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Government Procurement in the EPAs

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Abstract

The trade relationship between the EU and the ACP countries are currently being renegotiated under the framework of European Partnership Agreements. These EPAs are not only concerned with traditional market access commitments but are also targeting the 'Singapore issues' and especially the area of government procurement. The reason for this is found in the economics of trade theory that illustrate the trade restrictive effect that home biased government procurement can have on international trade flows, where such procurement regimes make up a non-tariff trade barrier. This disrupts the best allocation of resources and do thereby cause inefficiencies in regards to public spending, consumer prices and international specialisation. The remedies for such inefficiencies are increased transparency and non-discriminatory practises that could result in increased market access for foreign suppliers. These practises are believed to give ACP countries governments' better value for money, while in the same time opening up a prosperous export market for European producers, a potential largely connected with the fact that government procurement makes up an important portion of most countries government expenditure.

There are however, concerns that liberalization would lead to one-sided gains on behalf of the EU and not benefit the ACP countries to a large enough extent. This is also the reason why most ACP countries have objected to the inclusion of procurement regulations in the EPAs. In order to make the opening up of procurement markets more appealing for ACP countries there might then be a need to allow for divergence for an absolute unbiased procurement regime. These exceptions could then be used to address factors of special interest for the situation of ACP countries, such as the pursuance of secondary policies, the existence of tied aid and the lack of institutional quality.

Keyword: Government procurement, EPA, ACP

Abbreviations

ACP	African Caribbean Pacific
ADB	Asian Development Bank
CEMAC	Economic and Monetary Community of Central Africa
ECDPM	European Centre for Development Policy Management
ECOWAS	Economic Community Of West African States
EPA	European Partnership Agreement
ESA	Eastern and Southern Africa
EU	European Union
DAC	Development Assistance Committee
GATT	General Agreement on Tariffs and Trade 1947
GDP	Gross Domestic Product
GPA	Agreement on Government Procurement
GSP	General System of Preferences
FCE	Final Consumption Expenditure
FTA	Free Trade Agreement
H-O	Heckscher-Ohlin
IMF	International Monetary Fund
LDC	Least Developed Country
NAFTA	North American Free Trade Agreement
NEG	New Economic Geography
NGO	Non-Governmental Organisation
NTT	New Trade Theories
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
PTA	Preferential Trade Agreement
ROW	Rest Of the World
SME	Small and Medium Enterprises
TDCA	Trade Development and Cooperation Agreement
UN	United Nations
WTO	World Trade Organisation
WDI	World Development Indicators

1 Introduction

The increased regional interaction and the prominent place taken by trade in the globalised world of the 21st century has been achieved by a continuous reduction of tariffs since the adoption of the GATT more than sixty years ago. The decreased level of tariff barriers has meant that more attention has been given to non-tariff barriers, leading to increasing efforts to open up government procurement markets for foreign competition.

Government procurement or public procurement, as it is sometimes referred to, is the term used to describe the purchasing activities of government or government controlled entities. This term is rather wide and covers purchases of *'everything from papers clips to computer systems, waste water plants, ship building or consulting services'*.¹ Government procurement is not just far-reaching in the number of goods, but also in regards to budgetary expenditure where procurement markets makes up well over 20 percent of GDP for an average OECD country. The importance of government procurement has lead to its inclusion in negotiations within the multilateral trade regime, as one of the so-called 'Singapore issues' and it is also the reason why it is discussed in negotiations under the European partnership agreements. The EPAs are the newest trade instrument in the long-time relationship between the EU and the ACP countries, which goes back all the way to the Yaoundé Convention in the seventies. This cooperation is only likely to increase in importance as globalization develops further, thereby making government procurement in the EPAs an interesting issue from several aspects.

This thesis purpose is to theorize the economic effect of government procurement in the light of the EPAs between the EU and the ACP countries. The focus will be on the trade implication of government procurement, which is quite natural considering that the issue is discussed in the EPAs that in essence are free trade agreements. There are however several complications that may arise when liberalising trade between developed and developing countries, where the general differences in capabilities between the EU and ACP countries risk creating an imbalance in the potential gains from an opening up of procurement market. The implications of these differences do therefore warrant an in-depth analysis.

1.1 Method and scope

The method chosen for this thesis is a literature study, which foremost addresses the trade implications of government procurement and the development perspective of the EU-ACP cooperation. Apart from the academic literature, the thesis does also make great use of official

¹ http://ec.europa.eu/trade/issues/sectoral/gov_proc/index_en.htm

publications and studies from international organisations such as the EU, IMF and OECD. The analysis of government procurement will mainly be carried out from a microeconomic perspective, utilising the most common trade theories in order to exemplify the effects of the EPAs. This analysis of the trade impact of procurement is mostly theoretical and does not empirically evaluate the impact on trade; even of some empirical data is used to illustrate the likely effects.

The intended scope of this paper is to examine the role of government procurement in the EPAs. The discussion whether the EPAs are the best available instrument for these relations, will not be addressed, and the discussion will instead be focused on their theoretical and legal implications. This limitation do also encompass that the thesis will not enter into any analysis of which trade scheme that are best fit to replace the old unilateral trade preferences between the EU and the ACP, a question that otherwise have been extensively debated in the academic literature.

1.2 Disposition and definitions

The disposition of this thesis is as follows. *Chapter 2* will give a general description of the EU-ACP relations, with special focus on the EPAs. *Chapter 3* do then provide the economic theory of government procurement. This theory explains the gains of a liberalised and unbiased procurement regime both from the perspective of market access and in regards to the most commonly used trade theories. *Chapter 4* provides a brief account of the size of procurement market, with a specific focus on the ACP countries' markets. *Chapter 5* does then address a number of specific consequences for the EU-ACP relations and especially a number of development related implication of the inclusions of procurement in these relation. *Chapter 6* contains the conclusion and the result of the findings in the preceding chapters.

As a clarification, it might be warranted to clarify the use of *public* vs. *government* in regards to procurement. The two notions will be treated as synonyms throughout the thesis and both will only be used because of linguistic reasons.

2 European Partnership Agreements

The European Union has a number of preferential trade agreements with various regional country groups. The most important are arguably the ones governing the relationship between the EU and the ACP countries. The first of these agreements were the Yaoundé Convention that was signed between the EC and several ex-colonies in Africa and concerned trade preferences and financial aid. The first Lomé Convention did in 1975 replace the Yaoundé Convention and did in addition to the countries covered by the Yaoundé Convention; include countries from the Caribbean and the Pacific. The Lomé Convention constituted the first non-reciprocal trade-agreement between the EC and the ACP countries and was later followed by several subsequent conventions, until the new Cotonou Agreement replaced the last Lomé Convention (IV) in 2000. It is thus under the framework of the Cotonou agreement that the EU has been establishing European Partnership Agreements.

The EPAs are free trade agreements between the EU and the ACP countries and are thereby considered to foster the gradual integration of the ACP countries into the global economy.² The EPAs are a relatively new instrument and trade relations between the country groups have traditionally been undertaken under a non-reciprocal basis under the WTO's GSP regime, while financial and humanitarian aid to the 77 existing ACP countries have been given in form of ODA.³ There has however been increasing efforts to replace these agreements with new EPAs, which are of reciprocal nature. The main reason behind this is that the earlier regime has been deemed incompatible with WTO-rules in general and GATT Part IV in particular. Since the previous trade agreement gave preferential treatment to ACP countries, it did thereby discriminate against countries outside this group and more particularly against non-ACP LDCs.⁴ The violation of WTO rules was confirmed in the *Banana Disputes*⁵ and since the EU did not succeed to bring its legislation in accordance with these rulings, it was awarded a waiver until December 31 2007 to come up with new WTO compatible trade agreements with the ACP countries.⁶ Another reason for the increased interest in reciprocal trade agreements has been attributed to the decline in relative trade flows between the EU and ACP countries,

² Desta, *EU-ACP Economic Partnership Agreements and WTO Compatibility: An experiment in North-South Interregional Agreements?*, Common Market Law Review 43:5 (2006) p. 1346 ff.

³ Senior Nello, *The European Union – Economics, policies and history*, McGraw-Hill Education, Berkshire (2005) p. 380-381

⁴ Borrman et al., *EU/ACP Economic Partnership Agreements: Impact, Options and Prerequisites*, Intereconomics 40:3 (2005) p. 169

⁵ EC Bananas III - Panel Report, WT/DS27/RW/EEC & AB Report, WT/DS27/AB/R

⁶ Alavi et al., *EU-ACP Economic Partnership Agreements (EPAs) – Institutional and Substantive Issues*, Danish Institute for International Studies (2007) p. 14

wherefore the new approach with EPAs is seen as a tool to rejuvenate these relations.⁷ The EU did then start up negotiation with the ACP countries in an effort to conclude reciprocal EPAs, a process that however, have proceeded very slowly. The Caribbean country group or the CARIFORUM is therefore the only group with which the EU has successfully negotiated a full EPA as of January 1 2008, while several other ACP countries have concluded EPAs without entering into an agreement for their entire country group. The remaining ACP countries have instead had to conclude interim agreements with the EU, in order not to violate WTO obligations. Interim agreements that have been concluded under either the GSP or the EBA regimes.⁸

2.1 Government Procurement in the EPAs

The EU has not limited the scope of the EPAs to the traditional issues of trade concessions and market access commitments, but has also been pushing for the inclusion of the ‘Singapore issues’ in the EPA negotiations. These issues are *trade facilitation, competition, investments* and *government procurement* and were first raised under the inaugural WTO Ministerial in Singapore (hence the name) in 1996.⁹ The focus on these trade related issues and ‘behind border’¹⁰ trade barriers has been considered critical to the EU’s commercial interests, which lead the EU to push for an inclusion of the Singapore issues as a part of the Doha negotiations.¹¹ This approach was nonetheless largely unsuccessful due to the strong resistance from many developing countries, wherefore *trade facilitation* is the only remaining issue that is still included in the negotiations.¹² The opposition from ACP countries has also lead the EU to somewhat soften its demands for the inclusion of the Singapore issues in the EPAs and the EU has not taken any official position on the mandatory inclusion of the issues. The EU has instead chosen to approach the issues in informal negotiations, an approach that was confirmed by Pascal Lamy who, while being EU Trade Commissioner in 2004, stated that:

‘Investment, public (government) procurement and competition are areas which we are always addressing in our bilateral free trade agreements.’¹³

This position has later be relaxed and Deputy DG Trade Karl Falkenberg has claimed that the EU only emphasis *investments* as a necessary

⁷ The EU are however the main trading partner for most ACP countries and for virtually all African ACP countries; http://ec.europa.eu/trade/issues/bilateral/regions/acp/index_en.htm

⁸ For a summary of the state of the EU-ACP agreements, see Annex 1.

