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Developing Countries and the Political Economy of the Trading System

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ABSTRACT

This paper analyzes a number of the challenges confronting developing countries seeking to use the WTO Doha negotiations to promote their economic growth and performance. A precondition for success is to have clear objectives and to take a pro-active stance. But a key necessary condition for success will be to recognize the political economy of reform—both at home and in partner countries. Little progress will be made on key issues unless there are major stakeholders within countries that perceive the overall package to be beneficial. A number of possible focal points that could be used both as targets and as benchmarks for reciprocal negotiations are discussed, as is the need for mechanisms to increase the domestic 'ownership' of WTO agreements.

1. INTRODUCTION

The November 2001 "Doha Development Agenda" puts development concerns at the core of WTO deliberations. The challenge now is to achieve an outcome that supports poverty reduction and economic growth. The implementation problems associated with a number of Uruguay Round agreements, combined with the persistence of tariff peaks and OECD production and export subsidies for agricultural commodities has led to a 'development credibility' deficit for the WTO. The extent to which remaining market access barriers are removed, the development relevance of WTO rule-making is improved and implementation issues and constraints are addressed will determine whether the Doha Development Agenda lives up to its name.

A precondition for a good outcome from a development perspective is that political economy constraints are recognized up front. These arise at various levels, but ultimately boil down to the need that agreements have the support of domestic stakeholders. Normative economists use change in national welfare as the criterion on which to judge changes in policies, and trade economists have built large, complex simulation models to assess the magnitude of national and global welfare impacts of alternative policy reforms. But the reality of the policymaking process is that it is driven by interest groups, by industries, by communities, by labor unions, and so forth. As a result, governments are rarely the social welfare maximizing decision-makers found in textbooks given the need to balance the interests of different groups in society.

Developing countries have historically played only a minor role in the multilateral trading system. Until the Uruguay Round (1986-93), their participation was à la carte, with many not making commitments. This changed with the entry into force of the WTO in 1995. Because of the so-called Single Undertaking, developing countries became subject to most of the disciplines of the many agreements contained in the WTO (albeit after transition periods had expired). At the same time, a number of the agreements increasingly came to be seen as having little benefit—indeed, in the case of some agreements (TRIPS) the perception rapidly emerged that benefits were highly skewed towards rich countries. The resulting 'Uruguay Round hangover' led to a great deal of skepticism regarding the benefits of WTO membership. Many governments and civil society of developing countries view the prospect of additional agreements and disciplines in the WTO with great suspicion. The Uruguay Round hangover has made them very aware of the downside of signing on to agreements that are ill understood and that have little if any backing by domestic stakeholders. Many developing countries are now actively seeking to improve their 'terms of trade' in the WTO.

However, industrialized countries appear to be less enthused about active multilateral engagement. Industry in OECD countries already operates in an environment where much of what they trade is duty free (due to duty drawback and similar schemes, regional trade agreements and past negotiations that reduced MFN tariffs on their products substantially). And, other interest groups have come to the fore that would like to introduce binding disciplines on non-trade policies such as labor standards and environmental regulation into the WTO, and more generally, seek to move the WTO ‘behind the border’.

Thus, developing countries confront a three-fold challenge: inducing high income countries to improve market access and the rules of the game; ensuring that any regulatory (non-trade) rules support economic development; and convincing domestic stakeholders that there are significant net positive payoffs to engagement in the WTO. Much of the burden of rebalancing the trading system to support economic development more effectively lies with developing countries. They are the major demandeurs and have the greatest stake in using the system to help them to adopt better domestic policies.

Success will require active use of reciprocity, the basic engine of WTO negotiations. The WTO process involves giving export interests that want better market access abroad an incentive to put pressure on import-competing sectors to concede opening of the home market. This political dynamic began to break down in the late 1980s, with the spread of regional integration agreements and duty-free treatment provisions for imports used in export production, many multinationals have little incentive to invest resources in support of traditional merchandise trade liberalization. As a result, reciprocity must be sought increasingly in other areas such as services and domestic regulatory policy commitments. The latter are complex to negotiate. Negotiations to lower tariffs can be safely delegated to trade negotiators with little need for oversight from civil society (as the outcome would generally be welfare improving). When it comes to domestic regulation it is not easy—and perhaps impossible—to trade ‘concessions’. The practice to date has been to focus instead on the identification of specific rules that should be adopted by all—usually ‘good practices’ that have gradually emerged in OECD countries.

Developing countries must identify the priority issues to pursue in the WTO—what should be sought from trading partners; where can the WTO process be used to implement priority reforms at home that will improve trade capacity and stimulate productive investment? In doing this, political economy issues must be considered explicitly. What can be offered to powerful interests in OECD countries that will induce them to actively support an outcome that benefits developing countries? Can such concessions in turn be sold at home? Is there enough support to ensure that the overall package can and will be implemented? These are complex issues, made substantially more complex because the WTO agenda is beginning to go beyond market access. Indeed, a major issue is to determine if a strategy where regulatory-type commitments are linked to market access commitments is needed.

