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International Trade Strategies, JM module  
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## EU trade strategy and RTA network

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## Content

### EU trade strategy

- Today's global context
  - Globalisation, vertical specialisation, new economic powers,...
- Goals
  - active negotiating agenda, deepening relations with strategic partners, EU rights enforcement
- Dimensions
  - Multilateral (WTO): Bali 2013 progress**
  - „Regional“, cross-regional**
    - New generation of RTA in the EU
    - Assessing impacts of RTAs
    - Implications for business
  - Unilateral: New GSP scheme**



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## Today's context of EU trade policy

- Global and regional VC  
Increasing share of supply-chain trade
- Emergence of new economic powers  
China, India, Brazil
  - 90% of global economic growth by 2015 is expected to be generated outside Europe, a third of it in China alone (IMF)
- Economic downturn  
Trade is part of the solution → **trade based crisis exit strategy**



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## Global economy

Regionalism (RTAs)

„Global“ Multilateralism (WTO)

A global race for RTAs

WTO PUBLIC FORUM 2012  
“Is Multilateralism in Crisis?”  
24-26 September 2012  
Geneva, WTO headquarters



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## The changing nature of regionalism

- 20th century regionalism: “made-here-sold-there”
  - Shallow RTAs: focus on tariffs**
- 21st century regionalism: “made-everywhere-sold-there”
  - Deep RTAs: tariffs + provisions to foster international production sharing**
    - include rules on *making* goods as well as *selling* them to foster international vertical integration and supply chain trade;
    - Attention is shifted from where exports is booked towards where value is added.

International goods (processed), 2012




Table 1.1 – Revealed comparative advantages by technology intensities in manufacturing 2011

	High tech	Medium high tech	Medium low tech	Low Tech
EU	0.85	1.14	0.89	1.01
Japan	0.73	1.59	0.86	0.16
US	0.88	1.22	0.96	0.68
Brazil	0.32	0.76	0.87	2.50
China	1.56	0.72	0.85	1.29
India	0.40	0.49	1.93	1.33
Russia	0.08	0.45	2.74	0.49

Source: UN COMTRADE

### European competitiveness under dominance of GVC trade

Figure 10. Foreign Contents in Gross Exports: High-Technology Sectors

Percentages indicate the share of foreign value added in gross exports

Gross Exports (USD Bilion)


1995 2005 1995 2005 1995 2005 1995 2005

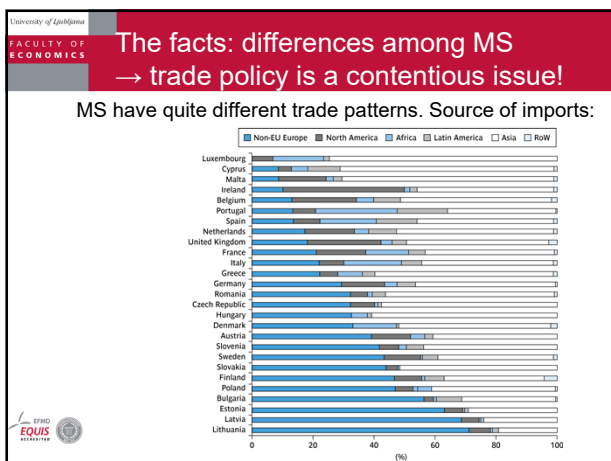
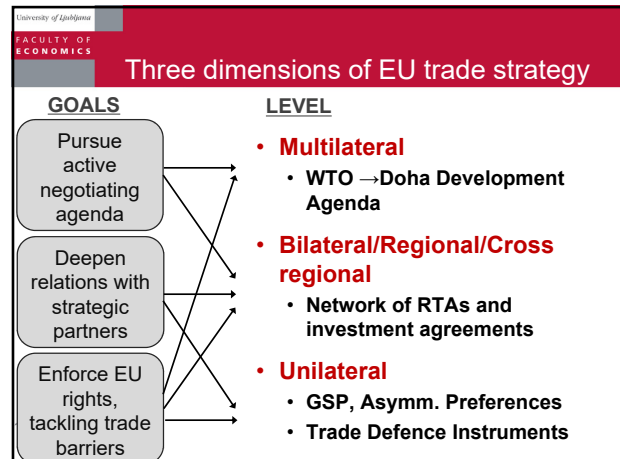
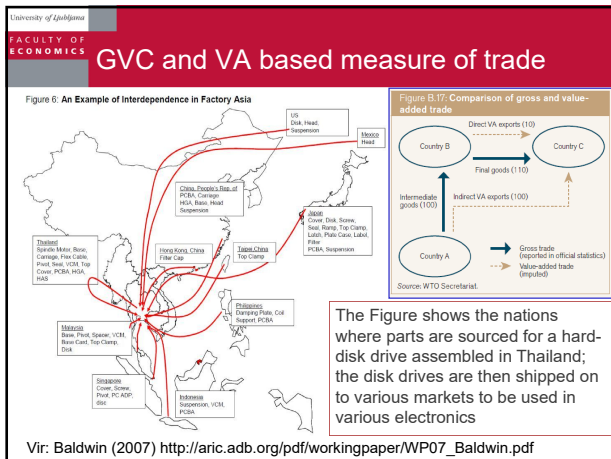
China Japan USA Germany

