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Is GSP+ a Plus?

A Mixed Method Review of
Trade Preference Scheme GSP+

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Abstract

The EU, being the largest trading partner for many developing countries, offers a General Scheme of Preferences (GSP) as a voluntary trade promoting scheme. Through GSP+, an extension of GSP, the EU offers additional market access conditional on commitment to sustainable development and good governance. Using a Gravity Equation, I find insignificant trade creating effects on GSP+ in comparison with standard GSP. With the help of stakeholder interviews in GSP+ beneficiary Sri Lanka I find several examples of how the scheme has had incentivising effects on respect for human and labour rights. The quantitative results are in line with previous research and point to the fact that improvements could be made to GSP+. Some possible problems found surrounding the scheme are; strict Rules of Origin, information asymmetry and uncertainty of access.

Keywords: EU, Trade Preferences, GSP, GSP+, Gravity Equation, PPML, Field Study, Sustainable Development

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Acronyms and Abbreviations

ACP: African, Caribbean and Pacific

DFQF: Duty-Free Quota-Free

EBA: Everything But Arms

EC: European Commission

EU: European Union

FE: Fixed Effects

FGLS: Feasible General Least Squares

FTA: Free Trade Agreement

GPML: Gamma Pseudo Maximum Likelihood

GSP: General Scheme of Preferences

GSP+: Special Incentive Arrangement for Sustainable Development and Good Governance

GATT: General Agreement on Tariffs and Trade

ILO: International Labour Organization

LDC: Least Developed Countries

MFN: Most Favoured Nation

NLS: Non-linear least squares

NB: Negative Binomial

PPML: Poisson Pseudo Maximum Likelihood

QR: Quantitative Restrictions

RE: Random Effects

RoO: Rules of Origin

SME: Small and Medium Enterprises

UNCTAD: United Nations Conference on Trade and Development

WTO: World Trade Organization

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1. Introduction

International trade can be a powerful engine for sustainable development and poverty alleviation, capable of improving standards of living all over the world. Trading helps countries create new job opportunities, promote efficient use of resources as well as improve economic diversification, growth and development. Developing countries are defined partly by the relatively small size of domestic markets. This limited home market demand due to small size makes export performance important for economic growth (Hvidt Thelle et al 2015). One of the options available to try and increase exports from developing countries is non-reciprocal unilateral trade preferences, which have been used for such countries by the European Union¹ (EU) since at least the 1960s (Persson 2012).

When one country offers trade preferences to another country, it means that the latter country faces less restrictive trade barriers than the donor country's other trade partners. In practice this takes the form of preferential access given to the inner market of the EU, allowing preference beneficiaries to face lower tariffs than the Most Favoured Nation (MFN) tariffs. The term has come to specifically refer to when high-income countries offer lower trade barriers to developing countries than to high-income trade partners, without being offered more beneficial market access in return (Persson 2012). It can be viewed as a voluntary transfer from the high-income country, constituting an alternative to development aid. The EU was a forerunner as the first high-income importer to introduce a Generalised Scheme of Preferences (GSP), and is today the largest trading partner for many of the world's developing countries (Persson 2012). The European Commission (2018) describes its GSP programme as one allowing vulnerable developing countries to pay fewer or no duties on exports to the EU, giving them vital access to the EU market, contributing to growth and poverty eradication by expanding exports from countries most in need. Hence, GSP is meant to support economic growth and job creation in the beneficiary countries by generating increased export revenue, leveraging export diversification and allowing for firms to increase competitiveness through increased productivity and economies of scale (Hvidt Thelle et al 2015; Persson & Wilhelmsson 2007).

While the European Union provides different preference schemes, this thesis focuses mainly on the extended version of the General Scheme of Preferences (GSP), referred to as GSP+. The scheme intends to bring about social and ecological benefits for countries in addition to the economic benefits usually believed to come from increased export volumes. It is being offered with positive conditionality on commitment to sustainable development as well as respect for human and labour rights through a demand of ratifying and implementing 27 United Nations Conventions. GSP+ therefore has potential effects going beyond trade creation. If the preference has trade creating effects, it constitutes an

¹ More accurately; the European Union or one of its predecessors such as the EEC. For the sake of simplicity, I will however refer to the EU throughout this thesis.

incentive for developing countries to try and become beneficiaries. This would in turn mean that developing countries have an incentive to ratify the 27 relevant international conventions on human and labour rights, environmental protection and good governance – as well as ensuring their effective implementation.

The purpose of this paper is to analyse whether preferential trade agreement GSP+ increases export volumes, as well as if it has a positive effect on sustainable development and respect for labour and human rights in developing countries. The scope of the thesis includes an empirical quantitative evaluation of export flows from GSP+ accession countries, as well as interviews with stakeholder representatives in GSP+ beneficiary country Sri Lanka. In the paper, I evaluate if GSP+ is trade creating by comparing trade flows over time for several countries, out of which some have upgraded to GSP+ during the time. I use a gravity model with panel data containing 58 countries over 26 years. With the Poisson Pseudo Maximum Likelihood (PPML) estimation method, suggested by Tenreyro & Silva (2006), I find insignificant results for GSP+ as compared to standard GSP. Using stakeholder interviews in GSP+ beneficiary Sri Lanka, I find examples of how the scheme has benefitted respect for human and labour rights in the country. My contribution consists combining econometric analysis with qualitative interviews to draw more in-depth analysis of both the trade creating and sustainable development ambitions of GSP+.

The paper proceeds as follows: the next section provides an overview of EU trade preferences, section three outlines previous research and section four establishes a theoretical framework. In section five the quantitative empirical method, data and results are presented after which the qualitative method is outlined in section six. Finally, section seven leaves some concluding remarks, policy recommendations and suggestions for future research.

2. EU Trade Preferences for Developing Countries

2.1 Legality and Historical Background of Preferences

This section outlines the background of EU preferential trade agreements, its legality and some reforms made to the agreements.

In 1964, the first United Nations Conference on Trade and Development (UNCTAD) recommended that developed countries would grant all developing countries non-reciprocal trade preferences. However, the EU had in practice already been providing preference treatment since the Treaty of Rome of 1957 associated European colonies special status (Persson 2012). Non-reciprocal trade preferences are not to be viewed as normal contractual trade agreements, with expectations on both/all parties to lower tariffs. Instead, they are voluntarily provided by high-income countries to developing countries with eligibility to apply for.

Offering non-reciprocal and non-discriminatory unilateral preferences for some countries would normally break GATT Article I; Most Favoured Nation (MFN). However, offering developing countries lower tariffs than other trading partners gained a 10-year waiver in 1971 (Persson 2012) which has since 1979 had permanent legal ground in GATT under the name "*The Enabling Clause*" (Grossman and Sykes 2005). Today, virtually all developed countries offer voluntary preferences of some sort (Bartels 2003). The EU preferences long consisted of duty free quotas and ceilings, but have since the global removal of quantitative restrictions (QR) in 1995 instead consisted of tariff reductions. The size of the tariff reductions is determined with respect to the sensitivity of products (Persson & Wilhelmsson 2007).

Over the more than 60 years the EU has offered trade preferences, systems have been added and updated, leading up to a reality where few developing countries today lack preferential access of some sort to the inner market (Persson & Wilhelmsson 2007). While EU trade preferences in general cover all developing countries, certain groups of countries receive better preferences within the regimes. There used to exist arrangements more beneficial than GSP, stemming from colonial ties and geographic proximity (such as one for Mediterranean countries) (Persson & Wilhelmsson 2007). Those preference schemes have today generally been replaced by other setups, such as FTAs. Deeper analysis of those preference schemes is outside the scope of this thesis. Questions however rise how the EU could provide greater market access to some countries that did not abide by the sustainable development conventions stipulated in GSP+, thus risking damaging the incentive at play for part of the time-period assessed in this thesis. Criticism has also been raised over the fact that reciprocal FTAs do not include the same conditionality on sustainable development. The critics claim core principles of the EU, such

as respect for human rights, should be equally important to demand from all trade partners. Accordingly, critics ask what differing between partners does for the moral credibility of the EU in promoting sustainable development (Bilal et al 2011).

The one-sided offering of preferences has implications since it constitutes a power imbalance between benefactor and beneficiary. The providing party can decide to suspend preferences at any time, leading to insecurity for exporting firms, normally considered negative for trade. Another problem that has arisen around preferences is that parts of the systems risk skewing the market away from its optimality. According to Özden and Reinhardt (2005), non-reciprocal preference schemes could be harmful in that they allow beneficiary countries to refrain from trade liberalisation. Looking at the American GSP system, they find evidence that countries being excluded from the scheme adopt more liberal trade policies.

2.2 GSP and GSP+

The Generalised Scheme of Preferences (GSP) consists of three arrangements: 1) Standard GSP, 2) GSP+ and 3) Everything But Arms (EBA). The least developed countries (LDCs) are granted more market access. Following the EBA initiative in 2001, they now export all goods except arms and ammunition duty free and quota free (DFQF) to the EU. The GSP+ scheme offers benefits larger than those of standard GSP, but smaller than those of EBA. Standard GSP today involves tariff reductions on about 66% of tariff lines, while GSP+ has further tariff cuts on essentially the same 66% tariff lines (EC 2018₂).