The premise in what follows is that priority should be given to a ‘traditional’ market access agenda that focuses on all products—goods *and* services—without exception, that is, including agriculture and labor-intensive manufactures such as apparel. There is still great scope to use traditional reciprocity dynamics to reduce barriers to trade. That said, attention should also focus on ensuring that WTO rules support development, and are *seen* to be doing so by stakeholders. This is a vital element of enhancing the development relevance of the WTO and building the support that is needed to implement agreements. In addition to actions in the WTO, supply-side initiatives to address national trade capacity constraints and improve the investment climate in developing countries are needed. As discussed in the next section, there is a large trade agenda confronting many developing countries. Identifying what can be done by the WTO and what requires complementary action outside the WTO is a first priority.

2. THE TRADE AGENDA AT THE NATIONAL LEVEL

Despite efforts to liberalize trade, success in integrating into the world economy is far from universal. In part this reflects continued anti-export biases created by remaining border trade policies and the absence of an enabling environment for supply-side responses to changed incentives to emerge. 'Behind the border' barriers to trade integration—for example, lack of access to finance, high cost and low quality distribution and transport services—are often more important obstacles than border barriers such as tariffs. Absent supporting health and education services that expand human capital, the long-term dynamic gains of trade liberalization will be limited.

To benefit from liberalization, measures to lower trade-related transactions costs and regulatory reforms may be called for to ensure that economic responses to liberalization are efficient, equitable and enduring. Priorities will differ depending on country circumstances. In some low-income economies priority areas for action are to strengthen institutions such as customs, reduce transport costs and ensuring that export marketing and product standards are satisfied. In others, reducing tariffs and other trade barriers remain a priority. Table 1 provides a summary illustrative matrix mapping 'types' of countries against possible priority areas.

Table 1: Illustration of possible national priorities in different types of countries

Country type	Traditional trade policies		Behind the border trade policies	
	Policy	**Institutions**	**Policy**	**Institutions**
Low income: weak institutions, high fiscal dependence on tariffs	Reduce tariff dispersion; develop domestic tax bases	Strengthen customs; consider free trade zones as catalyst for exports	Enhance efficiency of transport and transit regimes; maintain competitive real exchange rate	Strengthen national capacity to design trade and regulatory policies; Upgrade product standards bodies
Low income: strong role of the State, high protection; high transactions costs	Reduce border barriers significantly; reduce tariff dispersion	Reduce red tape; adopt drawback or temporary admission customs schemes	Promote competition in service industries, including through FDI and privatization	Strengthen standards setting and certification bodies. Efficient regulation to achieve social objectives
Transition economy	Maintain relatively low and uniform tariffs	Develop customs and related infrastructure	Develop legal and regulatory regimes for services	Develop national capacity to design/enforce regulatory policies
Middle income, small, low average protection	Lower tariff peaks	Adopt ex post controls to facilitate trade	Enhance technology and E-commerce-related policies	Strengthen enforcement of prudential regulation
Middle income, large, high protection	Reduce average and dispersion of protection	Reduce red tape; implement trade facilitation measures	Services liberalization; end monopolies; develop competition policy	Pro-competitive and prudential regulation; establish competition authorities

2.1 Border Barriers

Despite significant liberalization by many developing countries, traditional trade policies continue to imply significant anti-export biases in a number of regions, most notably South Asia. Average (unweighted) tariffs in the Middle East and sub-Saharan Africa are in the 20 percent range (Table 2). However, the 'border agenda" in many low-income countries is more institutional than trade policy related. Although non-tariff barriers have come down substantially in most developing countries (Table 3), inefficiencies in public administration are often an impediment to trade. Customs clearance and logistics related transactions costs can be a major disincentive for investment in tradable sectors, especially in activities that are time sensitive or where it is important to be integrated into global production networks that operate on the basis of just-in-time supply chain management. Exporters must have access to imported intermediate inputs at world market prices in order to be competitive. In countries where tariffs continue to be needed for revenue mobilization this requires well-functioning customs regimes that refund taxes paid on imported inputs, or, preferably, allow exporters to import inputs duty free (so-called temporary admission or green channel treatment). Many countries do not have well-functioning drawback regimes, creating anti-export bias.

Table 2: Average Unweighted Tariff Rates By Region

Region	1978-80	1981-85	1986-90	1991-95	1996-99
Africa	38.2	29.3	26.9	22.3	17.8
East Asia	23.5	26.9	20.7	14.6	10.4
Latin America	28.1	26.4	24.1	13.9	11.1
MENA (ex-OPEC)	29.6	24.6	24.1	22.9	19.3
South Asia	NA	71.9	69.8	38.9	30.7
Europe/Central Asia	12.0	21.6	14.9	8.1	10.1
Industrial economies	11.9	8.9	8.2	6.8	6.1

Source: World Bank.