20.1 % 48.5 % 10.0 % 21.5 % 16.6 % 17.4 % 24.1 % 31.2 %

Service Rest of world USA Euro area Non-euro area OEA Japan China OVA

Source: IMF staff estimates using OECD Input-Output Tables, UN Comtrade, and OECD STAN data.





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- ## A. Multilateral level
- ### The Doha Develop. Round – recent developments
- Launched in 2001
  - Modest progress till Ninth Ministerial WTO Conference in Bali, 3-7- December 2013:
- “Bali Package”**
- trade facilitation: cutting red tape and speeding up port clearances;
  - development issues, incl. food security in developing countries and cotton;
  - a number of other provisions for least developed countries;
  - a political commitment to reduce export subsidies in agriculture, and to reduce obstacles to trade when agricultural products are imported through quotas.

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## Bali Ministerial Declaration and decisions

These are the Bali Ministerial Declaration and the ministerial decisions that were adopted on 7 December 2013.

- WTO/MIN(13)/DEC, The Bali Ministerial Declaration

The declaration refers to the following decisions adopted by ministers:

**PART I – REGULAR WORK UNDER THE GENERAL COUNCIL**

- TRIPS Non-violation and Situation Complaints – Ministerial Decision – WT/MIN(13)/11 – WT/L/906
- Work Programme on Electronic Commerce – Ministerial Decision – WT/MIN(13)/28 – WT/L/907
- Work Programme on Small Economies – Ministerial Decision – WT/MIN(13)/23 – WT/L/908
- AG for Trade – Ministerial Decision – WT/MIN(13)/34 – WT/L/909
- Trade and Transfer of Technology – Ministerial Decision – WT/MIN(13)/25 – WT/L/910

**PART II – DOHA DEVELOPMENT AGENDA**

**Trade Facilitation**

- Agreement on Trade Facilitation – WT/MIN(13)/16 – WT/L/911

**Agriculture**

- General Services – Ministerial Decision – WT/MIN(13)/27 – WT/L/912
- Public Stockholding for Food Security Purposes – Ministerial Decision – WT/MIN(13)/29 – WT/L/913
- Understanding on Tariff Rate Quota Administration Provisions of Agricultural Products, as Defined in Article 2 of the Agreement on Agriculture – Ministerial Decision – WT/MIN(13)/20 – WT/L/914
- Export Competition – Ministerial Declaration – WT/MIN(13)/40 – WT/L/915