⁹ http://www.wto.org/english/thewto_e/whatis_e/tif_e/bey3_e.htm

¹⁰ Speaking points of Commissioner Mandelson, October 4 2006;

http://ec.europa.eu/commission_barroso/mandelson/speeches_article/sppm117_en.htm

¹¹ Goodison, *The future of Africa’s trade with Europe: ‘New’ EU Trade Policy*, Review of African Political Economy 34:111 (2007) p. 140

¹² Alavi et al., *supra* note 6, p. 60

¹³ http://www.bilaterals.org/article.php3?id_article=610

component of any EPA.¹⁴ The Singapore issues and government procurement regulations have however, been included in some of the EU's bilateral trade agreements outside the EU-ACP relations, such as the agreements between the EU and Mexico and Chile.¹⁵ This is also the case for the only major EPA in place, namely the one between the EU and the Caribbean countries, which was concluded on December 16 2007. This EPA encompasses trade related issues such as competition, environmental concerns, intellectual property right, as well as public procurement. The public procurement chapter is mostly concerned with provisions intended to increase transparency and regulates the manners in which the public procurement process is carried out.¹⁶ This focus on transparency is something that the EPA's public procurement regulation has inherited from the WTO framework, which for a long time has been centred on transparency.

The EPA between the EU and the ACP countries finds its legal basis in Article XXIV GATT, which makes up an exemption from the *most favoured nation* rule for the establishment of *free-trade areas*. This exemption is allowed because global trade liberalization is perceived to occur faster if pursued within regional trading block.¹⁷ The free-trade areas have to be reciprocal in nature even if they may be asymmetrical, in order to take account of the developing status of most ACP countries.

The position taken by the EU and the pursuance of reciprocal trade agreements have however been criticised by several NGOs,¹⁸ in regards to which Oxfam has urged that the EU should include non-reciprocity and exclude the Singapore issues from the negotiations with ACP countries.¹⁹ These critics have then lobbied for alternatives to the EPAs such as agreements based on the EBA or GSP regimes, which would not 'force trade liberalisation' on ACP countries, while they in the same time would bring EU-ACP relations into accordance with WTO legislation.²⁰ The use of trade schemes under the GSP system, as a replacement for the old EU-ACP agreements, has also been advocated in the academic literature as a more beneficial alternative, especially for the ACP countries.²¹ This argumentation has however been criticised by the European Commission for making use of models that are 'not legally feasible', since their assumptions are not WTO compatible, wherefore EPAs still is the 'first-best optimum for

¹⁴ http://www.bilaterals.org/article.php3?id_article=5206&

¹⁵ http://ec.europa.eu/trade/issues/bilateral/countries/mexico/fta_en.htm

http://ec.europa.eu/trade/issues/bilateral/countries/euchlagr_en.htm

¹⁶ *European Partnership Agreement between the CARIFORUM states, of the one part, and the European Community and its member states, on the other part*, Article 168 ff.

¹⁷ Van den Bossche, *The Law of the World Trade Organisation* (Cambridge University Press, Cambridge (2005) p. 651

¹⁸ Alavi et al., *supra* note 6, p. 15

¹⁹ Oxfam, *Making trade work for development in 2005 – What the EU should do*, Oxfam Briefing Paper (2005) p. 20

²⁰ Bilal, & Rampa, *Alternative (to) EPAs – Possible scenarios for the future ACP trade relations with the EU*, Policy Management Report 11, ECDMP (2006) p. 65 ff.

²¹ Perez, *Are the Economic partnership Agreements a First-best Optimum for the African Caribbean Pacific Countries?*, *Journal of World Trade* 40:6 (2006) p. 1015

the ACP countries'.²² The purpose of this paper does however not aim at analysis which trade regime that may be most preferential for the ACP countries, but rather evaluate the effects on the alternative chosen. The EU has also maintained its preference for EPAs and continued to pursue agreements including the Singapore issues.

2.2 Economics of EPAs

The general rationale for the establishment of EPA is the same as for trade liberalisation as a whole, where it is considered to result in efficiency gains for all concerned parties. The effects of EPAs can, according to the theories of economic integration, be thought of as *trade creation*, when domestic products are substituted by imports of low-cost goods produced by the partner country, and *trade diversion*, which occurs when the imports shift from the least-cost exporter to the more expensive product of the partner nation.²³ This can be exemplified in *Figure 1*, by two small developing countries home (H) and partner (P), which initially has formed a PTA, as in the real situation of many ACP countries. In the pre-PTA equilibrium there is no difference in the cost of imports from the EU and ROW. The size of the supply of (H) and (P) is relatively small to the EU and the ROW who supply at constant prices. The presence of discriminatory trade policies as a result of the PTA, could then give rise to both trade creation and trade distortion (if one further assumes that $P_{EU} > P_{ROW}$). D_H is furthermore home's demand and S_P the partners supply, while S_{EU} and S_{ROW} is the supply of the groupings outside the PTA. The imposition of a tariff on imports stemming from outside the PTA lead to the price $P_{ROW}^t (= P_{ROW}(1+t))$.²⁴ The home country imports OM_2 , where OM_1 comes from the partner country and the amount M_1M_2 from the ROW. The welfare of the home country, W_{FTA} , is then made up by the consumer surplus (the triangle ABP_{ROW}^t) and the tariff revenues from imports from the EU and the ROW (area $a+b$). If the PTA would conclude an EPA with the EU, the EU would maintain its tariff against ROW but allow duty free imports from the countries of the PTA. The relevant price would then be P_{EU} , with imports increasing to OM_3 , imports that now exclusively stems from the EU. The EPA does then create three main effects; *consumption expansion effect* (M_2M_3), a *trade diversion effect* (M_1M_2) and a *trade creation effect* (OM_1). The trade diversion is present since more imports are made from the less efficient EU rather than the ROW, meaning a loss for the PTA countries due to less tariff revenues, equal to b . The consumption effect is represented by e , the trade creation effect is equal to c , which together with the loss in producer surplus for the country exporters d , allow the consumer surplus to increase by $(c+d+e)$.

²² Curran, *Response to the Article 'Are the Economic partnership Agreements a First-best Optimum for the African Caribbean Pacific Countries?'*, Journal of World Trade 41:1 (2007) p. 243

²³ Borrman et al., *supra* note 4, p. 171

²⁴ Since the cost of the EU supplier is higher than the ROW, P_{EU}^t does not have to be accounted for in the model.

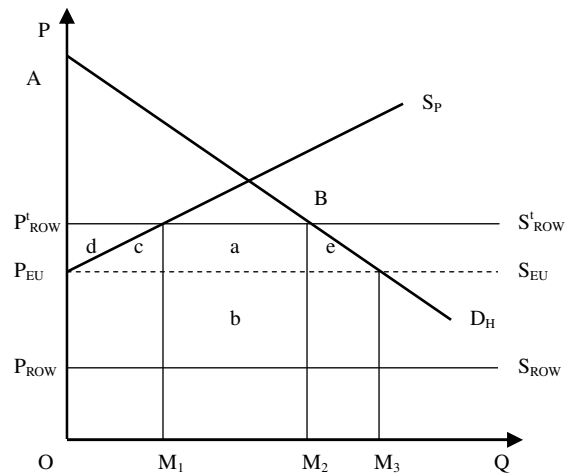


Figure 1. Effects of an EU-ACP EPA

Source: Milner et al., p. 333 & McKay et al., p. 6

The all-together welfare effects for the home country is then given by $\Delta W=(c+d+e)-b$. The size of the gains for the home country is thereby highly dependent on the size of the trade diversion, which should be kept to a minimum to make the EPAs as welfare improving as possible. This also mean that the more efficiency the EU is and the closer its prices are to the ROW, the greater the gains will be for the home country, until the situation where $S_{EU} \rightarrow S_{ROW}$, which creates the same outcome as with free trade.²⁵ The EPA may not be as welfare maximising as the situation of free trade but the gains for domestic consumer is thought to outweigh the potential loss caused to domestic producers. These does then, in addition to the gains for foreign producers that now have increased access to the market of (H) & (P); clearly make a strong case for the theoretical gains of EPAs.

In addition to the above accounted for *static welfare effects* there are also *dynamics effect* connected with the establishment of EPAs, effects that are likely to add to the benefits that the ACP countries can experience. These effects may include:²⁶

- increased levels of investments;
- lock-in effects of domestic policy reforms
- conventional gains from rigorously implemented regional integration
- transfer of technology
- increased competition

These effects do then need to be included into the evaluation of EPAs, in order to fully appreciate its overall economic effect.

²⁵ Milner et al., *Some simple analytics of trade and welfare effects of Economic Partnership Agreements*, Journal of African Economies 14:3 (2005) p. 334

²⁶ Matambalya & Wolf, *The Cotonou Agreement and the Challenges of Making the New EU-ACP trade Regime WTO Compatible*, Journal of World Trade 35:1 (2001) p. 125

The imposition of an EPA will thus give rise to both positive and negative effects, even if economic theory suggests that the positive outweigh the negative. These effects do however have special implications for ACP countries that might not possess the capabilities to cope with these effects in the same manner as many high-income nations. The loss of tariff revenue as a consequence of an EPA is such an effect that will greatly affect many ACP countries, since income from tariffs make up an important part of most developing countries governments' budget revenues.²⁷ Wherefore a tariff decrease will clearly restrict the governments' possibilities to supply public goods such as education and infrastructure.²⁸ The fact that the reduction in tariffs revenue might be outweighed by gains for domestic consumers will then be little consolation for governments seeing their income plunders. The special situation of many ACP countries then mean that a 'true' estimate of the impact of EPAs cannot be evaluated theoretically but must be analysed empirically.²⁹

2.3 Empirical evidence

The different empirical studies that have tried to estimate the effects of FTAs such as the EPAs have usually come to inconsistent conclusions. The trade effects, in the case of the ECOWAS countries, have been rather small, even if *trade creation* seems to dominate *trade diversion* in all the measured countries. The negative impact of tariff reduction is also significant with an overall decline in government revenues estimated between 4 to 9 percent.³⁰ Another study on the effect of the FTA within the East African Cooperation between Kenya, Tanzania and Uganda, came to largely the same findings as in the study in the ECOWAS countries.³¹ There does therefore not seem to be any conclusive empirical evidence that would allow a general conclusion in regards to the prevailing welfare effects of an EPA. This then establishes the need for economic analysis on a case-to-case basis, in order to take account of the special situation of the regions in question.