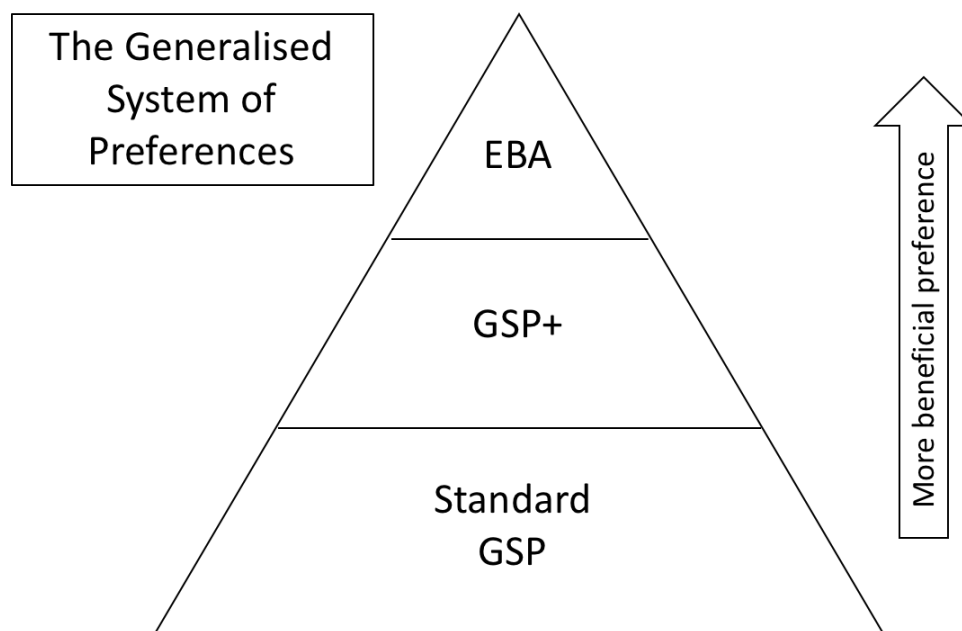


Figure 1: Hierarchy within GSP preferences. Idea based on figure from Persson & Wilhelmsson (2007), depicting the formerly existing hierarchy between the GSP and earlier schemes based on colonial and geographical ties.

Not only being a tool for economic development through increased market access, the GSP scheme also has a purpose of promoting values and principles that the EU deem important (Bilal et al 2011). The EU, having a history of trying to include human rights clauses in its trade agreements (Yap 2013), probably goes furthest with its GSP+ scheme. One of the criteria for being granted GSP+ is the *sustainable development criteria*. This entails the effective implementation of 27 core international conventions on human- and labour rights, environmental protection and good governance (EC Annex VIII). For a full list of the applicable conventions, see Appendix A. To ensure beneficiary countries abide to its commitments, the EU conducts dialogues with authorities and monitors compliance continuously with the help of various stakeholders (EC 2018).

Box 1: Conditionality GSP+ beneficiary countries must adhere to

Further GSP+ Conditionality

In addition to the sustainable development criteria, there are also *vulnerability criteria* for accessing GSP+. This consists of one diversification criterion and one import share criterion (EC 2018). The vulnerability criteria of GSP+ determines that beneficiaries cannot compose too large a part of the EU's import in any good. This could lead to exporters policing themselves in how efficient they produce a certain commodity, afraid to become too successful and thus losing preference accession.

Furthermore, beneficiary countries must fulfil the general GSP criteria, which stipulates that countries achieving high- or upper-middle income economy status during three consecutive years will not be eligible for the preferential scheme (EC 2019). While GSP was originally seen as a temporary measure, it has been continuously prolonged and is in its current regulation valid until 2023 (EC 2018). The fact that the scheme is not permanent has implications on exporters ability to count on it. Another important aspect is what type of products are included in trade preference schemes. Products that a country holds comparative advantage in leverage larger effects on export volumes. An issue here is that comparative advantages can change with the development of an economy and preference schemes will often not be amended in the required rate (Persson 2012).

Beneficiary countries must also adhere to certain rules, one being the Rules of Origin (RoO). Rules of Origin exist partly to promote domestic value addition into production, yet if they are too strict, production can be hindered in the beneficiary country. Constriction arises as beneficiary countries struggle to import inputs needed for production. On the other hand, too relaxed RoO can cause trade deflection, as the beneficiary country risks being used as a transport hub – rather than being a producer and exporter.

For countries affected by the production and trafficking of illicit drugs, there used to be a preference arrangement referred to as *the Drug Regime* (Persson & Wilhelmsson 2007), whose conditionality meant to prevent drug trafficking. The Drug Regime together with two arrangements having conditionality on labour rights and environmental protection respectively were however all replaced by GSP+ in 2005, following a ruling against the EU's Drug Regime scheme by the Appellate Body of the WTO (Bartels 2007). GSP+ has since served as the *Special Incentive Arrangement for Sustainable Development and Good Governance* (EC 2018). GSP+ has conditionality on compliance with more UN Conventions (such as labour rights, human rights and environmental deference) than its predecessor, and is offered to a broader group of beneficiaries than the Drug Regime ever was. The Drug Regime

however largely held the same benefits as the replacing scheme when it comes to product coverage and tariff preference.

Table 1: Drug Regime and GSP+ beneficiary countries between 1991 and 2017.

	The Drug Regime														GSP+													
	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	
Armenia																												
Azerbaijan																												
Bolivia																												
Cabo Verde																												
Colombia																												
Costa Rica																												
Ecuador																												
El Salvador																												
Georgia																												
Guatemala																												
Honduras																												
Kyrgyz Republic																												
Moldova																												
Mongolia																												
Nicaragua																												
Pakistan																												
Panama																												
Paraguay																												
Peru																												
Philippines																												
Sri Lanka																												
Venezuela, RB																												

Changing global circumstances for trade and development has created a need to update the preferential trading schemes (EC 2018₂). As MFN tariffs have been lowered (WTO 2019), the difference between MFN and preference tariffs has diminished, meaning preference schemes must top what they are offering to avoid preference erosion. Enough preference margin is also needed between general GSP scheme and GSP+ if the EU wants to create an incentive for sustainable development and good governance. Increasing the product coverage should also improve trade effects from preference schemes.

In 2014, the EU made significant changes to the GSP scheme. More products were included to receive preferential treatment, while the amount of countries benefitting from the scheme was decreased (EC 2018₂). GSP+ has been subject to additional changes in the form of; further product lines added; its monitoring scheme revised to be stricter; and the import-share ratio relaxed under its vulnerability criteria. This latest GSP reform coming into effect 1 January 2014 has been set to sustain for 10 years whereas it was earlier reformed every three years (EC 2018₂), meaning the certainty for exporters should increase.

3. Previous Research

3.1 Trade Creation Studies

Trade preferences have caught criticism for not having the intended effect on exports from developing countries (Persson 2012), but previous research confirms that they in general have increased export volumes (Persson & Wilhelmsson 2016). Some older studies of the general GSP from the 1980s, -90s and early -00s find significant positive results – see e.g Sapir (1981) and Nilsson (2002) – but can be criticised for using cross-sectional methods unable to control for unobserved heterogeneity (Persson 2012). More sophisticated econometric studies have however also found significant positive results for preference schemes. Carrère (2004) and Peridy (2005) find significant results for EU’s Mediterranean and ACP preferences respectively. Frazer & Van Biesebroeck (2010) find positive results for the African Growth and Opportunity Act offered by the U.S. They note that import responses grow over time and are larger in product categories where the tariffs removed are large. Persson (2012) in a sort of meta-paper looks at earlier studies of several different EU preferential trade agreements and finds mixed results. For example, GSP is concluded to have a positive effect. The effects of the GSP+ predecessor “the Drug Regime” is however found to be insignificant with a sample period of 1960-2002 (Persson & Wilhelmsson 2007). That study can benefit from being updated with new data, including also the replacing GSP+.

Hvidt Thelle et al (2012) assess GSP and GSP+ employing a triple-difference model to isolate preference impacts from other effects. They use data disaggregated to product level, including almost 4000 products for 176 countries between 1995 and 2012. They do not only employ a dummy variable for preference access, but also include detailed tariff information, making it possible to calculate preference margins. This however means that the group used to estimate GSP+ contains only the countries eligible for the scheme when introduced in 2005. They find robust results showing that the GSP scheme has significantly increased exports to the EU from developing countries, but with no visible impact coming from GSP+ at the aggregate level. The insignificant result should be expected, given that the GSP+ effect they capture is for most countries merely going from the Drug Regime to its successor GSP+; two very similar schemes.

3.2 Sustainable Development Results and Sri Lankan Case Studies

For the social and ecological intents of GSP+, evaluation has concluded that the scheme has had an overall positive effect on social development and human rights in beneficiary countries, while only limited effects on environmental protection (Ioannides 2012). Gasiorek et al (2011) find evidence on ratification of the UN Conventions following GSP+, but point out that the evidence for implementation

is weaker. Putte and Velluti (2018) find that the EU threatening with removing GSP+ benefits have prevented upheaval of UN Conventions in Bolivia and El Salvador. Wijayasiri (2007) evaluates EU and U.S GSP schemes in Sri Lanka looking at coverage and utilisation. For the EU scheme, he finds high coverage rates, but low utilisation rates, concluding the Rules of Origin (RoO) have a limiting effect. Democracy Reporting International (2016) notes GSP+ had a positive impact in Sri Lanka, referring to significant tariff drops as compared to standard GSP in important sectors.

Compared to previous research, one of my contributions consists of combining econometric analysis with qualitative interviews to draw more in-depth analysis and suggestions for improvements. While Persson and Wilhelmsson's (2007) study of the Drug Regime could benefit from being updated with new data, an issue with the later study of Hvidt et al (2012) is the narrower GSP+ group included. Their group consist only of the eligible countries as of 2005, capturing mostly the transition from the Drug Regime to GSP+. I therefore apply new data, updating the evaluation from year 1988 up until 2014, allowing for more entries into GSP+ to have occurred. With new data and interviews in GSP+ beneficiary country Sri Lanka, I attempt to better answer the question of whether GSP+ constitutes an incentive for sustainable development and respect for human and labour rights.

4. Theoretical Framework

In this section I focus on the theoretical effects on export volume from trade preferences. As mentioned in the first part of the thesis, the main aim of implementing trade preference schemes is increasing export volumes from developing countries. Other theoretical benefits regard positive impacts on production diversification and industrialisation. They usually include theories on infant industry protection and heterogeneous firm trade theory (Persson 2015). The main theoretical basis used in this thesis is that trade preferences through lowering tariffs cause increased exported volumes. A deeper preference means higher export volumes, *ceteris paribus*. Theoretically, the scenario can be studied equivalently to when a country enters a unilateral preferential agreement. I construct a basic partial equilibrium model of a supply-demand relationship in the price-quantity plane, adapted to my purposes to represent the situation in GSP+ beneficiary countries. The base theoretical ideas are mainly drawn from Grossman & Sykes (2005), Bacchetta et al (2012) and Persson (2015). I use three parties; EU15 as importing and preference granting party, the standard GSP preference beneficiaries, and the deeper preference GSP+ beneficiaries. This because my assessment concerns the effects of gaining GSP+ preference compared to having standard GSP preference. An assumption made is that GSP+ beneficiaries are small economies unable to affect world price. The assumption should be valid empirically given the vulnerability criteria needed to be fulfilled by GSP+ beneficiaries and the fact that they collectively are a small group of countries.

