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Trade in the WAEMU: Developments and Reform Opportunities

Manuela Goretti and Hans Weisfeld

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Trade in the WAEMU: Development and Reform Opportunities

Prepared by Manuela Goretti and Hans Weisfeld[1]

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Abstract

This paper provides an overview of trade reform in the West African Economic and Monetary Union (WAEMU) since 1996 and a quantitative assessment of potential effects on trade patterns and tariff revenue of the current reform agenda. Despite evidence of significant trade complementarities within WAEMU, implementation of the union's current trade regime still suffers from persistent non-tariff barriers and administrative weaknesses. Based on an assessment of prospects for further trade integration, the paper also recommends strengthening the implementation of the present tariff union and supports the plan to extend it to all ECOWAS members. Finally, the paper stresses that an Economic Partnership Agreement with the EU could bring to the region the political momentum needed to address the weaknesses of the current trade regime, while also underlining the corresponding challenges in terms of trade diversion and tariff revenue losses.

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Author's E-Mail Address: mgoretti@imf.org; hweisfeld@imf.org

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A. Introduction

The creation, between 1996 and 2000, of the West African Economic and Monetary Union (WAEMU) customs union was an important step toward greater regional integration in western Africa. It was part of an initiative to boost regional integration and policy effectiveness after the CFA franc was devalued relative to the French franc in 1994. The WAEMU customs union entails free movement of goods between member countries and application of a common external tariff (CET) on imports from other countries.

Although creation of the customs union streamlined the region's trade regime, both structural constraints and competitiveness concerns have impeded its implementation. There are still costly border procedures; lack of compliance with community rules, especially rules of origin; weak governance; and inadequate transport infrastructure.

Recent trade initiatives bring both opportunities and challenges. First, an ECOWAS-wide customs union could boost trade between the WAEMU and its West African neighbors.[2] Second, an Economic Partnership Agreement (EPA) with the European Union (EU) could bring far-reaching reciprocal trade liberalization between the WAEMU and the EU. Finally, global trade liberalization, for example through a revived Doha Round, could further enhance market access and affect world market prices for some of the region's main agricultural products.

This chapter reviews the main elements of the reform agenda and provides a quantitative assessment of some potential effects on trade patterns and tariff revenue. The next section describes the main characteristics of WAEMU's trade. The following section presents the current trade regime and its challenges. We then look at the scope for boosting intraregional trade, and discuss prospects for enhancing trade with other countries.

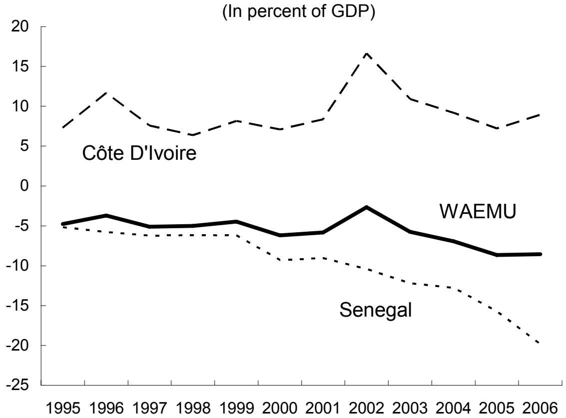
B. WAEMU Trade Characteristics

In recent years, trade in the WAEMU has suffered from significant shocks, both foreign and domestic. Among them are an appreciation of the CFA franc against the U.S. dollar resulting from the CFA's fixed parity with the euro and the depreciation of the dollar, a strong increase in oil prices, and a reduction in the profitability of major export commodities. As a result, the region's trade deficit has slowly but continuously grown from 3 percent of GDP in 2002 to 8 percent in 2006 (Figure 1). Senegal has particular problems; its trade deficit is almost 20 percent of GDP, owing in part to difficulties in the phosphate and fishing industries. As the WAEMU's only oil exporter, Côte d'Ivoire has been the only member to benefit from the

[2] ECOWAS consists of the WAEMU countries and Cape Verde, The Gambia, Ghana, Guinea, Liberia, Nigeria, and Sierra Leone. In 2006, ECOWAS GDP was 4.7 times WAEMU GDP.

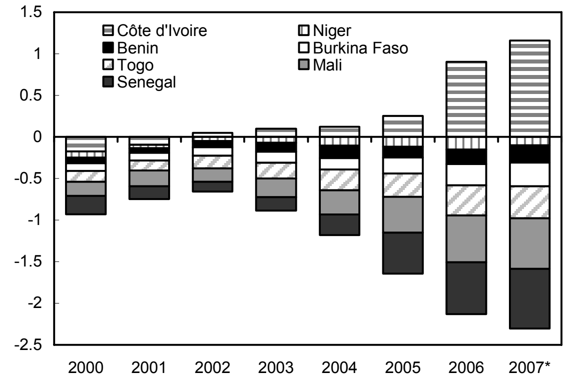
recent increase in oil prices. The oil-importing member countries have suffered under rising oil bills (Figure 2).

Figure 1. Trade Balances
(In percent of GDP)



Source: IMF

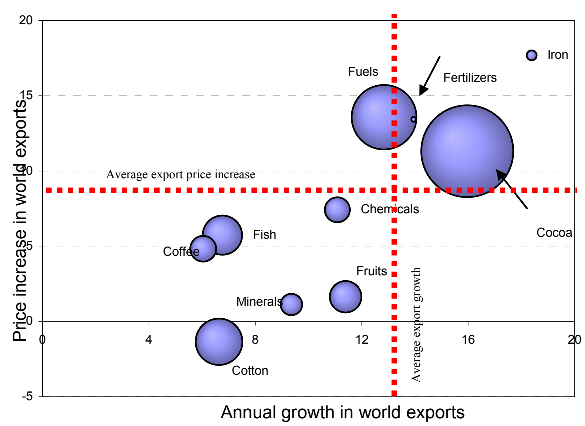
Figure 2. Oil Trade Balance of WAEMU Countries
(In billions of US dollars)



Source: IMF

Some of the region's main export sectors are not profitable. Figure 3 summarizes export performance in WAEMU by product.[3] World prices and demand have been declining for cotton—one of the main exports of Benin, Burkina Faso, Mali, and Togo—in the past five years. Cotton exports have also suffered from developed country subsidies for their cotton production, as well as from increased competition from Brazil and China. In contrast, cocoa and oil products—both exported by Côte d'Ivoire—have seen robust increases in both prices and demand. In general, WAEMU exports are not diversified, so the region's trade performance is exposed to substantial terms of trade and other shocks.