2.4 Existing procurement regulations

The Singapore issues and especially public procurement has previously been extensively addressed within the global trade forum of the WTO, even if public procurement is outside the scope of multilateral trade agreements and is exempted from the general national treatment obligation.³² The issue has

²⁷ Todaro & Smith, *Economic Development*, Pearson Education, Harlow, 9th Edition (2006) p. 631

²⁸ Borrmann et al., *supra* note 4, p. 171

²⁹ Ibid.

³⁰ Busse & Großmann, *The trade and fiscal impact of EU/ACP economic partnership agreements on West African countries*, Journal of Development Studies 43:5 (2007) p. 808

³¹ McKay et al., *The trade and welfare effects of a Regional Economic Partnership Agreement*, Credit Research Paper No. 00/08 (2000) p. 19

³² Article III:8 GATT & Article XIII:1 GATS

instead been targeted under bilateral negotiations, where the first international agreement on government procurement was negotiated under the Tokyo Round. The outcome of these negotiations was the Agreement on Government Procurement (GPA), an agreement that was later replaced by a new agreement, signed at Marrakesh on April 15 1994.³³ The objectives of the new GPA are found in its preamble, which reads:

'[C]ontribute to greater liberalization and expansion of world trade; eliminate discrimination among foreign products/services or foreign suppliers; and enhance the transparency of relevant laws and practices.'

The version put into place by the Uruguay Round does not only aim at the central government but also peripheral government such as state, province, district etc.³⁴ Unlike its predecessor, the agreement does also contain a strong and fast enforcement mechanism as well as various provisions aimed at improving transparency and equal treatment of supplier of services.³⁵ The agreement's main aim is to strike a balance between, on the one hand, the 'free trade' concerns of non-discrimination and transparency and, on the other, the governments' ability to implement legitimate domestic policies.³⁶ The GPA has mostly attracted developed countries as signatory members, and developing countries have been very reluctant to join the agreement. This strong opposition from both developing countries and transition economies has then lead the EU and the US to shift the focus away from the general liberalization of procurement markets towards achieving increased transparency in these markets.³⁷ The has however not pleased critics who see multilateral agreement on transparency as just another way of sneaking in public procurement in the trade relations with developing countries.³⁸

The EU policy toward the inclusion of procurement in the EPAs is partly due to is own experience of the issue, where the EU has had a long internal regulation within public procurement. Such internal legislation is fundamental since a non-discriminatory public procurement regime is necessary to sustain the foundations of European integration such as the freedom of movement of goods and services.³⁹ Studies that have been made on the undergone liberalization of public procurement in the European market have shown that the increased competitiveness of the Community procurement market has had large effects on public spending. This has then

³³ Hoekman, & Mavroidis, *The World Trade Organization's Agreement on Government Procurement – Expanding Disciplines, Declining Membership?*, World Bank Policy Research Working Paper 1429 (1995) p. 1

³⁴ Gordon et al., *The Economic Impact of the European Union Regime on Public Procurement: Lessons of the WTO*, Blackwell Publishers Ltd, London (1998) p. 162

³⁵ Trionfetti, *Discriminatory Public Procurement and International Trade*, *The World Economy* 23:1 (2000) p. 59

³⁶ Arrowsmith, *Reviewing the GPA: The role of and development of the plurilateral agreement after Doha*, *Journal of International Economic Law* 5:4 (2002) p. 767

³⁷ Panagariya, *Developing countries at Doha: A political economy analysis*, *The World Economy* 25:9 (2002) p. 1216

³⁸ Khor, *Government procurement in FTAs: An outline of the issue*, *Third World Network* (2005) p. 3

³⁹ Bovis, *EC Public Procurement Law*, Longman, Harlow (1997) p. 102

led to better and cheaper quality goods, as well as lower service costs and is estimated to have contributed to a 30 percent decrease in prices.⁴⁰ The possible efficiency wins, as been experienced by the EU, has then led it towards its current favouring of the introduction of public procurement into its bilateral trade agreements. It is however not solely altruistic reasons behind this approach, and the prospect of increasing export market for EU exporters is surely an important factor.

⁴⁰ European Commission, *Report on the functioning of public procurement markets in the EU: benefits from the application of EU directives and challenges for the future* (2004) p. 15

3 Economics of Government procurement

Government procurement has always been used as a way for governments to give preferential treatment to domestic suppliers.⁴¹ The general underlying assumption in this analysis is therefore that government wants to discriminate against foreign producers or suppliers when awarding contracts.⁴² Such discriminatory practises permits the channelling of government funds to domestic producers and are considered 'fair' since the funds initially belonged to the taxpayers.⁴³ The awarding of preferential government contracts is also used as a tool to implement countries strategic trade policy, as a part of their overall industrial policy. Other rationales have also be advocated, such as national security considerations or other non-economic objectives, like supporting SMEs and reserving a certain number of contracts for businesses; owned by minorities, or located in certain regions.⁴⁴ The level of public expenditure and its direction can furthermore be seen as an important macroeconomic instrument, which could be used to counter economic downturn in times of recession.⁴⁵

The following exemplification of the economic implications of government procurement will first focus on the potential gains that follow from increased market access. The effect of discrimination in procurement markets will then be analysed in the light of the most common trade theories.

3.1 Market access

The main gain for the EU from the inclusion of government procurement in the EPAs is the potential increase in market access for European exporters.⁴⁶ The gain stemming from a larger export market may seem rather clear-cut, but a basic model can nonetheless exemplify the situation. The basic implication of an EPA is that European producers will gain increased preferential market access to ACP countries markets. The efficiency implication will depend on the size of the home (H) and partner (P) countries, but in the case of the EU-ACP countries, it is likely that the EU is much larger than the partner country wherefore it seems reasonable to

⁴¹ Baldwin, *Trade in Policies in Developed Countries*, in *Handbook of International Economics Vol 1*, R. Jones & P. Kenen (eds.), Elsevier Science Publishers B.V. (1984) p. 602

⁴² Hoekman & Mavroidis, *supra* note 33, p. 13

⁴³ Miyagiwa, *Oligopoly and Discriminatory Government Policy*, *American Economic Review* 81:5 (1991) p. 1320

⁴⁴ Evenett & Hoekman, *Government procurement: market access, transparency, and multilateral trade rules*, *European Journal of Political Economy* 21(2005) p. 16

⁴⁵ Khor, *supra* note 38, p. 5

⁴⁶ European Commission, *Global Europe: Competing in the world* (2006) p. 9

assume that the EU is not a price taker and thus enjoys regional market power. The model in *Figure 2* is initially meant to explain the impact of tariff preferences in regional markets, but it can also be used to explain the effects when EU producers gain increased market access to a regional ACP group.⁴⁷

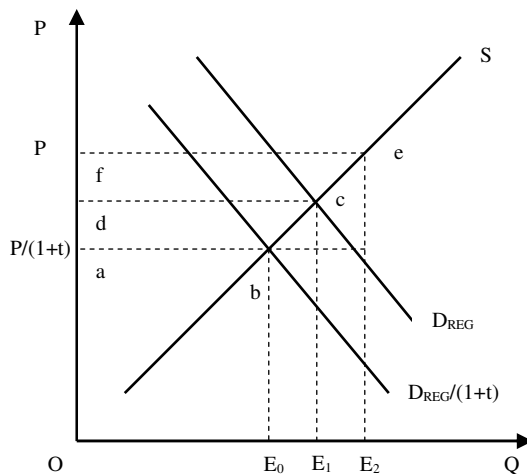


Figure 2. Gains of market access

Source: Bakoup & Tarr, p. 169

The supply curve for the EU to the ACP countries' market is S , the price $P/(1+t)$ and the initial demand for EU export in the ACP countries $D_{REG}/(1+t)$. If the EU is then gaining full market access in government procurement markets, it can be represented by a removal of the tariff giving the new equilibrium price and quantities is in d and E_1 . The effect will thereby be an expansion of the producer surplus of the EU's producers by $abcd$,⁴⁸ which then makes up the theoretical justification for the EU's persistent demands for increased market access for European producers within the EPAs.

3.2 Government Procurement

The gains of market access are foremost connected with European producers, while the effects within procurement markets are more relevant for the ACP countries. The three major theoretical models within the field of trade theory; the *Heckscher-Ohlin model*, the *New Trade Theory* and the theories of the *New Economic Geography*, will in the following exemplify these main effects. Even though this chapter will handle all three models, then focus will be on the perfect competitive model since it has been suggested by empirical studies that price-cost mark-ups moves towards

⁴⁷ Bakoup, & Tarr, *The Economic Effect of Integration in the Central African Economic and Monetary Community: Some General Equilibrium Estimates for Cameroon*, African Development Bank, Blackwell Publishers,(2000) p. 168

⁴⁸ If the EU was considered a price taker the gains would be even higher with the quantity rising to E_2 , and the additional welfare gains equalling $dcef$.

competitive conditions once the number of producers within a sector exceeds five.⁴⁹ This would then mean that the governments are able to source from a large number of small firms, none with market power, a market characteristic than fulfils the conditions of the H-O model.