P^* is the price at the EU15 market and $P^*/(1+t_{GSP})$ is the price to which GSP beneficiary producers can sell their market – and hence the domestic price faced by beneficiary countries' consumers. Q_{GSP}^C and Q_{GSP}^P are the domestic quantities of consumption and production respectively in GSP beneficiary countries. The exported volume is given by the difference between domestic production and domestic consumption: $(Q_{GSP}^P - Q_{GSP}^C)$

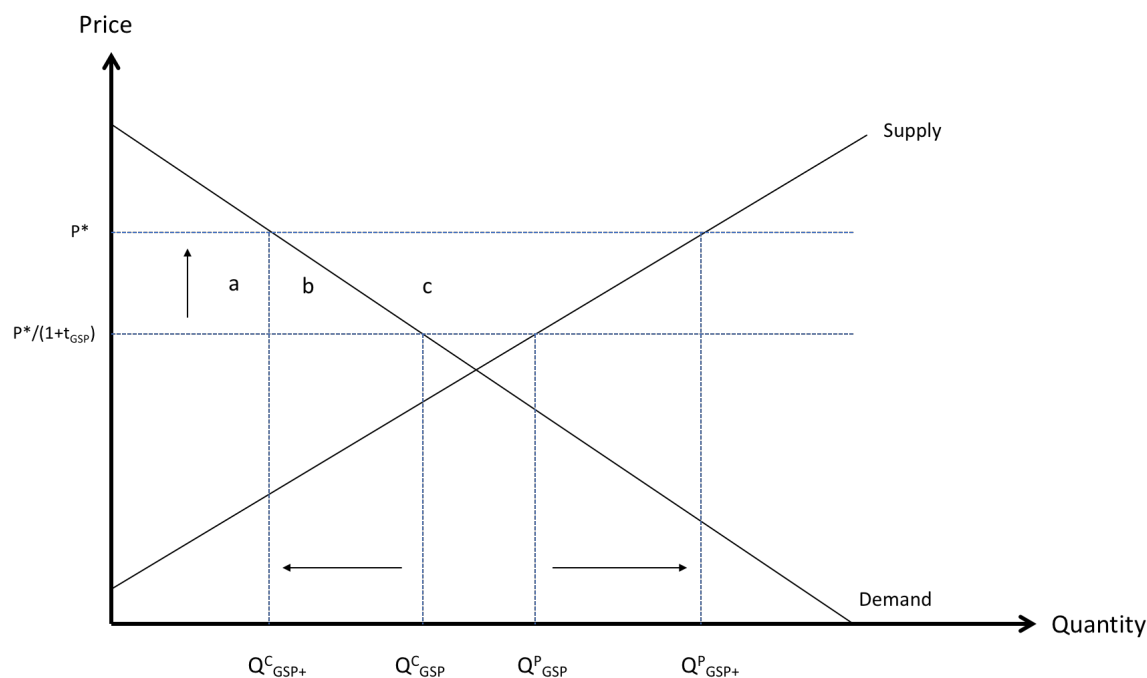


Figure 2: beneficiary country partial equilibrium analysis comparing GSP+ to standard GSP

As the beneficiary country gains deeper preference through accessing GSP+, the domestic producers can start exporting to EU15 at the price P^* and still stay competitive on the export market as the preference margin increases (tariffs fall). The same price will naturally be charged on the domestic market as on the export market. The increased price causes production to increase in the beneficiary country ($Q^P_{GSP} \rightarrow Q^P_{GSP+}$), while domestic consumption falls ($Q^C_{GSP} \rightarrow Q^C_{GSP+}$). Accordingly, exports will increase; $[(Q^P_{GSP} - Q^C_{GSP}) \rightarrow (Q^P_{GSP+} - Q^C_{GSP+})]$. Being granted GSP+ thus leaves domestic consumers worse off, while domestic producers are better off following that they can both charge a higher price and increase output (Persson 2015). The loss of consumer surplus is in Figure 2 is represented by $-(a+b)$, while the gain in producer surplus is represented by $(a+b+c)$. The total welfare effect for a country gaining GSP+ preference should be positive of the magnitude c . In the preference granting country, in this case EU15, the lost tariff income constitutes a voluntary transfer to the beneficiary country.

The theoretical effects of accession to GSP+ thus stipulate *trade creation* for the beneficiary (Grossman & Sykes 2005). In the following empirical analysis, that will be used to interpret the coefficient of the trade effect from gaining GSP+ accession as compared to only accessing GSP. While trade enhancing effects can be measured through both trade creation and trade diversion, this thesis will focus on trade creation following the theoretical framework outlined above.

5. Empirical Methodology and Data

5.1 Methodology

I apply an *ex post* study on trade levels to empirically assess whether export volumes have increased under GSP+. Since we do not know how trade patterns would have looked without trade preferences, it can be hard to estimate if preferences have increased trade volumes. A common solution is to estimate a gravity model (Persson 2012). A gravity model – which I apply – produce a counterfactual; how trade would have looked like in the absence of the preference (Persson 2015). The *gravity equation* (by analogy with the Newtonian theory of gravitation) approximates the size of bilateral trade flows between any two countries by considering variables such as size of countries' economies and the distance between them. Just as planets are mutually attracted in proportion to their sizes and proximity, countries trade in proportion to their GDPs and proximity (Bacchetta et al 2012). The gravity model has been very successful, providing strong predictions for decades, and complies with important theories of trade such as the Heckscher-Ohlin, the Ricardian approach and the model with increasing returns to scale (Nilsson 2002; Yotov et al 2016). With some adjustments made throughout the years, it remains the workhorse model for trade policy analysis. In earlier papers, it was common to use cross-sectional data to estimate the gravity equation. Today, it is common sense to instead use panel data, as it enables controlling for country heterogeneity (Gómez Herrera & Milgram Baleix 2009).

Mayer and Zignago (2005) point out that market access has changed significantly over time from other factors than tariff liberalisation. Thus, estimating a gravity model entail issues of endogeneity (Bacchetta et al 2012) due to unobserved heterogeneity. In this case, the endogeneity can consist of the GSP+ dummy being correlated with the error term, due to increased trade stemming from omitted variables such as peaceful relationship between countries. One way to tackle this is using instrument variables. There is however a lack of reliable instruments (Yotov et al 2016) that are correlated with GSP+ but not with trade. I instead include two fixed effects; one controlling for effects over time and another controlling for exporter country-specific effects.

The time fixed effect captures effects shared by all countries that vary over time which would cause bias from omitted variables (Bun and Klaasen 2004), such as business cycles (Mátyás, 1997). In practice, it operates as one dummy for each year, always taking the value zero for all trade *not* occurring during the year denoted by the dummy. The exporter country fixed effects capture all differencing country-specific characteristics, such as improved trade infrastructure and openness² from the exporting country. Other than controlling for country heterogeneity, it also controls for multilateral trade resistance. That is, the relative trade costs impacted by factors such as how far away the rest of the

² I have opted to not include variables for these due to the lack of data.

world is to two neighbouring economies (Andersson & van Wincoop 2001). To exemplify, one can think that it is reasonable Australia and New Zealand trade more with each other than most other neighbouring country pairs do, given the fact that most other countries are so far away from the two. Controlling for such relative trade costs is essential for a well-specified gravity model (Anderson & van Wincoop 2003).

Exporter-by-time effect is an alternative sometimes proposed (Olivero & Yotov 2012). It can however not be utilised in this model as it would serve its purpose to well, capturing possible effects of GSP+. Another alternative to fixed effects is random effects. Fixed effects are however preferred over random in gravity literature, as the random effects model is only consistent under restrictive assumptions. For example, using random effects would require me to assume that multilateral resistance is normally distributed, which theoretical gravity models do not acknowledge they are (Shepherd 2016). Another alternative at hand to account for multilateral resistances is to use GDP and bilateral distance to construct so-called remoteness indices. Such indices have however been criticised for not mimicking the theory on multilateral resistance (Head & Mayer 2014), why I prefer using exporter country-specific and time-specific effects.

I specify my model as:

$$Imports_{ijt} = \exp(\beta_1) GDP_{it}^{\beta_2} GDP_{jt}^{\beta_3} Pop_{it}^{\beta_4} Pop_{jt}^{\beta_5} Dist_{ij}^{\beta_6} \exp(\beta_7 Comlangoff_{ij} + \beta_8 Col45_{ij} + \beta_9 Smctry_{ij} + \beta_{10} GSPplus_{jt}) \exp(\mu_j + \lambda_t) \varepsilon_{ijt}$$

Equation 1: Gravity equation regression model

The dependent variable *Imports* is the monetary value of bilateral import volumes from scheme beneficiaries (*j*) to EU15 countries (*i*). *GDP* is the real GDP for countries *i* and *j*, where *t* denotes the year of observation. *Pop* is the variable for population, and shares notations for *i*, *j* and *t* with GDP. Typically, empirical studies have estimated trade costs with bilateral distance (Bacchetta et al 2012) which in my model is specified as *Dist*. Following that distance is not considered enough to estimate economic trade barriers, I also use several additional variables to capture trade costs in lines with suggestions from Bacchetta et al (2012). I include dummies for common language and colonial history³ to capture information costs. *Comlangoff* represents official common language, which is expected to be positive for trade. Expected positive is also the occurrence of shared colonial history. The variable included to control for that is *Col45*, showing colonial history surpassing year 1945. Furthermore, the

³ Sometimes several variables for colonial status are included. I have opted for the variable seeming to be the best instrument, as too many variables lead to a poorly specified equation. Some variables, such as one for “common coloniser”, is by default collinear as no EU15 country has been colonised.

variable *Smctry* is a dummy for if two trading partners have ever been the same country, accounting for home bias. It is an exogenous variable that can control for discrimination between *intra-national* and *international* trade (Andersson and Yotov 2010).

