Strengthening the Global Trade Architecture for Economic Development: An Agenda for Action

An impasse looms in the run up to Hong Kong

This December, trade ministers will meet in Hong Kong to assess the progress made in implementing the mandate they gave to their negotiators in Doha, Qatar, at the end of 2001. This mandate called for the pursuit of multilateral negotiations to significantly reduce the use of trade-distorting policies and to bolster the development relevance of the World Trade Organisation. The Round has been dubbed the Doha *Development* Agenda, and the challenge confronting WTO members is to agree to a deal that delivers on development. Thus far they have fallen well short, and increasingly intractable negotiations could lead to an impasse in the months ahead.

Averting this impasse is vitally important. As argued in the Millennium taskforce report on trade, achieving an ambitious outcome—through deep liberalisation of access to markets, abolishing all tariff peaks, greatly lowering agricultural protection, and making substantial commitments on freer trade in services—will generate global gains that far exceed the losses. By enhancing trade opportunities for competitive suppliers and reducing prices for consumers everywhere, it will advance global development prospects and help to achieve the Millennium Development Goals. Deep multilateral liberalisation would also reduce discrimination in trade, which is becoming increasingly prevalent with the ever-expanding number of preferential trading arrangements (Sutherland et al., 2004).

The direct incentives for individual nation states are to pursue discriminatory access to markets, to the detriment of both global welfare and the interests of many poor households in developing countries. The WTO is the only instrument that can be used to deliver the global public good of non-discriminatory multilateral trade liberalisation.

Exploring options that could help enhance the development dimension of the WTO was the objective of a recent research project. This briefing paper summarises the major findings and recommendations from the project.[1]

A three-part approach to break the deadlock

WTO members can promote development through action on three fronts:

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[1] The project, Development and the Global Trade Architecture, was chaired by Ernesto Zedillo and supported by the Department for International Development, United Kingdom. Members of the Steering Committee and the research project comprised Simon Evenett, Joseph Francois, Eleanor Fuller, Gerry Helleiner, Bernard Hoekman, Hans Peter Lankes, Ricardo Melendez-Ortiz, Patrick Messerlin, Dominique Njinkeu, Howard Pack, Sheila Page, Susan Prowse, Jayanta Roy, Kamal Saggi, Jose Manuel Salazar, Sok Siphana, and L. Alan Winters. All members of this group participated in a strictly personal capacity. The project builds on the report of the UN Millennium Taskforce on trade (UN, 2005). A more comprehensive synthesis of the project research results and all background papers can be found at <http://www.ycsg.yale.edu>.

- *Agreeing to significant multilateral liberalisation of access to markets.* To achieve an ambitious outcome from the Doha Round requires explicit acknowledgment that there will be losers and that the benefits of reform will be distributed unequally across countries. To deliver the multilateral liberalisation that will benefit the world as a whole, individual countries need their own mechanisms to assist groups who will lose. The multilateral trading system should enable these adjustments. In the case of losses from the erosion of trade preferences, preference-granting countries should take bilateral actions to offset these losses.
- *Supporting the poorest countries to put in place measures to enhance competitiveness and productivity, and to address adjustment costs.* A significant increase in 'aid for trade'—that is, development assistance dedicated to increasing the recipient country's capacity for trade—would help to ensure that more countries benefit from trade opportunities, including those that derive from unilateral reforms.
- *Adopting an approach to negotiations that helps governments of developing countries to put in place the policies and undertake the investments they need to benefit from implementation of WTO rules.* This means shifting away from the current approach of defining 'special and differential treatment' for developing countries purely in terms of exceptions from WTO rules—which in our view has been ineffective in promoting development.

To date, progress on all three fronts has been disappointing. G-8 leaders have made a clear commitment to provide additional 'aid for trade', but this stance has emerged from the work of independent commissions (UN Millennium Trade Taskforce, 2005; Commission for Africa, 2005) and been driven by the international development and finance community. In the Doha deliberations, by contrast, defensive vested interests have dominated the negotiating positions of all WTO members, rich and poor. Participants have made too little effort to go beyond traditional negotiating modalities and approaches, as can be seen from the expanded efforts to negotiate additional preferential trade arrangements.