3.2.1 Heckscher-Ohlin

The first person to study the effects of discriminatory public procurement regimes was Baldwin, who made use of the Heckscher-Ohlin model to exemplify the effects on domestic output, prices and imports. The underlying assumption of the H-O model is a situation of perfect competition with homogeneous goods, as well as identical production function between countries, which comes from the assumption of identical technologies, which in turn leads to constant return to scale.⁵⁰

3.2.1.1 Ban of foreign suppliers

The basic H-O model provides for an illustration of what happened to the free trade equilibrium when the government implements a procurement regime that bans foreign suppliers of the good. The effect of such regime will depend on the size of government demand in relation to domestic supply, wherefore two possible scenarios are likely to occur.⁵¹

If government demand is smaller than domestic supply ($D_G < S_H$) and the government impose a procurement ban on foreign producers; there will not occur any change in equilibrium prices, imports or the quantity supplied by domestic firms, because the foreign producers that are being discriminated can solely shift their supply to domestic consumers.⁵² The domestic suppliers can not affect the price charged by the government since other domestic producers are ready to step in and supply at the existing world price. These finding continue to hold in the long run perspective with the allowance of entry of new firms, since the procurement ban does not change the profitability of the domestic producers. The other possible scenario is when government demand exceeds domestic supply ($D_G > S_H$). The imposition of a ban on procurement from foreign suppliers would then lead to an increase in the price received by domestic suppliers since the government is willing to pay a higher price to fill its demand. The price increase creates higher profits for the domestic firms and restricts the market access for foreign firms that lead to a reduction in imports. The finding are upheld in the long run scenario if no new firms are allowed entrance onto the market, while the possibility of new entrants means that new domestic

⁴⁹ Bresnahan & Reiss, *Entry and Competition in Concentrated Markets*, The Journal of Political Economy 99:5 (1991) p. 996 ff.

⁵⁰ Markusen et al., *International Trade – Theory and Evidence* (McGraw-Hill, Singapore, 1995) p. 98

⁵¹ Baldwin, *supra* note 41, p. 603

⁵² Trionfetti, *supra* note 35, p. 65

firms will enter until all profits are eliminated and prices are restored at world market prices.⁵³

3.2.1.2 Price preference policy

The assumption of a complete ban of foreign producers might be somewhat unrealistic, wherefore a more realistic approach would be a discriminatory price preference policy. This policy would then increase the supply price of foreign producers with a certain percentage, meaning that these foreign suppliers would still have market access even if they face other terms of competition. The policy implies that the government would purchase from the foreign suppliers at their actual price (without the increase), if the foreign producers' inflated price would be lower than the price at which the domestic producer were willing to supply. The procurement would thus be made from the domestic suppliers in situations where the domestic price is less than the inflated foreign price; giving domestic suppliers a clear competitive edge in the awarding of government contracts.

If government demand is less than domestic supply ($D_G < S_H$); one will get the same result as with a ban, i.e. none. Whereas the effect when government demand exceeds domestic supply ($D_G > S_H$), will depend on the size of the price preference. If the price preference is large enough, it will price out foreign suppliers from the market and only domestic producers would meet government demand. This would then lead to an increase in the price paid by the government, increasing domestic output, and an elimination of imports, since solely domestic producers can supply the government. If the price preference is smaller it would not price out foreign suppliers and still allow for some imports, giving rise to a smaller increase in prices and domestic output. The price preference is thus creating distortions to consumption and resource allocation, thereby creating rents for domestic firms. If new firms were allowed to enter, they would therefore continue to do so until all rents are eliminated, reducing the long run equilibrium of imports to zero.⁵⁴

3.2.1.3 Non-tradable goods

Government procurement is not only concerned with goods but also with services, which are considered non-tradable goods. These goods will then lack world prices and their prices will instead be dependant on the costs of local factors and differences in production technologies.⁵⁵ If the government impose a ban on foreign procurement and the market conditions are ($D_G < S_H$), there will just as in previous examples only be a reallocation of customers to foreign affiliates and no effects on price or domestic output.⁵⁶

⁵³ Evenett & Hoekman, *supra* note 44, p. 170

⁵⁴ *Ibid.* p. 174

⁵⁵ The ban on foreign procurement is considered to apply to subsidiaries of foreign firms that have already established presence on the home market (allowing the same basic model to be used as in previous examples).

⁵⁶ Evenett & Hoekman, *supra* note 44, p. 176

If ($D_G > S_H$), there will be a segmenting of the market where home producer will supply the government at a higher price than the price at which the foreign affiliates are left supplying the private sector. The short run effects will therefore give rise to both consumptions and production distortions, even if the consumers will (unlike the case of goods) experience higher welfare. The reason for this effect is that the exclusion of foreign supply to the government will create an excess supply than can only be swallowed by the domestic consumers if the price is lowered to correspond with their willingness to pay. This situation cannot be maintained in the long run since foreign suppliers are losing money and will chose to exit the market, until they reach their break-even price. The domestic producers' profits will also decline with the entry of new domestic suppliers, until all firms make zero profit. The long run effect is therefore an increase in the number of domestic supplier and a decrease in foreign entities, and another consequence is that both the consumers and the government will end up facing the same price.⁵⁷

The above-described situations are carried out under the somewhat unrealistic assumption of perfect competitive market conditions, wherefore there is a need to expand the analysis to encompass also non-competitive markets.

3.2.1.4 Oligopolistic markets

The basic model developed by Baldwin has been extended by Miyagiwa to cover situations that share the characteristics of an oligopoly market. The study showed that the findings of Baldwin continues to hold if the goods are perfect substitute, and the discriminatory procurement regime will thus affect neither the output nor the equilibrium price, thereby not making any difference in regards to the import levels or the gains of specialisation.⁵⁸ Miyagiwa did also investigate the case of heterogeneous goods, in regards to which the findings proposes that import potentially could be increasing because of discriminatory procurement practices, while in the same time raising the price of the domestic goods. This finding is however conditional on the presumption of a sufficiently convex demand function.⁵⁹ The main contribution of the Miyagiwa model was thus that it extended the findings of Baldwin's study to oligopoly markets with homogenous goods.

Public procurement in non-competitive market is also investigated under the models of New Trade Theories and New Economic Geography that take account of increasing returns to scale and monopolistic competition.

⁵⁷ Ibid. p. 177

⁵⁸ Miyagiwa, *supra* note 43, p. 1322

⁵⁹ Ibid. p. 1325

3.2.2 New Trade Theories

The New Trade Theories or New Growth Theories were developed to handle with situation that meant a relaxation of the underlying assumption of the H-O model, wherefore the model emphasises increasing returns to scale and imperfect competition.⁶⁰ The most common referred to non-competitive market condition is monopolistic competition, which has many producers supplying the same commodity, while each one produces a different variety of the commodity.⁶¹ The notion of increasing returns to scale is furthermore a result of the allowance of differences in production technology, which brings with it economies of scale and falling average costs as output increases. The NTT do then assume that a country with a relatively large domestic demand for a commodity are going to specialise in the production of that product, since demand is endogenous and the country's relative demand relates to the country relative output of the commodity. The imposition of a home biased government procurement regime is then going to increase the size of the domestic demand for the commodity and consequently increase the domestic output of the good.⁶² Thereby reducing imports and increase domestic production, and in effect becoming a barrier to trade which limit trade flows, a result in line with the general effects under the H-O model.

3.2.3 New Economic Geography

The New Economic Geography retains the assumption of increasing returns to scale, monopolistic competition and endogenous demand from the New Trade Theory, but emphasis that demand depends of the relative size of output thought agglomeration and dispersion forces. The model takes note of trade cost and focuses on agglomeration forces that will originate as a consequence of the producers will to produce where demand is large and producers can benefit from low trade costs. The agglomeration will then lead to a relocation of production until the dispersion forces takes over, which will happened when the increased competition makes producers move out from the region to find new markets. The deciding factor for whether agglomerations or dispersion forces prevail will then be the size of trade costs, wherefore an increasing reduction of trade cost are likely to reinforce agglomeration forces and give rise to an increasing international specialisation.⁶³ This specialisation will express itself in that the production of the commodity will agglomerate in countries or regions where the initial demand is large.⁶⁴ These patterns of specialisation of production has been

⁶⁰ Markusen et. al, *supra* note 50, p. 419

⁶¹ Trionfetti, *supra* note 35, p. 66

⁶² *Ibid.* p. 67

⁶³ Ottaviano & Puga, *Agglomeration in the Global Economy: A survey of the 'New Economic geography'*, *The World Economy* 21:6 (1998) p. 724

⁶⁴ Krugman, *Geografi och handel*, SNS Förlag, Stockholm (1996) p. 51 ff.

found present in the European and American markets, even if the market characteristic between the two differs in some ways.⁶⁵

The imposition of public procurement regime can thereby work both as an agglomeration and dispersion force depending under which conditions it is implemented. The sector with a relatively large public procurement regime, will tend to specialise in the production of that good, where the procurement in essence work as a production subsidy, thus leading to a divergence from the free trade equilibrium and an accompanying welfare loss.⁶⁶ The welfare loss is however no conclusive, since discriminatory procurement regimes may also improve welfare. This comes from the 'second best' notion that since markets are already characterized by distortions in form of monopolistic competition and trade cost, the introduction of a third distortion (i.e. discriminatory government procurement) will not necessarily be welfare reducing.⁶⁷ Government should then in order to minimize government spending; favour domestic producers in industries where the producers have a comparative disadvantage and favour foreign producers when domestic industries have a comparative advantage.⁶⁸ These industrial policy interventions are however, contingent on the successful identification of these key industries and sector. This is not easily done wherefore the most efficient and welfare maximising solution is likely to be a non-discriminatory procurement regime.⁶⁹

The empirical examination of agglomeration and dispersion forces have supported these theoretical implications and shown that agglomeration will occur in market that are characterised by non-competitive conditions. This has been the case in many European countries, where countries with a home biased government procurement regime, tend to host a relatively large share of the world production of the 'supported' good.⁷⁰ The existence of dispersion forces that will work against global agglomeration have also been examined empirically. The existence of dispersion forces or the 'spread effect' have then been found within several European markets, where industries with a relatively large support of public procurement will be less concentrated across European countries.⁷¹ The theoretical explanation for dispersion forces is that the government policy will encourage suppliers from moving by ensuring that these producers will make larger profits from their transactions with the domestic government, then possible if they adhered to agglomeration forces and relocated production to foreign market.

