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Agricultural trade and the Barcelona Process: is full liberalisation possible?

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Summary

The Barcelona Process has so far avoided full inclusion of agricultural trade in the Euro-Mediterranean Free Trade Area (EMFTA). Given the importance of agriculture in Mediterranean countries, an end to the agricultural exception would give an opportunity for the Southern Mediterranean Countries (SMCs) to reduce the adjustment costs of 'reciprocity' in bilateral trade with the European Union (EU). This paper reviews the measures that constrain the intra-regional agricultural trade. Southern European fears of the Mediterranean integration relate to 'North–South' asymmetries, including imbalances of Common Agricultural Policy (CAP) support among the EU regions. Rural development appears to be compatible with co-operative strategies to remove the political inertia regarding full introduction of agriculture in the Barcelona Process.

Keywords: regional integration, Mediterranean agriculture, preferential trade, rural development

JEL classification: Q17, O19

1. Introduction

Since the mid-1980s, the Mediterranean region has made progress towards a new institutional framework for more liberal agricultural trade. This comes from a growing consensus that economic globalisation is unavoidable for fostering economic development, and is in line with World Trade Organisation (WTO) Agreements. This consensus was behind the integration process launched by 27 countries in Barcelona in November 1995.[1] This is the so-called 'Barcelona Process', aimed at a 'sustainable and balanced economic development with the view of creating an area of shared prosperity, taking into account the different degrees of development' across the Mediterranean region (Barcelona Declaration, 1995). The main economic target of this process is to create the Euro-Mediterranean Free Trade Area (EMFTA) by 2010, although the Barcelona Process has also referred to a number of issues that go beyond trade liberalisation, such as financial aid for co-operation related to regulatory reform, government procurement, and the harmonisation of standards. Thus, with European assistance, the Barcelona Process could potentially lead to deep regional integration.

1 The 15 EU Member States plus 12 Mediterranean countries (Algeria, Morocco, Tunisia, Egypt, Turkey, Lebanon, Jordan, Syria, Israel, Malta, the Palestinian Authority and Cyprus).

The main instruments of the Barcelona Process are the Euro-Mediterranean Agreements (EMAs) negotiated by the European Union (EU) and individual Mediterranean partners, to be complemented by agreements between the partners themselves. By early 2002, EMAs were in force with Tunisia (1998), Morocco (2000), and Israel (2000), and with the Palestinian Authority on an interim basis (1997). Most of the agreements with the remaining partners have been signed and await ratification (Jordan, 1997, and Egypt, Lebanon and Algeria, 2001). Meanwhile, negotiation with Syria is in its final stages. Relations with Cyprus, Malta and Turkey are framed by a first generation of agreements concluded in the 1960s and 1970s providing for custom unions, followed by the status of candidates for EU membership.

Until the second half of the 1990s, most Mediterranean countries already enjoyed non-reciprocal preferential access under the former co-operation protocols with the European Communities. Trade concessions were granted by the EU, on a unilateral basis, for Mediterranean exports of manufactured goods and for a limited number of agricultural products. The new generation of EMAs is taking further steps for trade liberalisation on a bilateral basis. This involves reciprocal liberalisation for industrial trade and gradual liberalisation for agricultural and fisheries products. Thus, reciprocity for industrial trade makes a substantial difference with respect to the earlier generation of co-operation protocols. Agriculture, however, remains an exception. In spite of the deep-integration approach framing the Barcelona Process, trade in agriculture is subject only to weak liberalisation within the present EMAs. This has given rise to serious disputes during the negotiations between the EU and developing Mediterranean countries, which will be called Southern Mediterranean countries (SMCs) hereafter. Most of the EMAs have been delayed by the refusal of formal ratification by certain EU member states that object to some of their agricultural provisions.

Several Euro-Mediterranean Conferences (European Commission, 2000) have emphasised the need to revitalise the Barcelona Process. However, EU member states, especially in Southern Europe, have been reluctant to grant the agricultural debate a higher political profile at top-level meetings. Thus, agriculture appears as a source of 'North–South' conflict between the developed and the developing shores of the Mediterranean basin (Massot, 1999). This paper argues that a more open discussion regarding the costs and benefits of including agriculture in the EMFTA is needed.

This paper discusses whether or not full liberalisation of agricultural trade between the EU and SMCs is an attainable target. After considering the current situation of the Euro-Mediterranean agricultural trade, we first ask why intra-regional trade liberalisation is relevant, taking the Barcelona Declaration as a reference. Second, we assess how far we are from the liberalisation target. Third, we explore the likely economic impact of fully integrating agricultural trade within the EMFTA. Fourth, we discuss European fears of including agriculture in the EMAs. Fifth, we identify possible ways of overcoming the remaining constraints on agricultural trade liberalisation in the Euro-Mediterranean area. The paper draws on the relevant literature, with the hope of establishing where we stand and where further research is needed.

Economists have not completely neglected the study of the EU Mediterranean policy. Since the 1980s, the literature has paid attention to the impact of trade preferences on Mediterranean trade (Pomfret, 1986; Yannopoulos, 1986; Swinbank and Ritson, 1991). Most of the literature on the Euro-Mediterranean partnership refers to the assessment of long-term cost and benefits of the EMFTA derived from anchoring economic reforms engaged by SMCs in the last decades (Lorca and Escribano, 2000). Recent studies have provided insight into the agricultural trade effects of the EMFTA (Grethe and Tangermann, 1998a; Lorca, 2000). However, research remains insufficient to clarify current uncertainties regarding the economic impact of the EMAs on the agricultural sector on both shores of the Mediterranean basin.

