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EU-Tunisia DCFTA: Good Intentions Not Enough

Shift Needed from Deep to Deliberate, Comprehensive to Coherent and from Free to Fair Trade

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The European Union has been negotiating a new free trade agreement (DCFTA) with Tunisia since 2016, seeking to expand mutual market access for all goods, and also services and investments. But great obstacles remain to be overcome. The EU hesitates to grant concessions on agriculture that would make a deal attractive to Tunis, while overall resistance exists within Tunisian civil society, business and politics. A shrewd agreement could promote economic modernisation and growth, to strengthen and stabilise Tunisia's young democracy. That is obviously also in the EU's interest. But substantial progress cannot be expected until after elections to the European Parliament and parliamentary and presidential elections in Tunisia in late 2019. The intervening period should be used to generate a broader consensus in Tunisia and to enable Tunis to create a negotiating strategy of its own.

Since Tunisia's democratic awakening of 2011 Europe has made substantial symbolic and material investments in political and economic cooperation, on top of development measures. Although Tunisia has made great progress on democratisation, it has failed to find a path out of an economic crisis that has dragged on since 2011. Tunisia urgently needs high-value exports to generate economic momentum and create employment especially for its young population. The European Union is Tunisia's most important trading partner: more than 50 percent of Tunisia's imports come from the EU, almost 80 percent of its exports go there. Tunisia's principal imports are machinery and equipment, vehicles, chemicals and mineral fuels. Its exports are dominated by textiles, electrical goods and agricultural products (above all olive oil and dates).

For the European Union, on the other hand, trade with Tunisia is marginal, at less than 1 percent of its global trade. The EU does nevertheless stand to profit from greater market access, for example through an opening of Tunisia's heavily protected agricultural sector. First and foremost, though, Brussels hopes that an agreement will contribute to stabilising the only country in the region to have experienced a democratisation process in the course of the so-called Arab Spring. Tunisia has also become increasingly important to the EU in connection with counter-terrorism and migration issues.

Starting Point for Talks

An association agreement (AA) with Tunisia came into effect in 1998, embedded in the Southern Dimension of the EU's Neighbourhood Policy. Like all the EU's agreements with southern Mediterranean countries, the association agreement differs in a crucial respect from EU agreements with other third states and above all with developing countries: Whereas the Economic Partnership Agreements (EPA) with EU member states' former African, Caribbean and Pacific colonies grant complete opening of EU markets for all goods, AAs to date have restricted far-reaching market opening only to industrial goods (including Tunisia's crucial textile sector). As an "upper middle income country" Tunisia is excluded from the complete market opening for all goods the EU grants to LDCs under the "everything but arms" (EBA) regime, nor does it benefit from strong tariff reductions under the generalised system of preferences (GSP). In fact, improving market access with Tunisia creates a dilemma for the EU: If, as intended, the EU offers Tunisia complete abolishment of tariffs this would deprive the states of Sub-Saharan Africa of their comparative advantage and — in the agricultural sector for example — turn them into direct competitors.

Since the EU-Tunisia AA came into effect in 1998 there have been continuous negotiations about liberalising agricultural trade, seeking greater and reciprocal market access. To date, only certain products — like dates and spices — benefit from duty-free access. Those negotiations came to halt with the political upheavals in late 2010, and were only resumed in 2015 at the EU's initiative, with the objective of concluding a Deep and Comprehensive Free Trade Agreement (DCFTA). The European Union seeks such agreements with its southern and eastern neighbours (and talks have also begun with Morocco), applying a comprehensive model similar to those directed towards economically strong partners: besides agriculture, services, public procurement and access for investors, the DCFTA also aims to address higher-level issues such as regulation and sustainability addressing labour and environmental regulation. As in the EPAs, asymmetry and progressivity are fundamental principles: The EU opens its markets completely and immediately, whereas Tunisia is granted more time with the possibility to exclude sensitive products.

To date the talks have been sluggish: Alongside two official rounds (April 2016 and May 2018) there was also a technical round. The third round, scheduled for October 2018 has been postponed to early December. In early November it was still unclear whether it would take place at all, after the Tunisian lead negotiator was appointed transport minister.