⁶⁵ Brülhart, *Economic Geography, Industry Location and Trade: The Evidence*, Blackwell Publishers Ltd. (1998) p. 797

⁶⁶ Markusen et. al, *supra* note 50, p. 250

⁶⁷ Trionfetti, *Public Procurement, Market Integration and Income Equalities*, Review of International Economics 9:1 (2001) p. 28

⁶⁸ McAffe & McMillan, *Government procurement and international trade*, Journal of International Economics 26 (1989) p. 304

⁶⁹ For more on the efficiency implication of industrial policy measures, see Nordeman, *State Aid in the EU – Economic and Legal Aspects*, Lund University Bachelor thesis (2008)

⁷⁰ Brülhart & Trionfetti, *Public expenditure, international specialisation and agglomeration*, European Economic Review 48 (2004) p. 871

⁷¹ *Ibid.* p. 875

Tabel 1. The effects of discriminatory public procurement

	Effect on price	Domestic industry output	Quantity of imports
Heckscher-Ohlin			
- Procurement ban			
$D_G < S_H$	0	0	0
$D_G > S_H$			
Short run	+	+	-
Long-run			
<i>No free entry</i>	+	+	-
<i>Free entry</i>	0	+	-
- Price preference			
$D_G < S_H$	0	0	0
$D_G > S_H$			
Short run	+	+	-
Long-run			
<i>No free entry</i>	+	+	-
<i>Free entry</i>	0	+	-
Nontradable goods*			
- Procurement ban			
$D_G < S_H$	0/0	0	
$D_G > S_H$			
Short run	- / +	+	
Long-run			
<i>No free entry</i>	0/+	+	
<i>Free entry</i>	0/0	+	
Oligopolistic markets			
-Price preference	0	0	0
New Trade Theories	0	+	-
New Economic Geography	+/-	+/-	+/-

0: no change from the initial long-run equilibrium; -: decline; +: increase.

* Since a ban on foreign-owned firms segment the market, there will be different prices facing the consumers and the government; in table (P_C/P_G).

3.3 Common Trade effects

The different models do not provide for any general conclusion on the efficiency and trade implication of public procurement practise, since there are a certain number of special case scenarios and assumptions have to be fulfilled for each model to apply. There do however seem to be sufficient backing of the notion that discriminatory public procurement creates a divergence from the free trade equilibrium, giving rise to an efficiency loss and thereby constituting an obstacle for the fulfilment of economic integration and gains of specialization. The effects that the described models entail for price, domestic production and imports are summaries in *Tabel 1*.

The effect of a ban or a price preference in regards to procurement will thereby be foremost decided depending on whether government demand exceeds domestic supply. In regards to which it has been argued, that government demand only makes up a fraction of domestic supply for most goods, thus keeping any effects rather limited.⁷² The contrary might however, be truer for many developing countries with lacking production capability, wherefore the described effects will be applicable to many low-income ACP countries. The limited production possibilities for many ACP countries would then increase the likelihood that government demand exceed domestic supply, wherefore the resulting trade restrictive effects are more likely to be present in regards to these countries. Another factor of great importance is also the difference between the ban and the price policy in the long run, where the later can eliminate imports completely. Thereby implying that even a small price preference can create a long run increase in domestic production and a corresponding reduction in imports, wherefore both bans and price policies risk distorting international trade flow.

The decrease in gains of specialization depends on which model that is examined. The H-O model will only experience a loss if the procurement is large enough to effect output and thereby cause a misallocation of resources. While the NTT and NEG models predict that any discriminatory procurement will affect output even if the distortion is too small to cause a misallocation of resources. These models do thereby constitute a theoretical basis for the implementation of small-scale procurement schemes, which might achieve its intended industrial policy goal without interfering with efficiency decisions in private production and consumption.⁷³

All these three models can favourably be considered in combination, in order to provide the best possible description of home biased procurement. An approach that has been utilized in studies that have shown that the two different market structures, one with constant returns to scale and perfect

⁷² Baldwin, *supra* note 41, p. 603

⁷³ Trionfetti, *supra* note 67, p. 68

competition and the other with increasing returns to scale and monopolistic competition, indeed can coexist in a single model.⁷⁴

3.4 Discriminatory public procurement compared to other trade barriers

It is evident from trade theory that discriminatory procurement practises are likely to reduce imports and favour domestic industry much like other protectionist trade policies. These effect on trade can also be exemplified by a comparison between bias procurement regimes and other common obstacles to trade.

The imposing of an *import tariff* will give rise to an efficiency loss, while in the same time raising the prices facing consumers, thereby distorting both the gains from exchange and specialisation, while creating a source of revenue for the government.⁷⁵ The *production subsidy* is another common barrier to trade which like discriminatory procurement practises might be used to promote domestic industries. The subsidy will lessen the actual production cost for the receiving producers, while leading to higher consumers prices. The gains of exchange will however remain the same and the only loss will be to the gains of specialisation.⁷⁶ Discriminatory public procurement will support domestic industries, but unlike the subsidy, do this without distorting consumer prices. The government will in the same time experience an efficiency loss since it will be faced by a higher price than if foreign producers could supply the good. Since the government will discriminate foreign suppliers, it follows quite naturally that, it will not be able to maximize output, unless the most efficient solution would coincide with the same purchase pattern as under the discriminatory practise.

The perhaps most relevant effect for the EPAs is then the implication of government procurement on trade. This effect does then legitimate the need to address the issue in global trade negotiations since discriminatory practises indeed create obstacles to trade. Adding to this notion is also the considerable size of public procurement in relation to most countries total government expenditure.

⁷⁴ Helpman, & Krugman, *Trade Policy and Market Structure*, MIT Press, Cambridge (1989) p. 155 ff.

⁷⁵ Markusen et al., *supra* note 50, pp. 247-248

⁷⁶ *Ibid.* p. 252

4 Size of Public Procurement markets

There are always some inherent problems when handling ACP country data due to the lack of reliable statistics. The statistics in government procurement for developed countries are however well known and can be used as a benchmark for comparison with developing countries. Most developed countries are according to IMF data estimated to have government procurement expenditure at an average between 20-30 percent of GDP. There are large variations among countries, with countries like the US is near 20 percent, while e.g. the UK just exceeds 40 percent of GDP.⁷⁷ These figures do however overestimate the size of public procurement markets since they include expenditure as social security, pension transfers and health care.

In addition to the data from the IMF, there are also some complementary surveys on government expenditure made by the OECD and the UN.⁷⁸ The OECD and UN surveys are based on the same data, and are therefore perfectly compatible. The data includes all levels of government and not only central government, which in that case, would largely underestimate the size of government procurement. The major flaw in the data is however present in regard to developing countries where the difficulties in accessing accurate figures for these countries have lead to that only central government figures are accounted for, leading to a significant underestimation of the actual procurement levels.⁷⁹ Keeping these limitations in mind one might nonetheless study the available figures to get an idea of the magnitude of public procurement in developing countries.

The study by the OECD makes use of the System of National Accounts (SNA), and includes the size of public procurement in 106 non-OECD countries (of which 30 are ACP countries).⁸⁰ The data in the study is based on the final consumption expenditure (FCE) which accounts for government expenditure that include all net cost of service production by governments such as compensation of employees, consumption of fixed capital and indirect taxes. The FCE average for non-OECD countries is estimated to 14 percent of GDP, while the corresponding numbers for OECD countries are 17 percent of GDP.

The FCE data are however too general and its scope covers too many government activities for it to provide an indication of the size of procurement market that could actually be opened for foreign competition.

⁷⁷ IMF - *Government Finance Statistics*, GFSM (2001)

⁷⁸ OECD, *National Accounts*; UN, *National Accounts: Main Aggregates and Detailed Tables*

⁷⁹ Trionfetti, *supra* note 35, p.59

⁸⁰ OECD, *The Size of Government Procurement Markets*, Paris (2002) Annex Table A2

For this purpose, it is then better to use the FCE data, with the exclusion of defence expenditure (*excl. def.*) and compensation of state employees (*excl. comp.*). These numbers are unfortunately not well accounted for among non-OECD countries and only six ACP countries have comparable data provided for, data that is found in *Table 2*.

Table 2. Size of Government Procurement in some ACP Countries								
Region General Government	Consumption expenditure (%)				Total expenditure (TE) (%)			GDP 1998 (USD Billions)
	FCE	Excl. comp.	Excl. def.	Excl. comp. & def.	TE	Excl. comp.	Excl. comp. & def.	
Kenya	16,27	3,16	14,43	2,75	19,17	6,06	5,66	10,37
Mauritius	11,23	3,23	11,73	3,07				4,20
Nigeria	3,89	1,23						36,14
Namibia	29,33	9,89			35,78	16,34		3,00
South Africa	19,74				21,77			116,73
Bahamas	14,06	3,42	13,42	3,27	14,62	3,92	3,83	4,12

This data source has obvious limitations, but can still be used as an estimation of the general procurement market in developing countries. The small sample of ACP countries is even smaller in regards to the contestable expenditure that is only accounted for Kenya, Mauritius and Bahamas. The contestable consumption is the around 3 percent, which seem rather low, but due to the limited data source it would be unwise to draw any further conclusions based of this statistics.