Figure 3. WAEMU: Export Performance by Product, 2000–05



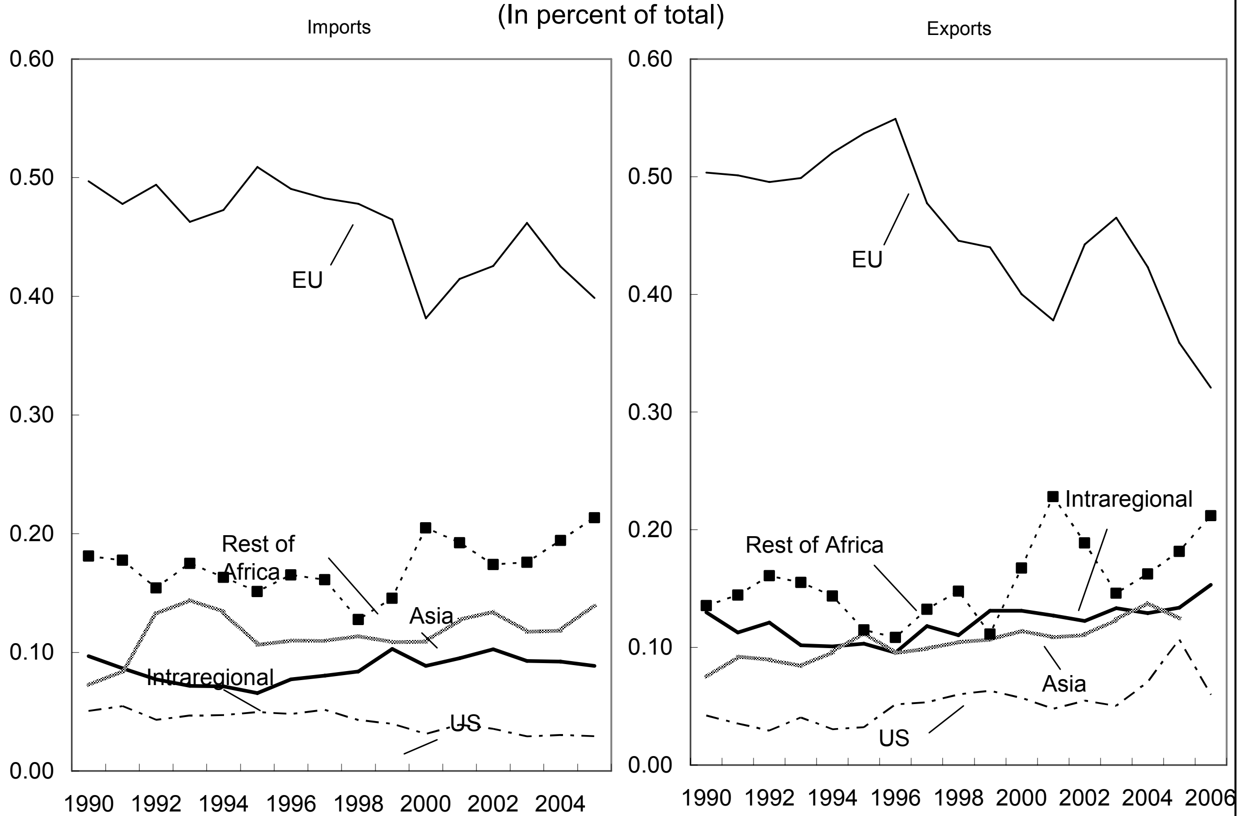
Sources: IMF staff calculations; and UN COMTRADE database.

Oil products, cereals, vehicles, machinery, and mechanical appliances are among WAEMU's main imports. Whereas exports are usually denominated in U.S. dollars, imports tend to reflect trading partner currencies, notably the euro. The appreciation of the euro has thus affected exports and imports asymmetrically: it has penalized most exports, but on the import side it has helped lessen little more than the impact of higher U.S. dollar oil prices.

[3] The figure shows price increases and growth in world exports for the main WAEMU exports; bubbles reflect the relative size of each sector and are based on the ratio of WAEMU's total exports to GDP.

Although the EU is still WAEMU's main trading partner, its weight has fallen over the years. Asian and other African countries are increasingly important; Asia now accounts for 13 percent, Africa for 20 percent, and the EU for 38 percent of WAEMU trade (Figure 4).

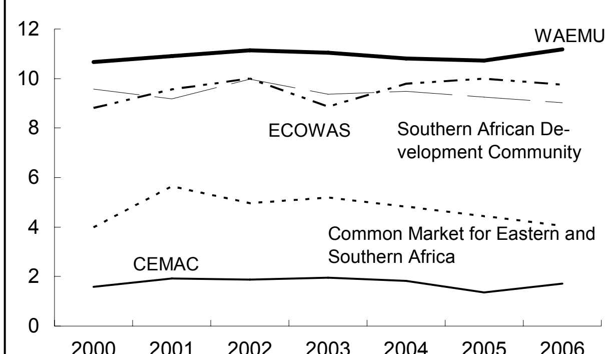
Figure 4. Composition of WAEMU Trade with Various Partners
(In percent of total)



Source: IMF

Intraregional trade in the WAEMU has increased only marginally since the free trade area was created in 1996. It was relatively stable at about 11 percent of total trade from 2000 through 2006 (Figure 5). Nevertheless, the WAEMU still has more intraregional trade than any other region in Africa.[4]

Figure 5. Intraregional Trade: WAEMU and Other Selected Regional Groups
(In percent of total trade)



[4] Official statistics do not capture WAEMU's informal trade, which is considerable, especially in fresh products.

C. The Current Trade Regime

Characteristics and deficiencies

The adoption of the free trade agreement in 1996 and of the CET in 2000 reduced tariff rates and streamlined the tariff structure.[5] Although no tariff or quantitative restriction is applied to intraregional trade in domestic products, levies on imports from third countries are based on four tariff bands, ranging from 0 percent for "social" goods (for example, medicines), "cultural" goods (for example, books), and capital goods to 20 percent for finished consumer goods.[6] The simple average most favored nation (MFN) tariff rate is 14.2 percent,[7] with almost 40 percent of imports classified under the 10 percent tariff band (Table 1) and a little less than 50 percent of imports being manufactured products (Table 2).

Table 1. WAEMU: Sources of Imports and Tariff Revenue by Import Tariff Band 2005

(in percent of total)

Tariff Band	Imports	Tariff Revenue
5%	32.0	14.1
10%	38.9	34.4
20%	29.1	51.4

Sources: Data provided by the authorities; and IMF staff estimates.

Table 2. WAEMU: Sources of Imports and Tariff Revenue by Product Type 2005

(in percent of total)

Tariff Band	Imports	Tariff Revenue
Agricultural products	20.1	22.5
Manufacturing products	47.2	45.1
Oil products	27.3	16.2

Source: Data provided by the authorities; and IMF staff estimates.

Tariff receipts fall substantially short of estimates based on the CET schedule, which suggests that CET implementation is generally weak (Table 3). Shortfalls are particularly pronounced in Côte d'Ivoire, Guinea-Bissau, and Mali.[8]

[5] The WAEMU customs union was put into place in two steps: in 1996 member countries removed tariffs and quantitative restrictions on intraregional trade (tariffs on trade in industrial products were phased out over four years); and in 2000 they adopted a common external tariff, which reduced tariff rates and tariff dispersion substantially.