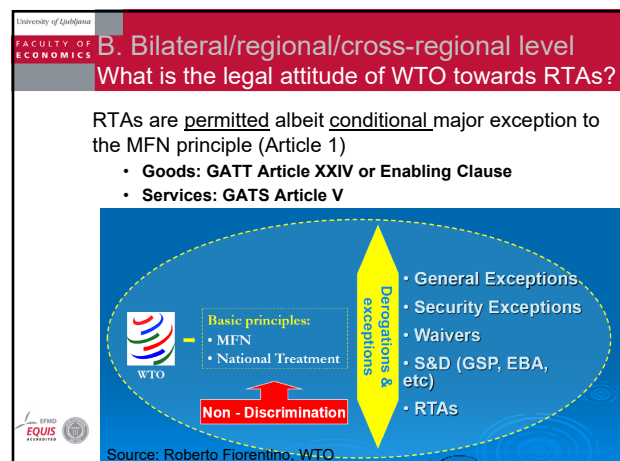
**Cotton**

- Cotton – Ministerial Decision – WT/MIN(13)/41 – WT/L/916

**Development and LDC Issues**

- Preferential Rules of Origin for Least-Developed Countries – Ministerial Decision – WT/MIN(13)/42 – WT/L/917
- Operationalization of the Waiver Concerning Preferential Treatment to Services and Service Suppliers of Least-Developed Countries – Ministerial Decision – WT/MIN(13)/43 – WT/L/918
- Basic Free and Quota-Free Market Access for Least-Developed Countries – Ministerial Decision – WT/MIN(13)/44 – WT/L/919
- Monitoring Mechanism on Special and Differential Treatment – Ministerial Decision – WT/MIN(13)/45 – WT/L/920

[http://wto.org/english/thewto\\_e/mini\\_e/mc9\\_e/temppocs\\_e.htm](http://wto.org/english/thewto_e/mini_e/mc9_e/temppocs_e.htm)



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## Trade structure and economic growth

Does the EU export the right goods to the right markets?

- Arora and Vamvakidis (2005): positive effects of cooperation with fast-growing markets on domestic growth
  - strengthening the ties with these markets may also be regarded as one of the potential remedies to the negative effects of the economic crisis.**

Lets see if EU's RTA network supports this strategy!

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## Complex net of free trade agreements

Source for this section: Baldwin and Wyplosz (2012), <http://ec.europa.eu/trade/policy/countries-and-regions/>

The EU's external trade policy is extremely complex; in the European Mediterranean area:

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## European-Mediterranean area (1)

**EFTA** (without Switzerland) + EU (= **European Economic Area - EEA**) + Swiss bilateral agreements

- Allowing EFTA to participate in the EU's single market; certain exceptions.

**Euro-Med Partnership:** Morocco, Algeria, Tunisia, Egypt, Israel, the Palestinian Authority, Lebanon, Jordan, Syria and Turkey.

- Euro-Mediterranean Association Agreements** in force with most of the partners (exceptions Syria and Libya).
  - Asymmetric (EU cuts its tariffs faster) free trade in manufactures.
- Turkey unilaterally in Customs Union in manufactures.
- Asymmetric dependence (e.g. 70% of Morocco's exports to EU, but <1% of EU to Morocco)
- EFTA's "FTA union" with EU; EFTAs mimic EU to avoid discrimination against EFTA-based exporters.

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## European-Mediterranean area (2)

Mediterranean

- Palestinian Authority** - Association Agreement, 01 July 1997
- Syria** - Co-operation Agreement, 01 July 1977
- Tunisia** - Association Agreement, 01 March 1998
- Morocco** - Association Agreement, 01 March 2000
- Israel** - Association Agreement, 01 June 2002
- Jordan** - Association Agreement, 01 May 2002
- Lebanon** - Interim Agreement, 01 March 2003
- Egypt** - Association Agreement, 01 June 2004
- Algeria** - Association Agreement, 01 September 2005

A way to go: **Deep and Comprehensive Free Trade Agreement (DCFTA)**

- Morocco started negotiating DCFTA with the EU in 2013.
- The Commission has also a mandate to start a similar process with Tunisia, Egypt and Jordan.

