LDC)

The GSP always has provided the LDCs with larger tariff reductions on a larger set of products than other developing countries. Since March 2001, the EU's "Everything But Arms" (EBA) policy provides 42 of the 49 LDCs access to EU markets without duties or quotas for all primary and processed fruits and vegetables with the exception of bananas. The tariff reductions for bananas will be phased in by 2006.

The EBA is a major departure in EU agricultural trading relationships because it eliminates the mechanisms by which the CAP manages sensitive imports, preventing low-priced imports from undermining internal EU prices. Preliminary analyses by the EU Commission have indicated that the export potential of the LDCs is not adequate to affect CAP markets for fruits and vegetables except for bananas (Commission of the EU, 2001).

LDC exports of sensitive fruits and vegetables to the EU have been negligible. As a group, the LDCs are surplus producers only of grapes and tree nuts. They are marginally less than self-sufficient in fruits and vegetables. However, individual LDCs do export to the EU, indicating some have the infrastructure to support exports of some fruits and vegetables beyond bananas.

The greatest danger to EU producers may result from EBA provisions that allow the LDCs to import agricultural products for domestic consumption at world prices and export their own production to obtain higher EU prices. The LDCs do have appreciable production capacity for citrus fruit and pineapples, and even tomatoes. Other provisions could allow LDCs to include some raw products from non-LDCs in processed products legally exported to the EU duty free. The attraction of high EU prices could induce foreign investment in the productive capacity of the LDCs. Such investments, however, require time and training; thus, the potential effects will likely not be felt for a few years. In fact, for the EBA countries, fruit and vegetable exports declined slightly during the 2001-03 period ($101 million) when EU tariffs and quotas were abolished compared with the 1998-2000 period ($109 million) when they were still in effect.

Particularly difficult for LDCs will be the EU's traceability rules that will force exporters to trace their product back to the plot and the seed it came from. The same logic applies to the 77 Cotonou countries, some of which are also EBA countries, in that they will face the same stricter EU food rules on January 1, 2005. However, many of these countries have made some investments with assistance from the EU to meet current EU standards. It remains to be seen whether sufficient investments will be forthcoming because of the added costs that the new rules imply for these exporters.

Euro-Mediterranean Agreements (EMA)

The EMAs are bilateral FTAs between the EU and the Palestine Liberation Organization (PLO) (1997), Tunisia (1998), and Israel and Morocco (2000). Negotiated agreements with Jordan and Egypt await implementation. Unlike the GSP and ACP arrangements, the EMA provide for reciprocal concessions, including free trade in nonagricultural products within 12 years. The EMAs replace nonreciprocal agreements dating from the 1970s, some of which remain in force for Algeria, Lebanon, and Syria pending EMA negotiations. The EU envisions a Euro-Mediterranean free-trade area by 2010.

EMA preferences for fruit and vegetable exports to the EU are limited largely to historical trade volumes. Much of that trade is administered through quotas. Seasonal restrictions and minimum import price requirements also apply. The EMA countries are important suppliers of citrus fruit and vegetables, particularly in the early and late seasons.

Europe Agreements (EA) and Neighboring Countries

The EAs are FTAs that the EU negotiated in 1994 with Eastern European and former Soviet Union members: Hungary, Poland, the Czech Republic, the Slovakia, Bulgaria, Romania, Estonia, Latvia, Lithuania, and Slovenia. The goal is to provide reciprocal free trade in industrial goods within 10 years. Associated "double zero" agreements eliminated export subsidies in bilateral trade and provided for duty-free EU imports of some sensitive agricultural products within quotas whereas trade is now unhindered for the new member states[1] (Bulgaria and Romania remain candidate countries for 2007) of the EU if standards and regulations are met. Non-EU members Bulgaria and Romania continue to observe the conditions of the agreement. Similar agreements provide some agricultural preferences to nonmember countries in southeast Europe. Because climatic and other conditions in these countries are similar to those in the EU, production is largely of the same products and EU imports of those products are carefully controlled.