Bilateral trade between the EU and the SMCs is largely characterised by asymmetric relationships. Let us consider a group of eight Mediterranean countries (collectively called 'MED8'), including Turkey, Morocco, Tunisia, Egypt, Cyprus, Lebanon, Syria and Jordan. Of course, size matters, and the EU is a more important trading partner for MED8 than the MED8 group is for the EU. Over 50 per cent of total exports and imports of this group of countries is traded with the EU (Annex 1). Dependence on the EU is lower when agricultural trade is considered, but it is still high. The EU is the destination for 42 per cent of MED8 agricultural exports and the source for almost 29 per cent of MED8 agricultural imports. Only 3.6 per cent of total EU agricultural exports go to MED8 and only 7 per cent of total EU agricultural imports originate in MED8. This asymmetry provides part of the explanation of why Mediterranean partners are not at the top of the EU agenda as far as trade negotiations are concerned.

On the other hand, the EU's political stance could also be influenced by the strong market competition for some Mediterranean products that are typical of the region. SMC exports to the EU show a marked specialisation in Mediterranean products. In the period 1997–1999, 42.7 per cent of Mediterranean countries' exports to the EU was fresh fruit and vegetables, 12.9 per cent was processed horticultural products, 7.7 per cent was fats and oils, and cotton exports represented 5.8 per cent (see Annex 2). In fact, several Mediterranean countries show a very similar composition of agricultural exports mainly based on 'speciality products' such as fresh fruit and vegetables, nuts, and preparations of these products. Turkey, Israel, and Morocco are among the main suppliers to the EU of these typical Mediterranean products and compete directly with Southern European countries in sensitive products such as fresh fruit and vegetables, citrus products, tomatoes and olive oil. Whereas Southern European farmers fear competition from SMCs, many SMCs feel that the provisions of the Common Agricultural Policy (CAP) applied to some of these products clearly restrict their opportunities to export to the EU.

2. Mediterranean interests in agricultural trade liberalisation

The Barcelona Declaration (1995) set the basis for considering agricultural trade as an exception to the liberalisation programme. This Declaration states: 'Taking as a starting point traditional trade flows, and as far as the various agricultural policies allow and with due respect to the results achieved within the GATT negotiations, trade in agricultural products will be progressively liberalised through reciprocal preferential access among parties, . . . ' The key words of the paragraph are 'traditional' and 'progressively'. Together we can take this to mean that agricultural trade might not be completely liberalised once the EMFTA is completed. In fact, under the EMAs, the EU has not offered significant new concessions to SMCs in terms of market access for their agricultural exports (Togan, 1998). By contrast, at the end of a fixed schedule for phasing out tariffs on EU manufactured products, these will benefit from duty-free access to Mediterranean markets. Consequently, whereas agricultural trade is implicitly constrained to 'traditional flows', trade liberalisation for manufactured products will be reciprocal.

The EMAs are usually seen as part of the programme for long-term structural reforms needed to encourage private sector exports and orient SMCs towards global markets (Hoekman and Djankov, 1996). The aim of the EMAs is modernisation of the SMCs, assisted by technical and financial aid from the EU. Success in the EMFTA is crucial, given the existing North–South asymmetries in the Mediterranean region: the GDP per capita ratio is 18.5 between France and Morocco, 15 between Italy and Egypt, and 9 between Spain and Algeria (see CIHEAM, 2001). However, the potential benefits of the reform process could be undermined unless the 'progressive liberalisation' of agriculture is speeded up.

But why should the SMCs be interested in the full inclusion of agricultural trade in the Barcelona Process? We can refer here to four challenges for SMCs, all of them closely linked to the risks involved in the EMFTA: (i) adjustment costs; (ii) fiscal losses; (iii) 'hub and spoke' effects; (iv) rural poverty.

(i) The promised modernisation will not prevent the relatively high adjustment costs likely to face the industrial sector in SMCs. The agro-food industry will be most affected by the increasing openness of SMC economies, given the fact that it is one of the sectors with the highest tariffs (Augier and Gasoriek, 2001). As a result of trade liberalisation, consumers in SMCs will probably increase their consumption of imported European goods, at least until domestic industry reacts with increased efficiency and quality. Further trade imbalances and certain transition costs may take place in the, possibly painful, reallocation of resources and industrial adjustment.

(ii) The EMFTA will entail a fall in import tariff revenues for SMCs, particularly for those countries with higher import dependence on EU products. Abed (1998) reported that import taxes on the exchanges with the EU during 1994–1996 accounted for significant shares of fiscal revenue in most SMCs: up to 19.2 per cent in Algeria, 7.9 per cent in Egypt, 12.1 per cent in Jordan, 28.8 per cent in Lebanon, 10.3 per cent in Morocco and 15.9 per cent in Tunisia.

(iii) Another challenge is the possible 'verticalisation' of trade relations and the emergence of a 'hub and spoke' system in the Mediterranean region, in which the EU would be the hub and the individual Mediterranean countries the spokes. In the previous generation of co-operation protocols, a significant part of Foreign Direct Investment (FDI) in some SMCs was linked to the unilateral trade preferences that the EU granted to these countries. In the EMFTA context, European investors might not find it appealing to establish in SMCs unless the EMAs (and the related domestic economic reforms) are able to provide sufficient incentives for increased FDI. Given the importance of agriculture in most of the region, excluding agricultural trade from the reciprocal concessions would mean reducing the opportunities for private investment to take advantage of the Euro-Mediterranean partnership.

(iv) Almost three-quarters of the poor in SMCs live in rural areas (Bishay, 1998). Alleviating rural poverty is increasingly understood as essential for economic and social development (Khan, 2000). Therefore, rural development should appear at the top of the agenda concerning the rules governing globalisation. It is a matter of determining the priorities of policy objectives. Without underestimating the advantages of a diversified production base in rural economies, appropriate agricultural incentives are still crucial for any national strategy on rural development, especially for developing countries.