Table 3: Frequency of core NTBs in developing countries, 1989–98

Country	1989–94	1995–98
	%	%
East Asia and the Pacific (7)	30.1	16.3
Latin America and the Caribbean (13)	18.3	8.0
Middle East and North Africa (4)	43.8	16.6
South Asia (4)	57.0	58.3
Sub-Saharan Africa (12)	26.0	10.4

Note: Parentheses indicate the number of countries per region for which data are available.
Source: World Bank.

2.2 The 'Behind the Border' Trade Agenda

A supporting legal and regulatory environment is vital for sustained growth. While this goes far beyond trade-related policy, elements of the associated 'behind the border' *trade* agenda that affect the investment climate include policies and institutions that support the participation of national firms on international markets and measures to enhance their competitiveness by ensuring access to crucial services inputs—both public and private. Key areas for many countries are product standards and the domestic service sector. Modernization of standards systems, including institutions and infrastructure for certification and conformity assessment is needed to operate in the current global trade environment. Meeting international standards for quality, health and safety is increasingly a precondition for contesting international markets and has become a major factor constraining the ability of many exporters in least developed countries (LDCs) from benefiting fully from recent preferential access initiatives. Many low-income countries are not adequately equipped to deal with rapidly tightening product standards and labeling requirements and confront major investment requirements in order to do so (Henson et al. 2001; Wilson, 2002).

The availability of low cost, high quality services is a critical determinant of the competitiveness of national firms. An efficient, diversified and well-regulated financial sector is necessary to fund investment needs and allocate resources to where they have the highest returns. Telecommunications are both a vital intermediate input and crucial to the dissemination and diffusion of knowledge. Transportation costs are a major determinant of competitiveness—the cost of international transport is often above the applicable tariff in export markets, and intra-national transport costs can be a multiple of international costs (Fink, Mattoo and Neagu, 2000). Research has shown that measures aimed at reducing the cost of services that facilitate trade can easily have economy-wide welfare benefits that are a multiple of those associated with merchandise liberalization (Stern, 2002), and, indeed, may be a precondition for benefiting from such liberalization.

Initiatives to strengthen private and public service institutions that support export development—access to credit, modernization of product standards conformity assessment systems—and to reduce the cost of key inputs (transport, telecoms, insurance, finance, etc.) should be pursued in the context of an overall national strategic framework that identifies where the payoff to reform and public investment is largest. Careful policy analysis is needed to identify both priorities and options for reform. In many cases pro-competitive reforms will be needed, as greater competition (contestability of markets) is a major engine for reducing prices and increasing the variety of goods and services. The competition agenda is often a complex one that involves numerous policy instruments, from liberalization of trade and elimination of entry restrictions through pro-competitive regulation and enforcement of competition law.

Whatever the priorities are, in all countries there is a need for complementary macroeconomic, education, health, distribution, etc. policies (Rodrik, 2002). Separating out the trade agenda from the development agenda more broadly defined is difficult, if not impossible. The key need is that trade is integrated into the national development strategy. Only then will an informed assessment be possible regarding if and how issues should be addressed in the WTO. Clearly the primary role of the WTO is as a mechanism to address the negative externalities that countries impose on each other, through trade policies. But it is also a potential mechanism to help countries adopt good policies.

3. IMPROVING MARKET ACCESS

A great deal of research has documented that there is still a large market access-related agenda. Further liberalization will significantly increase real incomes and reduce poverty in developing countries (World Bank, 2001). The extent to which developing and industrialized country trade barriers are lowered, tariff peaks and escalation removed, export subsidies eliminated and production subsidies replaced with less trade distorting measures will define to an important extent the development relevance of WTO talks. Such actions will primarily benefit consumers and taxpayers in the countries pursuing reform, whose gains would greatly exceed the losses of affected workers and industries.

Most-favored-nation tariff rates of developed countries are less than 5 percent on average. Indeed, much trade is now duty-free as a result of zero ratings, preferences and free trade agreements. However, tariffs for some commodities are over 100 percent. Such tariff peaks—rates above 15 percent—are often concentrated in products that are of interest to developing countries. In 1999, in the US alone, imports originating in LDCs generated tariff revenue of $487 million, equal to 11.6% of the value of their exports to the US, and 15.7% of dutiable imports (US Department of Commerce, 1999).[1] Although the LDCs are by definition among the poorest countries in the world, in absolute terms most of the poor live in non-LDCs such as China, Egypt and India. From a poverty alleviation perspective, it is therefore vital that market access improves for *all* developing countries. As discussed below, this will require reciprocity; unilateral liberalization in the OECD is not politically feasible—governments must be able to point to 'compensating' reductions in developing country trade barriers.

Protection in OECD countries currently imposes costs on developing countries that exceed official development assistance flows (some $45 billion per year). Benefits to developing countries from abolishing their own protection are over $60 billion. Global protection of trade in merchandise costs the world economy some $250 billion (Hertel and Martin, 2000). If current policies restricting trade in services are considered, the figure can easily double or triple (Stern, 2002). Add in the trade chilling effect of instruments of contingent protection (antidumping, safeguards)—see below—and the real income gains from elimination of redundant red tape at borders and it is clear that the benefits of reducing market access barriers are enormous.