[1]The new member states are Poland, Hungary, the Czech Republic, Slovakia, Slovenia, Estonia, Latvia, Lithuania, Cyprus, and Malta.

The EU also has arrangements with several neighboring countries not likely to become members of the EU in the near future, including Iceland, Norway, Liechtenstein, Switzerland, Turkey, and Andorra. These arrangements extend the EU internal market throughout Western Europe for industrial products. Agriculture is, however, largely excluded from these agreements, except for some processed products.

Most-Favored-Nation (MFN)

A contradiction in terms, MFN treatment is, in reality, the least favored treatment given EU imports. MFN treatment applies to all imports from the United States, Canada, Japan, South Korea, China, Taiwan, Hong Kong, Singapore, Australia, and New Zealand, and for imports of fresh fruits and vegetables from Mexico, Chile, and Thailand. All other countries have trade agreements with the EU that provide more preferred treatment than MFN for some agricultural products.

The Significance of Preferences

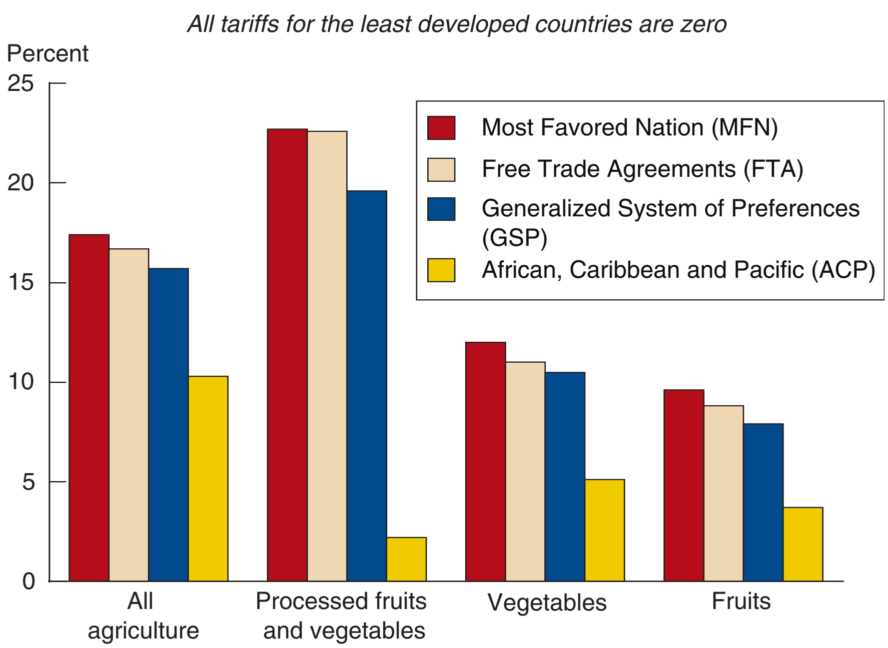
The overall value of EU trading preferences is difficult to assess because preferences vary greatly among products and among preferred trading partners. Preferences also vary by season for fruits and vegetables. Concessions may include reduced tariffs, reduced minimum import prices, or less seasonally restrictive conditions. While the preferences provided by the GSP, LDC, and ACP arrangements differ substantially, every country within each arrangement receives the same preferences. The numerous countries view the benefits differently, however, because their export potential varies. Among the FTAs, product coverage and other provisions vary significantly.

EU preferential agreements commonly provide a tariff rate lower than the MFN rate on imports outside of quotas, although much lower tariffs often are applied within quotas. The WTO Secretariat has provided an assessment of the simple average tariffs applied outside of quotas on the assumption that every country uses the lowest tariff for which it is eligible (fig. 1). Of course, the zero tariffs accorded the LDCs are now the most beneficial. Outside of quotas, the concessions for the ACP also are significant, particularly for processed products. Out-of-quota tariff concessions in FTAs are quite limited, while somewhat greater concessions are accorded through the GSP (WTO, 2000).

