CHAPTER 7

HOW TO INCREASE THE BENEFITS OF THE DOHA DEVELOPMENT ROUND FOR THE LEAST DEVELOPED COUNTRIES

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INTRODUCTION

Until the Uruguay Round in 1986-94, the interests of developing countries did not figure prominently in the series of trade negotiations undertaken under the General Agreement on Tariffs and Trade. The Uruguay Round Agreement contained provisions for special and differential treatment for developing countries. For example, the Agreement on Agriculture (AoA) provided an extended period for the implementation of agreed reductions in domestic support, export subsidies and tariffs for developing countries; the least developed countries (LDCs) were exempted from such reductions. Following the failure of the third WTO ministerial meeting in Seattle in 1999 the interests of developing countries were much more prominent at the meeting in Doha, Qatar in 2001. The Ministerial Declaration from that meeting that launched the current round of WTO negotiations contains no less than 24 references to developing countries, and 26 references to the least developed countries. The round has since come to be known as the Doha Development Round.

This paper assesses what can be done to increase the benefits for Least developed Countries (LDCs) from a new WTO agreement. To a large extent any assessment of the balance of advantages and disadvantages has to be conjectural at this stage; much of the detail remains to be determined. Only a framework for modalities was established at the negotiating session in Geneva in July 2004. Nevertheless, the content of that framework and its potential implications for LDCs are assessed. While much of the focus is on the implications of a new agreement for agriculture, because of the importance of that sector for LDCs, other areas of

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concern, such as tariffs on non-agricultural goods such as textiles and apparel, are noted.

THE TREATMENT OF DEVELOPING COUNTRIES IN THE GATT/WTO

Several developing countries were involved in the creation of the General Agreement on Tariffs and Trade (GATT) in 1947 – 12 of the original 23 contracting parties to the GATT would not have been classified as industrial countries at the time[1]. Roughly two thirds of the current 148 members of the WTO are identified as developing countries. The original treaty did not provide any special treatment for these countries. The fundamental principles of the GATT – non-discrimination through the application of the Most Favoured Nation (MFN) principle and equality of treatment with domestic products (national treatment) were supposed to apply to all signatories. However, in 1955 a revision of Article XVIII, dealing with government assistance to economic development, introduced some flexibility for those contracting parties "the economies of which can only support low standards of living and are in the early stages of development" in the use of quantitative restrictions to address balance of payments problems and in the use of tariffs to promote the development of a particular industry. Further changes were introduced in 1965 through Article XXXVI on trade and development. In that article the developed countries identify the reduction and elimination of barriers to trade for the products of developing countries as a high priority. The article also introduces the concept of non-reciprocity in trade negotiations between developed and developing countries, i.e., the extension of trade concessions by developed countries that are unmatched by concessions by developing countries. A subsequent decision in 1979 known as the 'Enabling Clause' solidified the concept of special and differential treatment and non-reciprocity in trade negotiations. It legitimized preferential tariff treatment for the exports of developing countries within the Generalized System of Preferences (GSP) and provided differential and more favourable treatment on provisions relating to non-tariff measures; it sanctioned regional or global arrangements for the reduction or elimination of tariffs among developing countries; and provided for special treatment for the least developed countries in the context of measures for developing countries as a whole[2]. Of the 50 countries currently identified by the United Nations as least developed countries, 32 are members of the WTO (Table 1), a further 8 are in the process of accession and 2 are WTO observers.

The Uruguay Round Agreement contains special measures that recognize the interests of developing countries. These relate to: 1. provisions that address the interests of developing and least developed countries in a general manner; 2. an easing of the rules or obligations to be met under the Agreement; 3. the provision of a longer time-frame for the implementation of commitments; and 4. technical assistance. In the Agreement, LDCs were required to make fewer commitments than other countries and WTO members were encouraged to use a fast track approach for the application of concessions on tariffs and non-tariff measures for imports of particular relevance to LDCs.

***Table 1**. Selected agricultural trade characteristics of LDCs*

Country *	WTO status	Share of ag. in GDP		Ratio of ag. trade to GDP	Leading ag. export	Share in total exports	Share of food imports in total imports
		percent		percent		percent	percent
		1998		1998	1997-99	1997-99	1997-99
Sao Tome	O	21		41	Cocoa beans	69	25
Malawi	M	36		36	Tobacco leaves	59	13
Kiribati	N	21		34	Copra	42	26
Mauritania	M	25		29	Cattle	4	78
Gambia	M	27		26	Groundnuts, shelled	20	37
Sierra Leone	M	44		23	na	na	86
Guinea-Bissau	M	62		23	Cashew nuts	48	22
Djibouti	M	4	a	22	Cattle	18	24
Lesotho	M	12		21	Wool	2	13
Yemen	A	18		19	Coffee, green	<1	30
Solomon Is.	M	na		19	Palm oil	10	11
Samoa	A	42	b	19	Copra	12	20
Vanuatu	A	25	a	18	Copra	43	12
Maldives	N	16		16	na	na	10
Mali	M	47		16	Cotton lint	30	10
Togo	M	42		15	Cotton lint	23	14
Cape Verde	A	12		15	Apples	1	24
Benin	M	39		14	Cotton lint	33	16
Niger	M	41		13	Cigarettes	9	24
Senegal	M	17		13	Groundnut oil	3	30
Burkina Faso	M	33		12	Cotton lint	39	14
Comoros	N	39		11	Vanilla	34	40
Ethiopia	A	50		11	Coffee, green	62	10
Burundi	M	54		10	Coffee, green	22	12
Chad	M	40		10	Cotton lint	37	9
Eritrea	N	17		10	Sesame seed	4	11
Bhutan	A	38		9	Oranges	4	9
Tanzania	M	46		9	Cashew nuts	16	16
Haiti	M	30		9	Coffee, green	8	35
Uganda	M	45		9	Coffee, green	54	11

Table 1 (cont)

Table 1 (cont)

Country *	WTO status	Share of ag. in GDP	Ratio of ag. trade to GDP	Leading ag. export	Share in total exports	Share of food imports in total imports
		percent	percent		percent	percent
Zambia	M	17	9	Sugar	2	17
Sudan	A	39	8	Sesame seed	13	12
Centr. Afr. Rep.	M	53	7	Cotton lint	11	15
Rwanda	M	47	7	Coffee, green	43	30
Angola	M	12	6	Coffee, green	<1	15
Eq. Guinea	O	22	6	Cocoa beans	2	23
Cambodia	M	51	5	Rubber	9	27
Madagascar	M	31	5	Coffee, green	12	15
Laos	A	53	4	Coffee, green	4	3
Congo, D.R.	M	58 a	4	Coffee, green	10	38
Nepal	M	41	4	Wheat flour	5	7
Bangladesh	M	22	3	Jute	2	18
Afghanistan	N	na	na	Skins (goats)	14	18
Liberia	N	na	na	Rubber	9	14
Myanmar	M	53	na	Beans, dry	13	7
Somalia	N	65	na	Cotton lint	23	50
Timor	N	na	na	na	na	na
Tuvalu	N	na	na	na	na	14

* Ordered on the basis of the ratio of agricultural trade to GDP (where data exist).