[6] Details on the tariff bands applied to each tariff line are shown in WAEMU Regulation 23/2002/CM/UEMOA.

[7] This tariff rate does not include other charges and duties applied on consumption goods: a statistical fee of 1 percent; the 1 percent WAEMU Community solidarity levy (PCS), applied to goods of non-WAEMU origin; a 0.5 percent ECOWAS levy applied to goods of non-ECOWAS origin; and in some cases, a charge for the inspection and verification of imported goods of 0.75 -1 percent.

[8] Curiously, in Benin actual receipts exceed what could be expected based on the CET schedule. This points to data inaccuracies.

Table 3. Actual and Expected WAEMU Tariff Receipts

	Actual, Based on Official Data on Customs Duties		Based on CET Tariff Schedule					
	In percent of total revenue[1]	In percent of GDP	In percent of total revenue[1]			In percent of GDP		
	2003	2003	2003	2004	2005	2003	2004	2005
Benin	15.0	2.5	14.0	20.7	20.0	2.4	3.4	3.3
Burkina Faso	12.0	1.5	18.4	19.1	22.3	2.2	2.4	2.8
Côte D'Ivoire	8.2	1.4	20.3	25.2	22.7	3.4	4.4	3.9
Guinea-Bissau	11.8	1.8	34.5	16.9	26.6	5.2	2.9	4.7
Mali	10.4	1.7	20.8	16.5	6.5	3.4	2.9	1.2
Niger	12.0	1.2	26.8	39.4	40.1	2.6	4.4	3.9
Senegal	12.7	2.3	18.6	32.3	28.5	3.4	6.0	5.5
Togo	14.6	2.5	18.3	17.4	53.5	3.1	2.9	8.4
WAEMU	10.9	1.7	19.5	24.9	23.8	3.1	4.1	3.9

Sources: Data provided by the authorities; and IMF World Economic Outlook and staff estimates.

[1] Excluding grants.

Substantial differences in factor costs between WAEMU countries have led to the introduction of nontariff barriers. Although some differences can be explained by the geographical characteristics of the countries (for example, landlocked versus coastal) and transport costs, many distortions in prices are caused by differences in taxes, notably on oil products. Togo has the lowest factor costs in the region and Burkina Faso the highest (Table 4). Box 1 presents an analysis of Benin's inefficient transport system and high costs.

Table 4. Factor Costs in the WAEMU 2006

Factors	Benin	Burkina Faso	Côte d'Ivoire	Guinea-Bissau	Mali	Niger	Senegal	Togo	West African Economic Montary Union	
									average	standard deviation (in percent)
Labor										
National minimum wage[1] (CFA/mo.)	27,000	28,723	36,607	n.a.	28,460	18,899	36,174	13,757	27,089	31
Employer's social contribution rate[1] (%)	16	22	14	n.a.	17	15	8	14	15	26
Land										
Urban area (unbuilt)[1](CFA/m2)	2,975	8,667	8,175	n.a.	1,673	6,000	106,042	n.a.	22,255	185
Capital										
Average lending rate (end-year) (%)	10.1	10.1	7.3	12.3	9.9	11.2	6.1	10.1	9.6	21
Tax rates on business profit[1] (%)	38	35	35	n.a.	35	35	33	40	36	7
Tax rates on securities (avg)[1, 2] (%)	14	25	11	n.a.	18	16	11	10	15	35
Energy and water										
Premium gasoline (CFA/liter)	425	607	615	710	635	661	600	525	597	15
Diesel (CFA/liter)	415	587	545	520	525	586	568	515	533	10
Kerosene (CFA/liter)	385	490	395	430	440	456	454	375	428	9
Electricity (low tension) (CFA/Kwh)	93.3	86.0	61.2	175.0	59.4	96.4	83.8	65.8	90.1	41
Electricity (medium tension) (CFA/Kwh)	63.3	121.0	51.9	115.0	88.0	79.9	78.5	63.3	82.6	30
Water[1] (CFA/m3)	307	1,040	684	n.a.	321	403	576	379	530	50
Transports										
Freight (food)[1] (CFA/TK)	53	n.a.	18	n.a.	29	24	n.a.	n.a.	31	49
Freight (non-food products)[1] (CFA/TK)	51	n.a.	31	n.a.	30	24	n.a.	n.a.	34	35
Telecommunications										
Local telephone call[1] (CAF/min.)	23	30	59	n.a.	15	25	21	20	28	53
Monthly Internet subscription[1] (CFA/mo.)	9,505	15,000	15,000	n.a.	30,000	4,950	10,000	9,000	13,351	61

[1] 2005 data.

[2] Tax rates on returns from equities, bonds (short-term and long-term issuances), and other dividends.

Source: Banque Centrale des Etats de l'Afrique de l'Ouest (BCEAO).

Box 1. Deficiencies in the Transport and Transit System: The Case of Benin

Poor transportation services, roadblocks, and administrative delays owing to transit and customs procedures are major obstacles to trade in the WAEMU. Although landlocked countries tend to have the highest costs to trade and the longest delays, coastal countries also suffer from lengthy procedures and excessive transportation costs. Let us use Benin as an example.

Benin has some of the highest transport costs in the region (see Table 13.4). For example, to ship a ton of rice from Benin to Niger costs about CFAF 71 a kilometer but from Togo only CFAF 47 a kilometer, for a total cost of CFAF 75,000 versus CFAF 70,000, even though the distances are shorter and Benin borders Niger.

- The Cotonou port, the main entry point for imports to Benin, accounts for about 40 percent of the country's tax revenue. Despite its gateway role for landlocked countries and its strategic position next to Nigeria and, the port's traffic is below potential owing to both deficiencies in infrastructure and organizational and procedural problems. Port users are subject to several unofficial fees. The high costs and long delays affect the port's competitiveness. To address these issues and speed reform, the authorities have recently handed over management of the port to the U.S.-funded Millennium Challenge Account Benin unit.

- The majority of transit declarations from Cotonou port, accounting for 68 percent of the total value of transit, are not documented (World Bank, 2006). A number of goods, especially used cars, tend to be declared as being in transit to landlocked countries in order to suspend tax payments, but are instead smuggled to Nigeria.

- The planned adoption of the CET at the ECOWAS level (as described in the section on expanding intraregional trade) and the respect of the *Transit Routier inter-Etat* program should help avoid double taxation and multiple controls on goods in transit and thus reduce the incentive to replace formal trade relations with smuggling.