The variable for GSP+ preference takes the form of a binary dummy. The dummy is constructed so that countries eligible for preferences of GSP+, or its predecessor the Drug Regime, are captured by letting the dummy take the value one for each beneficiary country every year the country benefits from the scheme. An argument to include the GSP+ predecessor the Drug Regime is that it offered very similar tariff reductions and product coverage as its replacement. I however also try regressing the model with GSP+ excluding the Drug Regime. The interpretation of the GSP+ dummy is gross trade creation of the extended preferences of GSP+ compared to standard GSP. The variable μ denotes exporting country fixed effects with index j for each country and the variable λ is the time fixed effect with index t for each year. Therefore, the error term has indices for importing countries (i), exporting countries (j) and time (t).

Sometimes included in gravity equations are dummies for landlocked countries and common borders. These dummies reflect the hypotheses that transport costs are higher for landlocked countries, while a shared border is supposedly positive for trade. They are not included in my regression, as they would bias the results given the data set. Most GSP+ beneficiaries are geographically in the global south, so only two of the GSP+ countries in my dataset share a border with EU15 countries. The fact that a few countries are landlocked should be captured by the exporter country fixed effects.

5.2 Data

I use yearly data for EU15 as the importing countries to cover a period from 1988–2014. The period is restricted not to pass 2013 due to the amendments of GSP+ coming into effect on January 1st 2014, as mentioned in section two. Data on Nominal imports in US\$ is from DOTS (IMF 2019), while population, real GDP in constant 2010 US\$ and US GDP-deflator are from World Development Indicators (World Bank 2019). The nominal imports have been converted to real imports using the US GDP deflator. Data for the remaining gravity variables come from the CEPII database (2019). The dummy variables for GSP and GSP+ were made available through a database of all GSP and GSP+ countries accession years (Persson 2017). Data is used for 30 countries benefitting from GSP and 18 countries benefitting from GSP+ or its predecessor the Drug Regime. This is after having excluded:

- a) All countries having available deeper preferences (LDCs, ACP and Mediterranean)
- b) All countries that have FTAs with the EU
- c) All countries that have joined the EU

- d) The so-called transitional economies, which are post-Soviet countries, having transitioned from planned to market-based economies at the same time as gaining GSP accession. These would otherwise skew the result in a way that is not caught up by fixed effects
- e) China, which, like the post-Soviet countries, has transformed into more of a market economy. Another important reason why China produces Method Variable Bias is that it joined the WTO in 2001. China's admission into the WTO is believed to have induced a significant shift in trade patterns (Autor et al 2016)⁴
- f) The small island states British Virgin Islands, Cayman Islands, Northern Mariana Islands, Turks and Caicos Islands, that did not exist in databases

Beneficiaries with eligibility for deeper preference are excluded because the programmes are overlapping, making it hard to distinguish the GSP+ effects. More importantly, it would not be logical to believe that countries export under GSP while having a more generous scheme available to them. The GSP countries serve as a control group, meaning I can deduct the extra benefit from exporting under GSP+ compared to GSP. In other words; the effect that constitutes an incentive to implement the 27 conventions on sustainable development and good governance. For a list of all countries included in the data set, see Appendix B.

An additional elucidation of data, not found in previous research, is to eliminate data points for GSP beneficiaries for the years after they graduated from the standard GSP scheme. This means all standard GSP beneficiaries losing access to GSP after graduation due to for example reaching a too high income level are dropped from the year of graduation. This should provide a stronger estimate, since graduation effects are prevented from disturbing the GSP+ effect. Keeping the data points would mean assuming that losing preference from graduation has the exact opposite effect of gaining the preference, which is theoretically dubious.

5.3 Estimation

There are several different techniques at hand for estimating the gravity equation. One standard approach has been to use OLS taking logarithms of all continuous variables, including the dependent one (Baccetta et al 2012). An issue with taking the logarithm of trade flows is that all zero trade flows will be dropped out of the estimates, following the fact that the log of zero is undefined (Santos Silva & Tenreyro 2006). Zero trade values can reflect missing values. However, if unreported trade in the data is indeed zero, or reflects very small trade flows, throwing the data points out of the sample means

⁴ I test estimations both with and without China in the dataset, finding that the country indeed induces Method Variable bias

losing useful information and leads to inconsistent results (Baccetta et al 2012). In the presence of heteroscedasticity, log-linearized regressions such as OLS produce biased result that distort the interpretation. Heteroscedasticity is to be expected in trade data, and running a Breusch-Pagan test⁵ on my data I confirm presence. Accordingly, OLS is not an appropriate estimator and inferences from it can produce misleading conclusions (Santos Silva & Tenreyro 2006).

Some available non-linear alternatives are: *Non-linear least squares (NLS)*, *Feasible General Least Squares (FGLS)*, *Gamma Pseudo Maximum Likelihood (GPML)*, *Negative Binomial (NB)*, *Tobit*, *Heckman Sample Selection*, and *Pseudo Poisson Maximum Likelihood (PPML)* Models.

Frankel and Wei (1993) have estimated multiplicative models using nonlinear least squares (NLS), which could be a valid estimator for the gravity equation (Santos Silva & Tenreyro 2006). Alas, the NLS estimator ignores heteroscedasticity, which is present in my data, and is inefficient as it gives more weight to observations with larger variance (Santos Silva & Tenreyro 2006). Feasible Generalised Least Squares (FGLS) instead weighs observations to the square root of their variance. Gamma Pseudo Maximum Likelihood (GPML) is similar to PPML, but assign less weight to observations with a larger conditional mean (Martínez Zarzoso et al. 2007).

The Negative Binomial (NB) estimator is more general than PPML and treats the Poisson assumption as a special case. A strength is that it allows to account for overdispersion (a variance greater than the mean) (Shepherd 2016). The PPML estimation is however still consistent in the presence of overdispersion (Shepherd 2016), as it makes no assumption about it. Bousquet & Boulhol (2010) and Shepherd (2016) point out that the Negative Binomial estimator is not scale invariant and is therefore inappropriate when applied to a continuous dependent variable which unit choice is arbitrary. They find results of the NB estimator depend on whether using imports expressed in trillions of dollar or thousands of dollars, and that it is therefore not adequate for applied research.

Tobit estimators use left-censoring at zero on the log of trade plus a constant to solve the zero-trade issue. The appropriateness of this approach has been questioned. The censoring of trade flows below some positive value can be correct for some countries – but it is unrealistic for countries where trade data are reported at a very high degree of accuracy (Bacchetta et al 2012). As I have imports statistics from EU15 countries, generally being good with reporting accurately, the Tobit estimation cannot be fully justified. The Heckman (1979) approach, later developed by Helpman et al (2008) is preferred by some since it complies well with trade theory. Econometrically, it does however not perform as well. It does not deal well with heteroscedasticity, and fixed effects Heckman models suffer from the incidental

⁵ The Breusch-Pagan test result p-value is 0.000

parameters problem, introducing bias and inconsistency into the estimates (Bacchetta et al 2012; Shepherd 2016).

Instead of relying on the mentioned models, I specify a multiplicative exponential form of the gravity equation using the Pseudo Poisson Maximum Likelihood Model. PPML estimates the non-linear form of the gravity model, thus avoiding dropping zero trade (Bacchetta et al 2012). The PPML model is to be considered a robust alternative in presence of heteroscedasticity (Santos Silva & Tenreyro 2006), which is established. The PPML approach has been used in influential gravity papers, such as Westerlund and Wilhelmsson (2006), and Monte Carlo simulations have shown that PPML estimates robustly even with large numbers of zeros (Yotov et al 2016). PPML is one of the few nonlinear maximum likelihood estimators which is consistent with fixed effects. This gives it an advantage over many other nonlinear estimators, that have poorly understood properties in the presence of fixed effects (Shepherd 2016). Another trait differing PPML from other non-linear alternatives is that it assigns the same weight to all observations. Following Santos Silva and Tenreyro's (2006) suggestion, it is the natural choice without further information on the pattern of heteroscedasticity. Just as the gravity equation is the workhorse for trade policy analysis (Bacchetta et al 2012), PPML can be described as the workhorse for gravity equation estimation (Shepherd 2016).

To conclude, I choose to employ the Pseudo Poisson Maximum Likelihood (PPML) model with support from the facts outlined above. As a way of checking robustness, I run OLS and Negative Binomial regressions in addition to the PPML. As mentioned, a puzzle in gravity equations is that we cannot be sure whether unreported trade represents zero trade or a missing value. The OLS regression ran with logarithms of imports serves de facto as a comparison showing the effect of zeroes in the data set.

5.4 Quantitative Results

The number of observations is 17 865 in the baseline PPML estimation, however alternating with the different specifications. Estimation results are presented in Table 2. The PPML estimation produces effects expected from classical gravity equation theory. Significant positive effects are found for exporter and importer GDP as well as exporter population size, while distance has a significantly negative effect on trade. Also in line with expectations, a shared language has significant positive effects on trade, as does history of colonial relation and having been the same country.

The coefficient for GSP+ is very close to zero on the negative side, but insignificant, meaning there is no support for a trade creating effect for countries going from accessing GSP to accessing GSP+. Lack of support for the intended effects on exports means the scheme should not constitute any incentive for complying with the UN Conventions. In other words; there is empirically no support of a trade creating

incentive to commit to sustainable development as well as human and labour rights. The result is counterintuitive to theory, as deeper preferences should produce more trade. It is however in line with previous research, for reasons to be explored further later.