M = member; A = in process of accession; O = observer; N = non-member

a = 1997; b = 1993; na = not available

Sources: WTO website and FAO (2002).

The AoA, which represented the first serious attempt to liberalize agricultural trade within the framework of the GATT, contains provisions on market access, export subsidies and domestic support. Bound tariffs were established and reduced by an agreed percentage; imports of some products at lower rates of duty were managed though tariff-rate quotas (TRQs). The permitted value of export subsidies and the volume of subsidized exports were capped and reduced. Limitations were placed on the amount of trade-distorting (Amber Box) domestic support through the use of the concept of the aggregate measure of support (AMS) and the maximum permissible amount of that support was reduced. For developing countries, the required reduction in tariffs and in Amber Box support was lower than for developed countries, and the implementation period was longer (10 years rather than 6 years). Developing countries were granted a higher level for Amber Box support that was exempted from the AMS reduction commitment – the so-called *de minimis* level. This was set at 10% of the relevant value of production as opposed to 5% for developed countries (i.e., the value of production of an individual commodity for the commodity-specific *de minimis* and value of total production for the non-product-specific *de minimis*). Certain forms of domestic support that are part of development programs were also exempted from the reduction requirement. Most important, the LDCs were not required to make any commitments on market access, domestic support or export subsidies.

The Uruguay Round resulted in several other important agreements. From the perspective of the export interests of LDCs one of the more significant was the Agreement on Textiles and Clothing (ATC). Prior to that agreement, a substantial share of world trade in textiles and clothing was regulated by import quotas. Under the ATC quotas were gradually relaxed until their final elimination on January 1, 2005.

THE CURRENT TRADE LIBERALIZATION PROPOSALS

In launching the current round of international trade negotiations at the Doha meeting in November 2001, the WTO ministers declared “we shall continue to make positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development. In this context, enhanced market access, balanced rules, and well targeted, sustainably financed technical assistance and capacity-building programmes have important roles to play.” (WTO 2001, paragraph 2). The declaration also states “We recognize the particular vulnerability of the least developed countries and the special structural difficulties they face in the global economy. We are committed to addressing the marginalization of least developed countries in international trade and to improving their effective participation in the multilateral trading system.” (WTO 2001, paragraph 3).

Since the Doha meeting, it has proved difficult to reach agreement on the details of a package of trade reform measures, particularly for agricultural products. Following the failure of the following Ministerial meeting in Cancún in September 2003, a Framework Agreement for completing the negotiations was finally concluded in August 2004. According to the Ministerial declaration this agreement is intended to provide “the additional precision required at this stage of the negotiations and thus the basis for the negotiations of full modalities in the next phase” (WTO 2004, paragraph A-1).

The framework agreement on agriculture

The major elements of the Framework Agreement for agriculture address the three principal elements (pillars) of the Uruguay Round AoA: domestic support, export competition and market access. The principal components are:

Domestic support

- Substantial reductions in overall trade-distorting support (defined as the sum of the total AMS, *de minimis*, and Blue Box support[3]) with a strong element of harmonization to be applied by developed countries – higher levels of support will be subject to deeper cuts through a tiered approach; product-specific aggregate measure of support (AMS) will be capped at average levels to be agreed.
- Reductions in the final bound total AMS and *de minimis* levels, a capping of payments at 5% of the total value of production with respect to an agreed historical period, and a capping of the AMS for individual commodities.
- The criteria for Green Box support (identified as minimally production and trade distorting) are to be reviewed and clarified to ensure that payments have no, or minimal, trade distorting or production effects; there is to be improved monitoring and surveillance of such payments.

Export competition

- Elimination of export subsidies.
- Elimination of export credits, credit guarantees or insurance programs with repayment periods beyond 180 days; disciplines to be imposed on shorter-term credits.
- Elimination of trade-distorting practices of exporting state trading entities (STEs).
- Disciplines to be imposed on certain types of food aid with the aim of preventing the displacement of commercial sales.
- These measures to be implemented in a phased manner by an agreed end date.

Market access

- Reductions in tariffs from bound rates using a tiered formula that will produce deeper cuts in higher tariffs.
- A ‘substantial improvement’ in market access for each product to be achieved through combinations of MFN commitments on TRQs (increased quota levels) and tariff reductions.
- Members may designate some products as ‘sensitive products’ with a given number of tariff lines (to be negotiated) that will be subject to less liberalization.

The Framework Agreement states that “special and differential treatment for developing countries will be an integral part of all elements of the negotiation, including the tariff reduction formula, the number and treatment of sensitive products, expansion of tariff rate quotas, and implementation period” (WTO 2004, paragraph 39). Specific provisions for developing countries are:

- Domestic support – longer implementation periods and lower reduction coefficients for trade distorting domestic support. Exemption from reductions for countries that allocate ‘almost all’ *de minimis* support to subsistence and resource-poor farmers.

- Export competition – longer implementation periods for the gradual elimination of all forms of export subsidies and differential treatment for least developed and net food-importing countries with respect to disciplines on export credits, guarantees and insurance programs. Ad hoc financing arrangement may be agreed in exceptional circumstances to meet import needs. STEs in developing countries that preserve domestic price stability and food security are to receive special consideration in retaining their monopoly status.
- Market access – smaller tariff reductions or tariff quota expansion commitments than for developed countries. Flexible treatment for products designated as ‘special products’. Creation of a special safeguard (SSG) mechanism for developing countries to address surges in imports. Full implementation of the commitment to liberalize trade in tropical products. The issue of tariff preference erosion ‘will be addressed’.

The LDCs will have access to all the provisions applicable to other developing countries. In addition, they will not be required to make any reduction commitments.

Cotton

Cotton is an important commodity for a number of LDCs; cotton policies in developed countries proved to be a contentious issue at the Cancún ministerial meeting. In the run up to the meeting Benin, Burkina Faso, Chad and Mali launched a joint ‘cotton initiative’ to address the impact of subsidies provided to cotton producers in developed countries. The WTO held a workshop on cotton in Benin in March 2004 to address the development assistance aspects. As a result of these efforts, the Doha work program document includes a specific section on cotton that “reaffirms the importance of the Sectoral Initative on Cotton” (WTO 2004, paragraph 1). That section indicates that the trade-related aspects of the Initiative will be addressed in the agricultural negotiations. It should also be noted that Brazil brought a successful case against U.S. cotton policies under the WTO dispute settlement procedure in 2004. As a result of the judgment in that case, the United States may make changes in a range of measures that were judged to have depressed world cotton prices.