Most nontariff barriers arise from national trade regulations that conflict with WAEMU rules. Quantitative restrictions are still present in the form of minimum levels of imports and exports; Burkina Faso, Côte d'Ivoire, and Senegal still use reference values in their customs valuation of certain products; a "statistical fee" is often applied to products in transit through the trade corridors of the union; three countries impose a charge for verifying imported goods to remunerate inspection companies; there are still some disputes on CET tariff lines, although the number has been substantially reduced in recent years; double taxation on transit goods still applies to some imports; and temporary tariff surcharges introduced with the CET in 2000 and scheduled to expire in 2006 are still in place in some countries.[9]

[9] The *Taxe Dégressive de Protection* (TDP) was established to compensate for the decline in protection related to installation of the CET. Until December 2006 the TDP entailed a 5 percent levy on specific products, such as vegetable oils, cigarettes and tobacco substitutes, matches, and textile bags. Senegal and Côte d'Ivoire still apply the *Taxe Conjoncturelle à l'Importation* on some products (flour, sugar, tomato concentrate, and so forth). Its purpose is to mitigate the effect on community production of sharp fluctuations in international prices. The authorities wish to replace the *Taxe Conjoncturelle à l'Importation* with a regional safeguard arrangement.

Some countries do not fully implement the WAEMU rules of origin. These rules are used to certify products as being of WAEMU origin and therefore as free of import tariffs. A recent simplification of the rules and their management has reduced the time needed to obtain certification from 6 months to an average of 15 days.[10] Nevertheless, Mali and Côte d'Ivoire have generalized disputes on certificates issued by other countries and often apply the CET to imports from other WAEMU members (Box 13.2 details Mali's implementation of the trade regime).

Cumbersome and inefficient administrative practices hamper the functioning of the customs union. The World Bank's *Doing Business Survey* 2006 suggests that the business environment is poor in all WAEMU member states.[11] With reference to trading across borders the WAEMU ranks below most other countries and the sub-Saharan African average. Mali and Niger have particularly burdensome procedures; import processing is lengthy and the number of documents to be presented for both imports and exports is unreasonable (Table 5).

Table 5. Doing Business Survey, 2006: Trading Across Borders

	WAEMU									CEMAC	SSA
Indicator	Benin	Burkina Faso	Côte d'Ivoire	Guinea-Bissau	Mali	Niger	Senegal	Togo	*Average*	*Average*	*Average*
Documents for export (number)	8	9	9	8	10	..	6	7	*8*	*8*	*8*
Time for export (days)	35	69	21	27	66	..	22	32	*39*	*47*	*40*
Cost to export (US$ per container)	980	1215	781	1656	1752	..	978	463	*1118*	*1804*	*1561*
Documents for import (number)	11	13	19	9	16	19	10	9	*13*	*13*	*12*
Time for import (days)	48	66	48	26	61	89	26	41	*51*	*60*	*52*
Cost to import (US$ per container)	1452	1700	1395	1749	2680	3266	1674	695	*1826*	*2128*	*1947*
Rank	130	154	132	125	167	174	94	64	*130*	*138*	*124*

Sources: World Bank, Doing Business Database 2006; and IMF staff calculations.

[10] The use of a common nomenclature has also facilitated custom procedures. Most WAEMU members are adopting the 2002 version of the Harmonized System (HS) and use the Automated System for Customs Data (ASYCUDA). Guinea-Bissau still does not follow the HS, and Senegal uses another customs data system.

[11] The survey covers 175 economies.

Box 2. Implementation of the Trade Regime: The Case of Mali

Mali's average tariff rate has fallen from 22.1 to 15.0 percent since the CET was introduced. This includes supplementary duties equal to 2.5 percent (some imports are also subject to a contribution to the Import Inspection Program). Despite the reduction and the significant unification of customs duties, the country still faces several challenges in implementing the WAEMU trade regime. Continuing exemptions and limited compliance with community rules substantially raise the country's de facto level of protection:

- Mali still classifies 10 tariff lines differently from the regional CET. Because it has general disputes on products of origin, it tends to levy the CET rate on imports from WAEMU members. Mali's authorities say these actions are taken because coastal countries, notably Côte d'Ivoire, do not respect the rules concerning products in transit.

- The country continues to apply a special import tax (Taxe Conjoncturelle à l'Importation) of 55 percent on imports of sugar from non-WAEMU countries and restricts imports of cigarettes, tobacco, beef, and live cattle. These and other measures have created incentives for smuggling through neighboring countries.

- Mining and other companies approved under Mali's Investment Code are exempt from customs duty; and although the country has no export subsidy program, enterprises with an export content above 80 percent of production are granted tax concessions.

- The customs process is marred by lengthy and costly clearance procedures, entailing a very high number of customs documents; the cumbersome system has even hampered the ability of the WAEMU Commission to send CET compensation payments to Mali in a timely manner because of the time it takes to review the paper documentation.

Sources: WTO 2004 Trade Policy Review; 2004 World Bank Diagnostic Trade Integration Study for Mali; Malian authorities, and IMF staff estimates.

Among the physical barriers to trade are numerous ineffective police and customs checkpoints along trade corridors. A double control system at the borders considerably lengthens clearance times without reducing illegal practices.

Finally, sociopolitical developments in the region and poor road security have further impeded free movement of goods across borders. In particular, the crisis in Côte d'Ivoire has forced some countries, notably the landlocked ones, to channel part of their trade through ports outside of Côte d'Ivoire. Regional programs to facilitate transport and improve security have not been very effective so far.

Conclusions and policy recommendations

Member country implementation of the customs union is uneven and hampered by nontariff and other barriers. Both WAEMU and ECOWAS are putting in place regionwide programs to address cumbersome custom procedures and uneven application of the rules. The institution of national committees to monitor the implementation of rules of origin is an important step. Nevertheless, national governments will have to commit to implementing the regional reforms and guarantee the correct functioning of the customs union if trade is to be effectively facilitated.

Realizing the Regional Economic Program could help mitigate country differences in factor costs and help strengthen the trade regime. The projects on road transport, energy, and water distribution should reduce and harmonize factor costs, which in turn should increase incentives to comply with the customs union rules.

D. Prospects for Enhancing Intraregional Trade

The WAEMU countries show significant trade complementarities, particularly between coastal and landlocked countries.[12] This can be seen with the help of Michaely's trade complementarity index (TCI: Michaely, 1996). The TCI measures the similarities between the import structure of one country and the export structure of another. It is defined as

$$TCI_{ij} = 100 - \sum_{k} \frac{\left| M_{jk} - X_{ik} \right|}{2},$$

where X_{ik} is country *I*'s total exports of product *K*, and M_{ik} is country *J*'s total imports of product k.[13] The index ranges from zero, indicating no complementarity, to 100, indicating perfect complementarity between the export and import structures of the two countries. Estimates for the WAEMU based on trade data at the HS's two-digit classification level, suggest considerable complementarity; the average level of the index is 30 percent, compared, for example, to only 17 percent for the Central African Economic and Monetary Community (CEMAC).[14]

Trade complementarities vary from country to country. Côte d'Ivoire and Senegal present average export complementarity indices of 51 percent and 39 percent, because their economies are diversified and these two coastal countries are more likely to reexport to landlocked ones. In contrast, for Benin, Niger, and Burkina Faso the average export complementarity is less than 25 percent, suggesting that what they export only partially meets the import needs of other member countries (Table 6).