The EMFTA is consistent with open regionalism where the free trade area would stimulate modernisation and efficiency in SMCs. There is hope that trade creation will exceed trade diversion in the Euro-Mediterranean area (Chaherli, 1999). However, according to *ex ante* quantitative simulations (Guesquiere, 1998; Boughanmi and Buccola, 2000) static welfare benefits from the EMFTA are not likely to be crucial for SMCs. This leads to the almost unanimous view that the EMAs can be justified only by the non-traditional and non-static macroeconomic effects of regional integration extending beyond simple tariff elimination for intra-regional trade to a full integration of rules (Zarrouk and Zallio, 2000). Most benefits are expected in the long term as the result of the economic reforms encouraged by the EMAs. From a political viewpoint, all SMCs might demand more reciprocity with the EU, including improved EU market access for agricultural products, to justify the measures undertaken to open domestic markets to industrial imports. Some researchers have referred to the agricultural sector as a source of comparative advantages in SMCs (Yeats, 1996; Haddad, 2000). This suggests that agricultural export growth could help to lessen the transition costs that are faced under the EMA by other sectors with lower comparative advantage.

Of course, increased market access does not guarantee development in SMCs. The way trade liberalisation fosters development depends to a large extent on the institutional capacity of the countries that are opening to globalisation (Kherallah and Kirsten, 2001). Domestic policies are key to being able to exploit opportunities of access to capital and technology, and to counteract some of the negative impact of trade liberalisation on income distribution. However, within the context of a trade-creating EMFTA, one wonders whether it is acceptable or not for SMCs to give up new opportunities for their agricultural exports.

3. How far are we from full liberalisation?

EMAs signed with Mediterranean partners have tended to exclude 'sensitive' agricultural products from the liberalisation schedule.[2] All EMAs include preferential agricultural trade in the form of tariff concessions, with or without quantitative limits. Agricultural preferences granted by the EU are generally limited to fruit and vegetables, flowers, spices, wine, olive oil, durum wheat, fish and some meats, and certain processed products. For continental products such as meat, dairy products and cereals, the EU applies most favoured nation (MFN) tariffs, which are prohibitive in many cases. Current concessions are still far from full liberalisation, as a result of the impact of largely non-tariff measures: tariff-rate quotas (TRQs), entry price system and other trade barriers.

3.1. Quantitative constraints and TRQs

Tariff concessions are unconstrained for many products, but reductions are limited to negotiated quantities for a number of 'sensitive' products.[3] Published work casts serious doubt on the positive impact of EU tariff concessions on SMC exports (Alvarez-Coque and Bautista, 1994; Grethe and Tangermann, 2000). First, concessions tend to be more generous for products and seasons in which EU imports do not compete directly with domestic production. Second, tariff preferences are very often granted under quantitative limits in the form of TRQ or reference quantities (RQ). Third, when TRQs are established, their administration becomes a problem. This is one of the most contentious issues in current multilateral trade negotiations (Josling and Tangermann, 1999; IATRC, 2001; Abbott, 2002). Tariff concessions create a quota rent whose distribution between the exporter and the importer depends on the method adopted to allocate import licences. If

2 Agricultural flows represent around 14.8 per cent of total MED8 exports to the EU. This provides some margin for considering sensitive agricultural products within the 10 per cent of trade that can be excluded in accordance with article XXIV of the 1994 GATT. This is consistent with the Barcelona Declaration's reference to a 'progressive liberalisation' of agricultural trade between the associated countries, but not to a 'total liberalisation'.

3 The formal structure in all EMAs is very similar, although they may differ in the specific quantitative parameters of trade concessions in agriculture (tariff reduction, products covered and quantitative limits). Annex 3 provides examples of products for which tariff concessions are subjected to quantitative limits.

the licences are issued to European importers, as is normally the case, the exporting country can lose part of the rent. For some products, the issuing of import licences to manage the TRQ has been prevented by an agreement in the form of an Exchange of Letters. In the case of tomatoes, the EU and Morocco agreed that Morocco would accept to export no more than the agreed tariff quotas. The European Commission reserved the right to issue import licences if the export flows exceeded the agreed quota. The system was tested in October 1999 when the tomato exports from Morocco to the EU exceeded the amount agreed for that month by 190 per cent. The Commission then issued import licences. Import certificates acted not only to control whether or not the MFN tariff was applied, but also as a real non-trade barrier. During January the Moroccan tomato exports dropped dramatically and 1 month later the voluntary export control system was re-established. Thus, the European Commission proved to have effective means to limit imports when market perturbations were felt in the EU market. Another illustrative case refers to that of Syrian cotton yarn exports to the EU. The surge in Syrian exports of cotton yarn to the EU market from €7 million in 1995–1997 to €19 million in 1997–1999 was attributed by the European Commission to the drop in Syrian export prices over the same period. In April 2001, the European Commission introduced import licences as a monitoring system, provoking a sharp drop in exports. The fact that Syria was not a WTO member facilitated this unilateral action. As a result of the TRQ administration, it is not clear which part of the rent really flows to the exporting country. Nor is it possible to guarantee the predictability of the trade rules. It is not a matter of protection, but rather one of an apparent lack of transparency.

3.2. Entry prices

The entry price system applies to a group of fruits and vegetables considered particularly sensitive by the EU. It guarantees that imports are not sold on EU markets below a minimum entry price. According to Swinbank and Ritson (1995), the system is in conflict with the spirit of tariffication, being the 'lesser of two evils' offered to the EU's trading partners. Third countries apparently accepted this approach as a *quid pro quo* for the continuing opportunity to export to the EU at high prices without facing high tariffs. Although to a lesser extent than the old reference-price system, the entry price system continues to penalise low-cost suppliers (Grethe and Tangermann, 1998b). On the other hand, the entry price system seems to offer opportunities for circumvention by importers, either legally or illegally (De Gorter and Martin, 1998). In practice, importers tend to declare a CIF price above the entry price, intending not to pay any additional charge. Much of the fruit and vegetable trade is on consignment and no agreed CIF price exists when the import is carried out. To simplify the system, import prices are usually monitored at the wholesale EU markets, where prices can be registered by origin. All these elements contribute to increasing the administrative burden of the system. Significant reductions of entry prices for limited quantities of some products have been negotiated and agreed with Morocco, Cyprus, Egypt and Israel, creating a quota rent. However, the benefit must be qualified by the fact that entry prices faced by non-preferential exporters have been reduced in line with the EU's WTO commitments.