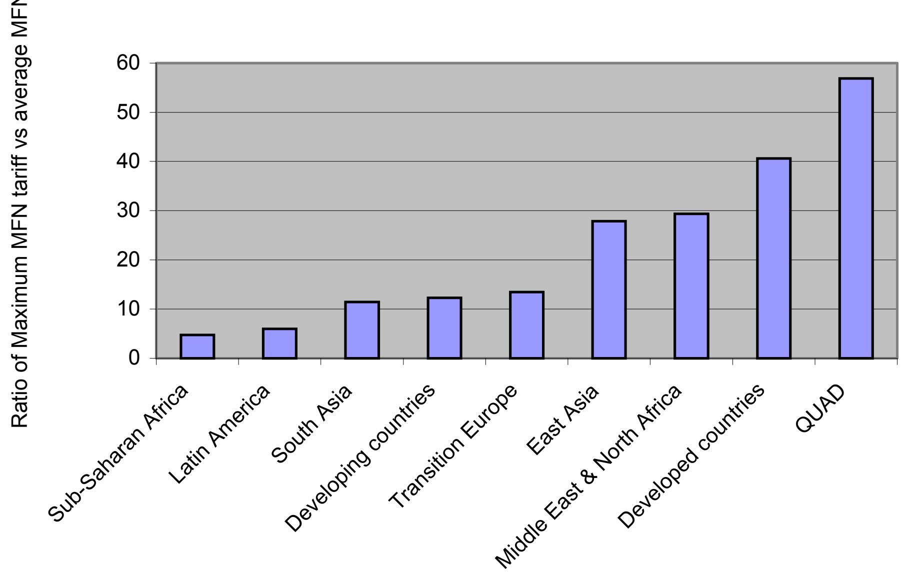
Over 30 percent of LDC exports and 15 percent of all developing country exports are potentially affected by a tariff above 15 percent in the Quad (Hoekman Ng and Olarreaga, 2002a). Tariff peaks are also common in developing country tariff schedules, adversely affecting South-South trade. Bangladesh, Costa Rica, Egypt, India, Mexico, Morocco, Pakistan, Poland, Ukraine and Zimbabwe (among others) have tariffs above 200 percent for some products. However, on average, tariff peaks (relative to average levels of protection) are higher in OECD nations—where the highest tariffs are on average 40 times the average tariff, whereas among developing countries, the ratio is 12. For the Quad, the ratio is 55. On the other end of the

[1] This calculation excludes Angola, 95% of whose exports are oil-related and not dutiable. The LDCs comprise 49 low-income countries, mostly in Africa.

spectrum are Sub-Saharan African countries for which this ratio is only around 5—indicating a much more uniform structure of protection (Figure 1).

Moreover, the tariff structure of developed countries shows significant tariff escalation, so that market access for more processed products (embodying greater value added) is more restricted. For example, fully-processed manufacturing food products face tariffs twice as large as products in the first-stage of processing in the EU and Japan, with final goods confronting an average MFN tariff of 24 and 65 percent, respectively. In Canada the ratio is even higher: tariffs on fully processed food products are 12 times higher than for 1st stage processed products (the MFN tariff on fully processed is 42 percent) (Hoekman, Ng and Olarreaga, 2002a).

Figure 1: Excessive tariff protection across WTO members



Source: Hoekman and Olarreaga (2002).

Because average tariff barriers in developing countries are higher than in industrialized nations, much of the potential welfare gains from reducing trade barriers will arise from own liberalization. The large potential payoff from reciprocal tariff liberalization provides a strong rationale for developing countries to engage in traditional GATT-type tariff negotiations—greater efficiency in home markets and cheaper access to imports will be complemented by better access to export markets. This argument applies to LDCs as well. As noted by Winters (1999), a useful mnemonic in this connection is WYDIWYG: what you do is what you get. When it comes to trade policy, the payoffs to negotiations and liberalization are primarily a function of domestic action—the extent to which own protection is reduced.[2]

[2] Fiscal constraints may imply that low-income countries need to maintain tariffs above the average prevailing in more advanced economies for revenue collection purposes. In such cases, countries should consider greatly reducing the dispersion in duty rates by moving towards a uniform tariff (Tarr, 2002).

Two sectors that matter greatly for developing countries are textiles and agriculture. Although the WTO Agreement on Textiles and Clothing requires the abolition of all textile quotas by January 1, 2005, tariff barriers to trade in this sector remain high. Highly distorting agricultural support policies in many OECD countries has a major detrimental effect on developing countries (discussed further below).

Market access has a number of additional dimensions. For example, reducing the uncertainty of access by disciplining the use of contingent protection could have a high payoff. The same is true of actions to reduce the trade diverting effects of RIAs. (The latter issue is discussed in Section 5.) The threat of safeguards and related policies (especially antidumping) reduces the value of trade liberalization to exporters. Antidumping has become a frequently used instrument in both industrialized and developing countries. Indeed, Finger et al. (2000) document that not only have developing countries become frequent users of antidumping, but on a per dollar of import coverage basis they are the most intensive users of antidumping (Table 4).