[12] Reexports, notably between coastal and landlocked countries, are important to WAEMU (and ECOWAS) regional trade. Although customs procedures for products in transit are in place, a significant amount of imports are registered as imports and then reexported after a transformation sufficient to change their certificate of origin.

[13] Both variables are expressed as a percent of the total.

[14] As found in the literature and reported in Martijn and Tsangarides (2006), a TCI is considered as an indicator of strong complementarities once it reaches a threshold of 25 percent.

Table 6. Trade Complementarity Index in WAEMU

Importer	Exporter: Benin	Burkina Faso	Côte d'Ivoire	Guinea-Bissau	Mali	Niger	Senegal	Togo
Benin	…	27.1	43.1	…	31.0	27.0	48.9	43.0
Burkina Faso	17.4	…	35.7	…	24.8	15.9	50.3	33.6
Côte d"Ivoire	18.1	19.0	…	…	25.6	15.9	56.9	33.1
Guinea Bissau	…	…	…	…	…	…	…	…
Mali	14.0	17.1	37.2	…	…	13.8	49.5	36.4
Niger	24.5	26.2	41.8	…	28.7	…	50.2	37.4
Senegal	19.9	21.7	38.9	…	26.3	15.9	…	36.3
Togo	19.3	21.9	38.5	…	23.9	20.4	51.6	…

Source: United Nations COMTRADE database.

On this basis, there is room for more intraregional trade. An analysis based on the potential for expansion of production in certain sectors suggests that WAEMU could satisfy internally another 3 percent or so of its import demand.[15] With production patterns unchanged, the current level of intraregional trade could thus be expanded from 11 percent of total trade to about 14 percent. A diversification of production would allow this value to increase further.

Conclusions and policy recommendations

Although intraregional trade has grown only marginally in recent years, policy efforts to promote diversification of the production base and guarantee effective application of the customs rules could promote a significant expansion of intraregional trade. Regional and national programs targeting development of the secondary sector could further enhance trade complementarities between WAEMU countries. In addition, the recent adoption of the *Transit Routier inter-Etat* program to correct the functioning of the trade corridors and introduce a joint control system should help expedite customs procedures and reduce informal trade within WAEMU.

E. Prospects for Enhancing Trade with Countries Outside the Region

Enhancing trade within the ECOWAS

Trade integration within the ECOWAS has so far been limited to the WAEMU. At present, trade between WAEMU members and the other ECOWAS countries is subject to substantial tariff barriers: WAEMU countries apply the CET to imports from the other ECOWAS

[15] We select products at the six-digit classification level for which a country's net exports exceed US$125,000. We consider net exports, instead of exports, in order to control for the significant amount of re-export from third countries within the region.

countries, and in turn these countries apply country-specific tariffs to imports from the WAEMU (and all other countries, including other ECOWAS countries). Even though average tariff rates of non-WAEMU ECOWAS countries do not differ markedly from the WAEMU average rate, the structures of tariff systems vary widely.[16]

For several years ECOWAS has been planning to form a customs union. In early 2006 the ECOWAS heads of state agreed to extend the CET to ECOWAS as a whole and form a free trade area among ECOWAS members, with the end of 2007 as the target date. To provide some flexibility on the CET, it was decided that countries could suggest a list of products to be temporarily or permanently moved to another tariff band. When these are negotiated, the parties should strive to ensure that the new average tariff levels and tariff dispersion are no higher, and preferably, lower than those current in the WAEMU.[17] It was also agreed to introduce measures, similar to those used in the WAEMU, to temporarily offset tariff revenue losses. Finally, it was decided to allow countries to apply safeguard measures in line with WTO rules.

The trade complementarities between ECOWAS countries are substantial, which could promote trade. The trade complementarity index for WAEMU countries as exporters and the other ECOWAS countries as importers (see Table 7) is 29 percent, higher than the index level of 25 percent that is thought to indicate strong potential for enhancing trade.

Table 7. Trade Complementarity Index in ECOWAS

			Exporter															
			WAEMU									Non-WAEMU						
			Benin	Burkina Faso	Côte d'Ivoire	Guinea-Bissau	Mali	Niger	Senegal	Togo	*WAEMU*	Cape Verde	The Gambia	Ghana	Guinea	Nigeria	Sierra Leone	*Non-WAEMU*
Importer	WAEMU	Benin	…	27.1	43.1	…	31.0	27.0	48.9	43.0		34.7	26.3	21.2	8.0	16.5	7.7	*19.1*
		Burkina Faso	17.4	…	35.7	…	24.8	15.9	50.3	33.6		38.2	19.4	17.8	8.0	24.0	8.4	*19.3*
		Côte d'Ivoire	18.1	19.0	…	…	25.6	15.9	56.9	33.1		40.7	23.6	24.8	10.8	23.9	8.3	*22.0*
		Guinea-Bissau	…	…	…	…	…	…	…	…		…	…	…	…	…	…	…
		Mali	14.0	17.1	37.2	…	…	13.8	49.5	36.4		37.6	18.7	18.7	9.9	22.3	9.4	*19.5*
		Niger	24.5	26.2	41.8	…	28.7	…	50.2	37.4		31.9	32.2	21.7	9.6	16.5	9.0	*20.2*
		Senegal	19.9	21.7	38.9	…	26.3	15.9	…	36.3		37.4	21.5	21.6	10.7	23.9	9.2	*20.7*
		Togo	19.3	21.9	38.5	…	23.9	20.4	51.6	…		40.9	24.9	20.7	8.4	22.9	7.5	*20.9*
		WAEMU									*…*	*37.4*	*23.8*	*20.9*	*9.3*	*21.4*	*8.5*	*20.2*
	Non-WAEMU	Cape Verde	21.6	20.7	34.9	…	26.2	16.7	35.2	40.6	*28.0*	…	24.0	23.9	9.4	10.1	10.4	
		The Gambia	21.9	25.0	38.5	…	25.6	23.1	43.7	37.6	*30.8*	27.5	…	22.4	11.0	14.5	10.3	
		Ghana	18.6	20.2	39.3	…	26.2	18.4	47.8	35.2	*29.4*	32.2	24.7	…	11.7	15.4	8.5	
		Guinea	19.5	21.9	37.2	…	25.6	18.4	51.2	35.9	*30.0*	38.5	24.2	18.1	…	23.8	8.6	
		Nigeria	14.4	17.1	29.9	…	24.4	15.0	38.9	37.9	*25.4*	25.5	20.8	23.1	12.3	…	9.5	
		Sierra Leone	24.6	25.1	37.6	…	27.3	17.1	47.0	37.1	*30.8*	53.2	20.8	18.7	7.7	41.7	…	
		Non-WAEMU	*20.1*	*21.7*	*36.2*	*…*	*25.9*	*18.1*	*44.0*	*37.4*	*29.0*							*…*

Source: United Nations COMTRADE database.

[16] Average tariff rates in ECOWAS range from 12 to 16 percent (except for Cape Verde, which has lower rates).