In order to include more countries in the data, one can also include non-OECD countries that are not ACP countries. The exclusion of compensation to state employees and defence expenditure does then give the total government expenditure open for contestable expenditure, which is 5,1 percent of GDP in non-OECD countries, while the corresponding figure for OECD countries was 7,6 percent of GDP. The size of theses markets do also seem quite small when seen in normative terms, where South Africa is the only ACP country (out of a total of six non-OECD countries) that had government procurement market that exceeded \$10 billions.⁸¹ Since these numbers are thought of as the potential size of the government procurement markets, some authors have questioned the potential size of the gains for EU countries if they were allowed market access to ACP countries procurement market.⁸² Even if these markets are substantially smaller than the markets in OECD countries, the data does however, shows that reforms in ACP

⁸¹ Evenett, & Hoekman, *International Cooperation and the Reform of Public Procurement Policies*, World Bank Policy Research Working Paper 3720 (2005) p. 6

⁸² Ibid.

countries' procurement markets can bring forth efficiency gains with significant positive effects for the economy of that country.⁸³

The analysis of the potential gains must be extended to appreciate the 'true' procurement markets. Such an extension is the recognition of the existence of tied development aid in many ACP countries, which then excludes a large fraction of government procurement from foreign competition, since the aid is tied to purchases of goods and services from the donor country.⁸⁴ The size of foreign aid in relation to government expenditure on goods and services was estimated to 35 percent of expenditure in low-income countries, 16 percent in lower middle-income nations, and 6 percent in upper middle-income economies.⁸⁵ Since most ACP countries are low-income countries and barely a handful reach up to the levels of middle-income economies,⁸⁶ there is good ground for the belief that government procurement in many ACP countries are financed by tied aid.

The size of public procurement market and the possible gains from increased competition do seem to increase with the size of GDP, both from the perspective of the size of the market but also in regard to how this procurement is financed. One should therefore be careful when drawing any general conclusions from the brief statistical examination in this chapter, but it could nonetheless serve to show some of the complications that are imbedded when estimating the size of procurement markets in ACP countries

⁸³ La Chima, *The link between EU-ACP Economic Partnership Agreements (EPAs) and Institutional Reforms - Public Procurement*, Final Report submitted to DG Trade European Commission (2007) p. 45

⁸⁴ Hoekman, *Using International Institutions to Improve Public Procurement*, The World Bank Research Observer 13:2 (1998) p. 266

⁸⁵ Ibid. p. 264

⁸⁶ As measured by GNI/capita; World Bank, *World Development Indicators*, Washington D.C. (2007)

5 Implications for EU-ACP relations

The general theoretical models in Chapter 3 exemplified the potential gains from unbiased procurement regimes both in regards to efficiency implications and trade effects. This image does however need to be complicated further, in order to appreciate the actual situation for procurement in the EU-ACP relations.

5.1 Positive implications

The previous economic efficiency analysis gave a general support of a liberalised and non-discriminatory application of government procurement regimes. These positive implications are what have led to the existing procurement regulation within the EU and WTO framework, and the general perception is that these positive effects can then be transferred to the EU-ACP relations.

5.1.1 Gains market access

The general improvement of market access will, as exemplified in Chapter 3, provide an increase in national welfare, due to more efficient government spending. This has led the European Commission to state that the opening of public procurement markets make up:

‘an area of significant untapped potential for EU exporters.’⁸⁷

The ACP countries markets do then, even though being relatively small, make up a large export market when seen as a whole. The potential gains for European suppliers is also considered to be especially promising in developing country markets, since a large portion of government procurement in these countries are made up by markets in which the EU has strong production capabilities such as high technology and other capital goods. This can be exemplified by the fact that investments in the power sector have accounted for more than 25 percent of government expenditure in developing countries during recent years.⁸⁸

The interest of the EU is not only concerned with its own commercial interest, but is also concerned with the existence of aid transfers to ACP countries. Such aid brings with it an inherent interest for the EU to make

⁸⁷ European Commission, *supra* note 46, p. 9

⁸⁸ Vinod, *Transparency in Government Procurement- Issues of concern and interest to developing countries*, *Journal of World Trade* 35:4 (2001) p. 496

sure that these funds are used for its intended purposes. The effective use of such aid will then not only leave ACP government with more efficient policies, but also satisfy taxpayers in donor countries (i.e. the EU) who wish to see 'their' money being put to better use.⁸⁹

5.1.2 Gains increased transparency

The importance of transparency in regards to government procurement is already evident as it is a main part on both the GPA and in the EPA in place between the EU and the Caribbean. Several other trade agreements on procurement do also include rules on transparency, as a support of a prohibition on discriminatory practises.⁹⁰ The prevention of discrimination has therefore been the main goal of the transparency regulations within e.g. the EU and the NAFTA.⁹¹ The main factors that are considered to render a government procurement regime transparent are:⁹²

- In order for all participants to know how to behave themselves, the existence of *clear government procurement rules* is required.
- In order for all interested suppliers to participate, *government procurement opportunities should be public*.
- To ensure that decisions are made on commercial considerations, opportunities should be given to *scrutinise decisions and to enforce the rules*.

When these transparency factors are employed, they are considered to bring several economic effects with them. The general economic benefits from increased transparency is an improvement in the efficiency,⁹³ and the absence of transparency will then create an efficiency loss much like the one discussed in Chapter 3. The reason for the efficiency loss in a non-transparent regime is that the government will not be able to grant procurement contracts to the most efficient contractor, due to lack of proper information on which to take the decision. The excess cost of such inefficiencies have been estimated to 25-50 percent of a projects total cost.⁹⁴ Non-transparency will also increase information costs, which in turn raises the marginal costs of firms, thereby leading to an upward shift of the supply curve of domestic firm and an increase in the price at which foreign companies compete.

⁸⁹ Collier & Gunning, *Trade Policy and Regional Integration: Implications for the Relations between Europe and Africa*, The World Economy 18:3 (1995) p. 407

⁹⁰ La Chima, *supra* note 83, p. 46

⁹¹ Arrowsmith, *Transparency in Government Procurement: The Objectives of Regulation and the Boundaries of the World Trade Organisation*, Journal of World Trade 37:2 (2003) p. 287

⁹² La Chimia, *supra* note 83, p. 47

⁹³ OECD, *Transparency in Government Procurement: The benefits of Efficiency Governance and Orientation for achieving it*, Paris (2003) p. 6

⁹⁴ Rose-Ackerman, *The Political Economy of Corruption*, Viewpoint Vol. 74, World Bank, Washington D.C. (1995); cit. in Evenett & Hoekman, *supra* note 44, p. 178

Increased transparency will then help promote better value for money.⁹⁵ This is due to the increased possibility for governments to acquire goods and services at the lowest prices, which lead to an overall reduction in costs and budgetary expenditure.⁹⁶ This will lead to that more resources become available for other objectives such as social services, infrastructure and other public goods. These cost saving effects have been found in several case studies in developing countries where increased transparency has led to e.g. reducing in medicine expenditure in Guatemala and savings in regard to water and sewerage services in Pakistan.⁹⁷

There are no extensive studies on the economical effects of increased transparency in government procurement in the ACP countries, wherefore one has to resort to other studies to make estimates for the potential implications for these countries. One such study was made by the European Commission in 2004 and regarded government procurement within the EU. The study investigated the effects of increased intra-community competition, as a result of employed transparency directives in government procurement. Findings of the study showed that the application of procurement rules had significant implications for prices and estimated that the absence of transparency directives in the EU would lead to 40 percent higher prices.⁹⁸ The cost of entry for foreign producers can thus be lower by improved transparency, much in the same way as the abolition of discriminatory practises will. Transparency will then give rise to increased market access for foreign firms, who earlier found it to costly to enter into the home market. The effect on market access and national welfare are however not conclusive, since the prevailing effects will be depended on the size of government demand and domestic supply. There is therefore no clear-cut empirical evidence that increased transparency leads to increased market access, which casts some doubts on the continued emphasis in the GPA and EPAs to include transparency regulations in regards to government procurement.⁹⁹

There are however, several other important effects that is perceived to follow from increased transparency, a decrease in corruption being one of them.

5.1.3 Less corruption

The link between government procurement and corruption have been emphasised by developed countries and especially the US administration as a way to revive global negotiation on procurement within a new setting.¹⁰⁰ Corruption can generally be characterised as the abuse of public trust for

⁹⁵ Arrowsmith, *supra* note 91, p. 296

⁹⁶ Vinod, *supra* note 88, p. 499

⁹⁷ OECD, *supra* note 93, p. 8

⁹⁸ European Commission, *supra* note 40, p. 15

⁹⁹ Evenett & Hoekman, *supra* note 44, p.181

¹⁰⁰ Khor, *supra* note 38, p. 7

private gain, wherefore its elimination is important for all economic development.¹⁰¹ The problem of corruption has further been considered particularly widespread within public procurement.¹⁰² The manner in which corruption influence government procurement involve several different practises, such as the granting of government contracts;¹⁰³

- On the basis of bribes
- To firms which one has a personal interest
- To political supporters

The granting of government contracts for the above listed reasons will then meant derogation from the most efficient contractor, and lead to that the best value for money is not achieved. The existence of bribes and corruption are also likely to deter both domestic and foreign suppliers to compete for future government contracts, which in turn may raise prices due to the lack of competition.¹⁰⁴

The obvious antidote for the plague of corruption is a transparent procurement system that may foster the competition for procurement contracts. Such a system does not only need a formal legal framework but also an efficient enforcement mechanism, which surely is not an easy task as the persistence of corruption in many countries can confirm. The problem of corruption is especially prominent in many developing countries, were the low salaries of governmental officials is the primary reason for the prevalence of corruption. The lack of government resources does also prevent higher salaries for government officials, making the persistent corruption difficult to counter.¹⁰⁵

The nature of corruption means that the problem cannot be targeted exclusively in the government procurement perspective, and must instead be addressed with simultaneous reform in the election system and within the legal and administrative frameworks; an approach has also been advocated in international transparency agreements.¹⁰⁶ The actual imposition of anti-corruption regulations may however lead to distortions of competition and trade if unequal transparency laws are applied between countries. Since such regulations could then prevent a country's producers from participating in corrupt procurement practises abroad, thereby reducing the number of suppliers in the procurement process¹⁰⁷

¹⁰¹ Todaro & Smith, *supra* note 21, pp. 552-553

¹⁰² ADB/OECD, *Anticorruption Policies in Asia and the Pacific – Progress in legal and institutional reform in 25 countries*, Asian Development Bank (2006) p. 13

¹⁰³ La Chimia, *supra* note 83, p. 50

¹⁰⁴ *Ibid.*

¹⁰⁵ Vinod, *supra* note 88, p. 509

¹⁰⁶ *Ibid.*

¹⁰⁷ Arrowsmith, *supra* note 91, p. 301

5.2 Negative implications

The main opposition against including public procurement in EPAs does not surprisingly come from ACP countries. Even though most developing countries acknowledge the positive role that e.g. increased transparency in government procurement could have, they do still reject far-reaching agreements on the issue.¹⁰⁸ The main reasons for the developing countries reluctance towards the issues is the general perception the there is no benefits to be made and that a liberalisation of procurement markets would only brings forth gains for developed countries.