Other provisions

Developing countries will be affected by other elements of a final agreement; perhaps the most significant will be the final package of tariff reductions for non-agricultural products. The framework for market access for such products involves the application of a non-linear formula for the reduction or elimination of tariff peaks, high tariffs, and tariff escalation. These issues are of particular relevance to some commodities of particular relevance to LDCs, such as textiles (see below). There will be an attempt to increase the proportion of tariffs that are bound, to convert specific tariffs to bound *ad valorem* equivalents, and to eliminate low tariffs. As for agriculture, developing countries will be given greater flexibility in making tariff cuts and will have a longer implementation period.

LDCs will not be required to apply the agreed formula for tariff reductions but will be expected to increase the proportion of their tariffs that are bound. In addition, the agreement calls upon “developed country participants and other participants who so decide, to grant on an autonomous basis duty-free and quota-free access for non-agricultural products originating from least developed countries” by a year to be determined (WTO 2004, Annex B, paragraph 10).

Other aspects of importance to developing countries, such as capacity constraints, the problems faced by small, vulnerable economies and the need for technical assistance, are mentioned. The particular interests of LDCs are noted specifically with respect to trade in services and trade facilitation.

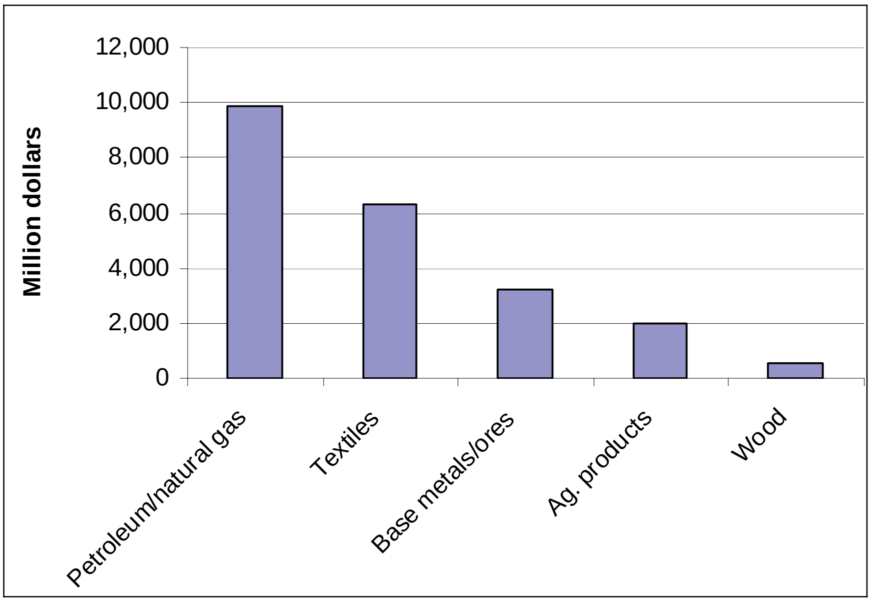
POTENTIAL IMPLICATIONS OF THE PROPOSALS FOR LDCs

It seems clear from the WTO framework document that LDCs will not be asked to make any significant concessions with respect to tariffs on non-agricultural products or tariffs and other measures applied to agricultural products in the current round of negotiations. There appears to be a willingness to continue to expand the trade-related technical assistance provided to developing countries, particularly for the LDCs[4].

Trade theorists generally point to the global benefits that can be realized from trade liberalization, resulting from increased consumer choice and enhanced production efficiency through specialization. Countries that participate in trade negotiations focus more narrowly on the potential implications of freer trade for their balance of trade. In the light of this, the most immediate concern for the LDCs would seem to be the potential impact of an agreement on the competitive position of their exports, and how an agreement would affect the prices of their imports.

The reduction of tariffs and other trade barriers, coupled with reductions in trade-distorting support and export subsidies, would be expected to reduce distortions in domestic and international markets. From a competitive exporter’s point of view, export prices would be expected to rise; export earnings would be expected to increase as a result of those higher prices and possibly through higher export volumes. Whether the world price effects of liberalization persist over time depends on the overall balance between global supply and demand. Whether any volume effect persists for an individual exporter depends on the long-run competitiveness of that exporter in international markets[5]. On the other side of the trade balance, an increase in world prices will affect import costs. Whether liberalization will improve or worsen the balance of trade cannot be determined *a priori*.

Agricultural products are not the principal source of export earnings for LDCs as a group. As may be seen from Figure 1, the value of agricultural exports ranked fourth among the leading commodity export groups in 2000-2001. Exports of textiles, for example, were more than 3 times larger than exports of agricultural products. However, much of the emphasis on the impact of further trade liberalization has been on agricultural products, because agriculture is a major sector of the economy in many LDCs and because domestic subsidies and trade-policy interventions are highly important for global agricultural trade. The OECD secretariat’s estimate of total transfers to the agricultural sector from consumers and taxpayers in OECD member countries (around $950 million per day in 2003) is often used as an indicator for the magnitude of distortions[6]. Alternatively, the average bound tariff of over 45% for imports of agricultural products in industrialized countries, compared to an average tariff of around 4% for industrial products, might also be cited[7].



Source: UNCTAD (2004).

Figure 1*. Leading exports of LDCs in 2000-2001*

A number of studies have been conducted on the potential effects of further global trade liberalization. A recent study by Anderson et al. (2005) estimates the effects on trade volumes and real income of the complete liberalization of global merchandise trade by 2015. These show an increase in the volume of trade of 20% for all developing countries and an increase in real incomes of developing countries of 0.8%. The study does not present results for LDCs as a group, but shows increases in both trade volumes (23%) and real income (1.1%) for Sub-Saharan Africa that are higher than the developing country average. The authors note, however, that some LDCs are slight losers in simulations of partial liberalization when LDCs do not reduce their own trade barriers, due to the impact of a reduction in preference margins in developed countries. In a second study, Anderson and Martin (2005) suggest that the real incomes of low-income developing countries as a group would be roughly $16 billion higher with complete liberalization, even though their terms of trade (ratio of export to import prices) would decline. In both of these studies, a range of partial trade liberalization scenarios are shown to result in increases in real incomes for the low-income developing countries.

Studies conducted for agricultural products suggest that the elimination of distortions created by tariffs and subsidies would lead to higher world prices. Some relatively conservative estimates are provided by Diao et al. (2001), who indicate that agricultural commodity prices would increase by roughly 12% on average as a result of the elimination of trade distortions (Table 2)[8]. The price effects are greatest for commodities that are most heavily protected in developed countries, such as livestock products, wheat and other grains, sugar, oilseeds and rice. Developing countries that are net importers of food would be negatively affected by the increase in prices. On the other hand, some of these commodities are major exports for LDCs (Table 1). Many other commodities of importance to LDCs, such as tropical beverages, already face low tariff barriers in developed countries and would be little affected by liberalization.