[17] Some ECOWAS countries seem to have suggested introducing much higher bands (for example, for rice, one of WAEMU's main imports).

For WAEMU countries as importers and the other ECOWAS countries as exporters, the index is 20 percent (27 percent if Guinea and Sierra Leone are excluded), which also suggests that there is potential for expanding trade. As with all reductions of preferential tariffs, an ECOWAS-wide customs union could also lead to some trade diversion; that is ECOWAS imports replacing imports from other countries. However, the limited overlap between WAEMU imports from the other ECOWAS countries and imports from the EU suggests that the scope for trade diversion is small.

Revenue losses resulting from the creation of an ECOWAS customs union are likely to be limited. Current tariff revenue from trade with ECOWAS countries averages 0.1 percent of GDP and ranges from close to zero in Mali to 0.6 percent in Burkina Faso (Table 8). A loss of this amount of revenue seems manageable. Actual losses are likely to be even lower, because Table 8 assumes that current tariff revenue is where it would be if the CET were applied flawlessly (we saw earlier that actual revenue is substantially lower than that). Some further revenue losses could occur through trade diversion.

Table 8. Introduction of the ECOWAS CET: Scenario for Tariff Receipts in WAEMU
(in percent of GDP)

	2005 Tariff Receipts Based on WAEMU CET Tariff Schedule		Expected Level of Tariff Receipts Under ECOWAS CET
	All trading partners	ECOWAS only	Total
Benin	3.31	0.14	3.16
Burkina Faso	2.75	0.56	2.19
Côte D'Ivoire	3.87	0.03	3.84
Guinea-Bissau	4.69	0.20	4.50
Mali	1.17	0.01	1.15
Niger	3.87	0.24	3.64
Senegal	5.52	0.04	5.48
Togo	8.41	0.15	8.27
WAEMU	3.89	0.13	3.76

Sources: Data provided by the authorities; IMF World Economic Outlook and staff estimates.
Note: We assume application of the current WAEMU tariff schedule to all non-ECOWAS exporters.

However, progress toward the customs union has been slow, and it seems increasingly likely that the year-end target date will be missed. So far there has been no agreement on the classification of goods into the WAEMU's CET bands. Also, the details of the accompanying and safeguard measures have not yet been agreed. Because unification of the trade regime is important for further trade integration with the European Union (see below) the discussions should be accelerated.

Enhancing trade with the EU[18]

Currently, trade between the WAEMU and the EU does not conform to the World Trade Organization (WTO) principle of nondiscrimination. Until now, the WAEMU's commercial relations with the EU have been framed by partnership agreements that the EU has entered into with developing countries in Africa, the Caribbean, and the Pacific (ACP countries). These agreements (the Lomé I agreement signed in 1975, Lomé IV signed in 1989, and the Cotonou Agreement signed in 2000 and covering EU-ACP cooperation through 2020) gave ACP countries preferential access to the EU market for all industrial and most agricultural products.[19] The agreements discriminate between ACP countries and other developing or least developed countries in that they give ACP countries better access to the EU market. The agreements are also nonreciprocal: ACP countries have better access to the EU market than the EU has to ACP markets. These features are inconsistent with the EU's obligation to respect the WTO principle of nondiscrimination and the rules that govern derogations of this principle.[20]

The Cotonou Agreement, while temporarily prolonging the nonreciprocal preferences, calls for a shift to WTO-consistent trade. It specifies that WTO-consistent agreements should be finalized by the end of 2007 to ensure that the new agreements can be phased in starting in January. Consistency with WTO rules will be ensured by establishing reciprocity. Full reciprocity is to be reached no later than 2020, when EU goods can enter the WAEMU free of import tariffs or quotas—though a limited range of products may be exempted.[21] The WTO membership endorsed this approach in 2001, and the EU was granted a waiver of its WTO commitments with respect to the Cotonou Agreement through 2007.

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[18] Parts of this section draw on Nielsen and Zouhon-Bi (2007).

[19] For overviews of trade preferences and their effects on development see, for example, Hoekman and Öezden (2005) and Panagariya (2002). These studies find that trade preferences did little to support development, in part because they lessened incentives for developing countries to open up to trade.

[20] In 1947, the General Agreement on Tarriffs and Trade (GATT) established nondiscrimination as the fundamental principle of international trade. It entails (i) the MFN principle, which obliges a country to extend to all members of the GATT/WTO the most favorable terms it offers to any of them; and (ii) national treatment, requiring that imported goods, once they have cleared customs and border procedures, be treated no worse than domestically produced goods. Nondiscrimination limits the role of strategic motives for sidelining particular sources of supply, such as small countries, helping to depoliticize trade and to keep the system predictable and rules-based. The GATT/WTO rules allow derogations from the nondiscrimination principle only (i) where developed countries provide preferential market access to all developing or least developed countries, or (ii) where members of reciprocal preferential trade agreements collectively discriminate against imports from other countries. The Lomé and Cotonou conventions do not satisfy condition (i) because they grant better EU market access to ACP countries than to other developing or least developed countries. The conventions do not satisfy condition (ii) because they are not reciprocal.

[21] Such limited exemptions are common in past EU agreements that have not been challenged by the WTO.

The negotiation of WTO-consistent trade agreements as part of an EPA is being conducted in parallel with six different regional groups, ECOWAS being one of them. Mauritania has joined this group for the purpose of negotiating the agreement. The negotiations, coordinated by the ECOWAS Secretariat, started in October 2003.

So far there has not been much progress on the EU-ECOWAS EPA negotiations. The ECOWAS therefore recently requested from the EU a three-year extension of the deadline negotiations, citing concerns about a lack of competitiveness and calling for EU aid to help build industries that could survive a removal of tariffs on imports from the EU.[22]

An EPA could help address institutional weaknesses affecting trade in the WAEMU. An EPA could provide the area wide political momentum needed for harmonizing rules and procedures and ensuring their implementation. Further, an EPA would encompass trade facilitation measures, including support for applying technical, sanitary, and phytosanitary standards and customs procedures, which could have a substantial impact on trade development.[23]

However, the prospective EPA also raises some problems. First, it is not only likely to create trade through higher imports from the EU, but it could also divert trade if imports from the EU replace cheaper imports from other countries (see Box 3, a case study of Togo).[24] Second, the EPA will put downward pressure on the fiscal position of WAEMU members because they will gradually lose customs revenue from EU-sourced imports as the tariffs on them are gradually removed. Customs revenue from other imports will also decline as result of trade diversion. Third, the poor business environment in the WAEMU, limited access to credit, and other factors could slow the reallocation of capital and labor set free through cheaper imports from the EU.

[22] The EU has publicly announced that there can be no delay relative to the end-2007 deadline. In any case, it seems likely that the WTO membership would permit a temporary prolonging of the current discriminatory arrangement only if the EU offers some WTO concessions.

[23] For an empirical analysis of the effects of trade facilitation on trade volumes, see Wilson, Mann, and Otsuki (2005).