Table 2: Estimation Results

VARIABLES	PPML	OLS	Negative Binomial
LnGDPexp	0.0117* (0.0713)	0.0241** (0.0121)	0.0342*** (0)
LnGDPimp	0.449** (0.0138)	0.104 (0.675)	0.0563* (0.0780)
LnDIST	-2.475*** (0)	-2.177*** (0)	0.226*** (0)
LnPOPexp	0.964*** (0.000506)	1.774*** (0)	0.246*** (0)
LnPOPimp	0.646 (0.470)	-0.825 (0.532)	0.512*** (0)
Comlang_off	0.388*** (0.00298)	0.988*** (0.000161)	0.613*** (0)
Col45	0.549*** (0.000406)	1.238*** (0.00141)	0.274*** (2.10e-05)
Smctry	0.521** (0.0334)	0.514 (0.252)	0.125 (0.750)
GSPplus	-0.0357 (0.720)	-0.178* (0.0503)	-0.00814 (0.703)
Constant	-6.033 (0.730)	10.44 (0.585)	-16.67*** (0)
Observations	17,865	15,999	17,839
Exporter Country FE	YES	YES	YES
Time FE	YES	YES	YES
RESET Test (p-value)	0.173	0.000	0.000

Robust p-value in parentheses
 *** p<0.01, ** p<0.05, * p<0.1

The OLS and Negative Binomial regressions, with the same fixed effects as the PPML regression, largely produce the same results, while there are different effects for some variables. The OLS regression finds weakly significant negative results for GSP+, but qualitatively I draw the same conclusion on GSP+ insignificance after seeing all results. The coefficient for a colonial link is much larger for the OLS than the baseline PPML, a result confirming bias from estimating with OLS originally found by Santos Silva & Tenreyro (2006). The Negative Binomial regression produces significant positive effects for distance, which is counterintuitive. Since I employ the two regressions as robustness tests, there is reason to dig deeper into these deviations. Before doing that, it can be repeated that OLS likely produces inconsistent results following the dropping of zero trade values. I attempt running OLS without truncation by replacing all zero trade flows with a small value, meaning the log of imports is zero. This produces different results from my original OLS estimation, further implying that the OLS estimator is not an appropriate estimator for this dataset. These results along with some of the coming robustness test results are found in Appendix C.

I try dropping Smctry from the PPML regression, given that the OLS and Negative Binomial models did not find significance for that variable. Dropping the variable and estimating the PPML again does not change my results notably, suggesting that the model is appropriately specified. I then run a Ramsey RESET test for misspecification on all three models. The null hypothesis of the test is no misspecification, in which case the coefficient of the fitted variable is zero. The fitted value is insignificant when the model has a correct specification. Following the RESET recommendations for PPML of Tenreyro & Silva (2006), I deduce the PPML regressor is not misspecified. Both the OLS and Negative Binomial models are however found to be misspecified, with the included variables and fixed effect approach being the same for all three models. This adds weight to the PPML results, suggesting only the PPML estimator is appropriate with this specification.

As an additional robustness test of my PPML estimator, I try an approach recommended by Bun and Klaassen (2004), namely to try a bilateral pair-specific fixed effect instead of the country-specific fixed effect. This is a way to account for country pair-specific alternation such as increased integration between an importer and an exporter. The pair-specific estimation produces the same results⁶, again adding robustness to the PPML estimation. Yotov et al (2016) recommend estimating the gravity equation with lags to allow for adjustments in bilateral trade flows in response to trade policy or changes in trade costs. Using three year lags again produces insignificant GSP+ effects, adding additional robustness.

⁶ In terms of GSP+, it produces a coefficient of -0.0279 with the p-value of 0.773

As earlier discussed, I employ a dummy variable taking the value one for all years a specific country is eligible for GSP+ and zero otherwise. A potential issue with using this method is that the effect of gaining and losing accession to GSP+ will be generalised to the direct opposites, which is not necessarily true. It is not certain that losing accession to GSP+ has the mirrored effect of gaining accession. I therefore try excluding GSP+ beneficiaries Pakistan, Panama and Sri Lanka from the years which they lose GSP+ accession. This again produces similar results for variable significance and coefficient direction⁷, adding weight to the result that GSP+ has not had a significant effect on export volumes.

As mentioned, the period included in the dataset is from 1988-2014, since the scheme after that changes significantly. It would be interesting to look at the time from 2014-2016 to see what effects GSP+ has had since the amendments. Alas, I do not deem it possible to run unbiased regressions for that period yet. The effect from joining GSP+ would be lost for most countries, as they benefitted from GSP+ since several years before 2014. As a means of further checking robustness, I instead break my dataset into two parts and estimate them individually. First are the effects for the Drug Regime (years 1988-2005) estimated exclusively, and then are the effects for GSP+ (years 2005-2014 and excluding countries who previously benefitted from the Drug Regime) estimated exclusively. I find insignificant results for both GSP+ and the Drug Regime. These results, found in Appendix C, add robustness and are in line with previous research; for example, Persson & Wilhelmsson's (2007) assessment of the Drug Regime and the Hvidt Thelle et al (2015) estimation of GSP+.

Developing countries often have poor trade infrastructure and instability, both affecting export capacity negatively. If there is a difference between GSP and GSP+ countries in terms of infrastructure and stability, one could suspect it to skew the results. These sorts of skewing conditions should however have been captured by my exporter country-fixed effects.

There are some different possible reasons for GSP+ lacking a significant trade creating effect. It seems that the preference scheme has been under-utilised. As an example; in Sri Lanka, utilisation rates were as low as 30-40% in early GSP+ accession years and around 50-60% in later years (Wijayasiri 2007; EC 2018_b). When a preference scheme is under-utilised, some prerequisites are interesting to study, one of them being preference erosion. Erosion occurs due to current MFN tariffs already being so low that the preference margin does not provide enough improvement for beneficiary countries to make use of the preference (Persson 2015). In the case of this study, the relevant preference gap subject to erosion to evaluate is between standard GSP and GSP+. The quantitative results suggest that the difference in preference depth between GSP and GSP+ is insufficient. With MFN tariffs today being low, the EU

⁷ Results available upon request

might be struggling with creating enough additional preference for its different preference schemes. This could mean that if the EU wants to use trade as an incentive for sustainable development, it might have to create negative GSP+ tariffs to widen the preference margin. This would in practice mean implementing import subsidies for GSP+ beneficiaries. However, as previously mentioned, research has found significant results on previous preference schemes more beneficial than GSP+ (Persson 2012). One solution for the EU to promote sustainable development could thus be to offer an updated [still conditional] GSP+ scheme with deeper preferences to all developing countries, while removing the EBA scheme.

Another possible cause for a preference scheme not working is low product coverage. GSP+ however generally has very high coverage rate (EC Trade 2018), for example potential coverage rates are upwards of 98% in Sri Lanka (Wijayasiri 2007). Yet, providing 100 % product coverage could make it easier for producers to adhere to GSP+, since research into what products are included in the scheme would no longer be necessary.

A third reason for under-utilisation is conditionality. GSP+ is a scheme granted with strict conditionality, not the least the 27 UN Conventions needed to be ratified and implemented by beneficiary countries, differing it from standard GSP. Adhering to the Rules of Origin is usually also mentioned as a key hinder for countries to utilise preference schemes (Persson 2015). Strict RoO can for example make imports of inputs needed for production harder, leading to under-utilisation of the preference. If costs associated with following the rules of origin are too high, businesses calculate benefits of GSP to be outweighed by the costs of complying with the requirements (Persson 2015; Democracy Reporting International 2016). GSP+'s strict RoO could also divert trade through stopping natural value chains.

A thing to note is that this paper applies data of merchandise trade, as GSP+ affects tariffs for trade in goods. The study does not say anything about trade in services. Given that the trade preference likely incentivises international companies to set up shop in beneficiary countries, exposure could lead to increased services export. One example of such service export is the tourism industry, being important for several developing countries. Good governance and sustainable development could also increase tourism levels. This effect remains for future research to be estimated.

To conclude, I find no support for a trade creating effect for countries going from accessing GSP to accessing GSP+. With several robustness tests, the insignificant result stands, meaning there is empirically no support for GSP+ having a trade creating incentive to commit to sustainable development as well as human and labour rights.

6. Qualitative Methodology

6.1 Sri Lanka

As the following part involves interviews conducted in Sri Lanka, some background on the country and its connection to GSP+ seem relevant.

Sri Lanka is a Lower Middle-Income country with a GDP per capita [in 2017] of USD 4,073 and a population of 21.4 million. The country has since the civil war ended in 2009 been quite stable, even though impunity for human rights violations and corruption remain problems in the country (CIA 2018). There have been some notable exceptions from stability in later years. In 2018, the country saw unrest following an unexpected removal of the elected Prime Minister by the President. The Prime Minister was however later re-instated (BBC 2018). The same year, Sri Lanka also saw ethnic tensions spark violence and burning of muslim-owned shops (Safi & Perera 2018). In April 2019, the Easter Sunday attacks on churches and hotels killed several hundreds. The attacks are likely to have effects on exports, not the least the important tourism sector, and had implications for the field research carried out for this thesis.

Today Sri Lanka is pursuing an agenda for export-led growth and has recently struck several free trade agreements (Wijayasiri 2007; Cooray 2018) while planning to join yet more (Wickremesinghe 2018). The economy is transitioning from being predominantly rural-based towards being more urbanised, oriented around manufacturing and services (World Bank 2018). In this context, strengthening export sectors is important for the country, and the World Bank (2018) states that the Sri Lankan economy's weak competitiveness is an issue to address. The country's main export products include apparel, tea & spices, rubber manufactures, gems and fish (CIA 2018). The largest export markets are the EU, the U.S and India (WITS 2017), and it has been claimed that GSP+ helped the EU to become the main export market (Democracy Reporting International 2016).

Sri Lanka benefitted from GSP+ before August 2010, after which the EU decided to stop giving preferential treatment under GSP+ to Sri Lankan imports. This because the country's government had failed to address human rights violations in the country. In 2015, the Sri Lankan government embarked on reforms aiming to achieve national reconciliation, respect for human rights, the rule of law and good governance, as well as sustainable development. This led Sri Lanka to start benefitting from GSP+ again in 2017 (EC 2018). The European Commission (EC) (2018_a) states that Sri Lanka has taken major steps to improve governance and respect for human rights. One example is re-establishing the independence of key institutions such as the National Human Rights Commission. At the same time, the EC emphasises that Sri Lanka needs to; put a stop to the use of torture, improve the rights of women

and children, and address the harassment of trade unions. These issues have been subject to GSP+ monitoring since May 2017 (EC 2018_a, EC 2018_b).

Suspending Sri Lanka from GSP+ likely constituted economic incentive for Sri Lankan businesses to actively engage the government on its human rights record (Yap 2013). Sri Lanka is set to graduate from GSP+ between 2021–2023 due to reaching Upper-Middle Income level (EEAS 2017). Graduating from GSP+ due to reaching a higher income level is not the same as being suspended for breaking the sustainable development criteria, and their effects should not have the same negative impact on the country’s exports.