Source: [http://ec.europa.eu/trade/policy/countries-and-regions/agreements/index\\_en.htm#\\_mediterranean](http://ec.europa.eu/trade/policy/countries-and-regions/agreements/index_en.htm#_mediterranean)

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## Western Balkans

- Stabilisation and Association Agreements (SAAs).**
- Former Yugoslavian states + Albania.**
  - SAS with Macedonia, Albania and Montenegro already in force
  - B&H: SAS signed in June 2008, Interim in force from July 2008
  - Serbia: SAS signed in April 2008, Interim in force from February 2010
- Candidate country status: Serbia, Macedonia, Montenegro and Albania.**
- Potential candidate country status: other WB countries.**

**Regional integration: CEFTA II**

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## Former Soviet republics

**Partnership and Cooperation Agreements (PCAs)**

These are **GSP+** (**GSP**=Generalised System of Preference). Russia, Ukraine, Georgia, Belarus, Armenia, Azerbaijan, Kazakhstan, Kyrgyzstan, Moldova and Uzbekistan.

**Association Agreements**

**EU has recently concluded negotiations for a Deep and Comprehensive Free Trade Area (DCFTA) with Moldova, Armenia, Georgia and Ukraine as a part of the Association Agreements.**


- The official initialling of the Association Agreements with **Moldova** and **Georgia** took place on 29 November 2013 in Vilnius.
- Armenia** decided to join the customs union of Russia, Belarus and Kazakhstan, hence the steps required for the agreement to become effective are not pursued at this moment.
- Ukraine:** DCFTA signed on 27 June 2014. *The provisional application of the DCFTA is delayed until January 2016, while continuing autonomous trade measures of the EU to the benefit of Ukraine during this period.*

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## Preferential arrangements with former colonies


- To avoid imposing the CET on imports from former colonies, EEC6 signed agreements with many of them: asymmetric deals where EU tariffs were set to zero but the poor nations did not remove theirs.
  - When UK joined 1974 extended to many Commonwealth nations.
    - "ACP nations" (Africa, Caribbean & Pacific); the new agreement = **Lomé Convention**.
    - Duty-free but subject to quota for sensitive items (sugar, banana, etc.).
  - These didn't help the ACP nations (c.f. Asian success w/o preferences).
  - When Lomé Convention renewed in 2000, the EU and the ACP nations agreed to modernise the deal.
  - Cotonou Agreement** → eventually reciprocal free trade.
    - ACP nations are committed to negotiate bilateral Economic Partnership Agreements (EPAs). The majority of ACP countries are either implementing an EPA or have concluded EPA negotiations with the EU



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## Non-regional FTAs

- Mexico, Chile, South Africa**
- Trade Agreement with **Colombia** and **Peru** done. Negotiations for accession of **Ecuador** were concluded in 2014.
- Most recent (2013): **Central America (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama)**
- Mercosur**:
  - negotiations were launched in 1999 but were, however, suspended in October 2004.
  - Negotiations with Mercosur were officially relaunched in 2010.
- the Gulf Cooperation Council** (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates):
  - Negotiations were suspended by the Gulf Cooperation Council in 2008.




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## EU trade not focused enough on rapidly growing markets

	% of total exports to more/less rapidly growing markets			Contribution to growth in world imports 1995-2002
	US	Japan	EU25	
10 most rapidly growing markets	79%	76%	48%	93%
20 least rapidly growing markets	8%	12%	13%	-5%

Source: Cepii



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## Response: The new generation of RTAs


A 2006 landmark communication from the Commission known as **Global Europe**: it identified

**New regional priorities**

- ASEAN, Korea, India and Mercosur as priority partners for new FTAs.
- 2013: US, China, Russia, Japan, India and Brazil

**Deeper agreements**


- New type of agreements that cover issues such as investment, public procurement, competition, IPR enforcement and regulatory convergence issues beyond the WTO agenda.



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## A new generation of RTAs

- Korea**: launched in May 2007, signed in 2010, enforced in 2011.
- India**: launched in the end of June 2007; slow progress, some open issues still.
- ASEAN**: launched in May 2007;
  - EU MS in December 2009 gave the green light for FTA negotiations with individual ASEAN countries:
  - Negotiations with **Singapore** concluded successfully in December 2012, with **Vietnam** in December 2015.
  - Negotiations with **Malaysia** were launched in 2010, with **Thailand** in March 2013.
  - Additionally, on-going talks on investment protection.