[24] Trade creation enhances welfare because it allows goods to be sourced from the lowest-cost producer. Trade diversion, the replacement of an import that has a low pretariff price by a similar import that has a higher pretariff import price, lowers welfare because it prevents such sourcing (Viner, 1950). The net welfare effects of an EPA for the WAEMU countries could therefore be positive or negative, depending on whether the volume of trade creation multiplied by the unit value of goods it affects exceeds or falls short of the volume of trade diversion multiplied by the unit values of goods it similarly affects. The unit values not being available, this paper does not calculate the welfare effects of an EPA.

Box 3. Potential Impact of the EU-ECOWAS EPA on Togo

ECOWAS members will lose tariff revenue with an EU-ECOWAS EPA and experience a change in trade patterns. The welfare effect of the change in trade patterns is uncertain because it depends on both welfare-enhancing trade creation and welfare-reducing trade diversion.

This box presents some stylized facts to suggest the effects that an EPA might have on Togo:

- Assuming that production and trade patterns are unchanged, the estimates in Table 13.9 suggest that the EPA would reduce Togo's trade tax revenue by more than 4.4 percent of GDP—more than half of total trade tax revenue. Efforts to recoup this substantial loss by raising more domestic tax revenue will be essential to preserve fiscal sustainability and continue valuable spending programs.
- Togo's imports from the EU currently account for 55 percent of total imports. This share could increase considerably after the EPA is operative. Almost all Togo's imports (at the six-digit classification level) are sourced both in EU and non-EU countries; only a minimal 1.3 percent of products come only from non-EU countries. This suggests that an EPA could lead to substantial trade diversion from non-EU to EU member countries.

Togo: Average Import Prices of Selected Products

Product description	HS six-digit code	Average import tariff [1] (in percent)	Average import price (per unit)	
			From EU members	From other countries
Spelt, common wheat and meslin	*10.01.90*	5.0	114	125
Petroleum oils (excl. crude)	*27.10.00*	7.9	246	260
Of which:	*.11*	7.9	299	249
	.19	7.9	192	271
Hot-rolled iron/steel bars and rods	*72.13.91*	5.0	133	258
Electrical apparatus for line telephony or telegraphy	*85.17.80*	10.0	100,119	101,966

Source: Data provided by the authorities, and IMF staff estimates.
[1] Average tariff rates based on CET tariff schedule. Oil products are subject to different CET tariff lines,

- For the EPA to generate welfare losses, trade diversion would have to entail replacement of low-cost products from outside the EU by more expensive imports from the EU. For five of Togo's main import products, which together account for almost 80 percent of total imports, imports from the EU are on average cheaper than from other countries (see Table above). Yet we cannot conclude that the welfare effects of trade diversion after the EPA is introduced will be small for Togo, because the presence of official aid from the EU on certain products and the aggregation of data may be distorting our estimates of import prices.

The scope for revenue losses seems large. Table 9 shows the effects of a loss of all revenue currently generated by tariffs on imports from the EU, as would happen with the eventual complete removal of such tariffs under an EPA.[25] As before, actual losses could be lower, because Table 9 assumes that current tariff revenue is where it would be if the CET were applied flawlessly (we saw earlier that actual revenue is substantially lower than that). Losses could also be higher because of trade diversion: some imports currently sourced from outside the EU will in the future be sourced from within. Table 10 shows projected fiscal revenue losses after taking trade diversion into account, as calculated by UNECA (2005) and Busse, Borrmann, and Grossman (2004) using the Verdoorn partial equilibrium model (Verdoorn,

[25] We ignore here the possibility that a small share of imports goods may still bear tariffs beyond 2020.

1960).[26] The average projected loss ranges from 4 percent of fiscal revenue in Mali to 12.5 percent in Togo.[27] As in Table 9, these calculations assume flawless application of the CET, and actual losses are likely to be lower.

Table 9. Impact of the EPA with the EU: Scenario for Tariff Receipts in WAEMU
(in percent of GDP)

	2005 Tariff Receipts Based on WAEMU CET Tariff Schedule		Expected Level of Tariff Receipts under the EPA	Expected Level of Tariff Receipts under the EPA and the ECOWAS CET
	Total	Receipts from the EU	Total	Total
Benin	3.3	1.6	1.7	1.5
Burkina Faso	2.8	1.4	1.4	0.8
Côte D'Ivoire	3.9	2.3	1.6	1.6
Guinea-Bissau	4.7	3.8	0.9	0.7
Mali	1.2	0.3	0.8	0.8
Niger	3.9	0.9	2.9	2.7
Senegal	5.5	4.1	1.4	1.4
Togo	8.4	4.4	4.0	3.9
WAEMU	3.9	2.2	1.7	1.5

Sources: Data provided by the authorities; IMF World Economic Outlook and staff estimates.
Note: We assume application of the current WAEMU tariff schedule to all non-ECOWAS exporters.

Table 10. WAEMU: Expected Revenue Loss from an EPA
(in percent of total fiscal revenue)

	UNECA 2005	Busse, Bormann, and Grossman 2004	Average
Benin	6.7	8.6	7.7
Burkina Faso	6.1	5.6	5.9
Côte d'Ivoire	5.6	4.6	5.1
Guinea-Bissau	19.4	5.6	12.5
Mali	4.5	3.8	4.2
Niger	7.6	3.6	5.6
Senegal	6.0	10.7	8.4
Togo	12.5	7.4	10.0

Source: Hinkle, Hoppe and Newfarmer (2006).

[26] This widely used partial equilibrium model provides easy-to-calculate formulas for trade creation and diversion after preferential tariff reductions. Combining these formulas with information about existing tariff rates makes it possible to calculate revenue effects.

[27] Projections vary in part because of different assumptions about the numerical values of certain behavioral variables that the Verdoorn model requires (price elasticities of import demand and the elasticity of substitution between imports from the EU and the rest of the world.)

Clearly, it will be essential for trade liberalization to incorporate measures to compensate for its impact on fiscal revenue. Revenue measures should aim to strengthen direct and indirect tax policies and administration. In principle, shifting from trade taxes to taxes on domestic consumption could fully offset the revenue loss while preserving the efficiency gains of tariff cuts, because domestic producers would now have to compete with world market prices. However, there is little room for raising tax rates on domestic consumption because the value-added tax rate in WAEMU countries is already quite high. Thus, additional domestic revenue will have to be generated mainly by broadening the domestic tax base and strengthening tax administration. The problem will be particularly challenging for low-income countries,[28] as the WAEMU countries fully recognize. They may wish to review whether the current regional framework for harmonizing and increasing domestic tax revenue is sufficient. Additional revenue could also be generated if customs were administered better. Finally, the WAEMU countries should strive to enhance public financial management and the efficiency of spending.