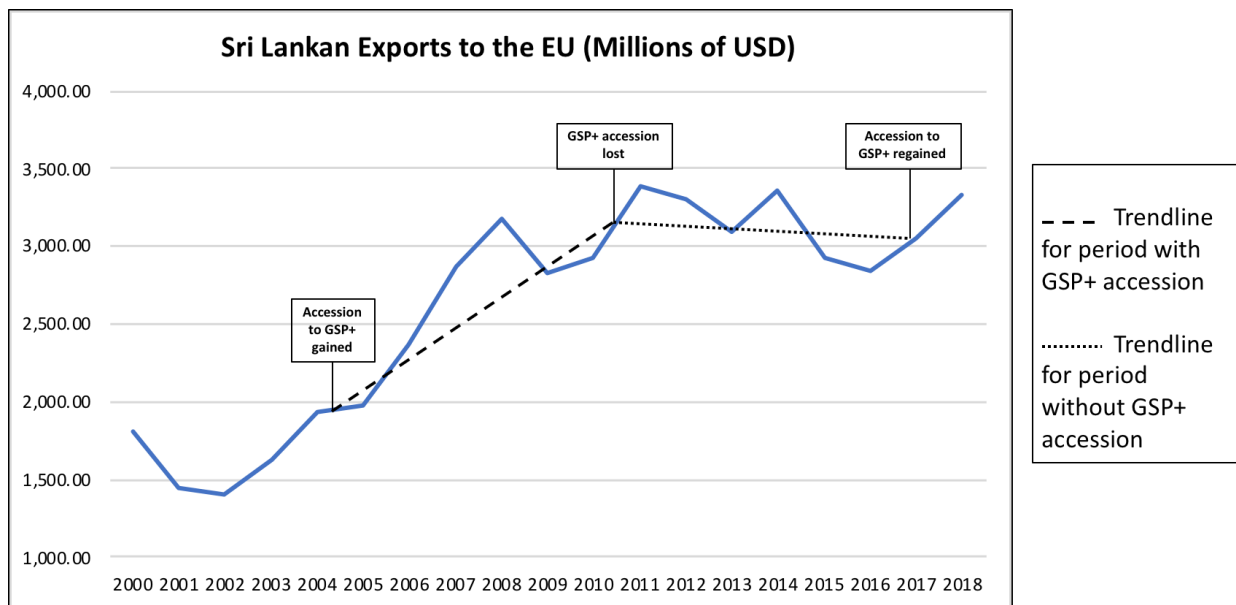


Figure 3: Sri Lankan exports to the EU 2000-2018, expressed in millions of USD. Source of data: DOTS (IMF 2019).

6.2 Methodology

While this thesis draws its main inference from quantitative results, I add a qualitative aspect to deepen the analysis in trying to evaluate the effect of GSP+ on beneficiary countries. The approach is to be viewed a mixed method *QUAN* → *qual approach*, where the quantitative method is prioritised (Bryman 2012). I conduct four semi-structured interviews with key informants representing different stakeholders in Sri Lanka. Semi-structured interviews are conducted having several questions prepared, while there is flexibility to amend – and add supplementary – questions during the interview (Bryman 2012). Interview questions regard Sri Lankan trade, GSP+ effects on export volumes, labour & human rights and sustainable development as well as knowledge and utilisation of the trade preference. For the set of questions interviews were based on, see Appendix D. The interviews are not to be viewed as randomly sampled, but instead what is called a *convenience sampling*, used to triangulate the effects of

GSP+ in my analysis and answer further questions in addition to my quantitative study. The interviews are not used to conduct statistical inference, but instead to explore the issues through the eyes of key stakeholders (Bryman 2012). When conducting field research, a challenge can be finding relevant respondents in the country (Murray & Overton 2003). Contact with the key informants was established through several *gatekeepers*, meaning persons holding contacts within the intended research field. An important aspect to remember is that a gatekeeper can hold a certain kind of contacts, meaning there is a risk to only be exposed to one sort of opinion. I approached the gatekeepers with requests for certain stakeholders and the interviewees were singled out from a larger proposition from the gatekeepers, where respect was paid to having different stakeholders. Once initial contact with informants was made, the mechanism usually called *snowballing* occurred. Snowballing refers to when one interviewee leads the interviewer onto another (Bryman 2012).

Table 3: The key informants interviewed, their organisations and the date of interview

Role(s)	Organisation	Interview date
1. Chief Economist and Economist	The Ceylon Chamber of Commerce (CCoC)	2019-03-26
2. Economist, Executive Technical Services	The National Chamber of Exporters Sri Lanka (NCE)	2019-03-28
3. Chief Technical Advisor	International Labour Organization, Country Office for Sri Lanka and the Maldives (ILO)	2019-04-03
4. Director	Ministry of Development Strategies and International Trade (MODSIT)	2019-04-09

The informants are chosen on the basis on their expertise on GSP+ and the fact that they are representing different stakeholders of GSP+. The private sector, the public sector and NGOs are included in the sampling. The ILO is chosen as the respondent representing NGOs with a special interest in the UN Conventions. One reason for choosing to interview ILO instead of labour unions, is that labour unions in Sri Lanka are generally connected with the political parties (Gamage 2013), meaning there is a risk that answers are biased by party-political views and allegiances.

The interviews are all conducted in the respective interviewee's office in Colombo, Sri Lanka. Language is a key concern in field research (Murray & Overton 2003). All interviews are conducted in English, a second language for me and several interviewees. This brings questions whether the recipient and I have the same understanding of what is said at the interviews. It should however be noted that all interviewees were professionals with excellent command in English. Further aspects to consider are that impunity for human rights violations and corruption is still an issue in Sri Lanka (CIA 2018) and significantly high state participation in the economy has implications on economic sectors and labour market dynamics (World Bank 2018). Conducting the interviews, I did however experience that all questions I had could be explored. The interviews are all recorded and abstracts are written shortly after

every conducted interview. I code and organise the answers based on themes to try and find common and general answers among the interviewees, as well as see what specific answers and thoughts individual respondents have.

The field research was planned to be carried out between March 23rd and May 18th, but was interrupted by the previously mentioned Easter Sunday attacks. Following the interruption, some scheduled interviews were not able to be carried out and thus limited the qualitative scope of this thesis. Plans were cancelled to interview the Department of Commerce and the textile industry, which both could have contributed important insights. Not a bene, however, that the four interviewees cover different stakeholder groups. The attacks are likely to have effects on Sri Lankan trade and economic integration with the world. Results should be interpreted with the knowledge that all presented answers were given before the attacks.

6.3 Qualitative Results

In this section I briefly summarise the results from the conducted interviews. See Appendix E for a longer account of responses.

The interviewees generally think trade is on the upswing in Sri Lanka, with new policy and trade agreements coming into place. It is however noted that the Sri Lankan economy is still protected, with complex laws and a lack of diversification. The respondents' organisations work with GSP+ in different ways; through advocacy, spreading information and providing technical assistance. The respondents generally think GSP+ has had a positive impact on Sri Lankan exports, naming significant tariff drops in important sectors such as apparel, rubber and porcelain compared to standard GSP. Other benefits mentioned includes raised product standards, incentivised by GSP+ to meet the high-quality demand in Europe. One respondent points out that GSP+ might have a positive impact by leading to more labour-intensive goods being exported, which would raise employment in beneficiary countries. The stakeholders agree that the country was hurt by losing access to GSP+, while a simultaneous fishing ban from the EU was in place. Respondents say that regaining GSP+ has benefitted the exports, while it is not yet back to the same level as before GSP+. This because foreign investors moved production to other countries when accession was lost, and it is now hard to regain that investment again. SME's are said to have been hurt the most from losing access to GSP+.

The respondents disseminate GSP+ to have a positive effect on both exports and labour and human rights in the country, while GSP+ effects on environmental concern seem harder to quantify. The different stakeholders find the conventions worthwhile to implement, and think the scheme constitutes an incentive for both exporting companies and the government. Examples are given of how the private

and public sector both have an interest that the relevant conventions are implemented, not wanting to risk losing access to GSP+ again. The private sector is said to have lobbied the government to comply with necessary human rights standard to regain GSP+ after accession was lost. Exporting companies are said to monitor their labour standards. The government has adhered to human rights regulations, said to be aware what they need to do to sustain access to GSP+. A concrete example given is the Sri Lankan President taking back a statement about enforcing the death penalty after having been warned by the EU it would have implications on trade. Labour standards in the country are said to be doing comparatively well, especially in export sectors.

The most common areas of improvement named concern 1) the Rules of Origin (RoO) and 2) lack of information, as they cause under-utilisation of the scheme. Qualifying the RoO is said to be especially hard for the large apparel sector. It is said that countries able to sustain their own raw materials have higher degrees of utilisation than Sri Lanka, who must import raw materials. This causes a problem, as breaking the RoO means they export under normal GSP regime instead of the GSP+ benefit. Several respondents point out that Sri Lanka is applying for increased regional accumulation with Asian countries, Indonesia being one of them. It is up to the EU to decide if Sri Lanka should be allowed more generous accumulation restrictions. When it comes to lack of information, respondents point out a dividend between larger companies and SME's. Several interviewees point out that it is to a larger extent the large-scale companies with their own research departments utilising GSP+. Many smaller companies are said to lack information on the existence of GSP+, and some of those who are aware of it lack capacity to fulfil the technical rules needed to benefit from the scheme. One respondent says an important reason for why especially SME's do not know of GSP+ is the language barrier. She claims it is often assumed that exporting companies understand information in English, which is not necessarily true for some SME's and that people in trade are even being exploited because of language.

One of the respondents stated that Sri Lankan companies now view GSP+ accession as a "*tax holiday*", referring to the fact that they are aware it is only temporary. It was also expressed that GSP+ is viewed as a somewhat political tool, and concern was raised whether future governments will continue complying with the relevant conventions.