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## On-going negotiations with major trade powers (1)

### USA: Transatlantic Trade and Investment Partnership (TTIP)

- Talks on a TTIP started in July 2013
- potentially the largest FTA in history, covering 46% of world GDP and large shares of world trade and FDI.
- Many open questions and scruples trigger revision of EU's trade and investment strategy
- Commission's proposal: „**Trade for All** - towards a more responsible trade and investment policy“

### China: EU-China Investment Agreement

- Just 2.1% of overall EU FDI is in China.
- November 2013: the launch of negotiations.
- Aim: progressive liberalisation of investment, the elimination of restrictions for investors and stronger protection to investors.



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# Does FTA matter?

## Estimating TC and TD: the gravity model

- Effects of RTAs on trade flows are finally an empirical question.
- Most studies use gravity model approach motivated by Newton's law of universal gravitation

$$F_{ij} = G \frac{M_i^\alpha M_j^\beta}{D_{ij}^\theta} \quad ; \alpha = 1, \beta = 1 \text{ in } \theta = 2.$$

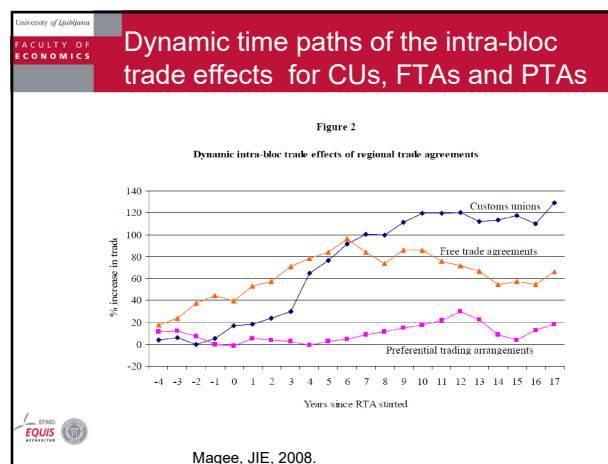
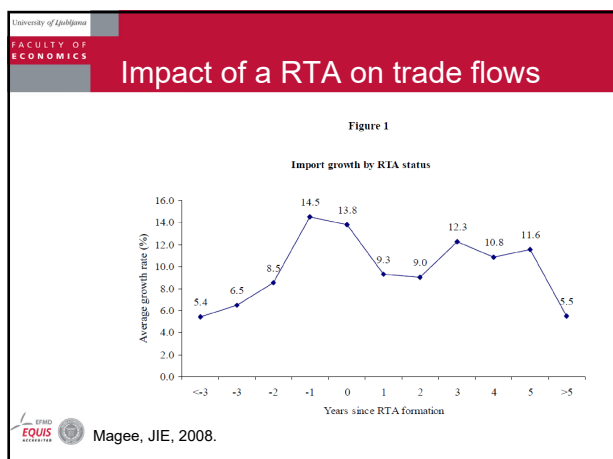
### Gravity model of bilateral trade flows (Magee, JIE, 2008)

$$(1) \quad \ln(m_{ijt}) = \alpha_t + \beta_1 \ln(Y_{it}) + \beta_2 \ln(Y_{jt}) + \beta_3 \ln(Y_{ijt}) + \sum_{k=1}^K \beta_k RTA_{ijt}^k + \beta_{K+1}^k TD_{ijt}^k + \alpha X_{ijt} + \varepsilon_{ijt}.$$

where  $m_{ijt}$  is the trade flow from country  $i$  to  $j$  in year  $t$ .  $D_{ijt}$  is the bilateral distance.  $Y_{it}$  and  $Y_{jt}$  are the GDP levels of the two countries.  $RTA_{ijt}^k = 1$  if countries  $i$  and  $j$  belong to regional trade agreement  $k$ .