Obstacles in Tunisia

For various reasons Tunisia has approached the talks with great caution:

Resistance in business and society. Tunisian civil society — which has been extremely vibrant since 2011 — and the powerful trade union confederation Union Générale Tunisienne du Travail (UGTT) have raised objections to a DCFTA. Opposition is also heard from certain sectoral organisations, such as the bar association and agricultural organisations. The employers' organisation UTICA is divided: Some members hope that the DCFTA will spur reforms, others fear the competition it will expose them to. Opponents of a DCFTA blame the current AA for deepening regional economic imbalances and trapping Tunisia in low-value-added activities. They demand that the AA's impacts be evaluated before negotiations on a successor begin in earnest. The great lack of knowledge about the actual substance of the talks — and thus the potential opportunities — also contributes to widespread scepticism towards a DCFTA. A survey in the agricultural sector (Tunisian Sigma Conseil and Konrad Adenauer Foundation in spring 2018) found that 90 percent ofrespondents had never heard of the DCFTA. This is likely to change as events unfold; both sides have stepped up their efforts to maximise transparency of information in Tunisia about the content and progress of the talks and to consult all relevant actors.

Lack of political backing. None of the principal actors in the governing coalition in place until November 2018 visibly supported the DCFTA — and there were no indications of a change with a new coalition and ensuing government reshuffle. The DCFTA does enjoy some backing among the leadership of the moderate Islamist Ennahdha Party, which is the largest party in government. Yet even there, the agreement is not a priority and the content of the talks is not widely known. Reservations within most parties in government and particularly in Nidaa Tounes, the largest opposition party after it pulled out of the governing coalition in November 2018, are not least rooted in vested interests of the economic elites of the old system represented in these parties. According to Tunisian observers the old elites fear that tighter labour regulations, heightened competition, greater transparency, and new bodies with civil society participation — all of which would be associated with a DCFTA — would threaten their influence and sinecures.

Finally, Prime Minister Youssef Chahed, who had been strongly challenged throughout 2018 but managed to consolidate his position with the government reshuffle, has little to gain from pushing an agreement. The DCFTA issue deepens rifts with actors like the UGTT, with which he is already forced to conduct difficult negotiations in the course of economic reforms required by the International Monetary Fund, but on whose support he is increasingly dependent. Hence, no significant government actors can be expected to rally behind the unpopular free trade agreement before the parliamentary and presidential elections scheduled for late 2019.

Capacity constraints. The Tunisian state appears to be overwhelmed by the multiple challenges of economic transformation and a young democratisation process. Actors within the European Commission and the member states complain of a lack of efficiency, coordination and communication in both government and administration (not only concerning trade questions). In the DCFTA process Tunisian agencies often take months or even years to respond to EU proposals and requests for data and statistics, leaving Brussels rather perplexed. While European officials do report improvements since the first round of talks — under a new lead negotiator who has himself now moved on — a clear Tunisian negotiating strategy and corresponding prioritisation are still lacking. This is also reflected in the fact that to date only the EU's draft negotiating text is publicly accessible.

Expectations and Possibilities

Despite fears and reservations, Tunisia could profit from a DCFTA. However, impact analyses indicate different effects on individual sectors and on the Tunisian economy as a whole. This calls for shrewd prioritisation. Both sides, moreover, have profoundly different interests and expectations concerning certain aspects of the DCFTA and related measures.

Agriculture: Tariffs and Standards

Both sides still maintain heavy protection of their agricultural sectors: For Tunisia this applies especially to milk, meat, cereals and beverages, while the EU in particular protects southern European products such as olive oil, fruit and vegetables.

Exceptions are the decisive point, in the sense of excluding individual sensitive products from abolition of tariffs. The size of the list of exceptions and the length of the period granted for dismantling tariffs will be crucial for Tunisia. In 2016 the EU originally proposed ten years. Tunis regards this as much too short, as EU imports would very quickly present stiff competition in its markets. Finally, modalities for imposing protective tariffs in response to crisis will also need to be negotiated.

EU tariff quotas are currently principally relevant for olive oil. Tunisia is the world's fifth-largest exporter, after southern European EU member states, and olive oil accounts for 40 percent of its total agricultural exports. But for most categories of olive oil the amount that can be imported into the EU tariff-free is restricted by quotas. Following the 2015 terrorist attacks and the associated slump in tourism, Brussels twice increased Tunisia's quota against considerable resistance from southern European producers. The EU has promised another increase for 2018 on condition that Tunisia agrees to open its markets for selected agricultural products of its own choosing ("mini trade package"). To date Tunis has rejected this, even though it favours a sectoral agreement — applying only to goods — over a comprehensive one. In fact a "mini trade package" would be a first step in that direction. Treated oil mainly does not currently benefit from tariff preferences.