To conclude, the respondents agree that GSP+ has had a trade creating effect in Sri Lanka. They also name several examples of how the scheme has benefitted human and labour rights in the country, while they have a harder time naming effects on environmental concern. The preference scheme seems to function as an incentive, making both companies and the government show concern for compliance of the UN Conventions. Some concerns around the scheme are the Rules of Origin (RoO), a lack of information and uncertainty of access.

7. Conclusion

This study has estimated trade creating effects of gaining access to trade preference scheme GSP+, as compared to accessing the standard GSP scheme. I have employed a PPML-estimated Gravity Equation and found robust insignificant results for trade creating effects from GSP+, compared to standard GSP. The results imply that GSP+ has no proven trade creating effect over standard GSP. The scheme should thus not constitute any incentive for complying with the UN Conventions on sustainable development and good governance. The result is in line with previous research, but counterintuitive to theory, as deeper preferences should produce more trade. I have also conducted stakeholder interviews in GSP+ beneficiary country Sri Lanka. Through the interviews, I found concrete examples of how the scheme has had positive effects on human rights and labour rights in the country. Results for GSP+ effects on environmental concern were however weaker, which is in line with previous research. I also find that GSP+ is thought to be trade creating in Sri Lanka and that it constitutes an incentive for both government and companies to seek compliance of the relevant UN Conventions.

Compared to previous research, one of my contributions consists of combining econometric analysis with qualitative interviews to draw more in-depth analysis and suggestions for improvements. With new data and interviews in beneficiary country Sri Lanka, I answer whether GSP+ constitutes an incentive for sustainable development and respect for human and labour rights. My results suggest that while GSP+ does not have any significant trade creating effect overall, it could still have had a trade creating effect for individual beneficiaries. My qualitative results suggest the scheme at least in Sri Lanka has fulfilled its purpose of incentivising respect for human and labour rights.

Since I found examples of how GSP+ contributes respect for human and labour rights, the scheme can be considered at least partly successful. The quantitative results however point to the fact that improvements could be made to GSP+. By far the two most named areas of improvements found in interviews with Sri Lankan stakeholders are 1) Rules of Origin (RoO) and 2) lack of information. Contingency is also mentioned in various forms. Previous research commonly mention RoO and contingency as issues with trade preference schemes. Forms of information asymmetries are however less explored in earlier research papers on trade preferences.

The EU could benefit GSP+ by simplifying the RoO. An example given by respondents in this study is to allow for more regional accumulation. Relaxation of RoO is likely done best in cooperation with the beneficiary countries, to avoid trade deflection. When it comes to lack of information, the reported findings point to what is usually called an *information asymmetry*. While larger companies with sufficient resources are aware of and make use of GSP+, SME's are reported to under-utilise the scheme. Reported is a lack of comprehensible information on the existence of the preference, how to

adhere to its rules, as well as a lack of translation of the same information into different languages. This information asymmetry could risk putting market forces out of play, as using the trade preference gives an advantage to larger companies over SME's. Considering GSP+ is meant to promote sustainable development and industrialisation, it should be in the EU's interest that SME's in poorer areas of beneficiary countries are also informed on the scheme. Information efforts are likely done best in cooperation with beneficiary countries' stakeholders. Results in this study suggest that such efforts mainly need be focused on SME's and companies outside of larger cities. Comprehensible information in all official languages should be made widely available.

Another concern is certainty of access, as contingency usually is considered harmful for trade. As found in the interviews of this study, multinational companies were swift to leave Sri Lanka when it lost accession to GSP+, and there was concern that a shift of government could lead to losing GSP+ accession. Beneficiary countries should therefore attempt to create broad political consensus for GSP+ alignment. Results confirm the importance to have broad stakeholder consensus for following the conventions in beneficiary countries, as losing access even temporarily damages the country's export sector on a longer term.

It is not necessarily the case that the insights gained from interviewing a few different stakeholders in Sri Lanka can be generalised for understanding GSP+ effects and areas of improvements in general. A future broader study including interviews from several GSP+ countries could therefore be advantageous. Updated econometric and stakeholder case-specific studies for each GSP+ beneficiary country could develop larger insights into how best improve GSP+ by allowing comparative analysis. After sufficient time has passed from the GSP amendments of 2014, a study of longer time-period and broken down to product level could be valuable. It could also be interesting to look at GSP+ effects on different sectors, comparing those who rely on domestic goods with those who need external input. In that way, one could deduct more closely effects of the RoO. Lastly, it would be interesting to look at the composition of what is exported, not only the value of it, to deduct if GSP+ creates more labour-intensive production and thus increases employment.

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9. Appendices

Appendix A: GSP+ Conventions: Annex VIII of Regulation (EU) No 978/2012 of 31 October 2012

Part A: Core Human and Labour Rights UN/ILO Conventions
1. Convention on the Prevention and Punishment of the Crime of Genocide (1948)
2. International Convention on the Elimination of All Forms of Racial Discrimination (1965)
3. International Covenant on Civil and Political Rights (1966)
4. International Covenant on Economic Social and Cultural Rights (1966)
5. Convention on the Elimination of All Forms of Discrimination Against Women (1979)
6. Convention Against Torture and other Cruel, Inhuman or Degrading Treatment or Punishment (1984)
7. Convention on the Rights of the Child (1989)
8. Convention concerning Forced or Compulsory Labour, No 29 (1930)
9. Convention concerning Freedom of Association and Protection of the Right to Organise, No 87 (1948)
10. Convention concerning the Application of the Principles of the Right to Organise and to Bargain Collectively, No 98 (1949)
11. Convention concerning Equal Remuneration of Men and Women Workers for Work of Equal Value, No 100 (1951)
12. Convention concerning the Abolition of Forced Labour, No 105 (1957)
13. Convention concerning Discrimination in Respect of Employment and Occupation, No 111 (1958)
14. Convention concerning Minimum Age for Admission to Employment, No 138 (1973)
15. Convention concerning the Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labour, No 182 (1999)
Part B: Conventions Related to the Environment and to Governance Principles
16. Convention on International Trade in Endangered Species of Wild Fauna and Flora (1973)
17. Montreal Protocol on Substances that Deplete the Ozone Layer (1987)
18. Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal (1989)
19. Convention on Biological Diversity (1992)
20. The United Nations Framework Convention on Climate Change (1992)
21. Cartagena Protocol on Biosafety (2000)
22. Stockholm Convention on persistent Organic Pollutants (2001)EN L 303/60 Official Journal of the European Union 31.10.2012
23. Kyoto Protocol to the United Nations Framework Convention on Climate Change (1998)
24. United Nations Single Convention on Narcotic Drugs (1961)
25. United Nations Convention on Psychotropic Substances (1971)
26. United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (1988)
27. United Nations Convention against Corruption (2004)

Appendix B: Countries Included in Data Set

EU15	GSP	GSP+
1. Austria	1. Aruba	1. Bolivia
2. Belgium	2. Albania	2. Colombia
3. Denmark	3. United Arab Emirates	3. Cabo Verde
4. Finland	4. Argentina	4. Costa Rica
5. France	5. Bahrain	5. Ecuador
6. Germany	6. Bosnia and Herzegovina	6. Georgia
7. Greece	7. Bermuda	7. Guatemala
8. Ireland	8. Brazil	8. Honduras
9. Italy	9. Brunei Darussalam	9. Sri Lanka
10. Luxembourg	10. Cuba	10. Mongolia
11. Netherlands	11. Gibraltar	11. Nicaragua
12. Portugal	12. Hong Kong SAR, China	12. Pakistan
13. Spain	13. Indonesia	13. Panama
14. Sweden	14. India	14. Peru
15. United Kingdom	15. Iran, Islamic Rep.	15. Philippines
	16. Iraq	16. Paraguay
	17. Kuwait	17. El Salvador
	18. Libya	18. Venezuela, RB
	19. Macao SAR, China	
	20. Malaysia	
	21. New Caledonia	
	22. Nauru	
	23. Oman	
	24. French Polynesia	
	25. Qatar	
	26. Saudi Arabia	
	27. Singapore	
	28. Thailand	
	29. Uruguay	
	30. Vietnam	

Appendix C: Robustness Test Results

VARIABLES	PPML With Lagged Explanatory Variable	OLS Without Truncation	PPML Without Smctry Variable	PPML Drug Regime Exclusive	PPML GSP+ Exclusive
LnGDPexp	0.0167** (0.0371)	0.0674*** (2.21e-06)	0.0117* (0.0712)	0.00143 (0.794)	0.0112* (0.0850)
LnGDPimp	0.364* (0.0647)	-1.805*** (5.41e-06)	0.449** (0.0138)	0.243 (0.195)	0.404** (0.0385)
LnDist	-1.661*** (4.80e-05)	-2.523*** (1.42e-10)	-2.475*** (0)	-2.508*** (0)	-2.603*** (0)
LnPOPexp	1.246*** (1.20e-05)	0.908 (0.100)	0.964*** (0.000506)	0.864* (0.0586)	0.998*** (0.000406)
LnPOPimp	0.835 (0.327)	12.06*** (1.23e-09)	0.646 (0.470)	4.187** (0.0439)	0.475 (0.617)
comlang_off	0.354*** (0.00406)	1.292*** (3.15e-05)	0.388*** (0.00298)	0.421*** (0.00180)	0.473*** (0.000903)
Col45	0.405*** (0.00457)	1.327*** (0.00197)	0.549*** (0.000406)	0.610*** (0.000229)	0.519*** (0.00116)
Smctry	0.707** (0.0186)	-0.381 (0.531)		0.465* (0.0579)	0.460* (0.0789)
GSPplus	0.0276 (0.775)	-0.465** (0.0236)	-0.0357 (0.720)	-0.0998 (0.350)	-0.0433 (0.793)
Three-year lag	8.93e-09** (0.0106)				
Constant	-13.34 (0.271)	-126.8*** (3.26e-05)	-6.025 (0.731)	-42.26 (0.108)	-2.284 (0.871)
Observations	15,705	17,865	17,865	11,925	13,575
Exporter Country Fixed Effects	YES	YES	YES	YES	YES
Time Fixed Effects	YES	YES	YES	YES	YES

Robust p-value in parentheses
 *** p<0.01, ** p<0.05, * p<0.1

Appendix D: Interview Guide

1. Can you briefly describe your organisation and your own role in it?
2. How would you describe the development of international trade in Sri Lanka in later years?
3. How would you describe the status for exporting Sri Lankan companies? Do they face any difficulties/challenges?
4. To what extent do you think that GSP+ has had an impact on Sri Lanka in terms of export volumes?
5. To what extent do you think that Sri Lankan companies have heard of, and make use of, GSP+?
6. How do you as an organisation work to increase usage of GSP+ and other trade agreements?
7. Some previous studies did not find any significant results on increased export volumes coming from GSP+ accession. What do you think could be the reason for that? Anything that could be improved?
8. For exporting companies who are currently not using the agreement, do you think that there is anything that could change for GSP+ to be used to a larger extent?
9. To what extent do you think that GSP+ has had an impact on sustainable development in Sri Lanka?
10. To what extent do you think that GSP+ has had an impact on human rights and labour conditions in Sri Lanka?
11. Do you think the Sri Lankan authorities are working to ensure the labour- and human right standards, as well as sustainable development, stipulated in GSP+? If so, how?
12. Do you think that exporting companies are aware of the link between on the one hand Sri Lanka's effective implementation and the following of UN conventions on human- and labour rights and sustainable development, and on the other hand the lowered tariffs that come from GSP+?
 - How do you think companies are working with this?
 - Do you think GSP+ serves as an incentive for companies to improve labour- and human rights and working towards sustainable development?
13. Finally, is there anything you would like to add?