3.3. Rules of origin and agricultural component

Other EMA trade issues relate to rules of origin and tariffs on food products. Published research has underestimated both areas, although these measures surely affect trade in textiles and in certain agro-food products (cereal derivatives and dairy products), and imply constraints on the vertical diversification of SMC exports. Rules of origin have, of course, their logic, which is to avoid 'arbitraging', i.e. the preferred country re-exporting an imported commodity to the country granting the preference. However, the EU has very strict rules of origin that define degrees of 'sufficient transformation' to be met for a product to be declared as 'originated in country X'. The cumulation of rules of origin allows that some processing operations carried out in any given country of the region are counted as local content. In the context of the EMFTA, three kinds of cumulation are used—full cumulation, diagonal cumulation, and bilateral cumulation—full cumulation being the most attractive for preferential countries. To benefit from preferential treatment it would be enough that all the processing operations carried out in the countries of the region constitute a sufficient transformation. However, the EU has been reluctant to take this approach, which has been permitted only in the case of North African countries. Regional full cumulation to the Near East countries is conditioned by the conclusion of the free trade area among these countries (CGP, 2000). As far as food products are concerned, the EMAs maintain the so-called 'agricultural component' of the tariff for processed products, and most of the tariff concessions are granted only for the industrial component. Almost no 'basic agricultural products' receive any preferential treatment because these are sensitive products in the EU (dairy products, cereals, rice and sugar). Consequently, a considerable basic component of the tariff is imposed on processed imports and it is not clear to what extent this estimated component creates tariff escalation, although it is perceived by SMCs as a real obstacle to export diversification towards processed foods.

Thus, SMCs' agricultural exports to the EU are still constrained by barriers other than tariffs. Trade preferences granted by the EMAs tend to freeze market shares in line with traditional trade flows, and there is no leeway for real exploitation of the export potential in key products such as citrus, tomatoes and olive oil. The management of import measures usually involves 'red tape' that reduces transparency and normally acts against the exporting country, taking into account that horticultural trade involves perishable products. Trade concessions appear to make room for imports, but the actual management of TRQs can easily neutralise the market access theoretically improved by tariff preferences. Even with relatively small tariffs, the introduction of a licensing system can become a psychological barrier for exporting countries.

Some of these barriers could be phased out under the current WTO negotiations. In one sense, SMCs may gain from the multilateral liberalisation while, at the same time, they pursue a regional integration strategy. It is true that the extension of multilateral tariff concessions under the WTO negotiations will reduce the existing preference margins for SMCs. Grethe and Tangermann (1998a) have estimated that the Uruguay Round (UR) commitments reduced the preference margin by 17 per cent for SMCs as a whole under the previous co-operation protocols. However, a comprehensive multilateral reform of horticultural trade will also benefit SMC producers, given the increased transparency in TRQ administration and the possible dismantling of the entry price system.[4]

Of course, trade measures are not static and they may change as the EMAs are renegotiated, as happened in the recent reviews for Tunisia (2000) and Morocco (2001). Nevertheless, the EU has been reluctant to extend the scope of concessions in the various reviews of the EMAs, perhaps because individual demands might spread across all SMCs and erode the community preference even more. As a result, there is still a long way to go before agricultural trade is fully included in the EMFTA.

4. Is trade liberalisation worth while?

Here we consider the potential benefits for SMC agricultural exports of a wider market access in the EU. If these gains were high, then the claim for including agriculture in the Barcelona agenda would be justified. We first consider the impact on trade flows and then look at other potential effects on FDI and the environment.

Research findings suggest that static gains for SMCs from EU tariff preferences granted under the current EMAs are fairly low. Tangermann (1997) and Grethe and Tangermann (1998a) calculated the preference margin for Mediterranean countries due to the EMAs. Preference margins calculated for Israel, Jordan, Morocco, Palestine and Tunisia under the respective EMA are 5.1, 4.8, 9.3, 4.6 and 9.9 per cent of agricultural export values to the EU. García-Alvarez-Coque (2001) applied the same approach to estimate a preference margin of 0.5 per cent of Syrian total agricultural export value.

One drawback of this method is that calculations are static; thus, they do not reflect the potential export growth that would result from full tariff liberalisation. This approach may be justified when trade flows are subject to strict quantitative limits. This may or may not be the case, although these calculations provide estimates based on 'traditional flows', which yield few gains for preferential suppliers. In addition, these calculations do not supply a picture of the potential structure of exports under full liberalisation (absence of quantitative limits). To realise export gains above such estimates, it is crucial

4 Erosion in preferences will also be determined by other concessions granted by the EU, such as the Generalized System of Preferences and the Lomé/Cotonou Agreement. This gives more weight to those who, in SMCs, argue in favour of comprehensive multilateral liberalisation. See Yamazaki (1996) for more details on the quantification of the erosion of preferences.

that TRQs do not constrain exports. Under this unconstrained assumption, Lorca (2000) indicates that the elimination of EU border measures on SMC agricultural exports, over a 5 year period, would yield significant gains for SMCs. Estimated export gains represent an increase of SMC exports in terms of GDP of around 1.4 per cent for Morocco, 2.3 per cent for Turkey, 3.3 per cent for Egypt and 0.4 per cent for Tunisia. These percentages may appear small, but if compared with the net official aid to development they are high and would justify the political stance that 'trade' would be better than 'aid' as a tool for Euro-Mediterranean partnership. The results are based on a quantitative model that makes use of assumed estimates of equivalent rates of protection (including the effect of non-trade barriers) and export-price elasticities.