Table 2. *Effects of trade liberalization on world agricultural prices*

Commodity	Full liberalization	Removal of:		
		tariffs	domestic subsidies	export subsidies
	percentage change from base:			
Wheat	18	3	12	2
Rice	10	6	2	2
Other grains	15	1	12	1
Fruit and vegetables	8	5	0	3
Oilseeds and oil	11	3	8	0
Sugar	16	11	2	3
Other crops	6	4	1	0
Livestock products	22	12	6	3
Processed food	8	5	2	1
All products	12	6	4	2

Note: the sum of the figures for the individual sources of distortion does not necessarily equal the full liberalization percentage due to interaction effects.

Source: Diao et al. (2001).

The agricultural trade characteristics of LDCs can be seen from Table 1. Countries are ordered on the basis of the ratio of agricultural exports to GDP. For some, the necessary data are unavailable so those countries are listed alphabetically at the foot of the table. For the 44 countries for which data are available, in just over half (26) agricultural exports were equivalent to 10% or more of GDP; for roughly 20% of the countries (9) the ratio was over 20%. Data are available for 46 countries on the principal agricultural export commodity. Beverages (cocoa and coffee) are the leading export in 13 countries, cotton in 8 countries and oilseeds in 8 countries.

From Table 3 it may be seen that average tariffs are generally low for these commodity groups (beverages and tobacco, fibres, oilseeds) in the major developed countries. However, other products of interest to LDCs, such as sugar, meat and meat products, and to some extent fruit and vegetables face higher average tariffs. There might be the potential for increased export earnings for LDCs if such tariffs were reduced, although middle-income developing exporters (for example, Brazil and Thailand) might have the most to gain from a general reduction in tariffs in developed countries.

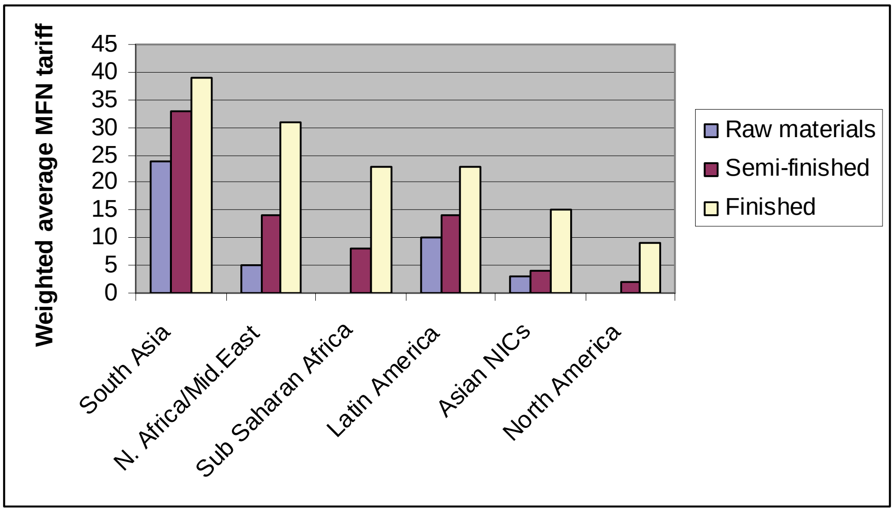
Table 3*. Agricultural tariffs by major commodity group in developed countries (%)*

Commodity	EU25	US	Developed Asia	EFTA	Developed Cairns
Paddy rice	5	6	288	18	0
Processed rice	4	4	287	11	0
Coarse grains	3	1	79	70	8
Wheat	11	3	106	136	6
Sugar	129	7	122	40	4
Oilseeds	0	3	77	46	0
Live animals	43	0	31	103	0
Animal products	8	1	11	48	12
Meat	98	6	23	197	7
Meat products	26	4	29	167	32
Dairy products	41	15	22	87	133
Fibres	0	9	0	0	0
Fruit and vegetables	10	3	21	37	2
Other crops	2	8	5	24	2
Fats	4	4	5	45	3
Beverages and tobacco	14	3	13	15	6
Food	11	5	12	23	9
Total agri-food	17	5	25	52	18

Source: Bureau et al. (2005).

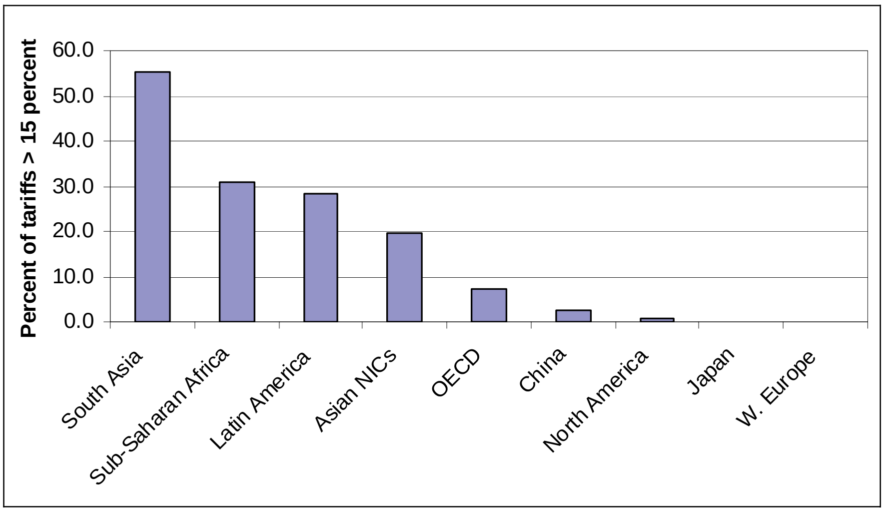
While the emphasis in this chapter is primarily on agriculture, it should be stressed that trade liberalization in other sectors could be important for LDCs. Table 4 contains average applied tariff rates in selected countries for various categories of products. From the table the relatively high rates applied to agricultural products are evident, but it is also clear that manufactures, in particular textiles, face high average tariffs in some regions. The figures also suggest that there is significant tariff escalation (increase in the size of tariffs with the level of processing) for agricultural products in Western Europe and Japan, as well as in Latin America and South Asia. Figure 2 illustrates that tariff escalation is also an issue for textiles in many regions. Indeed such escalation is more pronounced in developing countries than in developed countries. Even though import quotas on textiles were eliminated on January 1, 2005, high tariffs are still applied to textile imports in many countries.

Finally, it may be noted that tariff peaks (defined as tariffs greater than 15%) are more prevalent for trade in manufactures among developing countries, than for trade between developing and developed countries (Figure 3).



Source: UNCTAD (2003a).

Figure 2. *Tariff escalation for textiles*



Source: UNCTAD (2003a).