The existence of antidumping induces rent-seeking behavior on the part of import-competing firms, and creates substantial uncertainty regarding the conditions of market access facing exporters. Investigations have a chilling effect on imports (they are a signal to importers to diversify away from targeted suppliers) and are often facilitating devices for the conclusion of market sharing or price-fixing agreements with affected exporters (see Bloningen and Prusa 2002 for a survey of the evidence). The best policy in this regard has been known for a long time—abolish the instrument. Safeguards are a better and more honest instrument to address the problem antidumping is used for—providing import-competing industries with time to adjust to increased foreign competition (Finger, 1996). Greater discipline on the use of the instrument could involve determining the impact on the economy of imposing duties through so-called public interest clauses—current legislation and WTO rules only impose weak procedural disciplines on import-competing industries and do not give users of imports a voice. The problem is a political economy one: a necessary condition for reform is greater mobilization of countervailing forces in the domestic political arena.[3]

Table 4: Antidumping Initiations Per US Dollar of Imports 1995-99

Country/Economy Initiating	Against All Economies	
	No. of Antidumping Initiations	Initiations per US dollar of imports Index (USA=100)
Argentina	89	2125
South Africa	89	2014
Peru	21	1634
India	83	1382

[3] Given that no effort is usually made to determine whether markets are contestable, another way to reduce protectionist bias is for governments to put greater effort into determining whether the conditions alleged to give rise to 'unfair trade' actually exist. Suggestions that have been made in this regard include making antidumping conditional on a determination that the exporters home market is not contestable, and shifting away from an 'injury-to-competitors' standard towards an 'injury to competition standard' (Hoekman and Mavroidis, 1996).

New Zealand	28	1292
Venezuela	22	1174
Australia	89	941
Colombia	15	659
Brazil	56	596
Israel	19	418
Chile	10	376
Indonesia	20	330
Mexico	46	290
Turkey	14	204
Korea	37	185
Canada	50	172
European Union	160	130
United States	136	100
Malaysia	11	97

Source: Finger, Ng, and Wangchuk (2001).

There is a huge market access agenda in services trade, one that spans foreign direct investment as well as cross-border trade, and where to date only limited progress has been made in the WTO (Mattoo, 2001).[4] However, here again the greatest gains to developing countries would come from reforming their own policies—increasing the efficiency of service industries may generate welfare improvements that are a multiple of those associated with liberalization of goods trade. The reason is that in contrast to tariffs, services trade and investment restrictions do not generate revenue for the government. Instead, they tend to raise costs for users, imposing a 'tax' on the whole economy.[5] Liberalization of services is more complex than negotiating down tariff barriers, as it involves movement of people as well as foreign direct investment (FDI). A careful evaluation of services trade policy requires analysis of the conditions of competition in a particular sector and the need for regulation to achieve efficiency and equity.

In the area of services, market access and regulation are closely intertwined, and that it is necessary to address regulatory policies that impede effective entry into services markets. A key question is how to do so in the GATS context. Services are activities where there is often need for some type of regulation to address market failures or achieve social (noneconomic) objectives. Moreover, technological developments have major implications for the design of appropriate regulatory instruments to ensure both efficiency and equity. A good case can be made that many of the 'backbone' services that are critical to development—transport, energy, telecoms, finance—increasingly have become industries where network externalities are important. An implication is that regulation to ensure that markets are contestable needs to focus not only on 'traditional' types of entry barriers—outright bans, licensing, etc.—but on the ability to connect to the network at a reasonable price, apply the relevant technologies, etc. Designing and enforcing policies to achieve this is anything but trivial, suggesting a

[4] Walmsley and Winters (2002) estimate the global gains from allowing temporary entry of both skilled and unskilled labor services equivalent to 3% of the current workforce in OECD countries would be some 1½ times greater than the gains from merchandise liberalization.
[5] Stern (2002) surveys the literature.

cautious approach towards the setting of enforceable international standards in the WTO (see, e.g., Claessens 2002, Evans 2002 and Trolliet and Hegarty, 2002 for recent sectoral analyses). In many cases, regulatory thinking and economic analysis is still evolving rapidly when it comes to network industries, and technological developments may make specific types of interventions redundant or counterproductive. Careful assessments of the implications of alternative types of international cooperation—which may be regional rather than multilateral—are required to determine what options might be most appropriate for developing countries.

A final market access-related policy that cannot go unmentioned are subsidies. The Doha language calling for elimination of agricultural export subsidies is clearly of great importance for developing countries that have a comparative advantage in the products affected, both directly and indirectly. While attaining this objective will undoubtedly be difficult, the benchmark is clear and is a good one. The primary need is to establish a deadline to achieve it. Matters are more difficult when it comes to other subsidies. In principle, de-coupling subsidies from production makes sense, but in practice it will always be hard to achieve (enforce), given the plethora of potential instruments that can be used by governments. Even the EU—which goes far beyond the WTO in this area—has encountered recurrent difficulties in enforcing restrictions on the use of state aids within the Community. Given that there is a rationale for subsidies in many contexts and that the revealed preference of many governments to use subsidies, it would appear more effective to focus on reduction of border barriers and the abolition of explicit export subsidies. This would automatically impose serious constraints on the feasibility of production subsidies by greatly increasing their costs (Snape, 1987).