Following Lorca's results, EU imports of sensitive products would increase by 11 per cent. This does not seem to be dramatic over a 5 year period. In fact, the European Commission does not consider agricultural trade concessions to Mediterranean countries as a serious threat to European farmers (European Commission, 1997). Among 11 Mediterranean partners, only Turkey, Morocco and Israel appear as significant actors. For some horticultural products, seasonality supplies 'windows' for the EU market. These 'windows' depend not only on the availability of local production but also on the operation of tariffs and entry prices, which vary according to the season.

Non-price competition and market concentration in horticultural markets further impede an assessment of trade liberalisation for these products. Although farm-gate prices in SMCs are below those in EU countries for a number of fruit and vegetables, quality specifications and high marketing costs (including logistics, post-harvest operations, transport, etc.) still hinder their competitiveness. Ten retail holdings represent 36 per cent of food retail markets in Europe. Modern European distributors increasingly request shippers to accept certain specifications (grades, packing, environmental procedures, time of delivery, etc). Some large distribution firms in Europe are establishing certification (e.g. ISO 9002), which involves control procedures (Montigaud and Berger, 1997). Therefore, the market itself represents a significant challenge for horticultural exports, even in the absence of traditional trade barriers. Only a few countries, not necessarily those most endowed with favourable climatic conditions and abundant labour, are able to export the quality products demanded by high-income consumers. Many of the constraints on SMC exports are supply related. Thus, market access becomes a necessary, but seemingly insufficient, condition for improving export performance.

Although the link between trade measures and domestic prices in horticultural markets requires further research, it is unlikely that fully open market access for SMCs will significantly boost SMC exports to the EU, at least in the short term. Although perhaps disappointing for SMCs, it is probably good news for Southern European farmers. However, given the potential gains for SMC agricultural exports, their positive contribution to the success of the Barcelona Process should not be neglected. An initial condition for exploiting such potential gains is to obtain greater access within the EMA framework. This would send a message of confidence to trading agents in SMCs. This message would encourage efforts to improve quality and to adapt to European market demands. If this message is understood and backed by the EU with appropriate support for structural reforms, potential gains might become a reality.

One uncertain area related to the potential benefits from the EMFTA is FDI. At present, there is considerable scope for improving FDI in the agro-food economy of the region. A recent survey of regional integration concluded that there is little evidence establishing the link between FDI and regional integration (Panagariya, 2000). Constraints on FDI include restrictive policies regarding foreign capital and transaction costs related to financial services, transport, administrative burdens and general business climate (Alessandrini, 2000; Reiffers and Tourret, 2000). However, dynamic gains from FDI are expected in the long term, especially from the overlapping of the Euro-Mediterranean strategy with the Arab Free Trade Area (AFTA). Both regional processes can be seen as compatible for creating adequate conditions for FDI. The intra-Arab integration could effectively build up a regional trade pattern, which could help to attract European investment interested in supplying the area.[5] Again, increased EU market access would enhance incentives for potential foreign investors in the countries of the region. In the long term, FDI would improve the business climate and remove domestic constraints on the agro-food sector.

Environmental concerns represent another visible element of Mediterranean integration.[6] So far little has been done to assess the potential environmental effects of the EMAs (Akesbi and Garcia-Alvarez-Coque, 2001b). From the viewpoint of the environment, the EMAs should help to fight poverty and, indirectly, resource degradation. However, assuming optimistic prospects for exports to the EU, the increase in high-value crops will have an ambiguous impact on the environment. On the one hand, biological control and the EU's environmental and quality standards might affect Mediterranean agricultural sustainability positively. On the other, two main risks arise from the growth of horticultural production. The first is the extensive use of plastics. The second relates to water needs. As the demand for water grows, under current trends some countries of the region are expected to experience chronic water shortages within the next 20 years (Hamdy and Lacirignola, 1999). Whether water availability will become a limiting factor

5 There is also the perception that trade between SMCs (what can be called 'South–South' trade) has to develop more from its very low starting level to counterbalance their still strong trade dependence on the EU. Levels of intra-trade in the Arab region remain around 5 per cent (Zarrouk, 1998).

6 The EMAs contain a generic article referring to co-operation on a series of environmental issues. Failure to address environmental issues through regulatory harmonisation will leave future trade open to conflict. Harmonisation of environmental standards will require a great deal of co-operation because of the large number of countries involved in the process and the great disparity between existing regulatory systems.

on export crops remains questionable, given the possibilities for new production methods and modern irrigation systems (Akesbi, 1999).

5. European fears

The fact that EU preferences focus on selected Mediterranean products leads Southern European farmers to the paradoxical feeling that the EMAs undermine the principle of community preference. Fears about the EMAs arise in European horticultural regions that are under competitive pressure because of their production similarities with SMCs. Such fears are not surprising in spite of qualification on the trade impact of removing EU barriers. When the EMFTA is at issue, Southern European farmers usually pose two types of qualification. The first consists of the demand for fair play in international competition. The second argument is of a more domestic nature and relates to the possible discrimination against Southern European products by the CAP provisions.

As regards the first argument, in the EU producing regions there is a widespread belief that trade liberalisation with developing countries may impoverish EU farmers. This fear reduces the enthusiasm of EU negotiators to open trade for locally produced goods. Labour concerns are an argument frequently quoted by EU farm lobbies. Proximity to European markets and low labour costs suggest that the SMCs should be the natural base for many labour-intensive horticultural activities. The EU has been prone to support the implementation of core labour standards at a global level. The Commission has also suggested that core labour standards should have their place in bilateral agreements between Europe and third countries in the form of social incentive schemes (European Commission, 2001a). One drawback to this approach is that references to levelling the playing field for trade might result in non-co-operative stances, even among EU member states. This was indicated by the general opinion voiced at the Euro-Mediterranean Conference on Agriculture held in Strasbourg in June 2001, which favoured 'managed liberalisation'.[7] However, a typical opinion among trade economists is that foreign trade has not been a significant source of unemployment in OECD countries, which is determined much more by technical change in manufacturing and agriculture (Krugman, 1995). As far as fruit and vegetables are concerned, market developments are not just determined by labour costs, as shown by the fact that industrial economies also play a significant role in horticultural trade. International competitiveness is influenced by product differentiation, marketing, harvest and post-harvest technologies, facilities and transport. On the other hand, freer trade in the

7 See, for example, the opinion expressed by Friedrich-Wilhelm Graefe zu Baringdorf, Chair of the European Parliament's Agriculture and Rural Development Committee, who argued in favour of 'ensuring that the EU's own markets are not flooded with cheap products from non-EU Mediterranean countries' (see http://www.europarl.eu.int/conferences/euromed/agri/20010614/feedback/article_ euromed.pdf).