Figure 3. *Tariff peaks on imports of manufactures from developing countries*

Table 4. Average applied tariffs in selected importing countries and regions

Product group	China	South Asia	Latin America	Western Europe	North America	Japan
Natural resources	2	2	14	5	0	0	0
Primary agriculture	38	16	21	2	12	9	30
Processed agriculture	20	15	29	17	21	10	46
Textiles and apparel	8	13	28	15	5	10	6
Manufactures	5	6	24	11	2	1	0
Services	0	0	0	1	0	0	0

Source: UNCTAD (2003a)

The role of preferences

It might be concluded that given the prevalence of tariff barriers for agricultural products and labour-intensive manufactures, further trade liberalization would be advantageous for LDCs. Such a conclusion would need to be qualified by the fact that many LDCs already have preferential access for some of these products in developed countries. Preferential access is either provided through a reduction or elimination of the tariffs applied to LDC imports. In some cases, such concessions only apply to limited quantities of imports. The creation of the Generalized System of Preferences (noted earlier) has resulted in a number of preferential schemes. In addition, the European Union and the United States have regional schemes that benefit some LDCs. Box 1 summarizes the principal preferential schemes of relevance to LDCs in the four Quad countries (Canada, the European Union, Japan and the United States).

Relatively little empirical research has been conducted on the impact of tariff preferences on eligible countries (Tangermann 2002). It is difficult to estimate the short-term welfare gains resulting from preferences, and even more difficult to calculate any longer-term gains, for example, through the impact of preferential access on investment. Export earnings may increase due to the improved competitive position created for preference receiving countries relative to their non-preferential competitors. To the extent that preferential exporters are able to retain part of the preference margin, i.e., the difference between their supply price and the higher market price in the preference-granting country, this will also increase earnings. The opportunities for retaining such a preference 'rent' are greatest when preferential access is associated with a country-specific quota; otherwise much of the margin is likely to be captured by importing firms as suppliers compete for market share in the preference-granting country.

Some analysis has been undertaken of the effects of changes in tariff preferences, particularly in terms of the erosion of existing preferences that would be implied by a general reduction of MFN tariffs through the current round of trade negotiations.

Box 1: *Preferential tariff schemes for LDCs in the Quad countries.*

Canada

Market Access Initiative (MAI)
Introduced on January 1, 2003. All imports originating in an LDC (48 eligible countries) are granted duty-free, quota-free access with the exception of dairy, poultry and egg products which are subject to duties and quotas. Most of the 882 products affected by the Initiative are apparel and textile goods (760). A further 64 are food products and 43 are footwear items. LDCs were allowed duty-free access on a more restricted set of products since 1983 under Canada's General Preferential Tariff system – its GSP scheme. Cumulation of imports among countries eligible for GPT or the MAI is permitted.

European Union

Cotonou-Lomé (ACP Agreements)
A series of four Lomé agreements between 1975 and 2000 provided preferential access to the EU market for certain exports from African, Caribbean and Pacific (ACP) countries – the former colonies of the EU member states (includes 40 LDCs). Many agricultural products, particularly those supported under the EU's Common Agricultural Policy, were excluded. Some products (bananas, beef, horticultural products, rice, sugar, tobacco) were subject to low or zero tariffs up to a given level of imports. In 2000 the Cotonou agreement was signed. This will replace the non-reciprocal tariff preferences by a series of reciprocal Economic Partnership Agreements (EPAs) after 2007.

Everything But Arms (EBA) Initiative
From March 1, 2001 the European Union amended its existing GSP scheme to provide duty-free access for exports of all products (excluding arms) from 48 LDCs. Bananas, rice and sugar are subject to transitional arrangements and full liberalization will not occur until after 2009. Cumulation of imports among LDCs is not permitted under the EBA, but is allowed under the ACP agreements.

Japan

Generalized System of Preferences (GSP)
LDCs have duty and quota free access on a range of products under the GSP scheme. Other countries eligible for GSP have more restricted access and pay reduced tariffs. However, the list of eligible agricultural products for LDCs is limited. Some cumulation of imports among eligible countries is permitted.

Box 1 (cont.)

Box 1 (cont.)

United States

Generalized System of Preferences (GSP)
Eligible developing countries have duty-free access on roughly 3,000 products. LDCs are eligible for duty-free access on a broader range of products. The determination of eligibility is subject to a number of political and economic criteria. Currently 44 LDCs are eligible for duty-free access under general provisions of the GSP scheme and 41 are identified as LDC beneficiary countries. Products must meet a minimum value added requirement in an eligible country. Cumulation is allowed among eligible members of recognized associations, such as the Southern African Development Community (SADC). Duty-free access for a country may be subject to a quantitative limit if that country is determined to be too competitive.

African Growth and Opportunity Act (AGOA)
Signed in May 2000, the Act provides duty-free access on virtually all products in the GSP program for eligible countries in Sub-Saharan Africa. A more stringent set of criteria are applied than under the GSP to determine eligibility. As a result only 37 of the 45 African countries eligible under the GSP are also eligible under AGOA; 23 African LDCs are eligible. There are no quantitative limits on imports under AGOA.

Caribbean Basin Initiative (CBI)
The Initiative was introduced on January 1, 1984. Haiti benefits from duty-free access for its exports under this initiative. Product eligibility is similar to that under the GSP and AGOA.

Typically the methods used rely on fairly aggregate data and do not generate estimates for the LDCs as a group. In this chapter, the focus is on the impact of trade liberalization in general, rather than in particular commodity sectors such as agriculture. More detailed analysis of agricultural issues is contained in the chapter by Yu.

In a recent study, Alexandraki (2005) evaluates the impact of preference erosion for the G-90 countries, which includes both the LDCs and the ACP countries. She concludes that the impact of likely preference erosion under a new WTO agreement will be limited and that most of the effects will be confined to middle-income developing countries (Mauritius, St. Lucia, Belize, St. Kitts and Nevis, Guyana and Fiji) because of the implications for sugar and bananas and, to a much lesser extent, textiles.

In an earlier study, Subramanian (2004) examined the implications for LDCs of a 40% reduction in MFN tariffs for agricultural and manufactured goods in the Quad countries. The estimates were based on optimistic assumptions about the current gains accruing to LDCs from preferences, in particular, that the rules applying to preferential trade do not have any restrictive effects on their exports to the Quad countries. Under these assumptions Subramanian estimates that preference erosion would result in a reduction in the value of total LDC exports of less than 2%. Five LDCs face losses in excess of 5% of the value of their exports – Malawi (12%), Mauritania (9%), Haiti (6%), Cape Verde (6%) and Sao Tome and Principe (5%). In absolute terms, the larges losers are Bangladesh (US$ 222 million), Cambodia (US$

54 million); Malawi ($US 49 million), Mauritania (US$ 40 million) and Tanzania (US$ 29 million). On the basis of these estimates Malawi and Mauritania could face significant losses in both absolute and relative terms.