Strongly fluctuating yields have sometimes left the existing quotas unused. On the other hand, after the record olive harvest of 2018 — more than double the previous year's — the entire export quota was already allocated by the beginning of the year. But Tunisian exporters can also export unlimited amounts of untreated olive oil to the EU tariff-free (outside the quota) if this is blended with oil produced in EU member states ("inward processing"). While this channel does generate export revenues for Tunisian producers, it cannot be communicated politically as a negotiating success. Additionally this oil cannot be labelled and marketed as originally "Tunisian" and export volumes are subject to unpredictable business decisions.

The *EU import regime for fresh fruit and vegetables* includes seasonal quotas to protect particular producers with higher tariffs during European harvest periods. A controversial "minimum import price" system also applies a tariff if the import price falls below a defined threshold; this systematically disadvantages low-cost suppliers like Tunisia. Concessions to Tunisia in this sector would require the EU to create compensatory mechanisms for its own producers, which are located mainly in southern member states.

Finally, *standards*, such as bacteriological thresholds, form a decisive obstacle to imports from Tunisia, especially for milk and meat products. Unlike with tariffs, bilateral agreements cannot grant more favourable arrangements on binding legal standards to particular trading partners: all refer to existing WTO standards. Private standards, such as those operated by food retailers, are more flexible — but not covered at all by trade agreements. They are more dynamic but as non-binding rules open room to improve terms for exporters. In fact private standards are often stricter and more demanding than their statutory counterparts. The same applies to legally defined but voluntary standards such as those for organic produce — which represents a fast-growing sector in Tunisia. While Tunisian producers are not required to observe all these standards, they are a precondition for operating in particular market segments.

Protected quality schemes like geographical indications (GIs) secure the marketing of particular products, and are normally codified in trade agreements; the EU has proposed a long list of its own GIs. Tunisian GIs can not only boost value creation but also make a broader contribution to rural development, potentially through linkage to tourism activities. Although the EU side has since 2016 repeatedly suggested that Tunisia make proposals on this issue, Tunis has not responded to date.

Regulation: Unclear Acquis Demands

In addition to product-specific standards, agreements within the neighbourhood framework (and with close EEA partners like Norway) require partners to adopt the EU's *acquis communautaire*. This goes beyond classical European import regulations, with which every third state exporting to the EU must comply anyway. Adopting the acquis means not only adopting all the EU's regulations, but also copying administrative structures and case law. That would, for example, require Tunisia to automatically apply future changes in EU food safety standards without any reopening of negotiations on standards within the DCFTA. Tunis — like Ukraine in its own earlier AA talks — criticises this as unacceptable in the absence of an accession perspective.

Nevertheless, adopting the acquis does offer advantages: it steps up the pressure to realise reforms in strategic food sectors that will ultimately promote the quality of production. This is important for all trade, not only with the EU but also with other partners.

But actually for exports neither the acquis nor complete harmonisation with EU standards is required: mutual recognition of production processes offers an alternative. In the manufacturing sector this has long been envisaged for Mediterranean partners: agreements on conformity assessment and acceptance of industrial products (ACAAs) seek to facilitate trade by recognising verification procedures. To date however only one such agreement has been concluded, with Israel.

Textiles: Level of Processing

One third of Tunisian manufacturing jobs are in the textiles sector. A division of labour with the EU emerged in the 1970s: exploiting lower wage costs, European fabrics are finished in Tunisia and reimported to the EU under European preferential tariffs. The AA secures broadly open access to the EU market for textiles, but with different tariffs depending on the degree of processing.

The current rules of origin within the AA may function as barriers to trade. Under the so-called "double transformation" rule, tariff exemptions apply only if two transformation steps have been completed, for example from yarn to fabric and from fabric to finished apparel. But in cases where Tunisia lacks the second processing industry a higher tariff will apply.

At the same time Tunisia is a signatory to the Pan-Euro-Med Convention (PEM), which permits the cross-border use of individual national tariff preferences in relation to inputs from a large region covering the EU and most of its neighbours ("diagonal cumulation"). This encourages the development of regional manufacturing and value chains.

Tunisian textile processors argue for a "single transformation" rule, which would be a better fit for their current processing structure. That would also permit very cheap precursors from countries outside the PEM group — for example from Asia — to be processed without losing tariff preferences. However, such a simplification would override the PEM principle of uniform rules for all signatories and could encourage other countries to seek exceptions too. It would also become even more difficult to differentiate this from the policy the EU pursues — with its Economic Partnership Agreements (EPAs) and the "everything but arms" regime — towards developing countries, which so far profit exclusively from the "single transformation" rule.

