BULLETIN

ECIPE Bulletin No. 03/2012

Trade and Development at the crossroads?

By Roderick Abbott, a Senior Advisor at ECIPE (roderick.abbott@ecipe.org)

This paper seeks to look at EU Trade and Development policies which seem to be at a crucial moment - crucial in the sense of the point at which the two policies meet and cross each other. The two ought to go in tandem, hand in hand; but in reality there are increasingly obstacles at the crossroads. The paper starts with a short historical overview of the basic philosophy, and then examines recent developments and where this may lead.

The policy balance between Trade and Development is a very old debate, going back at least as far as the creation of UNCTAD in 1964. It has been the subject of many prescriptions by development experts: 'Trade, not Aid' was the main slogan in the 1960s, when commodity exports and import substitution were the preferred policy goals for LDCs; later it came to be realised that trade could not achieve the goal s of economic growth and more rapid development on its own and aid was still needed (Trade and Aid); later still aid was found to be dispersed across too many projects with broader societal goals and the impact on trade and capacity to trade was limited. The wheel has now turned full circle with 'Aid 4 Trade': trade will not grow unless the infrastructure and administrative environment is improved.

From the start it has been the conventional wisdom that preferential tariff treatment for developing countries is the best solution and provides the incentive to increase their exports. This was encapsulated in the GSP schemes introduced by major OECD countries from 1970 onwards, and imitated later by a scheme for negotiation of preferential tariffs among developing countries. But it has also been a story of unintended consequences; export growth tended to be focussed on a few countries, while the trade of the less competitive ones stagnated, and preference utilisation was often less than optimal. Successive multilateral trade rounds (Kennedy, Tokyo, Uruguay) also significantly reduced the value of preferential treatment – at least in the case of the major import markets.

Graduation – when a country exports more than a certain level of all GSP imports for a given product it would lose preference for that product – was the principal way to address the first of these issues. It was, however, at best only a partial solution, since the capacity to increase exports of other countries was lacking and switching production and investments, where feasible, also takes time. The second issue, utilisation, has to do with complexities within the systems – the issue of certificates of origin, rules of origin themselves – and in some cases with criteria of eligibility. Utilisation has remained sub-optimal, and as MFN tariffs have fallen, benefits have been eroded.

We should now look at recent events within the EU. First, in mid-2011, was the Commission's proposal for the renewal of GSP <Com (2011) 241>. This was a periodic event which recurs roughly every ten years, when the system as a whole comes up for review. The difference this time is that, after the entry into force of Lisbon Treaty, the EP now has co-decision powers with the Council to debate and amend Commission proposals before they are enacted. How would this affect future policy?

Second, the Commission has issued (in January) a paper on Trade, Growth and Development which surveys in a broader framework the EU record of providing assistance to developing countries <Com (2012) 22 >. Why this has been issued at this moment is not entirely clear, there was no particular timetable reason for a further review. The paper updates earlier reviews in 2002 and 2010, and was supplemented by more specific surveys - 'An agenda for change', and 'Human Rights and Democracy in external action'[1].

This Communication focuses on the changing world economic landscape. Factors such as low (or lower) levels of tariff and the reshaping of world trade patterns due to the growth of global supply chains are cited. Radical changes in the

[1] COM (2011) 637, in October and COM (2011) 886 in December.

developing countries themselves have taken place, with some - China, India and Brazil – now advanced to the level of leading world economies. "The notion of developing countries as a [homogeneous] group is becoming almost irrelevant".

In fact the paper may represent an effort to create a counterpoint to the negotiations with Canada and Japan, and in prospect with the USA - a recognition that a balanced approach to EU trade and development policies needs to be restated. The latter part of the paper contains some broad suggestions about how policy should evolve over the next decade, based upon three basic development regimes: the general approach, in GSP and GSP +; the Everything But Arms approach for least developed countries, and more specific regional integration initiatives such as the long-standing ACP agreements and new free trade areas.

Against this background of major changes it is odd that the conclusion is that no radical change will be needed. The principal tweak proposed to current policy is in fact a variant of the old graduation model, with preferential treatment to be limited in future to "those who need it most", as measured by the World Bank – that is, only to those countries falling below the higher and upper-middle income categories. The other elements such as GSP + and LDC special treatment will be largely unchanged.

In practice, this raises old familiar issues of effectiveness: will the results conform to the expectation? We are told that 40% of all GSP imports in the current system come from countries that will now be excluded: removing benefits for them will in theory help others, but will these others be able to fill the gap? Where they do not have the products (or in some cases the infrastructure) to increase exports, new investment will be needed; and this has always been the problem - the spotlight shifts towards the governance of the country and the policy choices that it makes.

One uneven outcome in the new system will be the differences that result from the application of the GDP criteria, which will distort competition. China, which is #2 or 3 in world trade in both goods and services, would remain inside GSP (GDP per head level is still low); but some other emerging economies such as Brazil and South Africa would not. India, rising up the table in world trade, would also remain inside the system, as would Indonesia; while Malaysia – a regional competitor – would not. However, in contradiction to this, the major exports of China especially would likely continue to be graduated out of preferences in practice.

In a broader perspective, the current policy for regional or bilateral free trade agreements will more and more come into conflict with more traditional policy approaches such as tariff preferences. These benefits for one country (eg Pakistan) would be eroded where free trade treatment is granted to another developing partner (eg India); and this would be even more remarkable if the free trade partner would otherwise be considered as having in effect already emerged and at an advanced stage of development (eg G20 membership). While free trade benefits are reciprocal, not unilateral, the fact remains that the concept of helping those in most need would be undermined.

Under such conditions, general preferences no longer appear to be an essential instrument in the development policy toolbox. Eroded on all sides by MFN cuts, by special selective schemes and by free trade areas, they are losing their attractiveness and may gradually disappear. We have to look for another way forward.