$TD_{ijt}^k = 1$  if one of the two countries is a member of regional agreement  $k$ , and  $X_{ijt}$  is a vector of other dyad characteristics. A positive coefficient estimate of  $\beta_{K+1}^k$  indicates that trade is rising between members of the regional bloc while a negative coefficient estimate of  $\beta_{K+1}^k$  suggests imports from countries outside the trading bloc are falling. Including fixed effects for each year ( $\alpha_t$  in equation 1)





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## Empirical studies' overview: TC and TD

Table 1. Relationship between gravity model controls and bilateral trade in past studies

		Relationship in past studies		
		Positive	None	Negative
Trade creation 0-1 dummies	$AFTA_{ij}$	3	2	
	$ANZCERTA_{ij}$	1		
	$APFC_{ij}$	3		
	$AP_{ij}$	3	2	
	$CACM_{ij}$	4	2	
	$CARICOM_{ij}$			
	$EEA_{ij}$	3	5	
	$EU_{ij}$	9	9	
	$LAIA_{ij}$	4	2	
	$MERCOSUR_{ij}$	2	3	
Trade diversion/open bloc 0-1 dummies	$NAFTA_{ij}$	1	3	
	$AFTA_{ij}$	2	1	1
	$ANZCERTA_{ij}$			
	$APFC_{ij}$			
	$AP_{ij}$		1	2
	$CACM_{ij}$		2	2
	$CARICOM_{ij}$			
	$EEA_{ij}$	1	1	
	$EU_{ij}$	2	1	
	$LAIA_{ij}$		2	2
Core gravity	$MERCOSUR_{ij}$		2	2
	$NAFTA_{ij}$	1	2	1
	$\log(DISTANCE_{ij})$		1	23
	$\log(GDP_i \cdot GDP_j)$	23	2	1
	$\log(\rho_{ij} \cdot \rho_{ij})$	9	1	2

Sources: Aitken (1973); Aitken and Lowry (1973); Baier and Bergstrand (2007); Baldwin and Taglioli (2006); Baxter and Kouparitsas (2006); Bergstrand (1985); Brada and Mendez (1988); Carrere (2006); Cheng (2005); Coe and Hoffmaister (1999); Eichengreen and Irwin (1996); Egger (2000); Egger and Pfaffermayr (2003); Feenstra *et al.* (2001); Frankel (1992); Frankel and Rose (1998); Frankel *et al.* (1995); Frankel and Wei (1993, 1996); Freund (2000); Montenegro and Soto (1996); Rose (2000); Solórzano and Winters (2001); Thursby and Thursby (1987); Wei (1996); Wei and Frankel (1998); Wei and Zhang (2006).

Source: Eichler, Henn & Papageorgiou (JAE, 2012)

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## Table II(A). Preferential trading arrangements