Services: Labour Migration

To date the EU has proposed a mixed approach: in principle, a positive list grants free market access in designated service sectors, while a negative list protects establishments. The possibility of temporary migration of workers to provide services in the partner country ("Mode 4" in the services chapter) is especially important for Tunisia. While this channel could in principle be used to shape labour migration, the EU's drafts so far lack specific sectoral proposals.

Options for working in the IT and communications sectors appear especially important to Tunisia. But such labour migration would require visa and work permit arrangements that lie beyond the scope of the trade agreement. Those rules are still defined by the individual EU member states, and across all national regimes the maximum working stay is restricted to six months. Entrenched differences between national migration strategies prevent the EU from making concessions on Mode 4.

Investment: Access Only

The DCFTA only addresses investor access to the Tunisian market. The protection of investments is regulated in bilateral investment treaties (BITs), which nineteen EU member states have concluded with Tunisia. Alongside the existing access rules these also include the much-criticised investor-state dispute settlement procedures under which businesses can sue states for compensation for expropriation. Tunisian critics continue to insist mistakenly that the DCFTA would create such a mechanism.

Gentle Acceleration

Little progress is likely to be possible until after Tunisia's presidential and parliamentary elections, which are scheduled for late 2019. But it is already time to prepare the ground for productive negotiations from 2020.

The EU has been supporting the Tunisian side in strengthening its negotiating capacity, coordination and communication, and has made more concessions than would normally be expected. Here the EU risks falling for the illusion that an agreement can be negotiated in the absence of political will on the other side. By doing Tunisia's work for it, Brussels also risks the DCFTA being perceived as an externally imposed neo-colonial project lacking in ownership and legitimacy. This would interfere with sustainable implementation of any agreement and risk the Tunisian public taking a negative view of relations with the EU for many years to come.

This leaves the EU attempting a balancing act, helping Tunis to shape an agreement without patronising its partner. It must also pressure Tunis to tackle reforms, while avoiding provoking internal conflict. The way out of these dilemmas is to disseminate knowledge in Tunisia, build capacities and generate a broad consensus over a DCFTA. A series of potential concrete starting points exist for building confidence on the Tunisian side:

Agricultural Sector: Use EU Offers

The EU could extend the implementation period, for example to the twenty-five years applied in most EPAs. In fact the Commission has even suggested that Tunisia could set its own timeframe. Tunis should make use of that opportunity. The proportion of exceptions from liberalisation could also be increased; in EPAs it is up to 25 percent.

The EU is also prepared to negotiate about increasing the quota for untreated olive oil under certain conditions. Such an offer was intended as an incentive for a "mini trade package" under which Tunisia would reciprocally open its markets to selected European agricultural products. Given that the autumn olive harvest season has just started, it would be reasonable to repeat this incentive for next year. But Tunisia could misconstrue it as blackmail. It should therefore be stressed that this basically corresponds to the Tunisians' own proposal of a sectoral agreement. The EU should present the "mini trade package" as a step in precisely that direction, to gather initial experience with a view to a possible sectoral agreement. Ideally this would create the trust required for more ambitious steps. Additionally, new preferences for categories of treated oil so far excluded could be offered as a step towards the general duty-free access envisaged under a final agreement.

European concessions on fruit and vegetables are less likely in view of the existing competition situation. Yet the EU-Morocco Association Agreement, in which the EU granted Rabat greater market access than Tunis, demonstrates that leeway does exist.

Here the EU first needs to find an internal compensatory mechanism for its own producers, possibly in the context of the upcoming reform of the CAP. Tunisia could also push for a reduction in the tariff applied in the minimum import price system. It would be more consistent to completely abolish the system, which is ultimately a hold-over from the strongly protective variable tariffs that were widely used in the past until they were largely abolished by the WTO's 1995 Uruguay Round.

Tunisian GIs can encourage production and marketing of the kind of high-quality, high-value products that generate employment and drive development. Definitions are thus a matter of urgency, using a dynamic list as is usual in EU trade agreements. Possible products could include olive oil and dates produced in certain regions or using particular traditional methods. Establishing this sphere of production will require financial support from the EU to ensure adequate quality, good marketing structures and integration into broader rural development programmes.