Also relevant in this connection is that from an economic perspective, border barriers matter more than subsidies, not least because this is the primary type of intervention used by developing countries. For example, Hoekman, Ng and Olarreaga (2002b) find that for both the LDC group and other developing countries a 50 percent tariff cut will have a much greater positive effect on exports and welfare than a 50 percent cut in subsidies, even if the analysis is limited to the set of commodities that are currently subsidized by at least one WTO member. This does not imply that negotiations can neglect domestic support policies. Most developing countries oppose further agricultural trade liberalization in an environment that is characterized by continued large-scale support for OECD farmers. Past experience has demonstrated that the gains from own liberalization are attenuated because of the market segmenting effect of OECD subsidy policies. Indeed, own liberalization in some instances—e.g., India—has proven to be politically unsustainable as farmers are subjected to large world price swings and import surges of subsidized commodities (Gulati and Narayanan, 2002). Substantial reduction in OECD agricultural support policies is therefore not just important for developing countries in its own right—in that it generates direct benefits for the many economies that are (potential) net exporters—but is critical from a political economy perspective. It is necessary to create the conditions to allow developing country governments to pursue domestic reforms. That is, subsidy reforms in OECD countries are necessary, although not sufficient, for developing countries to maximize the gains from the current WTO negotiations on agriculture, as this will require own liberalization.

3.1 Focal Points and Negotiating Modalities

Because developing country exports are disproportionately affected by tariff peaks (products subject to peaks represent 15 to 30 percent of total LDC exports to the US, EU, Japan and Canada), their elimination should be high on the WTO agenda. A challenge for developing countries in the coming months is to determine what type of negotiating modality would be most beneficial in addressing tariff peaks and escalation. Given that in many developing countries the ratio between peak and average tariffs is five—including in Sub-Saharan Africa—compared to an average of 40 in OECD countries (see above)—a target that might be considered is that all countries should bring down this ratio to less than five. This would be directly beneficial to developing countries in market access terms by reducing peaks and help improve efficiency by lowering the dispersion of effective protection in WTO Members. It would also have indirect benefits. Assume a benchmark is also agreed for a reduction in the average level of tariffs—say 50 percent, as in the Kennedy Round. Then, as the average tariff declines, the maximum tariff would also have to decline, indirectly providing further benefits to countries with limited ability (market power) to negotiate tariffs down on their exports through request-offer bargaining (Hoekman and Olarreaga, 2002). This is a major advantage of a formula-based negotiating process.[6]

The use of tariff-cutting formulae such as the one just discussed can be an effective means of moving towards greater uniformity of national rates of protection, which is very desirable from a development perspective (Tarr, 2002). While the request-offer approach used in the Uruguay Round reduces average levels of protection, it can easily increase the variance in protection and gives greater negotiating leverage to large countries. Formulae approaches to reduce dispersion in protection and move higher rates down more than lower ones were used in the Tokyo Round (1973-9), as well as earlier rounds. The experience with the use of formulae illustrates that this is a viable technique, but that the outcome depends substantially on the magnitude of exemptions that are invoked by countries. In order to achieve greater uniformity of protection as well as a decline in the average MFN rate, exceptions must be kept to a minimum. Monitoring and quantification of the implications of proposed exceptions is an important task for national policy researchers.

A major issue for developing countries is to obtain 'credit' for autonomous liberalization. In the past, efforts to obtain such credit did not succeed in part because negotiations center on tariff bindings, and developing countries bound only few tariff rates (reflecting the non-reciprocity strategy that was a pillar of the special and

[6] As first noted by Finger (1974, 1976), in GATT negotiations the 'concessions' offered by countries to each other were largely on items on which they were the 'principal' supplier, that is, there was a large degree of internalisation of the benefits measures in trade volume terms. In the Uruguay Round, Finger found that the balance of concessions made and obtained, again in a mercantilist sense, was skewed towards high-income countries (Finger, Ingco and Reincke, 1996).

differential treatment status) (Michalopoulos, 2001). The shift to full participation by developing countries implies that they have a lot to offer in terms of binding past unilateral liberalization—essentially the difference between applied rates and the much higher ceiling bindings or complete absence of bindings scheduled under the WTO. The problem confronting developing countries is that despite arguments that there is value to binding tariffs at levels above applied rates (see Francois and Martin, 2002a), in practice mercantilist negotiators are unwilling to 'pay' much for such bindings.[7] Instead, they want to see reductions in applied rates.