As a result, despite three years of multilateral negotiations, development objectives have yet to be seriously addressed.

Movement to reform trade-distorting agricultural policies has been limited, and those policies that cause the largest global distortions have yet to be put on the negotiating table in a serious manner. The effort being made to obtain a commitment to gradually abolish export subsidies is important. But it needs to be complemented by an equal ambition to lower border barriers to trade. Here the approach thus far adopted by protectionist interests in both the North and South looks unlikely to produce much effective liberalisation. A major example is the desire to exclude 'sensitive' products, which are often the goods that are the most highly protected.

Services are a major area of negotiation with large potential positive impacts on development, but here, too, not much ambition for change can yet be seen. For many developing countries, obtaining better access for their service suppliers through temporary movement of providers (migration) could make a big difference, as could liberalisation commitments by developing countries themselves. Thus far, however, offers on both sides have been limited.

For access to non-agricultural markets, the proposed negotiation modalities have great potential to lower the highest rates of protection the most, including crucial tariff peaks on textiles and other tariff peaks in the OECD, and the higher average tariff barriers in major developing countries. But here, too, little progress has been made.

Recognising political constraints is imperative

Not all groups and individuals will gain from global trade reforms. Clearly, if everyone stood to gain from them, the reforms on the Doha negotiating agenda would have been adopted years ago. In practice their effective and credible pursuit requires leadership in both the North and the South. This is a challenge on the doorstep of all governments, not just those of OECD countries.

For affected producers and workers there is nothing special about the effects of trade policy reforms, in the sense that changes in technology and consumer tastes, to give just two examples, impose very similar costs or gains. But because changes in policy entail clear government decisions, the projected costs of adjusting to trade policy can impede the realisation of a more liberal and open trade regime.

To achieve an ambitious round of trade liberalisation to benefit both developing and high-income countries, honesty is essential: domestic adjustment costs need to be openly recognised and explicitly addressed. The means to do this can easily be mobilised, given that an ambitious market access outcome will generate global gains that far exceed the losses. Mechanisms are needed that redistribute part of the gains to those groups that will lose.

Grand bargains are still possible … but need to go beyond the WTO

Sometimes the reason for lack of progress on market access is seen to be the lack of ‘enough on the table’ to interest exporters. There is some truth to this view. While for large countries there is more than enough on the table to negotiate—a potential ‘grand bargain’ clearly exists in the area of market access—the potential benefits are limited for many smaller and poorer countries that confront the potential loss of preferential access to major markets.

Large emerging market countries maintain much higher tariffs and other barriers to trade than do OECD countries. By reducing these barriers they will benefit OECD exporters and bolster South-South trade. This prospect should help mobilise some of the political support needed in the OECD to implement reforms. For these emerging market countries, then, the problem is not the agenda. It is that freeing trade is costly for those groups who currently benefit from trade protection.

For many smaller and poorer countries, too, potential adjustment costs are of concern. But a more critical problem is that they lack the international competitiveness and supply capacity with which to benefit from a freer global trade regime. This is one reason why it is important to complement a focus on an ambitious Doha outcome with a concerted effort to enhance their ability to exploit trade opportunities and address concerns relating to their capacity to manage the process of liberalization.

Adjustment costs in developing countries are an inevitable outcome of an ambitious Doha Round. The more ambitious their reforms, the greater the medium-term benefits for incomes, but the greater, too, are the short-term adjustment costs, including in the area of fiscal policy, in response to reduced trade tax revenues. Some developing countries may stand to lose from trade reforms that will enhance global welfare—in particular from deep non-discriminatory trade liberalisation that will erode the value of the trade preferences they receive, or increase the import prices they pay for some staples. For poor countries that have not diversified their economies and depend on preferential access to major markets, there may be little immediate gain, especially those that do not undertake own reforms in trade and domestic economic adjustments to improve their competitiveness.