Appendix E: Interview Answers

Brief description of the organisation and how it works with GSP+

CoCC represent their 600 member enterprises, working with trade initiatives, advocacy and information through seminars and events. The CoCC has written articles and set up a website containing information on GSP+ accession rules and how to comply with them, tariff reduction compared to GSP, and how to contact authorities for assistance.

NCE represents 500 exporting companies to which they provide technical assistance, policy assistance and information on GSP+ through seminars and e-mails. They also serve as a link between the private and public sector in spreading information on GSP+.

ILO works with government, workers and employers in Sri Lanka on policies for improving labour standards and employment.

MODSIT is the Sri Lankan government agency with responsibility for international trade. The agency has a specific action plan for raising stakeholder awareness on GSP+ and are trying to reach different regions in the country.

Development of international trade in Sri Lanka and status for exporting companies

All interviewees agree that Sri Lanka has made a lot of progress on trade in later years. Losing access to GSP+ and receiving a fishing ban from the EU around the same time is claimed to have lowered exports notably, but since re-gaining accession to GSP+ along with the fishing ban being lifted the country has seen an increase in exports. New policy has been formulated to support trade, even though the CCoC representatives point out they are working to have some outdated rules and regulations updated.

The MODSIT representative says the transition towards more outward-looking policy in the 1970's has changed a lot. The CCoC say the new government are making trade the engine of Sri Lankan growth. There has been an attempt to reorient the focus on domestic consumption to more trade as a growth model that will sustain growth for the future. The government's Vision 2025 document and the National Export Strategy are mentioned as contributors. Sri Lanka has had several trade negotiations recently, with several new free trade agreements in the last few years.

The interviewees from CCoC say a lot has been done on trade facilitation recently, especially from the private sector. The full benefit of reforms from public sectors has however not fully come through yet. They are currently looking at sectors which have a high level of protection and describe current times as a "transitory period" for international trade in the country. The ILO representative said there is still a disconnect between the governments strive and "policies on the ground" (ILO 2019), saying the Sri Lankan economy still is very protected, for example by import tax, with certain groups being especially protected. Imports are not viewed as positively as exports and he says laws are outdated and complex. He compares with Vietnam, who has allowed for a lot more competition. He said diversification and moving into higher-value products is needed. The MODSIT representative names similar issues, saying the export basket in Sri Lanka has not improved as in some other countries. The NCE also say increased diversification is needed, saying that some export sectors have done better than others and that a reason for why some are doing worse is that they are more dependent on imports.

Effects of GSP+ on Sri Lankan trade

All interviewees think GSP+ has had a positive impact on Sri Lankan exports and say that losing the accession hurt the country, while exports have increased since re-gaining accession. The NCE mentions for example the drop in tariffs from 9.8% to 0% following re-accession into GSP+ again to have boosted the important apparel sector. The CCoC interviewees also name further key products exported through GSP+, such as rubber and porcelain to have a significant change in tariff from GSP to GSP+ and say the tariff difference makes a big difference for the private sector. They say that re-gaining GSP+ has benefitted the country, but that is not yet back on the levels they were on before losing accession. They believe one issue is that when Sri Lanka lost accession, foreign investors moved production to other countries, and it is now hard to regain that investment again. They name another benefit with GSP+ that it has caused an incentive for Sri Lankan producers to raise product standards. This quality improvement

has been needed to meet the high-quality demand in Europe and is believed to have positive effect for future trade after graduating from GSP+.

The NCE representative says SME's were hurt the most from losing access to GSP+. Bigger firms could absorb the tariff increase better. She also thinks that after graduating from GSP+, the SME's will again be hit worst and face a larger risk of not being competitive enough. She however also says graduating from GSP+ will probably not cause as much disturbance as losing the accession did.

The interviewees in general did not think that GSP+ will leave Sri Lankan producers unfit for competition in post-GSP+ times. Interviewees instead talked about it being important with future plans. The MODSIT representative named trade adjustment programs as a way of mitigating the risk of not being competitive enough after graduating GSP+. When asked, all interviewees thought GSP+ might serve as a stepping stone to signing new FTAs with the EU. The CCoC claimed that Sri Lankan companies were aware that Sri Lanka will soon graduate from GSP+ and that it is more or less seen as "a tax holiday" (CCoC 2019). They said that the scheme therefore might boost current Sri Lankan producers more than bringing new players into the field.

Effects of GSP+ on sustainable development and human & labour rights

All interviewees agreed that GSP+ has a positive impact on sustainable development as well as human- and labour rights in Sri Lanka. While the environmental impacts were harder to quantify, respondents gave clear examples of how the scheme has had a positive impact on human- and labour rights. One example brought up by the ILO representative is an event in October last year. The Sri Lankan President was talking about enforcing the death penalty and the EU reacted saying that would have consequence for trade relations, after which the proposal was taken back immediately. The interviewee thinks that GSP+ served as an incentive in this case, saying "there is no question about that" (ILO 2019). The ILO representative also says labour standards are generally good in comparison with other countries in the region, saying Sri Lanka is doing well in enforcing the standards. He said labour standards are respected "especially in export sectors" (ILO 2019).

Interviewees agree that exporting companies, at least the larger ones, are generally aware of the relevant standards that must be met to access GSP+ and lobbies the government to uphold human rights in the country. The CCoC and NCE say there was a big drive from the private sector that Sri Lanka should compel with relevant human rights standards after GSP+ accession was lost. The CCoC representatives also say that GSP+ "brings in best practice" (CCoC 2019) and that GSP+ has helped companies monitor their labour standards, which is also needed to retain labour. The MODSIT representative exemplifies saying most tea exporters and garment factories "upgrade their systems" (MODSIT 2019) to meet expected standards. She says the authorities have worked together with stakeholders such as the private sector on GSP+ and affirms that the exporting companies campaigned the government to do what is necessary to regain GSP+ after it was lost.

Several interviewees mention that as Sri Lanka lost GSP+ accession it was a strike on exporting firms and that multinational companies moved their production elsewhere, such as Bangladesh or Vietnam. Companies are said to vote with their feet and that makes responsible government persons fully aware of what they must do to keep GSP+. This, along with exporters lobbying the government, seems to be creating an incentive for following the relevant UN Conventions on sustainable development as well as labour- and human rights.

Reasons for why GSP+ might not have had a trade creating effect and areas of improvement

All interviewees are surprised to hear that studies have not found significant effects for GSP+. The most common reasons named for the insignificant result are 1) the Rules of Origin (RoO) and 2) lack of information, as they cause under-utilisation of the scheme. The CCoC points out that qualifying the RoO has been especially hard for the apparel sector. The MODSIT respondent says that countries being able to sustain their own raw materials have higher degrees of utilisation than Sri Lanka, who must import raw materials. This causes a problem when breaking the RoO means they export under normal regime instead of the GSP+ benefit. Several respondents point out that Sri Lanka is already applying

for increased regional accumulation with Asian countries, Indonesia being one of them. It is up to the EU to decide if Sri Lanka should be allowed more generous accumulation restrictions.

When it comes to lack of information, respondents point out a dividend between larger companies and SME's. Several interviewees point out that it is to a larger extent the larger companies with their own research departments utilising GSP+. Many companies are said to lack information on the existence of GSP+, and some of those who are aware of it lack capacity to fulfil technical rules such as the RoO to benefit from the scheme.

The MODSIT respondent says that the Department of Commerce is working with stakeholder awareness in regions and that MODSIT have an action plan for increasing knowledge on GSP+. She thinks the EU could do more to increase information on GSP+. She thinks non-tariff measures (NTMs) could be troublesome for some companies to meet, and that it could be beneficial for exports if information on the standards would be easier to retrieve for "people on the ground" (MODSIT 2019). The NCE respondent says one important reason for why especially SME's do not know of GSP+ is the language barrier. She claims it is often assumed that exporting companies understand information in English, which is not necessarily true for some SME's and that people in trade are even being exploited because of language.

The ILO representative points out that even if export volumes have not increased, GSP+ might still have a positive impact by leading to more labour-intensive goods being exported, which would raise employment. He raises that the correct policies must be implemented after accessing GSP+, meaning Sri Lanka should be more open for competitiveness. He says one option for change of GSP+ could be to make some the benefits of the scheme dependent on reducing tariffs by the beneficiary country [making it reciprocal].

Miscellaneous

It was expressed in one of the interviews that GSP+ is viewed somewhat as a political tool, and concern was raised whether future governments would continue complying with the relevant conventions. No interviewee however raised any concern that GSP+ would in any way clash with Sri Lankan values. The CCoC, when asked about it, pointed out GSP+ is not something that has been forced upon Sri Lanka, but something that the country has sought access to.

Several of the interviewees mentioned they are worried with, and closely follow, Brexit. The UK being the biggest export market within the EU, Brexit has consequences for Sri Lanka. Interesting future research would be looking at how Brexit is impacting developing countries.