These studies focus exclusively on the erosion of existing preferences. As noted in Table 1, many existing schemes do not provide completely free access for imports from the LDCs. Some studies have analysed the expansion of preferences through the general application of a scheme similar to the Everything But Arms (EBA) initiative of the European Union to all imports from LDCs in the Quad countries. This would imply that the margin of preference provided to LDCs would be increased through the elimination of any remaining tariffs and the removal of any limitations on the volume of imports. The results of these studies are summarized by Achterbosch et al. (2003). They suggest that a strengthening of preferences in the Quad countries would increase the export potential of LDCs by 3-13%, primarily through the impact on textiles and clothing in Canada and the United States, and agricultural products in Japan. Hoekman et al. (2002) note that tariff peaks in the Quad countries have a disproportionate effect on LDC exports since such peaks tend to be concentrated in agricultural products (sugar, cereals and meat) and in labour-intensive products such as apparel and footwear. If the export potential that would be created by the strengthening of preferences were to be exploited by the LDCs, this would increase their economic welfare by 1-2%. Unfortunately, there seems to have been little analysis of the impact of extending preferences for LDCs to a broader range of importing countries, but it is likely that such an expansion could also help to increase the export potential of LDCs. The potential importance of this issue is discussed in more detail later in the chapter.

In conclusion, reductions in applied MFN tariffs resulting from a Doha Round agreement could result in the erosion of existing LDCs preferences. To some extent, this erosion could be offset by a further strengthening of those preferences in developed countries, by removing remaining restrictions on import volumes, eliminating any remaining tariffs, and ensuring that duty-free and quota-free access is extended to all products. For the few LDCs that may experience significant reductions in the value of their exports as a result of preference erosion, compensation could be provided through existing international financial mechanisms (Subramanian 2004).

ARE PREFERENTIAL SCHEMES IN THE LONG-TERM INTERESTS OF LDCs?

Proponents of free trade argue that partial trade liberalization is inferior to the complete elimination of barriers to trade. Neo-classical trade theory suggests that the elimination of trade barriers would maximize global welfare by enabling the world's resources to be used most productively. We should note that even in a free-trade world, the distribution of the increase in economic welfare within and among countries may be highly uneven since that is crucially dependent on the distribution of factors of production and the returns to those factors. Since the complete elimination of trade barriers seems to be a distant possibility, our attention must be directed to the merits of ‘second best’ or more limited approaches, such as that reflected by preferential schemes.

The arguments for preferences rest on the stimulus that these are assumed to provide to the economies of poorer countries, by increasing the demand for their exports in richer countries. By offering duty-free access for the exports of developing countries, their export industries are expected to expand, generating higher domestic income and employment. As their industries grow they may be able to increase their efficiency and exploit economies of scale, making them more competitive and enabling them to compete in non-preferential markets. This argument is crucially dependent on the existence of sufficient productive and export capacity in LDCs to take advantage of the economic incentives that are created by duty-free access (Wainio et al. 2005).

The arguments against preferences are that these can serve to lock the economies of preference-receiving countries into particular patterns of production that are not sustainable in the longer run, and create dependence on preference-granting markets. When a country imposes import restrictions, the relative prices of the affected products will increase. A country with preferential access will respond to the distorted prices of the protected market – its domestic resources may be drawn into the production of protected products, in the same way that the resources of the protecting country are drawn into such products. If the long-run prospect is for the eventual elimination of protection, industries in the preference-receiving country may face a similar issue of long-run sustainability as those in the preference-granting country.

Issues of distortion and dependency can be intensified when preferences are granted on a limited range of products. Countries may grant preferences on those products that are currently exported by poorer countries, rather than products that they might be able to export. The continued dependence of many poorer countries on a limited range of primary commodities can be criticized on this basis. Alternatively, countries may be reluctant to extend preferential access to ‘import-sensitive’ products in which poorer countries have a comparative advantage. Many parts of agriculture and labour-intensive manufactures, such as textiles and footwear in developing countries, have been affected by this approach to preference schemes in the European Union and the United States (GAO 2001).

It is difficult to escape the conclusion that preference schemes confer risks in terms of long-run sustainability. Particularly in countries that are likely to be highly dependent on trade in comparison to the size of their domestic economies, the development of a trade structure that could be undermined by the gradual elimination of preferences poses substantial risks. Balanced against that risk is the extent to which the development of export industries in preference-receiving countries can provide a stimulus to the overall development of their economies. Given the considerable economic challenges facing the LDCs, and the likelihood that the playing field of international trade is unlikely to be levelled in the foreseeable future, it could be argued that any measures that can be taken by the international community to stimulate the growth of exports by LDCs merit serious consideration.

STRENGTHENING PREFERENTIAL ARRANGEMENTS

As noted above, regardless of arguments over their advantages or disadvantages agreements that grant preferential access to markets in developed countries are important for developing countries. In recent years, there have been attempts to use these to give extra advantages to LDCs. This is reflected in Canada's Market Access Initiative, the Everything But Arms initiative of the European Union, and the LDC components of the Japanese and US GSP schemes. However, there are a number of limitations associated with existing preferential schemes that need to be addressed.

Eligibility. Schemes differ in terms of which countries are eligible for preferential access. While several countries follow generally accepted conventions on countries eligible for preferential treatment, such as the list of LDCs compiled by the United Nations, this is not always the case. For example, the LDCs eligible for special provisions in the US GSP only include 41 of the 50 countries currently on the UN list. Preferential arrangements for regional groupings, such as those provided to the African, Caribbean and Pacific (ACP) countries by the European Union, have traditionally been more limiting in terms of eligible countries. Indeed the European Union sought a waiver from the WTO for the current agreement (the Cotonou agreement) in 2001 because of this. Two GATT panels had earlier concluded the preferences (tariff and non-tariff) for the ACP countries provided under the Lomé treaty were contrary to GATT obligations[9]. US preferential schemes have always provided for the exclusion of certain countries on political or other grounds. The most recent example of preferential access, the African Growth and Opportunity Act (AGOA) continues that tradition.