Mediterranean area will open new opportunities for European operators to complete their supplies by importing off-season fruits and vegetables. This 'delocalisation' process should not necessarily be job destructive, as European firms benefit from the reallocation of their cropping areas to higher value-added activities. This is illustrated by the experience of some European co-operatives, especially in the citrus and fresh fruit industries, which have been able to maintain regular and assorted supplies by investing in SMCs while maintaining their activity in their region of origin.

Immigration to Southern European countries adds a new element to the 'North–South' debate. In Southern Europe, horticultural costs have been kept down by employing immigrant labour, especially in the fruit-picking season. The impact of labour costs on horticultural areas deserves further study by agricultural economists, given that comparative advantages in the most developed regions are moving from unskilled labour intensive activities to skilled labour and technology intensive ones. The European Commission and EU member states could support co-operative research to identify the scope for the horticultural economy in each Mediterranean country.

The second political qualification with respect to the inclusion of agriculture in the EMFTA relates to the imbalance of agricultural support among the EU regions. Mediterranean crops in Europe extend over Southern Europe, mainly in coastal regions, although comparable rates of horticultural production are also recorded for some regions in the Netherlands, France and Germany. Regional effects of trade liberalisation could be locally significant, although the income loss in specific regions has not been properly quantified. Studies of the regional distribution of CAP assistance to agriculture (e.g. European Commission, 2001b; García-Alvarez-Coque and Wieck, 2001) indicate that the Mediterranean coastal areas are among the EU regions with the lowest rates of both budgetary and total support. Although EU border protection levels for olive oil and certain fruits and vegetables are still significant, Southern European farmers blame the CAP for granting much more direct support to Northern European producers. Horticultural products, which account for 16 per cent of the final agricultural production, receive only 3.5 per cent of the total CAP expenditure. Cereals, by contrast, make up 12 per cent of agricultural final production and receive almost 40 per cent of the total budget. This overall imbalance has been intensified by Agenda 2000 proposals, as a result of the implicit principle of 'financial neutrality' that is adopted every time the CAP reforms Mediterranean crops. From the Southern European perspective, it is difficult to understand why the 'continental' farmers are compensated whenever institutional prices go down, as has been the case with CAP reforms since the 1990s. Of course, there is a political logic for this asymmetry. The horticultural sector in Europe is not considered a truly problematic sector, and it is widely accepted that farms in Southern Europe are less vulnerable to external pressures, possibly because of the presence of part-time farming. However, the 'prisoner's dilemma' explains why Southern European regions are not very keen on co-operative solutions such as full inclusion of agriculture in the EMAs.

By contrast, SMCs may also find allies in Europe, in particular on three fronts: (i) the trading sector (e.g. EUCOFEL, European Trading Federation) and trading authorities, which recognise the commercial gains from a regional integration covering manufactured as well as agricultural products; (ii) the European Parliament and a significant number of European politicians who recognise that only an area of shared prosperity in the Mediterranean can guarantee stability and development; (iii) in Northern Europe, where competing products are produced less.

These liberal views can be contradicted when economic interests are involved. Several Northern European governments defend border protection even when it might constitute a constraint to SMC export growth. These contradictions have been illustrated by the Dutch, German and Belgian concerns regarding the effects on their producers of increased Moroccan and Egyptian exports to Europe of cut flowers, tomatoes, and potatoes. It is also shown by the imbalance of support between 'continental' and 'Mediterranean' products, referred to above.

There is also the question of possible tradability of concessions for different products. Higher concessions by SMCs for 'continental' products imported from the EU might be exchanged for higher EU concessions for 'Mediterranean' products. Several Mediterranean countries are often cited as examples of growing dependence on food imports. FAO trade data indicate an annual import growth rate in cereal imports of 2 per cent for the West Asia–North African region during the 1990s (FAO, 2000). EU exports to SMCs are already considerable for sugar (€360 million in 1999), cereals (€715 million), and dairy products (€609 million). MFN tariffs on agricultural imports are still significant in most SMCs (Chaherli and El Said, 2000) although market access for EU agricultural exports to SMCs is improving through preferential tariffs without limits (Jordan) or through TRQs (e.g. Morocco and Tunisia). The EU could ask for a further opening-up of Mediterranean import markets for EU grains and other food products (livestock, beef, dairy products, sugar and processed products). However, land productivity and cost differences between the EU and SMCs for continental products (CIHEAM, 2001) suggest that greater market access for EU exports to SMC should be managed with care.[8] In addition, the pattern of specialisation of many agricultural regions implies that the economic impact of agricultural trade liberalisation is locally concentrated in specific territories.[9] From the political point of

8 Tariff liberalisation can proceed with different rates of abolition, according to the sensitivity of the products, e.g. the Tunisian agreement had three lists for industrial crops and one list for agricultural products, keeping substantial custom duties for several products. The maximum transition period for tariff liberalisation is up to 12 years after the entry in force of the EMA.

9 According to the REGIO database, Mediterranean crops account for over 50 per cent of the final agricultural output in 20 EU regions (18 in Southern Europe). By contrast, livestock production accounts for over 50 per cent of the final agricultural output in 52 EU regions (four in Southern Europe).

view, there is little room for tradability of concessions, which would have been easier with a more diversified production structure among rural regions in Europe. In other words, the tradability of concessions for the import and export side of the 'negotiation equation' seems questionable.