The challenge then is to design a mechanism that increases the mercantilist value of binding in the WTO negotiating context. One way to do this is to incorporate this in the formulae used for negotiation and the benchmark that is used to assess the outcome. Given that OECD countries have already bound virtually all their tariff lines at applied rates, any formula that gives weight to both *additional* bindings (increases in the ratio of the number of bound to unbound lines) and reductions in the absolute difference between bound and applied rates, will automatically give credit to developing countries in terms of attaining an agreed target level of liberalization. What this implies is that formulae need to focus on *bound* rates and not (or at least not exclusively) on applied tariff rates (cuts in average applied rates).[8] While a good case can be made that moving towards full binding and reducing average bindings has value, in practice developing countries are likely to have to make additional commitments to obtain a beneficial formula. As argued above, one area where they have a lot to offer is in the area of access to service markets.

Services. For the service negotiations, market access benchmarks and formulae to achieve them can also be developed. Given that there is only limited coverage of the sector-specific commitments on national treatment and market access in the GATS, the simplest benchmark would pertain to the sectoral coverage ratio and/or the number of sectors where no restrictions on national treatment and market access are maintained (Hoekman and Kostecki, 2001). For many developing countries the coverage of specific commitments is well below 25 percent of all services and modes of supply. Binding the status quo would help reduce uncertainty, while pre-committing to future reform can help increase the relevance of the GATS. Given the importance of movement of natural services providers as a mode of contesting foreign service markets for developing countries, explicit quantitative targets for 'mode 4' visas could be considered—for example, a minimum share of total service sector employment (Walmsley and Winters, 2002). Even if not used as the focal point for negotiations, this can be a metric for judging the outcome of negotiations.

There is an important political economy dimension to services liberalization. Because services often cannot be traded, increasing access to domestic service markets is likely to require the entry of foreign competitors through FDI. This will not only lead to the introduction of new technologies, but also (and in sharp contrast to what

[7] See Mattoo and Olarreaga (2000) and Michalopoulos (2001) for discussions of credit.

[8] A necessary condition for a formula approach to work is that all countries bind all tariffs at some level. Francois and Martin (2002b) propose a specific modification of the so-called Swiss formula (used in the Tokyo Round) for the Doha negotiations and explore the implications of alternative specifications. For general discussions of formulae, see Panagariya (2002).

happens with merchandise liberalization) entail demand for *domestic* labor. Foreign telecommunications or electricity operators, foreign banks or retailers, all need local labor. Thus, while liberalization (allowing foreign entry) inevitably will result in the restructuring of domestic industry, services reform has less far-reaching implications for sectoral turnover and aggregate employment than the abolition of trade barriers for merchandise.

Services reforms can also have a large indirect payoff by facilitating merchandise trade liberalization. The latter will invariably result in contraction/adjustment of domestic industries that benefit from protection, while industries in which the country has a comparative advantage will expand. Many of the latter initially are likely to be small and dispersed, whereas the former are likely to be concentrated. Thus the well-known political problem of building support for trade liberalization—those that stand to lose often will have a substantially stronger political voice as they have more information and more of an incentive to organize. Often it will not be known beforehand which sectors and activities will become growth areas—hence an additional lag between those who will lose and those who will gain from liberalization. This makes the early transition process politically difficult.

Such political constraints to trade liberalization may be relaxed by reforms targeting the service sector. Pro-competitive reforms that facilitate entry by new firms can generate employment opportunities for skilled and unskilled workers who currently are employed by government or import-competing private manufacturing, or who are unemployed. Indeed, a political precondition for public sector downsizing is likely to be that there is a perception that alternative employment opportunities will be created. The small-scale private sector must play a major role in this process, which in turn requires markets that are contestable. Of great significance from a political economy perspective is that industries that use services as inputs will all gain from measures that reduce service costs and increase their quality and variety. Thus, agricultural and manufactures producers should support service sector reforms.

This is important, as services liberalization efforts can rely less on reciprocal, market access-based negotiations. Reciprocal opening can play less of a role in services because little support for reform can be expected to emerge from (potential) exporters of services and because non-border protection is dominant. The former implies that in many developing countries opposition to services reform and liberalization cannot be counterbalanced by export interests seeking better access to foreign service markets; the latter implies that trade negotiators do not have equivalent focal points and the necessary information to employ the tools of their trade in a manner that guarantees the outcome is welfare improving. At issue in the services context are generally regulatory regimes that cannot (should not) be altered in incremental ways. In contrast to tariffs which can be changed smoothly and continuously, regulatory regimes are often "lumpy"—any change will generally be discrete. In short, the onus will be on identifying reforms that are in the national interest—a process that must be undertaken and led by central decision-makers.

Regulatory reform is a complex and complicated process. The design of policy reforms should start with a proper definition of the "relevant market" that is affected.

For instance, liberalizing air transport without liberalizing airport slots does not lead very far: the price of air tickets will mirror *both* competitive pressures in terms of routes (if there are several airlines in presence, which is not necessarily the case) *and* monopoly rents related to airport slot monopolies. Another example is maritime transport— Francois and Wooton (2000) estimate that the welfare gains from trade liberalization (better access to markets) may be doubled if complementary actions are taken to increase competition in the shipping sector. Concerted action in the context of a WTO agreement may facilitate services reforms by establishing benchmarks and focal points, ensuring the high-level attention that will be needed by senior decision makers and political leaders, engagement by civil society and a mechanism to "lock-in" a reform path.