Four areas for action

To carry out the promise of the so-called 'Development Round', action is needed in four specific areas, outlined in turn in what follows:

- explicitly addressing losses from the erosion of preferences, through financial transfers from preference-granting countries;
- significantly expanding dedicated grant-based funding, through an 'aid-for-trade' integration mechanism, to identify and address trade capacity constraints and improve competitiveness on a country-by-country basis;
- place expanded emphasis upon development goals and impacts of trade policies in developing countries rather than purely upon exemptions from WTO rules; and
- a concerted global effort to improve transparency through better data collection, analysis of the impacts of trade-related policies, and dissemination of relevant knowledge.

1. Preference erosion

Concerns about the erosion of trade preferences need to be addressed explicitly, for several reasons. Non-discriminatory trade liberalisation by WTO members has the characteristics of a global public good: everyone benefits in the medium term from the increase in efficiency that results from the removal of global distortions in prices, which encourages countries to produce according to their comparative advantage. An implication is that the lessening of trade preferences associated with a Doha-based global liberalisation augments this public good. This is not to deny that preferences are legitimate or to say that they do not benefit recipients. But preferences are distortionary and governments continue to seek more of them.

Research suggests that the global losses from the potential erosion of preferences will be limited when compared with the expected global net gains of an ambitious freeing of trade. But the issue of losses is a significant one for the affected countries, and needs to be addressed from a global perspective, because the countries concerned may otherwise block progress in the Doha Round. Just as important from a political perspective is that the preference erosion issue offers protectionist interests in the OECD an opportunity to argue that status quo policies need to be kept in place to assist the preferred developing countries. Concerns over preference erosion may well undermine efforts at liberalising market access across the board.

Seeking to address preference erosion concerns *within* the trade negotiating agenda is likely to be counterproductive. It will probably result in more rather than less discrimination between developing countries—in effect robbing Peter to pay Paul. (For example, giving a small country preferential market access for its service exports will prejudice the ability of larger exporters, not so favoured, to compete in that market, raising prices for consumers and making everyone but the preferred country worse off.)

A better approach is to use non-trade instruments, in particular bilateral development assistance, to compensate losers for the erosion of preferences. The main negative impact of the erosion of preferences follows from the removal of specific trade barriers in specific OECD countries. This suggests that the erosion problem is a matter to be addressed by preference-giving countries. The original intention of preferences was not to transfer resources directly but rather to help in the development of exports. Aid can help attain that goal. Many of the poorest countries of today have not managed to diversify and expand exports even *with* the preferences they receive, because they lack the necessary supply capacity or are not competitive. This is also a reason why granting more preferences to the poorest countries—for example, for access to large emerging markets—is unlikely to yield much benefit.

Thus, preference erosion should be taken seriously, and 'compensation' for associated losses should be made outside the WTO—with the goal being to reduce the prevalence of trade-distorting instruments. Specifically, a commitment could be sought through which preference-giving countries/trading blocs transfer to each recipient the assessed value of their current preference programs in the form of a financial grant. The political rationale for this is that it will help support a more ambitious Doha outcome, benefiting all WTO members. Such bilateral compensation will by necessity target only those countries that have successfully exploited preferential access opportunities. Countries that have proved unable to benefit much from such programs should be assisted through expanded aid for trade.

2. Dedicated funding for aid for trade: a multilateral trade integration program

An ambitious freeing of market access will benefit developing countries as a group. However, some countries—especially the poorest—may not gain much even from an ambitious round, given the discouraging environments they provide for investment and business.