6. Is there a way out?

Agriculture in the EMAs has frequently received an *ad hoc* treatment in the Euro-Mediterranean negotiations. Preferences tend to be more generous for such products and countries where the Commission does not anticipate a real danger of perturbing EU markets. Although the Euro-Mediterranean Conferences usually restate the commitment to trade liberalisation, the issue of agriculture has not been granted a high profile at top-level meetings. A full discussion about how to manage the transition to more open agricultural markets in the Mediterranean has clearly been avoided.

Apparently, the game of Mediterranean agricultural integration has few co-operative solutions. Not including agricultural trade in the EMFTA would mean that benefits from EMAs come only from the dynamic, long-term impact derived from economic reforms and investment. On the other hand is the risk of increased competition with specialised Southern European regions, which are not exactly in the richest areas of Europe.

Three possible developments could contribute to narrowing opposing positions about the appropriate rate of progressive liberalisation of agricultural trade in the EMFTA provisions. The first is the possible expansion of the domestic EU market for horticultural products that would probably be the result of the EU enlargement to Central and Eastern European countries. For example, Poland is now one of the main destinations for Spanish citrus exports, becoming an outlet for some of the most price-sensitive varieties and grades. An enlarged EU market might reduce the objections of those who today oppose wider market access to SMC horticultural and olive oil exports.

A second development would be a comprehensive CAP reform that makes it consistent with the 'shared prosperity' approach of the Barcelona Declaration. There is some confusion about the future role of governments in rural development. The CAP should work to break the 'North–South' conflict of interests. An acceleration of the CAP reform to enhance rural development in a compatible way with freer trade could be a desirable path. Southern European farmers might be in favour of CAP reform if the reform had the indirect effect of rebalancing the support between the North and the South of the EU. The EU horticultural and wine sectors have supplied pilot fields for policy innovations consistent with the rural development approach. For olive oil, a definitive reform will be again discussed by 2003 and will probably deal with a move from direct support to quality and environmental policies. Therefore, rural development might find allies in EU Mediterranean farmers. At present, rural development policies seem constrained by the inertia of the current CAP. The EU's direct payments under Agenda 2000 complete the picture of a distorted regional market in the Mediterranean region.[10] The external pressure on the CAP, for example from current WTO negotiations, will probably contribute in the long term to policies aimed at environmental concerns, rural development and small farmers. However, it is unlikely that dramatic CAP changes will take place over the Agenda 2000 time span.

A third development, probably linked to the second, would be the allocation of extra financial resources to facilitate the transition to a more open trading environment in Mediterranean regions. One unrealistic scenario would be an increase in the CAP budget. Another, less unrealistic, would be the reallocation of more CAP resources to rural development. Considering the potential benefits of the EMFTA for the whole economy of the participant countries, the process could envisage compensatory policies in specific areas along both Mediterranean shores. This idea is not new in the context of EU integration. It was behind the Integrated Mediterranean Programmes, before the Southern Enlargement, in the early 1980s and is currently suggested by some researchers. Thus, Lorca (2000) refers to the interest of a 'Mediterranean agricultural pact' that would compensate potential losers from the EMFTA in Southern EU countries.

Such an adjustment programme could reach both sides of the Mediterranean basin. Regnault (1997) and Akesbi (1999) point to an agricultural policy beyond the limits of the EU borders and propose the setting-up of a Euro-Mediterranean Fund of 'péréquation agricole'. The Agricultural Ministries of CIHEAM[11] Member States, at their third meeting in June 2001, proposed a Mediterranean programme for rural development, with the characteristics of the *Leader* programme, to be implemented in EU and non-EU Mediterranean countries (CIHEAM, 2001). Any of these policies would take the form of 'green box' policies, in the WTO terminology, and would become a complement to the Euro-Mediterranean economic space.

Moreover, the existing co-operation facility within the Barcelona Process, the MEDA programme, is not designed to fulfil the role of a structural fund, and it competes for funds with other financial priorities such as Eastern Enlargement. It is true that complicated administrative procedures for implementing projects led to a low disbursement rate under the MEDA programme. There is also a question about the ability of recipient countries to absorb co-operation funds. However, this should not be an excuse for allocating an unreasonably low amount of resources to 12 Mediterranean countries (€5.35 billion for 2000–2006), especially if we compare this amount with the funds foreseen for the Eastern Enlargement (around €28 billion for 10 countries between 2004 and 2006 according to the Commission proposal in January 2002). Extra resources for the Mediterranean agricultural package could eventually be conditioned to the rate of absorption of previous funds and to the direction and rate of economic reforms.

10 Diversification of rural economies and gains from bilateral trade liberalisation for SMCs will depend, to a large extent, on the pace of phasing-out export subsidies and probably the 'blue box' direct payments by the EU, marked by WTO talks.

11 Centre International de Hautes Études Agronomiques Méditerranéennes.

Two research questions might attract further interest from agricultural economists around the EMFTA. The first refers to the trade impact of the EMFTA on the EU agricultural sector. Although this paper has suggested that the direct impact of including agriculture in the free trade provisions would not be dramatic, there could be significant local effects on specific products, seasons and zones. An assessment of these local effects is beyond the scope of this paper, but represents an important task for research. The second question relates to the impact of trade liberalisation on the whole agro-food system, including services and manufacturing linked to agricultural production.[12] Further research might shed some light on the extent to which these related activities would expand with the delocalisation of investment to SMCs.