To allow that factors of production made redundant by trade liberalization to be quickly reallocated, an EPA should feature liberal rules of origin. The effect of an EPA on the manufacturing sector in the WAEMU will likely hinge on rules of origin. The evidence refutes earlier notions that restrictive rules of origin could support industrialization by promoting local supply chains that would provide inputs for domestic industries serving European markets (“backward integration”). Instead, a simple and low-value-added criterion is more likely to attract foreign investors into new export industries that would use inputs from outside the region—benefiting from inexpensive labor and tariff preferences.[29]

The risk that trade will be diverted by an EPA could be countered by parallel tariff cuts on imports from the rest of the world. However, such cuts would likely lead to further revenue losses.[30] These losses could be mitigated by the lessening of EPA-related trade diversion and the associated tariff receipts.

[28] Keen and Ligthart (2001), Baunsgaard and Keen (2005), and IMF (2005) discuss the challenge of offsetting losses in trade tax revenue through domestic revenue.

[29] The potential that such an approach could succeed is evidenced by the United States African Growth and Opportunity Act (AGOA) initiative. AGOA grants eligible African countries tariff-free access to the United States market; the rules of origin are relatively liberal. AGOA has triggered large increases in manufacturing production in several African countries, including Lesotho and Swaziland, often using cheap inputs from outside the region. It is to be hoped that AGOA can be helpful to the WAEMU countries, too. The WAEMU authorities report that the process of demonstrating AGOA eligibility can be cumbersome; only Senegal has been declared AGOA-eligible, though Benin and Mali have made progress in demonstrating eligibility.

[30] When initial tariff rates are high, tariff cuts can result in revenue increases. The WAEMU CET is, however, too low for this to happen.

The Cotonou Agreement recognizes that some countries might not be in a position to enter into an EPA. The possible alternatives present their own challenges.[31] ACP countries that decide not to participate in an EPA or to participate only later could export under the EU's nonreciprocal Generalized System of Preferences (GSP). Least developed countries also benefit from the special GSP arrangements known as the "Everything But Arms" (EBA) initiative.[32] Thus, any WAEMU member except Côte d'Ivoire that is not ready to enter into an EPA by 2008 could export to the EU under the terms of that initiative; Côte d'Ivoire would have to export under the less favorable GSP. Although the preferences of the initiative are more generous than those of the Cotonou Agreement, both the EBA initiative and the GSP have more restrictive rules of origin that could inflict considerable damage on West African exporters. Also, the GSP and the EBA initiative are unilateral arrangements that the EU can cancel at its discretion. Further, market access under these arrangements becomes more restricted as a country gains EU market share.

Enhancing trade through multilateral trade liberalization

Multilateral liberalization offers simple and broad market opening and holds the potential to enhance welfare by, for example, accelerating growth and reducing poverty.[33] Bilateral and regional arrangements cannot substitute for multilateral liberalization, for one reason because they lead to trade diversion and strain scarce technical capacity in Africa.

It has been questioned whether multilateral liberalization would be beneficial for sub-Saharan Africa at this time (Panagariya, 2004). Two elements could limit the benefits:

- Under multilateral liberalization, industrial countries would reduce subsidies for agricultural products, making their export to developing countries more expensive. This could benefit African food producers but would hurt African consumers.
- By liberalizing trade for all, multilateral liberalization would erode current trade preferences for Africa, such as those under the Everything But Arms initiative. This could hurt African exporters.

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[31] All WAEMU countries except Côte d'Ivoire are classified as least developed countries.

[32] This initiative provides duty- and quota-free access for almost all exports other than arms and munitions. The only exceptions are sugar and rice, which will be given free access only in the second half of 2009; in the meantime, duties on them will be gradually reduced and duty-free quotas increased.

[33] For recent reviews of the literature on the links between trade liberalization, economic growth, and poverty alleviation, see Winters (2002 2004) Berg and Krueger (2003), Winters, McCulloch, and McKay (2004) Dollar and Kraay (2004); Anderson (2004), and UK DTI (2004). Wacziarg and Welch (2003) show that for 1950 through 1998, countries that opened up (raising their trade-to-GDP ratio by an average of 5 percentage points) have experienced on average 1.5 percentage points higher GDP growth since doing so.

Recent quantitative research finds that sub-Saharan Africa (SSA) would still gain from comprehensive multilateral liberalization (Anderson, Martin, and van der Mensbrugghe, 2006). It also finds that Africa's poor would gain disproportionately because of the beneficial effects of liberalization on the agricultural sector, where the poor are concentrated. This makes multilateral trade liberalization a particularly valuable tool for reducing poverty. Further, as Yang (2005) notes, African countries have become increasingly dependent for trade on other developing and emerging countries, where barriers against African exports are substantially higher than in industrial countries. Hence, the potential gains for Africa from better access to these markets are large.

The WAEMU countries should therefore seek further multilateral trade liberalization, including in the Doha Round. WTO negotiations in the Doha Round were suspended in mid-2006 but resumed in early 2007. Regrettably, Doha Round proposals related to market access for African exports such as fishery products have been limited, and a large number of "sensitive goods" of interest to least developed countries have been excluded, reducing the potential gains for Africa. Nevertheless, Anderson, Martin, and van der Mensbrugghe (2006) find that sub-Saharan Africa could still gain from a successful conclusion of the Doha Round if it substantially reduced its own import tariffs.

A successful conclusion of the Doha Round would be particularly helpful for WAEMU cotton producers. Doha negotiations target comprehensive cotton sector liberalization, covering subsidies, market access, and export competition.[34] This could benefit WAEMU's cotton producers through both higher world prices and a larger export volume.

Conclusions and policy recommendations

The planned ECOWAS-wide customs union could enhance trade between the WAEMU and its West African neighbors without seriously diverting trade or causing losses of tariff revenue—as long as it does not raise the average tariff rate and tariff dispersion relative to the current WAEMU regime.

The planned EPA with the EU could provide the political momentum needed for good implementation of the current WAEMU or the planned ECOWAS trade regime, and could result in substantial trade creation through both lower tariffs and trade facilitation. However, an EPA could also result in trade diversion and substantial revenue losses. Strengthening domestic revenue will be crucial to preserving fiscal sustainability and valuable spending programs. That strengthening could be achieved mainly by broadening the tax base and

[34] As mentioned above, cotton is a major WAEMU export crop and producers have been struggling with low prices for several years. In Benin, Burkina Faso, Mali, and Togo, cotton exports amount to 5–8 percent of GDP and cotton production employs as much as one-third of the population. Subsidies to cotton producers in middle- and high-income countries are substantial; world cotton prices are significantly lower as a result.

firming up tax administration. Customs administration should be enhanced as well. Finally, WAEMU countries should strive to better manage public finances and make spending more efficient.

Trade diversion from preferential trade integration within the ECOWAS and between the ECOWAS and the EU could be mitigated through cuts to the WAEMU (or in future, the ECOWAS) common external tariff. The WAEMU should actively pursue multilateral liberalization, not least because of the potential gains for its cotton producers. Cutting the common external tariff could bring further revenue losses, reinforcing the case for strengthening domestic revenue.

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