To enhance the benefits of global market access commitments will require additional dedicated resources with which to provide expanded aid for trade. An important first step in this direction is the recent commitment by the G-8 Heads of Government to increase aid to developing countries to build physical, human, and institutional capacity to trade, and to grant additional support for trade capacity building, to take advantage of the new opportunities to trade that will result from a positive conclusion of the Doha Round.[2] In absolute terms, multilateral trade liberalisation will yield greater economic benefits to high-income countries than to developing countries. Trade is a good use of some of the additional aid that OECD countries have agreed to provide—in effect redistributing an increment of the gains from liberalisation to help developing countries bolster their trade capacity.

To undertake trade reform and participate effectively in the global trading system, poorer countries face a gamut of challenges. They must pay the costs of adjustment before they see offsetting economic activities emerge. Many of the poorest developing

[2] See G-8 Declaration, Gleneagles, 2005, Africa text: paragraph 22 (a).

countries are ill equipped to take full advantage of trade opportunities. Improved market access without the ability to supply export markets competitively is not much use. Similarly, to gain from liberalising their own trade policies developing countries need an environment that allows mobility of labour and capital and facilitates investment in new sectors of activity—requiring, among other factors, an efficient financial system and good transport/logistics services. Countries that depend heavily on tariff revenues for fiscal resources will need to reform their tax systems. Inevitably most poor countries will need to make complementary reforms prior to—and in conjunction with—trade reforms. Aid for trade can never substitute for progress on market access or unilateral domestic reform. But it can greatly increase the benefits of trade opportunities for many poor countries by supporting their own reforms and can help to deliver the global public good of substantially freer trade.

Though the modalities of how additional funding should be administered, allocated, and monitored will need to be resolved, the basic principles that should be satisfied by an aid-for-trade integration mechanism are simple: support should take the form of grants, be credible and predictable, cover more countries than just the least developed, be based on a process of identification of trade capacity needs that is truly country-driven and owned, and have its processes and outcomes independently monitored.

Particularly important is the credibility and predictability of funding. Previous 'best endeavour' promises to provide assistance for trade have not been realised. Making more promises provides little assurance to low-income countries that their concerns will be addressed. Experience demonstrates the need for a mechanism that provides dedicated funding to address the identified constraints on a nation's trade competitiveness and to help offset the adjustment costs of reform.

Although the earmarking of development assistance is generally not efficient, we support it in the case of the trade agenda on the basis of the global public good argument made earlier. Without such action an ambitious Doha outcome is much less likely. Our support for dedicated, additional funding for trade is not to deny in any way that support for trade competitiveness and integration should be aligned with country policies and programs. On the contrary. We therefore recommend that the funding commitment for dedicated trade assistance be time bound—to extend over the length of any implementation period agreed under a Doha agreement—and that a funding mechanism should be channelled through existing processes.

3. From exceptions for developing countries to helping meet development goals

One of the important questions facing policymakers in the Doha Round concerns the circumstances, if any, under which developing countries should be allowed to use trade policies to pursue development (for example by using import barriers to protect domestic industries). Our view is that the basic trade policy rules of the WTO make good sense for all countries, high-income and developing alike. However, these rules ignore the fact that governments may be forced to use trade policy because more efficient instruments are not available (for example, a country's weak tax base may preclude the government from using subsidies). Compliance with basic WTO rules is also more costly for low-income than for high-income WTO members, insofar as the negotiated rules reflect the status quo prevailing in industrialised countries.

Providing exemptions for the use of trade policies by developing countries—the traditional WTO approach and the focus of much of the Doha negotiations on special and differential treatment—will not always be the best way to help achieve development objectives. Instead of focusing exclusively on exemptions to allow the use of trade policy instruments, the trading system can be made more supportive of development by the provision of independent monitoring of the development impact of trade and trade-related policies, together with the proposed aid-for-trade integration mechanism. What is needed is to more actively assist developing countries to attain their trade-related objectives, and to move away from the exclusive reliance upon negotiating exceptions and exemptions for developing countries.