Abbreviation	Name of PTA	Start	Member countries
ANZCERTA	Australia-New Zealand Closer Economic Relations Trade Agreement	1983	Australia, New Zealand
APEC	Asia Pacific Economic Community	1989	Australia, Brunei, Canada, China (1991), Chile (1994), Taiwan (1991), Hong Kong (1991), Indonesia, Japan, South Korea, Malaysia, Mexico (1993), New Zealand, Papua New Guinea (1993), Peru (1998), Philippines, Singapore, Thailand, United States, Vietnam (1998)
AP	Andean Community/Andean Pact	1969	Bolivia, Colombia, Ecuador, Peru, Venezuela (1973). Former: Chile (1969-76)
AFTA	Association of South East Asian Nations (ASEAN) Free Trade Area	1967	Brunei (1984), Cambodia (1998), Indonesia, Laos (1997), Malaysia, Myanmar (1997), Philippines, Singapore, Thailand, Vietnam (1995)
CACM	Central American Common Market	1960	Costa Rica (1963), El Salvador, Guatemala, Honduras, Nicaragua
CARICOM	Caribbean Community/Carifta	1968	Antigua and Barbuda, Bahamas (1983), Barbados, Belize (1995), Dominica (1974), Guyana (1995), Grenada (1974), Jamaica, Montserrat (1974), St Kitts and Nevis, St Lucia (1974), St Vincent and the Grenadines, Suriname (1995), Trinidad and Tobago
EEA	European Economic Area	1994	Austria, Belgium, Denmark, Finland, France, Germany, Greece, Luxembourg, Iceland, Italy, Ireland, Liechtenstein, Netherlands, Norway, Portugal, Spain, Sweden, UK
EFTA	European Free Trade Association	1960	Iceland, Liechtenstein (1991), Norway (1986), Switzerland, Former: Denmark (1960-72), UK (1960-72), Portugal (1960-85), Austria (1960-84), Sweden (1960-84), Finland (1986-84)
EU	European Union	1958	Austria (1995), Belgium, Denmark (1973), Finland (1995), France, Germany, Greece (1981), Luxembourg, Ireland (1973), Italy, Netherlands, Portugal (1986), Spain (1986), Sweden (1995), UK (1973)
LAIALAPTA	Latin America Integration Agreement	1960	Argentina, Bolivia (1967), Brazil, Chile, Colombia (1961), Ecuador (1961), Mexico, Paraguay, Peru, Uruguay, Venezuela (1966)
MERCOSUR	Southern Cone Common Market	1991	Argentina, Brazil, Paraguay, Uruguay
NAFTA	Canada-US Free Trade Arrangement/North America Free Trade Agreement	1988	Canada, USA, Mexico (1994)
Bilateral/PTA	Bilateral Preferential Trade Agreements		All bilateral agreements considered are listed in Table II(b)

Source: Eichler, Henn & Papageorgiou (JAE, 2012)

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## Implications of FTAs for business

FTAs are not just about eliminating customs duties

- Making imports cheaper
  - by eliminating of substantially all customs duties
- Enabling preferential access to new markets
  - by reducing the landed costs to their customers
    - but up to 80% of companies in the EU are not aware of the potential benefits.
- Increasing investment opportunities
  - the right to establish operations
  - ease of access to the market
- Making trade faster
  - by facilitating goods' transit through customs, setting common rules on technical and sanitary standards
- Making the policy environment more predictable
  - by taking joint commitments on areas that affect trade such as IPR, competition rules and the framework for public purchasing decisions.

Source: EQUIS

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## Enabling preferential access to new markets (1)


FTAs require adjustment of firm's internationalisation strategy and adaptation of relations along the supply chain!

- Drop in prices of inputs originating from partner countries → **reconsider the choice of suppliers!**
- Opportunity for preferential access to partner's market (with full or partial customs exemption in partner's market) → **consider entering new partner market or increasing sales in partner market!**

Source: EQUIS

**Enabling preferential access to new markets (2)**

- But, preferential access conditioned on **preferential origin** of a good → **reconsider relations along the supply chain** in light of meeting the originating requirements of the agreement:
- weighing up the costs of compliance for preferential access and the benefits from preferential access to the partner markets.**
- Exporters need to make sure that:
  - the origin calculations are made correctly**
  - they present the correct documentation at the request of customs authorities.**



**The role of Rules of origin**

**Rules of origin –Rofo** determine the country of origin of a product

**Preferential Rules of Origin** define which products shall benefit from the preferences under FTA:

- Wholly obtained products**
- Sufficiently worked and processed products**
  - change of tariff heading (CTH) or subheading (CTSH)
  - manufacturing/processing operations (process rules)
  - “ad valorem” percentage rules (value limit)

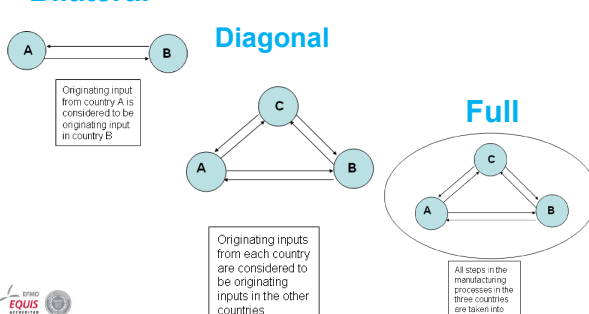
**Cumulation** is an instrument allowing producers to use imported inputs from countries in the system without undermining the origin of the final product.