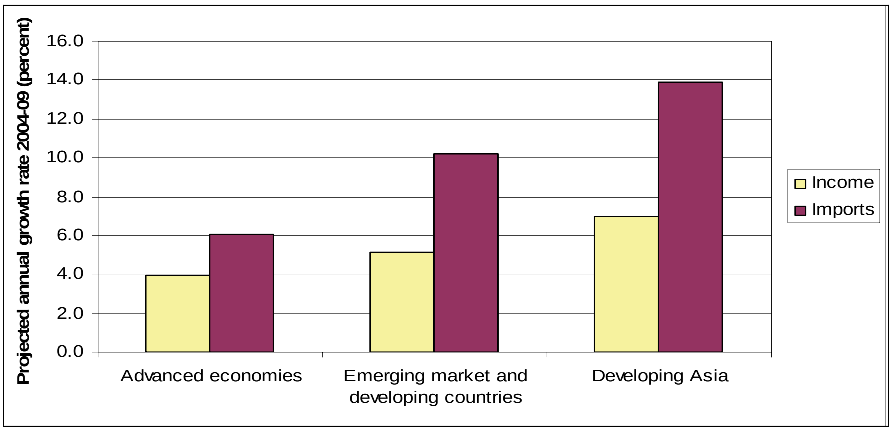
Product coverage. The amount of preferential access provided, in terms of product coverage and preferential rates of duty, differs significantly among agreements. The Japanese GSP scheme, even with the expanded product list for LDCs, provides only limited preferential access for agricultural products, but relatively broad access for industrial products. US preferential arrangements provide only limited access for textiles and footwear. The EBA scheme of the European Union seems to provide substantial potential access, once the transitional arrangements for sensitive products such as sugar are complete, by applying zero tariffs to imports from LDCs. Schemes that do not allow duty-free access can be designed to preserve a margin of preference for LDCs even with reductions in MFN tariff rates by expressing the preference as a percentage of the MFN tariff.

Rules of origin. There are substantial differences in rules of origin in preferential arrangements. Some involve the criterion of a change in tariff classification, others a percentage value added criterion and others apply criteria relating to manufacturing or processing. Some rules of origin discriminate against the integration of agricultural industries among developing countries and limit the opportunities for adding value to imported products that are subsequently re-exported. This is particularly problematic for small countries that would otherwise be able to develop a market for processed products, but are unable to provide their own raw materials. Several studies have suggested that the restrictiveness of rules of origin, the administrative burdens that these place on LDCs, and the resulting high transactions costs are responsible for low levels of utilization of preferences in some countries (e.g. Brenton 2003; Mattoo et al. 2002; UNCTAD 2003b). An Agreement on Rules of Origin was part of the Uruguay Round Agreement, but this was oriented towards the harmonization of non-preferential rules of origin. Apart from establishing some principles for the application of rules of origin under preferential agreements (essentially relating to transparency), the Agreement does not have anything to say about what types of rules are preferable. Member countries are merely required to notify the rules of origin that they apply under preferential agreements to the WTO.

Certainty of commitments. The amount of certainty on future market access provided under preferential programs differs considerably both in terms of the length of time to which agreements apply and whether countries can lose their eligibility. Schemes differ in the length of time for which they are in force. The Japanese GSP, for example, is renewed for significant periods of time. The current scheme extends to 2011. The renewal of the US scheme can be delayed by Congress. The scheme that expired in 1995, for example, was not renewed until 13 months later. Most schemes provide for the graduation of countries (loss of preferences) once a certain level of economic development is reached. That is relevant to LDCs if they are judged to have passed from the least developed to ‘normal’ developing country status. Of more immediate relevance is whether countries can lose their eligibility due to political factors. Most developed countries have suspended preferential access for Myanmar due to political conditions in that country, but many seem reluctant to take too active an approach to changing the list of eligible countries. The United States is an exception in this regard. For example, Chile and Paraguay were suspended from the GSP scheme during the 1980s on the basis of workers’ rights before eventually being reinstated in 1991. Nicaragua’s privileges were terminated in 1985 on the same grounds. After originally being included under AGOA, the Central African Republic and Eritrea were dropped as beneficiary countries from January 1, 2004 on the basis that they were not making sufficient progress towards policy reform[10]. The uncertainty created by the potential loss of eligibility for preferential access may reduce investment in export-oriented sectors in LDCs. Finally, countries that provide preferential access for developing countries still have the option of imposing higher tariffs on a ‘temporary’ basis, if the volume of those imports threatens to undermine prices in their domestic market. The existence of such ‘safeguard’ provisions adds an additional dimension of uncertainty to the commitments under preferential agreements[11].

Number of schemes. The number of countries that apply the generalized system of preferences for developing countries is limited. In addition to the GSP schemes operated by the Quad countries, a further 12 schemes have been notified to the UNCTAD secretariat. The countries involved are: Australia, Belarus, Bulgaria, the Czech Republic, Hungary, New Zealand, Norway, Poland, the Russian Federation, the Slovak Republic, Switzerland and Turkey[12]. It should be noted that some of these countries are classified as being in economic transition and some would not qualify as high-income countries on the basis of per capita GDP. It is noteworthy that under Part IV of the GATT, less developed contracting parties agree to take appropriate action in implementing the provisions of Part IV for the benefit of the trade of other less developed contracting parties. Furthermore, the framework agreement on agriculture for the Doha Round states that "Developed Members, *and developing country Members in a position to do so,* should provide duty-free and quota-free market access for products originating from least developed countries". (WTO 2004, paragraph 45, emphasis added).

Traditionally, the focus has been on the obligation of developed countries to open up their markets to developing countries. While this focus was undoubtedly justified in the past, one might question whether such a simple approach is appropriate for the future; particularly if one wishes to target preferences to LDCs. Currently, exports to other developing countries account for roughly 40% of LDCs total exports (UNCTAD 2004, Table 18). It is expected that income growth in developing countries will exceed that in developed countries for the foreseeable future. The IMF, for example, projected that average annual growth in real GDP for emerging market and developing countries will be roughly double that in advanced economies for 2004-09, with correspondingly higher growth in the volume of imports (Figure 4). Imports in developing Asia are projected to rise at an average rate of 14% per year. Furthermore, average applied tariffs are high and tariff peaks are common among developing countries, particularly for industrial products (UNCTAD 2003a). In order for the LDCs to take advantage of the opportunities for growth in exports to other developing countries, it would seem to be appropriate for many of the richer developing countries (e.g., Brazil, China, India, Malaysia) to develop preferential tariff schemes, targeted specifically at LDCs[13].



Source: IMF (2004)

Figure 4. *Projected growth of income and imports*

A Global System of Trade Preferences among developing countries (GSTP) was created in 1989 as a result of the efforts of the United Nations Conference on Trade and Development. There have been three rounds of negotiation under GSTP, the most recent in Brazil in 2004. However, only 44 developing countries have ratified the agreement, progress on negotiating improved market access has been slow, and the primary emphasis has been on reciprocal concessions rather than preferential access for LDCs. It should be noted that some developing countries have taken unilateral action to provide such access. Egypt, for example, has unilaterally reduced applied tariffs by 10-20% on 77 products of interest to LDCs and provided duty-free access for roughly 50 products.

Increasing the capacity of LDCs to take advantage of preferences. The application of preferences by a broader range of countries to all products, combined with improvements in how such preferences are implemented (as discussed above) could help to increase the opportunities for LDCs to broaden the range of products that they export and to increase their export earnings. However, it does not mean that LDCs would actually be able to profit from the new opportunities created. Many face considerable challenges in mobilizing their resources to take advantages to such opportunities. Some of these challenges are due to natural disadvantages created by geography, for example, distant location from expanding markets or land-locked locations. Some are characteristics of economic structures that constrain economic development, for example, limited natural resource or population bases. These factors can create substantial barriers to expanded participation in the global economy for some LDCs.