This more active approach does not imply ceasing to negotiate binding disciplines. Instead it would put the focus more strongly on a country's identification and pursuit of a national trade agenda and priorities and to link this to the proposed aid-for-trade integration program. The objective would be to reduce governments' perceived need to use costly trade policy tools, to place the implementation of WTO disciplines in a national context and to monitor the effects of trade and related policies.

Different, complementary options can be considered to operationalise this idea. The most limited is to build on the agreement that was reached in the area of trade facilitation, with implementation (enforcement) of negotiated disciplines being conditional on adequate assistance having been given by industrialised countries to developing countries. More ambitious is to establish a multilateral mechanism to help developing countries to pursue national objectives through instruments that do not distort trade. One specific proposal that would do this—but that does not have the support of all steering committee members—would be for WTO members to agree to a set of "core" disciplines that apply to *all* members, and allow developing countries to invoke a 'development defence' in disputes alleging violation of non-core rules. The longer summary of the results of the research papers expounds on these options in more detail.[3] Deciding on a specific approach will require deliberation by WTO members. Agreement to consider options that would move in this direction is one way in which the WTO can help achieve the goal of greater policy coherence for development.

4. A global program on policy transparency

Pursuing the development objective through multilateral trade policy reforms (market access) and addressing national trade priorities (trade capacity needs) requires information on prevailing policies. Detailed and timely data on policies and their impacts are needed to design liberalisation strategies, to determine the effects of national policies, and to monitor compliance with trade and aid commitments.

Such data are not readily available at present and are not collected and reported by the WTO or other international organizations on a comprehensive basis. Data on applied tariffs are poor, information on non-tariff policies (antidumping, safeguard actions, product standards), are poorer, and the available data on policies affecting services trade, investment, and the movement of people are even worse. Further, much of the data that are available are not in the public domain but restricted to governments.

[3] See at <http://www.ycsg.yale.edu>.

A concerted effort is required to collect such data and make them publicly available free of charge. Without such an effort, the effectiveness and feasibility of many of the proposals made previously would be much reduced as analysis and monitoring of impacts of policies is greatly impeded. How to proceed to collect such information is complex. We therefore propose that a group of experts be commissioned to develop a practical methodology for descriptive and monitoring purposes, to define what specific type of data should be collected, to determine the budgetary implications of sustaining a global effort to collect these and advise on the institutional preconditions that should be met to ensure comprehensiveness and free public access.

Conclusion

The group has found that there are immediate and practical ways for the Doha Round to deliver on its declared objectives and its promise to foster development. A commitment by all WTO members—North and South—to undertake far-reaching multilateral liberalisation of market access is the most direct way the WTO can promote development. The traditional mechanics of the WTO negotiating process are not generating the political support that is needed to implement liberalisation in sectors such as agriculture and services. While there is scope for a grand bargain to be made, achieving an ambitious outcome from the Doha Round requires a credible commitment to put in place alternative, non-trade-distorting instruments to assist groups who will lose from trade policy reforms that enhance global welfare. This need extends to developing countries that stand to lose the benefits of preferential access to major OECD markets, and it motivates our call for preference-granting countries to provide financial compensation for these losses. The rationale for compensating losers is not economic efficiency or social equity, but the recognition that compensation is a practical necessity to deliver the global public good of an ambitious Doha outcome.

Achieving improved non-discriminatory market access is necessary, but by no means sufficient, to bolster growth prospects in all developing countries. Many countries do not stand to benefit much from a Doha Round, whether ambitious or not. To enhance the benefits of trade for a larger group of countries requires expanded, dedicated funding for an aid-for-trade mechanism that provides predictable resources to address national competitiveness constraints, address regulatory weaknesses, and deal with adjustment costs—including assistance to help countries replace trade-distorting policies with alternative policy instruments that are less costly. In conjunction with a concerted global effort to improve availability and access to data on trade-related policies to allow better analysis and monitoring of the impacts of policies and policy reforms, the creation of a dedicated aid for trade mechanism would facilitate an ambitious outcome on market access, and provide tangible evidence that development objectives are being taken seriously.

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