Although quotas limit the benefit of the larger tariff reductions associated with them, they also provide what may be the most important benefit to the EU's preferred trading partners—some assured access to the world's largest market. Preferential reductions in minimum import price requirements also provide a competitive advantage to the preferred trading partner. However, the EU's minimum import prices effectively limit the quantity of EU imports from all sources because excessive imports would lower the internal EU price below the minimum price, making imports at the minimum price noncompetitive.

Minimum import price requirements are the EU's most fundamental policy mechanism because they assure that imports cannot suppress EU prices below the price objectives. Import quotas also increase internal EU prices by restricting import quantities. The real role of quotas, generally associated with preferential agreements, is to control the source of imports in addition

Figure 1
Simple average applied EU tariffs outside of quotas



Source: Secretariat of the World Trade Organization.

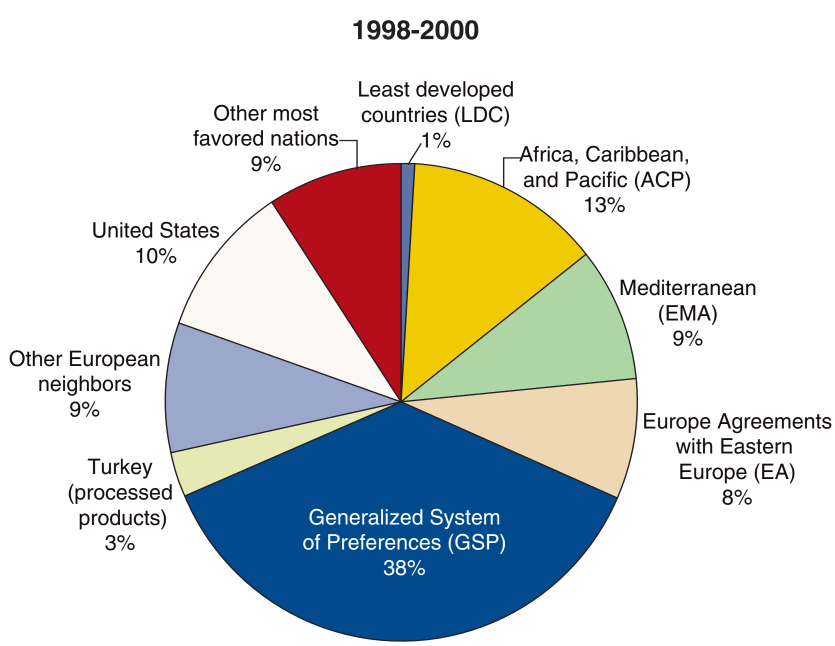
to the quantity and pricing of imports. The EU commonly allows quotas to be overfilled if EU market conditions permit. Allocation of rights to provide EU imports involves political issues beyond agriculture.

A comprehensive analysis of the EU's preferences in the fruit and vegetable trade is virtually impossible because of the great number of commodities involved, the variety of tariffs, the imposition of seasons, the overlapping of agreements and international obligations in GSP, MFN, preferential treatment, and the political nature of granting import rights. Even countries granted trade preferences are not assured of capturing the full value of the preference because the EU allocates import licenses only to EU companies, leaving the exporting countries to compete for EU import contracts. In the process, exporters may give up some part of the value of the preference to importers in order to obtain the contract. In practice, the trade is highly institutionalized with a few EU importers dealing with state export agencies.

The Effect of Preferential Agreements on Trade Patterns

Over 70 percent of EU imports of fresh and processed fruits and vegetables originate in countries having preferential trading arrangements with the EU, although all of that trade does not benefit from preferences, particularly under the GSP. The countries having the most preferred trading arrangements with the EU have not dominated EU fruit and vegetable imports as much as would be expected given their trade advantage (fig. 2). The LDCs provided only 1 percent of imports during 1998-2000, when LDC preferences were somewhat less substantial than those provided the ACP countries. Duty and quota-free access for the LDCs began only in March 2001

Figure 2
Share of total EU fruit and vegetable imports



Source: Secretariat of the World Trade Organization.

for the EBA countries and, as previously noted, exports to the EU had not increased through 2003. The concessions provided the ACP, Mediterranean, and Eastern European countries are important in fruits and vegetables, but they are limited by quotas and accounted for 30 percent of total EU fruit and vegetable imports. While this is a significant amount, preferential agreements clearly do not allocate all EU fruit and vegetable imports to preferred exporting partners.