The question also arises of whether a common approach for Mediterranean agricultural regions is possible. Whatever this approach may be, it should respect four ideas. First, the Euro-Mediterranean strategy cannot be completed without sufficient coverage of the products that could be potentially integrated into the trading arrangement, that is, without agricultural trade. Second, agricultural negotiations in the EMFTA should explicitly recognise the differences in development levels between the Northern and Southern shores of the Mediterranean basin. In a sense, this would involve accepting the concept of special and differential treatment (as in the WTO negotiations), which could lead to a higher degree of flexibility in the implementation of the commitments for trade liberalisation for developing Mediterranean countries. As in the spirit of the Barcelona Declaration, negotiations on agriculture should effectively take account of SMC development needs, including food security and rural development. Third, new economic approaches should inform agribusiness and policy-makers on the most appropriate way of dealing with EU markets for Mediterranean products, which are far from perfectly competitive. This implies that adequate agricultural policies should prepare farmers to adapt to a more demanding market, controlled to a great extent by the large distribution concerns. Finally, full consideration of agriculture in the Barcelona Process would require going beyond the present pragmatism of agricultural negotiations to the realms of 'high politics'. From this perspective, there is a danger that the Barcelona Process will lose impetus while the EU is particularly active on other regional fronts, such as the Eastern Enlargement and the 'Everything But Arms' agreement.

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12 The value added of services and industrial inputs connected with the horticultural production in the Almeria province of Spain alone reaches €300 million per year.

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Annex 1. Total trade and trade with the EU of selected Mediterranean countries; annual averages for 1997–1999

	Total exports and exports to the EU (in millions of Euros)								
	Turkey	Morocco	Tunisia	Egypt	Cyprus	Lebanon	Syria	Jordan	MED8
Total exports to the world (FAO), a	23,143	4,043	4,906	3,458	1,099	632	3,453	1,618	42,353
Total exports to the EU (Eurostat), b	11,872	4,750	4,017	2,637	373	154	2,027	174	26,002
b:a (%)	51.3	117.5	81.9	76.3	33.9	24.3	58.7	10.8	61.4
Agricultural exports to the world (FAO), c	5,206	832	530	442	740	144	1.037	139	9,070
Agricultural exports to the EU (Eurostat) d	1,990	992	366	202	89	25	160	12	3,836
d:c (%)	38.2	119.3	69.1	45.6	12.0	17.0	15.4	9.0	42.3
	Total imports and imports from the EU (in millions of Euros)								
	Turkey	Morocco	Tunisia	Egypt	Cyprus	Lebanon	Syria	Jordan	MED8
Total imports from the world (FAO), a	42,905	6,923	6,923	11,649	3,263	6,578	3,552	3,614	85,406
Total imports from the EU (Eurostat), b	22,377	5,329	5,285	6,758	1,959	3,095	1,354	1,200	47,357
b:a (%)	52.2	77.0	76.3	58.0	60.0	47.1	38.1	33.2	55.4
Agricultural imports from the world (FAO), c	3,609	1,262	802	3,031	860	984	747	730	12,025
Agricultural imports from the EU (Eurostat), d	1,067	341	319	680	246	436	190	147	3,426
d:c (%)	29.6	27.0	39.8	22.4	28.6	44.3	25.4	20.1	28.5

Sources: FAOSTAT for total trade and total agricultural trade; Eurostat for trade with the EU; author's calculations. FAO figures for total trade and Eurostat figures for trade with the EU are not exactly comparable and sometimes inconsistent, as the reporting sources are different.

Annex 2. Composition of Mediterranean countries' agricultural export value to the EU[a]

Products	% of average value 1997–1999
Live animals	0.1
Meat and edible meat offal	0.0
Fish and seafood	10.1
Dairy products and eggs	0.4
Other products of animal origin	2.4
Live trees and other plants	0.7
Edible vegetables and roots	11.5
Edible fruit and nuts	31.2
Coffee, tea, and spices	0.9
Cereals	0.5
Products of the milling industry	0.5
Oil seeds and oleaginous fruits	2.1
Gums, resins	0.6
Vegetable planting materials	0.4
Animal or vegetable fats and oils	7.7
Preparations of meat and fish	4.2
Sugars and sugar confectionery	0.8
Cocoa and cocoa preparations	0.1
Preparations of cereals, flours	0.3
Preparations of vegetables	12.9
Miscellaneous edible preparations	0.6
Beverages, spirits, and vinegars	1.3
Residues and waste from the food industry	0.5
Tobacco and manufactured tobacco	3.1
Hides and skins	0.9
Wool, neither carded nor combed	0.3
Cotton, not carded	4.7
Cotton waste	1.1
Total agricultural trade	100.0

[a] Med8 + Libya and West Bank + Gaza strip.
Source: Comext database and author's calculations.

Annex 3. Exported quantities to the EU and quantitative limits (tons)

	Cut flowers	New potatoes	Tomatoes	Concentrated tomato	Olive oil	Oranges
Morocco						
Exports						
1998	1,992	26,322	177,825	1,138	1,358	206,960
1999	1,728	80,183	195,195	685	9,492	195,315
Limit	5,000	120,000	168,757		[a]	380,800
Israel						
Exports						
1998	40,374	64,514	10,155	488	6	93,420
1999	33,636	81,442	11,633	377	17	69,971
Limit	20,100	22,400	1,000			200,000
Tunisia						
Exports						
1998	25	783	1,363	240	89,576	22,807
1999	71	5,399	1,032	705	139,980	20,815
Limit*	1,000	16,800	[b]	2,500	46,000	35,123
Jordan						
Exports						
1998	2	0	71	5,583		0
1999	0	0	57	4,030		0
Limit	100	1,000	[c]	4,000		
Egypt						
Exports						
1998	98	197,428	276	2	0	8,562
1999	146	128,247	227	2	0	6,518
Limit[†]		109,670				8,000
Syria						
Exports						
1998	0	388	0	0	1	0
1999	0	37,377	0	0	489	25
Limit						

[a] 5–10 percent tariff reduction.
[b] Tariff exemption for period between 15 November and 30 April.
[c] Tariff exemption for period between 1 February and 30 April.
Limits refer to TRQ and RQ: *Before the 2000 review; [†]before EMA signing
Sources: European Commission and author's calculations.

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