In other cases, barriers to export development can be overcome through a combination of appropriate domestic policies that stimulate investment in export-oriented industries, the development of the labour force and the acquisition and application of knowledge and information. Many factors are important in helping to overcome some of these barriers – including good governance, control of corruption, and the presence of a legal framework governing business transactions that is conducive to the development of a modern economy. Technical assistance, which has been increasingly emphasized by international organizations that work with LDCs, can also play an important role.

In the final analysis, expanded access to markets is a necessary but not sufficient condition for LDCs to be able to increase their participation in the global economy. It does not guarantee that this will be achieved.

CONCLUSIONS

It is unclear how much progress will be made in liberalizing international trade in the current WTO round of negotiations. Further reductions in tariffs and trade-distorting subsidies would likely lead to an increase in global economic welfare, but the impact on the least developed countries is unclear. The terms of trade of the LDCs could well deteriorate as a result of the impact of general reduction in MFN tariffs on the competitive advantage that LDCs secure through preferential access in some countries, and the price-enhancing effect that liberalization might exert on LDC imports. The effects on individual LDCs will depend on their export and import mix, and the extent to which the competitive position in their major markets is affected by a new agreement.

The negative effects of a general reduction in tariffs on the competitive position of the LDCs could be offset by strengthening their preferential access to markets in other countries. Regardless of the final outcome of the Doha Round, it seems likely that MFN tariffs in a range of products of importance to the LDCs will remain high, particularly in such commodity groups as agriculture and textiles. An expansion of duty-free/quota-free access to all LDC exports by developed countries could help to offset the erosion of tariff preferences, but this would not expand market access for LDCs in countries where the potential growth in demand is likely to be the strongest. To be really effective, the Doha Round would need to generate not only expanded access for LDC exports in developed countries, but also in higher-income developing countries. It is by no means clear that the Round will produce this result unless the LDCs (and their advocates) make a major effort to make this happen.

Furthermore, there are a number of significant limitations inherent in existing preference schemes for LDCs that need to be addressed. The schemes have a fragile legal status because they are created and managed on a unilateral basis by each preference-granting country. The terms of schemes vary considerably among countries. There is evidence that the rules of origin applied in existing schemes are burdensome for LDCs, result in limited trade creation, and actively discriminate against the development of value added exports. A second priority for LDCs in the current round of negotiations could be to bring preferential schemes under the GATT/WTO framework with the aim of establishing greater certainty and stability of access, provide unrestricted duty-free access for all LDC exports, and to simplify the rules to reduce transactions costs and actively encourage the development of value-added processing in LDCs.

If these measures were taken, they could help to achieve the stated objective of WTO ministers of improving the effective participation of LDCs in the multilateral trading system and satisfy their commitment to address the erosion of tariff preferences. But in the final analysis, such measures would only increase the potential for an expansion of exports by the LDCs. The least developed countries still face the challenge of mobilizing their economic resources to convert such potential into actual flows of goods.

NOTES

1 The developing countries were Brazil, Burma (Myanmar), Chile, China, Ceylon (Sri Lanka), Cuba, India, Lebanon, Pakistan, South Africa, Southern Rhodesia (Zimbabwe) and Syria. The other signatories were Australia, Belgium, Canada, the Czechoslovak Republic, France, Luxembourg, the Netherlands, the United Kingdom and the United States.

2 The concept of granting preferential tariff rates by developed countries for imports from developing countries was developed by Raúl Prebisch, the first Secretary-General of the United Nations Conference on Trade and Development (UNCTAD). It was formally adopted at the second UNCTAD conference in New Delhi in 1968. Certain preferential arrangements then in operation were exempted from MFN in the original GATT. In 1971 the Contracting Parties approved a waiver

to Article I in order to authorize the GSP scheme. The enabling clause created a permanent waiver for GSP.

3 The Blue Box was included in the AoA to accommodate direct payments to producers made under production-limiting programs, primarily by the European Union and the United States. The Framework Agreement proposes to expand the definition to include certain payments that do not require production. This would allow the United States to include its counter-cyclical payments (CCPs) in the Blue Box, rather than in the AMS

4 A joint technical-assistance program involving the FAO, International Trade Centre (ITC), UNCTAD, World Bank, WTO and UNDP was established after the first WTO Ministerial in Singapore in 1996.

5 It is often overlooked that the central message of neo-classical trade theory is that consumers are the ultimate beneficiaries from trade liberalization as a result of the price-reducing effects of increased productive efficiency and competition. Changes in the merchandise trade balance do not necessarily correlate with the changes in national welfare that are associated with trade liberalization. For an empirical example of this see Ingco (1997)

6 OECD. Producer and Consumer Support Estimates Database, 2004. Total Support Estimate (TSE) of $349.8 billion for OECD member countries in 2003. Database accessible through http://www.oecd.org

7 Data from USDA, Economic Research Service, http://www.ers.usda.gov/Briefing/WTO/tariffs.htm.

8 Van Meijl and Tongeren (2001) summarize the results of major studies on the impact of further agricultural trade liberalization in the current round of negotiations. The estimates of global welfare gains and gains to developing countries in Diao et al. (2001) are the smallest for the studies examined.

9 The EC had contended that the Lomé accords were free-trade agreements and were covered under Article XXIV of the GATT. The Lomé accords did not receive approval by the GATT as free-trade agreements.

10 It must be determined that countries have established or are making continual progress towards establishing the following: market-based economies; the rule of law and political pluralism; elimination of barriers to US trade and investment; protection of intellectual property; efforts to combat corruption; policies to reduce poverty, increase the availability of health care and educational opportunities; protection of human rights and worker rights; and elimination of certain child-labour practices.

11 The WTO has two safeguard instruments. These are Article XIX, as elaborated in the Uruguay Round Agreement on Safeguards, and the special safeguard provisions (SSG) contained in the Agreement on Agriculture. Both are designed to address sudden increases in imports that cause or threaten to cause serious injury to domestic producers. The number of countries that can use the SSG and the commodities to which it can be applied is limited. In contrast, all countries are able to use the safeguards provisions.

12 Norway and Switzerland apply the same duty-free access to LDCs as provided by the EBA. Hungary, the Czech Republic, New Zealand and the Slovak Republic provide duty-free and quota-free access to all imports from eligible LDCs. The preference schemes of new (2004) members of the European Union are now subsumed under existing EU schemes.

13 Although the enabling decision for preferential tariff treatment only refers to its provision by developed countries it provides for ‘the Contracting parties to consider on an *ad hoc* basis under the GATT provisions for joint action any proposals for differential and more favorable treatment” that do not fall under the provisions set out in the decision (GATT 1979, footnote 2)

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