The EU should also promote Tunisia's ability to implement standards. And Tunisia should certainly also harness voluntary and private standards to incentivise exploitation of the full market potential of higher-value products. The EU has already offered a range of support including aid for trade measures like professionalising test laboratories. The German Import Promotion Desk also offers targeted assistance to increase agricultural exports to the EU. But Tunisia should conduct its own analyses of support needs and prioritisation. In this, ecological standards must also be considered, as for instance better market access for olive oil might lead to an expansion of olive plantations, in turn increasing water and soil stress. Ecological regulation and labour rights will be covered by the agreement's chapter on sustainability. Even if the chapter's enforceability is limited, the ecological risks should be seen as a further argument to privilege quality and value over pure quantity.

Regulations: Clarity Essential

The term "acquis" triggers Tunisian fears and is a source of misunderstandings. It is therefore helpful to define more closely what "selective adoption" means and to help to enable Tunisia to make a choice. Above all the EU should strengthen its support for the mutual recognition approach — as pursued under the ACAAs — even if this is likely to be a longer-term affair in the food sector.

Textiles: Use Time-Limited Compromise

It is difficult for the EU to switch to the single-transformation rules of origin as applied to developing countries, because this could spill over to other PEM countries and also erode positioning vis-à-vis the EPA states. But Tunisia is also blocking the current revision of the PEM arrangement, which seeks to expand flexibility for easing tariffs on textiles outside the classical clothing sector (such as sheathing for gardening equipment). Here the EU could make a time-limited offer to enable progress to be made both in PEM and in the DCFTA talks. At the same time it should be emphasised that Tunisia certainly profits from the current two-transformation arrangement, which can promote higher-value production. The establishment of such a production structure should also be supported by additional EU funding.

Investment Protection: Benefit from New Model

EU-wide investment protection is recently often negotiated jointly with trade rules in agreements, however will be concluded in a separate agreement due to internal ratification requirements. Tunis can benefit from the improvements in the new EU-model as otherwise the old and limited member state BITs continue to apply to Tunisia. These potentially block future legal improvements envisaged through further domestic reforms, as such changes could lead to compensation claims on grounds of expropriation. The new EU approach leaves more scope for such legislative changes. Especially in relation to the search for more investment, Tunisia should seek corresponding rules in an extra agreement.

Services: Communicate the Red Line

A services liberalisation permitting labour migration is currently unrealistic for the EU, given the level of disagreement between member states over migration and refugee issues. This should be communicated clearly in order to avoid raising misplaced expectations.

Improve Impact Analyses

Tunisia insists — in part on account of pressure from its civil society — on an impact assessment funded independently of the EU before continuing negotiations, primarily to evaluate the existing association agreement. Even if the EU might regard this as a delaying tactic, it touches on what was until recently a deficit in the EU's own analysis exercises: Its impact assessments were conducted long before the agreement was even concluded, still less implemented. Although the EU did institute annual impact reporting in 2017, this could still be more systematically linked to revision clauses providing for amendments and improvements.

Use Cross-Learning

Similar difficulties to those experienced with this DCFTA arose in comparable negotiations with the EU's eastern neighbours, for example over the question of what adopting the acquis actually means. Advice from actors with experience in negotiating with the EU would therefore be desirable. An exchange of this nature — including lead negotiators — was arranged by the German-Tunisian Chamber of Industry and Commerce and the Bertelsmann Stiftung in June 2018 in Tunis — and could be institutionalised.

African Free Trade Area Must Not Form Obstacle

Nearly fifty states — including Tunisia — have so far signed an agreement to create an African Continental Free Trade Area. In the longer term they will have to merge and consolidate their regional EPAs, bilateral Association Agreements and any DCFTAs concluded by then. That perspective needs to be taken into account already. Over and above individual needs, unifying elements such as harmonised rules of origin are important. Despite the challenges presented by the ambitious long term objective of a pan-African free trade area it should not be abused to block any earlier regional and bilateral trade initiatives; instead the latter should be conceived as preparatory steps.

On the European side the upcoming elections to the European Parliament and the subsequent appointment of a new Commission mitigate against a rapid conclusion. This means it is also unclear what position the EU will adopt on the future design of the DCFTAs.

Neither side has an interest in retaining the outdated status quo. Solutions can be found for all the outlined differences — provided Tunis demonstrates the necessary political will and the EU offers judicious support. However, even a perfect trade agreement will not produce the desired positive economic effects unless it is supported by the broader political, administrative and legal structures in Tunisia. Weaknesses in governance and the business climate remain overarching challenges the EU needs to bear in mind in its negotiations with Tunisia.

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