**RTAs and cumulation of rules of origin**

**Bilateral**

**Diagonal**

**Full**



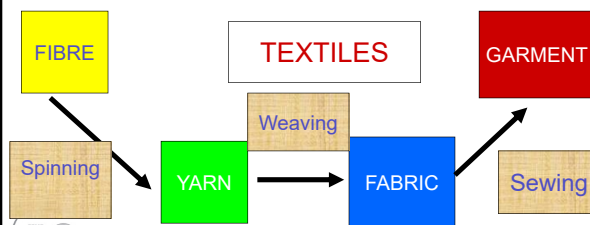
Originating input from country A is considered to be originating input in country B.

Originating inputs from each country are considered to be originating inputs in the other countries.

All steps in the manufacturing processes in the three countries are taken into account for origin determination.

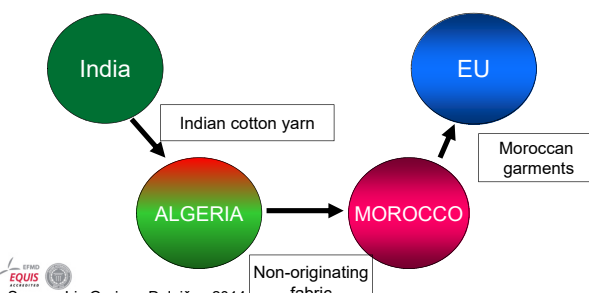
**Case of rules of origin for textiles**

ex Chapter 62	Articles of apparel and clothing accessories, not knitted or crocheted:	Manufacture from yarn <sup>(a)</sup> <sup>(4)</sup>
ex 6202, ex 6204, ex 6206, ex 6209 and ex 6211	Women's, girls' and babies' clothing and clothing accessories for babies, embroidered	Manufacture from yarn <sup>(a)</sup> or Manufacture from unembroidered fabric, provided that the value of the unembroidered fabric used does not exceed 40 % of the ex-works price of the product <sup>(5)</sup>



Source: Iris Gorjanc-Dolničar, 2014

**Full cumulation case**



Source: Iris Gorjanc-Dolničar, 2014

**C. Unilateral level: Generalised Scheme of Preferences (GSP)**

- 1971 GATT provision.**
- New GSP scheme: applied from 1 January 2014** (No. 978/2012)
- 90 eligible countries:**
  - 49 least developed countries under EBA
  - 41 Low income' and 'lower middle income' countries under standard GSP and/or GSP+
- Partners which are no longer eligible:**
  - 33 Overseas countries and territories (already have access—do not need GSP)
  - 34 Partners which have been granted preferences through other tracks (e.g. bilateral agreements, autonomous arrangements).
  - 20 'High income' or 'upper middle income' partners
    - Saudi Arabia, Kuwait, Bahrain, Qatar, United Arab Emirates, Oman, Brunei Darussalam, Macao,
    - Argentina, Brazil, Cuba, Uruguay, Venezuela; Belarus, Russia, Kazakhstan; Gabon, Libya, Malaysia, Palau

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**General scheme: approximately 2/3 of tariff lines covered**


- provides tariff reductions **without quantitative limitations** according to the sensitivity of products:
  - non-sensitive products enter the EU market duty free
  - the rate for sensitive products is mainly reduced by a flat rate of 3.5 % points or by 30% for specific tariffs.
- some categories of products have been excluded from GSP for China, India, Indonesia, Thailand, Ukraine and Nigeria.

**Special scheme for Least Developed Countries:**  
**"Everything But Arms" initiative (EBA):**

- Grants duty-free access to imports of all products from LDCs without any quantitative restrictions (except to arms and munitions).

**New special GSP+ for vulnerable countries = mostly duty free on 2/3 of tariff lines if the country meets criteria:**

- Ratification and implementation of 27 key international conventions
- A poorly diversified economy.

 *Armenia, Bolivia, Cape Verde, Costa Rica, Ecuador, Georgia, Mongolia, Paraguay, Pakistan and Peru*