5.2.1 Supply side constraints

The foremost reason for the perceived ‘one-way gains’ is the supply side constraints that face many ACP countries. This argument is not exclusive for government procurement, but is usually raised in regards to most aspects of reciprocal trade agreements. These constraints are manifested in the fact that most ACP countries lack the real capabilities to exploit new opportunities on the EU and world markets. The capabilities include factors such as; productive and technological capacities, marketing skills, transportation channels, and appropriate technical and sanitary regulations.¹⁰⁹ The absence of these factors will then mean that reciprocal access to the EU procurement market is little worth for ACP countries, which lack the proper tools to take advantage of new markets.

The supply constraints of developing countries are also largely intertwined with the H-O viewpoint of production patterns where ACP countries have access to relatively cheap labour that give them a price advantage in the production of primary products such as agricultural goods.¹¹⁰ These types of goods are however among the type of which government buy the least, while specialised capital-intensive products, such as telecommunications, transport or power-generating equipment, generally have a higher demand.¹¹¹ The restriction of the supply side in developing countries is also evident in the NTT perspective, when then increasing return to scale brings with it decreasing average cots as the market size increases. The general implication for EU-ACP relations are then that firm operating on the large EU market will produce at lower average costs, than firms operating on small ACP countries markets, solely because of the difference in market size. This do therefore lead ACP country governments to use discriminatory procurement as an industrial policy tool to increase the size of home markets, and reduce the cost disadvantage faced by domestic suppliers.¹¹² Biased procurement regimes can also be used in the NEG framework, as

¹⁰⁸ Panagariya, *supra* note 37, p. 1216

¹⁰⁹ Borrman et al., *supra* note 4, p. 170

¹¹⁰ Todaro & Smith, *supra* note 21, p. 589

¹¹¹ Hoekman, *supra* note 84, p. 263

¹¹² Trionfetti, *supra* note 35, p. 71

discussed in Chapter 3, as a tool to counter agglomeration forces. The use of such a scheme would then constitute a barrier to trade and give rise to higher trade costs, but could nonetheless serve as protection against foreign competition and the forces of globalisation.¹¹³ The use of procurement in this manner, would clearly constitute an overall efficiency loss, but could still be a highly tempting trade policy for governmental officials trying to protect certain sectors of the domestic industry, while coping with the constraints of the supply side.

5.2.2 ‘Infant industry’ argument

One of the main arguments against the opening up of public procurement is of a protectionist nature and has great similarities to the ‘infant industry’ argumentation. The approach of this argument can also be used as a rational and response to specific economic situations, such as imperfect competition and information asymmetries, and is usually seen as a remedy for a perceived market failure.¹¹⁴ The general rationale behind the infant industry argument is the strategy of import substitution, which promotes the idea that domestic production needs initial protection from foreign competition in order to grow up and then be able to compete on the world market.¹¹⁵ This policy was earlier widely used in many developing countries, but both the usage and its proponents among economists have diminished significantly during the last decades.¹¹⁶ The main problem behind this strategy is that it has been proven largely unsuccessful in achieving its intended aim and the protected industries have become both inefficient and costly to operate due to the absence of competition.¹¹⁷ The ineffectiveness of the infant industry argumentation as an instrument to promote industries has also been illustrated in several empirical studies.¹¹⁸ While other studies have shown that increased trade and less protectionism, contrary to what the infant industry arguments would imply, have led developing countries to industrialisation.¹¹⁹

The general infant industry argument is often used by groups opposed to the inclusion of government procurement in the EPAs.¹²⁰ There are however, problems with the approach, even if its basic argumentation is valid and the biased awarding of government contract indeed can help to foster infant industries. The problems are the same as have been found in regards to infant industry argument as a whole, namely that it fails to produce

¹¹³ Ibid.

¹¹⁴ Hoekman, *supra* note 84, p. 263

¹¹⁵ Krueger & Tuncer, p. 1142

¹¹⁶ Xu, p. 363

¹¹⁷ Todaro & Smith, *supra* note 21, p. 629

¹¹⁸ Dodzin & Vamvakidis, *Trade and Industrialization in developing economies*, Journal of Economic Development 75 (2004) p. 326

¹¹⁹ Ibid. p. 322

¹²⁰ E.g. Oxfam, *Urgent need for change in Europe’s approach to trade negotiations* (2007) p. 6; Bilal & Rampa, *supra* note 29, p. 6

industries and suppliers that are able to expand outside the domestic market and partake in international trade.

The obvious problems with the infant industry argument, does however not mean that there are not any potential benefits for ACP governments that use their procurement regime as an industrial policy tool. The use of procurement in this manner is an important policy instrument for government in both the EU and ACP countries and could still be used in this way, even when clear transparency rules regulate government procurement.

5.2.3 Secondary policies

The wish to retain government procurement as a tool for achieving secondary policies is common in most ACP countries position. The notion of secondary policies is meant to encompass all policies that pursue other objectives than just value for money. These objectives could be macroeconomic as the use procurement as an instrument to counter economic recessions,¹²¹ while other objectives are of a non-economic character, such as the protection of disadvantaged groups and minorities, and the support of SMEs.¹²² The objective can also be used to address regional differences, in order to make sure that certain provinces are receiving a certain share of the procurement contracts. Related to the regional use are also the boosting of local business and domestic demand by the awarding of government contracts, which becomes especially important, since increased trade liberalisation have limited other available instruments that the government can employ to achieve this goal.¹²³ The fear of not being able to pursue these secondary policies has then been an important factor behind the ACP countries reluctance to join the GPA and include procurement in the EPAs.¹²⁴ This fear is however ill-founded since there is no built in discrepancy between the adoption of transparency increasing regulations and maintaining exceptions in regards to secondary policies of e.g. a social character. In order to erase this fear, it has then been argued that agreements on government procurements should be amended as to clearly allow developing countries to establish transparent price preference policies in order to pursue certain secondary objectives.¹²⁵

5.2.4 Tied aid

The large amounts of ODA that are channelled into many ACP countries are, as mentioned earlier, somewhat of a limiting factor for the potential

¹²¹ Khor, *supra* note 38, p. 5

¹²² La Chima, *supra* note 83, p. 53

¹²³ Khor, *supra* note 38, p. 12

¹²⁴ Arrowsmith, *supra* note 91, p. 286

¹²⁵ Hoekman, *supra* note 84, p. 263

positive effects of liberalised government procurement regimes.¹²⁶ If the donor country has specified that the aid should finance projects carried out by the donor country's producers or suppliers, it will naturally fall outside the scope of any implemented non-discriminatory regulations. Tied aid has fortunately decreased as a percentage of total aid given by the EU, and does now make up less than 25 percent in most European countries. The aid given by the US has also become more 'free' even if as much as 80 percent of all US aid to LDCs remains tied, while the DAC average was that 30 percent of all aid was tied.¹²⁷ The importance of aid transfers for many ACP governments is also apparent, since aid make up a large part of these countries' government budgets. In addition to the numbers referred to in Chapter 4, additional ACP data could be used to exemplify the importance of aid in these countries. One example is that the Aid/GNI ratio in 2002 was as high as 47 percent in Sierra Leone, 78 percent in Guinea-Bissau and 120,2 percent in Malawi.¹²⁸ Most other countries did however not come close to these high ratios, even if overall aid level remains high in most ACP countries and especially in the ones in sub-Saharan Africa.

5.3 Institutional aspects

The importance of the institutional framework for the impact of trade liberalization have been emphasised in a number of studies.¹²⁹ These studies have shown on the need for taking account of the institutional quality when implementing trade polices in order for an appropriate institutional framework to be developed.¹³⁰ This is especially true for government procurement in ACP countries were the proposed transparency regulations need to be properly implemented and enforced, in order for the regulation to attain its intended purpose. This is not only a difficult task in developing countries, but also in developed countries were studies on the adherence to procurement rules in the EU has shown large problems of compliance among community firms.¹³¹ Studies aimed at measuring institutional quality and the overall performances by governments are usually constructed around six indicators:¹³²

1. Voice and Accountability
2. Political Stability and Absence of Violence
3. Government Effectiveness
4. Regulatory Quality

¹²⁶ Vinod, *supra* note 88, p. 496

¹²⁷ European Commission/OECD, *EU Donor Atlas* (2006) p. 11

¹²⁸ World Bank, *World Development Indicators*, Washington D.C., (2004) Tab 6.10

¹²⁹ E.g. Rodrik et al., *Institutions Rule: The Primacy of Institutions Over Geography and Integration in Economic Development*, Journal of Economic Growth 9 (2004) & Dollar & Kraay, *Institutions, trade and growth*, Journal of Monetary Economics 50 (2003)

¹³⁰ Borrman et al., *The WTO Compatibility of the European Partnership Agreements between the EU and the ACP countries*, Intereconomics Mars/April (2006) p. 117

¹³¹ Vinod, *supra* note 88, p. 512

¹³² Kaufmann et al., *Government matters III: governance indicators for 1996-2002*, World Bank Policy Research Working Paper 3106 (2003) p. 3

5. Rule of Law
6. Control of Corruption

These indicators have then been used to compare the differences in institutional quality between ACP and non-ACP countries.¹³³ The study shows that most high-income countries have relatively good institutions, not surprisingly giving non-ACP countries more favourable rankings than ACP countries. The study does also show a clear difference among ACP countries where the Caribbean get the best score, followed by the Pacific and the African countries. Africa is clearly the region with the worse conditions for implementing successful government procurement regimes with unfavourable outcomes in the categories: regulatory control, rule of law, and control of corruption. Encouraging examples can nonetheless be found in countries such as Botswana and Mauritius, both scoring clearly above the ACP average on governmental effectiveness.¹³⁴

The institutional quality will not only affect the possibility for the ACP to successfully reap the benefits of government procurement regimes, but it will also be a precondition for taking part of the general welfare effects that stems from increased global trade. The outlook for the ACP countries differs greatly in this respect, were the Caribbean and Pacific country group scores significant better then the African groups. There are 30 out of 39 countries in the ECOWAS, CEMAC and ESA groups that have excessive regulations, while the corresponding ration for the Caribbean and Pacific countries are 3 out of 23 countries.¹³⁵ The mentioned African country groups does also have a significantly bigger portion of their trade with the EU, wherefore the affect of lacking institutional quality is likely to influence any EPA and government procurement agreement to a higher extent for these countries.¹³⁶

There is no easy fix in order to improve institutional efficiency and the problem will require enormous policy changes in many ACP countries, and especially in the majority of the low-income countries in sub-Saharan Africa.¹³⁷ These factors must then be weight-into the analysis of the potential benefits of the conclusion of EPA and the liberalization of government procurement markets, since there otherwise is a risk of starring oneself blind at the efficiency gains in economic theory, while not paying attention to the actual effects on the field.

