

## **THE EUROPEAN PARTNERSHIP AGREEMENT: ITS CORE ELEMENTS, MEANING AND IMPLICATIONS FOR LESOTHO**

Economic Partnership Agreements (EPA) are a scheme to create a free trade area (FTA) between the European Union (EU) and the African and Caribbean and Pacific (ACP) countries. They are a response to continuing criticism that the non-reciprocal and discriminating preferential trade agreements offered by the EU are incompatible with WTO rules. The EPAs are a key element of the Cotonou Agreement signed in 2000, the latest agreement in the history of ACP-EU Development Cooperation and are to take effect as of 2008.

Lesotho and the 27 member states of the EU recently initialed a trade and development agreement, called the Interim EPA. Prior to this agreement being concluded the EU offered a large number of ACP states, including Lesotho, non-reciprocal preferential access to its market place.

### **ESSENTIAL FACTS AT A GLANCE**

- The EPA agreement with Southern African countries has so far been signed by Lesotho, Botswana, Swaziland, Namibia and Mozambique. South Africa has indicated that it would not sign at this stage.
- The EPA textile & clothing RoO are now much more closely aligned with the AGOA textile and clothing RoO
- **Timing:** in order to avoid trade disruption, the EU has provisionally adopted the Council Regulation 1528/2007, generally called Market Access Regulation, applicable from 01 January 2008 to Lesoth and all the ACP countries having initialled WTO-compatible agreements with the EU, and containing all the preferences granted under the EPA negotiations (including more relaxed rules of origin), while the Southern African countries will apply the agreement no later than by 01 July 2008
- The EPA will be **valid indefinitely**, but countries may give six months notice to withdraw from the agreement
- Within 5 years of entry into force of the EPA, the parties will together **review** it with a view to making changes
- EPAs are not only about trade in goods (such as textile products), but also cover areas such as **investment** (for example, investor protection between EU and SADC countries), **trade in services** (for example, provision of financial services) and **government procurement** (rules to facilitate essentially non-discrimination in government contracts). However, there is no final agreement yet on the details of these provisions
- The **outstanding issues** (notably trade in services, investment and government procurement) will continue to be negotiated throughout 2008, with an agreement in place by the end of that year.

## THE EPA HAS THREE CORE ELEMENTS

### 1. Reciprocity

Due to the continuing WTO incompatibility of previous arrangements, the EPAs' key feature is their reciprocity and their non-discriminatory nature. They involve the phased out removal of all trade preferences which have been established between the EU and the ACP countries since 1975 as well as the progressive removal of trade barriers between the partners. In order to fulfill the criterion of being a non-discriminatory agreement, the EPAs are open to all developing countries, thereby effectively terminating the ACP group as the main development partner of the EU.

The establishment of a reciprocal trade agreement confronts the EU with the problem of how to reconcile the special status of the ACP group with the EU's obligations to the WTO. The solution proposed for this dilemma is an agreement which is only as reciprocal as necessary to fulfill WTO criteria. In reality, the ACP countries will have some room to maneuver and to maintain some limited protection of their most vital products. The extent to which trade must be liberalised under the new EPAs is still a widely debated issue and it remains to be seen whether the WTO provisions regulating regional trade agreements will be revised in favour of the EPA scheme at the end of the Doha Round.

### 2. Regionalism

True to the Cotonou principle of *differentiation and regionalisation* the developing countries are encouraged to enter into the EPAs in regional groupings of which SADC is one.

### 3. Special treatment

The new regional grouping established due to the EPA scheme causes the problem of how to reconcile this approach with the previous special treatment of the group of Least Developed Countries (LDCs) among the ACP countries. Currently, 39 of the 77 ACP countries are defined as LDCs by the United Nations. The LDCs constitute a special group among the developing countries and have usually been treated separately.

Therefore, also EPAs will provide special arrangements for this particular group. As opposed to the other ACP countries, the group of LDCs will be invited to reject the EPAs and continue trade relations under the "Everything But Arms" (EBA) regulation. Launched in 2001 by the Council of Ministers, this amendment to the Generalized System of Preferences (GSP) has regulated the trade relations between the EU and the LDCs, granting duty-free access to all products from LDCs without any quantitative restrictions – except to arms and munitions. While this provision facilitates the situation of the LDCs under the new trade scheme, it has also been criticised that the EBA initiative prevents LDCs to open up their markets for EU products within the context of an EPA.

## ITS MEANING AND IMPLICATIONS FOR LESOTHO

This new reciprocal agreement means that both sides will open their markets to the exports of the other, although Lesotho (and other countries) have been given a much longer period of time within which to reduce their import duties for EU products. Lesotho on the other hand will enjoy the immediate scrapping of all import duties for

products exported into the EU from the start of 2008 (with a short transitional period for sugar and rice).

Rules of Origin (RoO) form a critical component of the new EPA preferential trade agreement. They are important to garment producers / exporters as they set the specific conditions under which a product can gain duty-free market access to the EU. In other words, the RoO stipulate how much processing of a product must be undertaken locally in order to benefit from duty-free access to the EU market place.

While some of the EU's RoO have been very strict in the past, especially for textile and clothing exports from Lesotho, new RoO have now been agreed. Under the EPA, Lesotho's clothing and textile exporters may export goods to the 27 EU member states free of import duties or quotas – a saving of up to 12% on most items. However, only goods that are considered as “originating” in Lesotho – by having complied with the applicable RoO – may benefit from the EPA. Goods that do not comply with the relevant RoO will continue being charged import duties by the EU.

In a major departure from the main RoO that have prevailed for almost the past four decades, the EU has now agreed to Lesotho's request, supported with analytical work by the Priority Support Programme, that the RoO for textile and clothing need to change. In effect the EU has now agreed, for textile and clothing products, to a general RoO that implies: ***there should be only one / “single stage” of transformation that takes place locally.*** ‘Single stage’ transformation is a term that refers to the conversion of yarn to fabric, or of fabric to a garment; in other words, one major process must take place locally to qualify the product for duty-free exports to the EU.

As has been the case previously, any textile and clothing products wholly produced in Lesotho are automatically considered as complying with the RoO and therefore have duty-free & quota-free access to the EU market. For clothing, the general rule is now based on the “single-stage” transformation requirement whereby only the making up of the garment must be undertaken locally; in other words, producers may source fabric from anywhere in the world without being disqualified from exporting clothing to the EU free of duty. However, two words of word of caution are needed. First, the fact that South Africa has not yet signed the agreement brings with it uncertainties regarding the **net impact** for Lesotho regarding SACU revenue streams. Second, it is not known how, and to what extent, manufacturers will respond to the EU market.

### **WHAT HAPPENS NEXT?**

The Priority Support Programme, amongst others, is providing assistance in two main areas over the coming months:

On the **demand** side: The EU market has to be broken down and specific countries, and buyers within these, have to be identified and relationships developed between them and their suppliers in Lesotho; and

On the **supply** side: Systems operating at the One Stop Shop have to be developed so that they comply with EU export procedures and those responsible for operating and private sector users (or exporters) need training in these same systems.