While the EU has preferential arrangements with all countries geographically close to it, the countries in Eastern Europe and the former Soviet Union not acceding to the EU in 2004 grow products also produced within the EU, and the CAP carefully restricts trade in those products through quotas, tariffs, and other restrictions. Turkey is an important exception because it is Mediterranean and the EU production of Mediterranean fruits and vegetables is inadequate to meet EU demand. Turkey has a special arrangement with the EU because it has applied to become an EU member and because it has a comparative advantage in the production of hazelnuts and sultanas, which are in great demand in the EU. Turkey has duty-free access to the EU for processed products, yet almost two-thirds of EU imports from Turkey are fresh products dominated by hazelnuts, sultanas, and grapes.

Almost 20 percent of EU imports are accounted for by the MFN countries, including the United States, which have no preferences. Furthermore, 38 percent of EU imports originate in the GSP countries, for whom preferences are relatively minor. The most important explanation for large EU imports from countries with limited or no preferences is that EU fruit and vegetable imports are dominated by products the EU cannot produce, particularly tropical products and counter-seasonal production from Southern Hemisphere countries. Large supplies of those products can be obtained only from dominant world producers, who may have limited or no preferential arrangements. In some cases, EU imports from countries with no preferences produce a product unavailable in the EU or any other market in the quantity and quality the EU consumer requires, such as U.S. almonds from California.

Bananas alone account for almost 14 percent of all EU imports of fresh and processed fruits and vegetables. The countries of Central and South America, which have only GSP preferences, account for 75 percent of that trade. Fruit juices account for another 11 percent of EU fruit imports with half of that coming from Brazil and another 10 percent from the United States. Fresh and dried nuts account for over 9 percent of EU fruit imports, and almost half are supplied by the United States and over a third by Turkey, both without preferences, while Iran provides another 10 percent with GSP preferences. These trade flows with limited or no preferences are the consequence of inadequate alternative supplies or available quality.

Conclusions

Ultimately, EU preferential trading arrangements have not expanded trade in fruits and vegetables. The basic objective of EU agricultural policy—the maintenance of targeted domestic price levels—determines the level of imports consistent with policy objectives. EU domestic price targets for fruits and vegetables have been largely unaffected by design through EU preferential agreements. Preferential agreements are extensions of the CAP, allowing the EU to manage the sources of imports and adjust import levels, depending on market needs and policy objectives.

For products produced within the EU and prices in EU markets above world prices, imports are carefully managed with quotas and minimum import price requirements that are enforced by the potential application of high MFN tariffs. Low-priced imports are not allowed to undermine internal EU prices. Nevertheless, the EU remains the world's largest importer of fruits and vegetables because of limited production potential for many products and strong demand from EU consumers due to high incomes, an aging population that prefers a healthy diet, and a historical preference for high-quality fruits and vegetables.

If EU preferential agreements do not generate trade, then what value are they to the preferred partners? EU preferential trading agreements do divert trade, and the preferred partners are the beneficiaries, gaining some assured access to the large EU market. Preferred traders also may capture some part of the value of reduced tariffs. MFN trading partners, including the United States, find their fruit and vegetable exports disadvantaged in EU markets because they face higher tariffs than countries with preferential trading agreements with the EU. Nevertheless, the United States is still able to export significant quantities of high-quality fruits to the EU because of the reliability of its supply of high-quality products such as almonds, dried plums, and raisins.

Preferential arrangements provide the EU with expanded control over the sources of its imports. The EU also achieves some limited preferences for its fruit and vegetable exports to countries with which it has FTAs. The EU has achieved larger advantages for its exports of other agricultural products. The EU plans to renegotiate arrangements with the ACP and Mediterranean countries and adopt FTAs with reciprocal advantages for EU exports by 2007.

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