¹³³ Borrman et al., *supra* note 4, p. 174

¹³⁴ *Ibid.* p. 175

¹³⁵ Borrman & Busse, *The Institutional Challenges of the ACP/EU Economic Partnership Agreements*, Development Policy Review 25:4 (2007) p. 407

¹³⁶ For EU-ACP trade levels, see Annex 2.

¹³⁷ Borrman & Busse, *supra* note 135, p. 414

5.4 Policy implications

The preceding account of positive and negative implication for the EU-ACP relations, raise several important issues that need to be addressed in the formulation of EPAs or any other government procurement agreement. Some policy modifications might therefore be needed in order to cope with the special situation of low-income developing countries, considerations that were not made in earlier government procurement agreements between predominantly developed countries. Economic theory does indeed foresee efficiency gains for developing countries, even if they are unable to take advantage of the increased market access to foreign markets due to their supply side constraints. The proposed policies might therefore need to acknowledge the reluctance of ACP countries, and make proposed agreement more appealing for these countries, while in the same time maintaining the gains of liberalised government procurement markets.

One policy suggestion that has been proposed is conditional market access in the form of mandatory joint ventures. Joint ventures would then lessen the fear of dominance of EU firms on ACP countries' markets and require such firms to form common cooperation's with ACP firms.¹³⁸ Such an arrangement would then promote technology transfer and thus facilitate developing countries access to knowledge. Joint ventures would also give market access to EU suppliers while in the same time allowing ACP countries to move up the value chain, build capacity and develop their own production capacity; which would enable ACP countries to eventually become competitive on the world market. Joint ventures have been used in this way as a successful tool in market openings in China, where the participation form has allowed for much needed foreign investment while it in the same time permitting for maintained domestic control of market access.¹³⁹

The adoption of a flexible approach has not only been argued in regard to market access, but only in regards to price preferences, where some leeway might be given to developing countries to somewhat lessen their reluctance towards international procurement agreements.¹⁴⁰ Increasing the scope of manoeuvre for ACP government has also been argued in regards to a 'fall-back position' for ACP countries, which could make their institutional difficulties more manageable in the EPA framework.¹⁴¹ Another important aspect of the opening up of procurement markets are the possible gains of regional integration,¹⁴² where the foreseeable difficulties for ACP countries to compete on the European market, does not preclude ACP firms from accessing other ACP countries' markets. This could then improve the outlook for ACP countries competitiveness and entails that procurement

¹³⁸ La Chima, *supra* note 83, p. 56

¹³⁹ Naughton, *The Chinese Economy- Transition and Growth*, MIT Press, Cambridge (2007) pp. 411-412

¹⁴⁰ Hoekman, *supra* note 84, p. 265

¹⁴¹ Borrmann & Busse, *supra* note 135, p. 414

¹⁴² La Chima, *supra* note 83, p. 55

agreements need to be adopted on a multilateral level allowing for ACP countries to access markets within their own country group, as well as markets within other regional groups. This kind of regime could then, if rightly formulated, increase the possible gain for ACP countries and thereby reduce their negative attitude towards the inclusion of government procurement in the EPAs.

6 Conclusion

It is not hard to understand the EU's persistent attempts to include the liberalisation of public procurement in the bilateral trade agenda from the theoretical perspective, since the potential gains for EU producers seem rather clear-cut due to their competitive advantages in production capabilities. These advantages are also likely to be more rewarding if the EU is given preferential market access, while other OECD countries with comparable supply capabilities, are not given the same status. The reciprocal market access do however seem less appealing to ACP countries, wherefore their potential profits are foremost concerned with efficiency gains in regards to their domestic procurement markets. These potential benefits are also conditional from the theoretical perspective, where they depend on the market conditions and the characteristics of the augmented supply and demand functions within the economy. This does then create an obvious need to address the issue from an empirical perspective.

The prevailing effects of a liberalised and unbiased procurement market are difficult to quantify for any developing country, and thus for most ACP countries. Some guidance can nonetheless be given by studies on developed countries, and the findings in such studies can be used as benchmarks for estimating the potential effects for ACP countries. Such studies in the EU show that clear potential benefits are expected as a result of the opening up of government procurement markets. There are however some crucial factors such as the size of procurement markets, tied aid and the quality of institutions, which complicate the comparison.

The size of procurement markets is, like its effects, not well account for in ACP countries. The few studies that have been made do however suggest that their amount makes up a considerably smaller part of GNP than for most developed countries. Many ACP countries do also finance their government expenditure with tied aid, which exempt these amounts from the potential gains of an unbiased procurement regulation. Another significant obstacle against the realisation of these gains is the lacking institutional quality in many ACP countries. This is especially evident in Sub-Saharan countries, which is then a factor that has to be considered when formulating bilateral procurement agreements

There are also several special implications for government procurement in the EU-ACP relations, solely due to the large number of low-income developing countries in the ACP group. These countries have special needs in regards to development goals, which have been acknowledged in the formulation of agreements under the WTO framework and need to be taken note of in the EPAs. There may therefore be unwise for the EU to push to hard for a complete liberalization of government procurement in ACP countries, and it might instead be better to pursue a gradual approach in order to continue cooperation on the ACP countries terms. In this respect, it

can therefore be wise to accept some compulsory joint venture regulations for foreign suppliers on ACP markets, in order to lessen the ACP governments' worries of one-sided gains. Attention must also be given to the need to pursue secondary policies by the employment of government procurement in the same manner as e.g. state aid regulations within the EU allow for non-economic considerations. Similar exception could then be adopted in public procurement regulations in order for ACP countries to take note of non-economic goals.

Even if there is a need to analyse the effects of a possible liberalisation of procurement markets from an empirical viewpoint, there are still some objections that can be dismissed on a theoretical ground. One such line of argumentation is the 'infant industry' argument, and the notion that initial protection can shield domestic firms from competition, allowing them time to become competitive on a global market. This approach has earlier proven highly inefficient for many developing countries as a measure to promote domestic production in goods, and a similar result is likely to follow in regards to government procurement. This does then call for other measure in order to help foster ACP production capabilities, where the earlier mentioned joint venture approach is one such policy suggestion. Another important approach will be to take note of possible policy implications that might be drawn from the EPAs already in place. By identifying so-called 'best practises' in e.g. the EPA with the CARIFORUM, other ACP country groups might draw crucial conclusion which can facilitating their own liberalisation of public procurement. When making such comparisons one does however have to keep the differences among ACP countries in mind, and not expect policy recommendations to translate well cross country groups, something that the difference in institutional quality exemplifies.

There is clearly a need to strike a balance between an unbiased, transparent and liberalised government procurement system on the one side, and the need for ACP countries to enter into a mutual advantageous situation on the other. If this balance is found, it will mean welfare gains for both European and ACP actors, and in the long run help many ACP countries in their economic development, a policy goal that always must remain in the focus of any EU-ACP relations.

Annex 1- ACP Market Access

Outlook as of January 1 2008.

Non-LDCs are shown in **bold** and all ACP countries are included except South-Africa.*

	EPA (9 LDCs, 26 non-LDCs)	EBA (32 LDCs)	GSP (10 non-LDCs)**
Caribbean	Antigua & Barb. Haiti Bahamas Jamaica Barbados St Kitts & Nevis Belize St Lucia Domenica St Vinc & Gren. Dom. Republic Surinam Grenada Trinidad & Tob Guyana		
Central Africa	Cameroon	Cen. African Rep. Eq. Guinea DR Congo São Tome Chad	Gabon Rep. Congo
Eastern / Southern Africa	EAC ESA Burundi Comoros Kenya Madagascar Rwanda Mauritius Tanzania Seychelles Uganda Zimbabwe	Djibouti Sudan Eritrea Zambia Ethiopia Malawi Somalia	
Pacific	Papua New Guinea Fiji	East Timor Kiribati Samoa Salomon Islands Tuvalu Vanuatu	Cook Isls. Tonga Marsh. Isls. Niue Micronesia Palau Nauru
West Africa	Côte d'Ivoire Ghana	Benin Mali Burkina Faso Mauretania Cape Verde*** Niger Gambia Senegal Guinea Sierra Leone Guinea Bissau Togo Liberia	Nigeria
SADC	Botswana Lesotho Namibia Mozambique Swaziland	Angola	

* South Africa is excluded since it continues to benefit from the TDCA.

** The pacific countries (with minimal goods trade with the EU) and Nigeria declined to negotiate an interim agreement

*** Cape Verde loses its LDC status in 2008 but has been granted a period of transition allowing to benefit from GSP EBA for 3 years

Source: European Commission DG Trade; [www.] Available:
<http://trade.ec.europa.eu/doclib/html/137335.htm> [2008, April 9]

Annex 2- EU-ACP Trade flows

ACP Region	Imports form the EU as % of total imports	Exports to the EU as % of total exports
ECOWAS + Mauretania	33	23
CEMAC+ São Tomé and Príncipe	56	30
ESA	30	29
CARIFORUM	19	18
SADC	26	29
Pacific	13	12
Total ACP	26	23

Source: European Commission, *External Trade EU-ACP* (Based on data from 2004);
 [www.] Available: <http://ec.europa.eu/trade/issues/bilateral/regions/acp/stats.htm> [2008, April 9]

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