4. WTO RULE MAKING, IMPLEMENTATION AND ENFORCEMENT

The Single Undertaking approach in the Uruguay Round led to the inclusion into the WTO of rules in many areas of a regulatory nature. This was the culmination of a process started in the Tokyo Round (1973-9). It shows few signs of abating. Negotiations are to be launched in 2003 on competition law, FDI policy, transparency in government procurement and trade facilitation, assuming agreement is reached on the modalities. Efforts are also likely to expand the ambit of the WTO in areas such as environmental policy. Such regulatory issues have become more prominent on the WTO agenda because the liberalization of traditional trade policy instruments increased the visibility of differences in national regulatory regimes. Calls for deeper integration at the multilateral level range from coordinated application of national policies to the harmonization of regulatory regimes. Such harmonization is sometimes held to be necessary to ensure 'fair trade' or an equality of competitive opportunities for foreign and domestic firms.

A key question from a development perspective is to determine the rationale for proposals to pursue deeper integration, and, if so, whether the WTO is the appropriate forum for this. In this connection one key criterion is to determine whether a particular regulatory policy is being—or can be—used to restrict market access. Thus the traditional WTO criterion for inclusion of an issue on the agenda: whether a policy is trade related, i.e., impedes market access or distorts competition on a third market. Regulatory measures can be a substitute for explicit barriers (e.g., product standards, regulation of interconnection prices in telecoms, transport safety standards, access slots to sea and airports, and so on). In principle, multilateral rules on preventing protectionist abuse of such regulatory standards can be warranted in order to ensure market access. Such rules may lead to reciprocal benefits similar to traditional trade liberalization: greater contestability of domestic markets and improved market access abroad (regulatory barriers in developed country markets can have major implications for developing country exporters. The challenge is to ensure that rules do not constrain the ability of nations to achieve their regulatory objectives, i.e. to separate what is legitimate regulation from protectionist abuse (needless discrimination).

In theory, an unbiased 'necessity test' could be envisaged as a way to do this—i.e., a mechanism to determine whether a specific policy is necessary to achieve a particular objective (Mattoo and Subramanian, 1998). However, in practice, it is difficult to conceive of making this binding, given the associated need for litigation and intrusive determinations by external agents such as WTO panels. Consequently, some kind of sectoral guidelines or limited harmonization may be unavoidable. In practice, as much of the regulatory agenda pertains to service industries, this is an area that will need to be addressed in the GATS context. The challenge will be to ensure that the focus is indeed on regulatory measures where the link to explicit barriers (market access) is clear-cut. In cases where it is not or where there is a very asymmetric balance of interests, harmonization will often not be desirable in any event, and questions should be raised regarding the appropriateness of including the policy area in the WTO.

From a development perspective there are at least two additional considerations. It is often argued that a major function of international agreements is to overcome domestic political economy constraints that prevent the adoption of welfare-improving policies. Thus, one can ask whether proposed regulatory rules make sense from a national perspective in terms of addressing priorities even if there are no externalities or market access considerations. Another question is whether there are overall benefits from engaging in negotiations on subjects that are not deemed to be priorities, because of expected payoffs in other areas. That is, does it make sense to pursue linkage strategies?

Conceptually, both questions are straightforward. In practice, answering them is very difficult and will require pro-active engagement by national stakeholders and extensive policy research. Both questions go to the heart of the political economy problem confronting developing countries in the Doha Development Agenda talks: how to mobilize constituencies at home *and* abroad that will support market access liberalization and the adoption of development supportive WTO rules. The linkage question boils down to how to design a socially beneficial grand bargain scenario—what can and should be offered in the context of WTO talks in order to obtain a desirable outcome? Determining the *net* national benefits of a package of proposals requires taking into account losses incurred by losers as well as benefits to those who gain, as well as the need for (and cost of) compensation mechanisms. Benefits will depend on the payoff to own reforms implied in the package, and the value of the package to trading partners. The latter will determine the feasible quid pro quo in terms of trading partner concessions on market access and on rules. This in turn will be a function of the intensity of interest and the (lobbying) power of affected groups that the foreign negotiators care about—their multinationals, NGOs, unions, etc.

WTO negotiations on 'behind-the-border' policies have proven to be more complex than traditional market access talks because it is much more difficult to trade 'concessions'. The focus therefore tends to be on identification of specific rules that should be adopted by the WTO (Hoekman and Kostecki, 2001). Given disparities in economic power and resources, the focal point of discussions tends to be the status quo in high-income countries. This may be fully consistent with development priorities of low-income countries, but there is no presumption this will be the case. Developing country worries regarding the rule-making dimensions of the WTO became increasingly prominent in the 1990s (Oyejide, 2000). Concerns centered on the costs associated with implementation of certain WTO agreements and the absence of adequate financial assistance; the failure of high-income countries to deliver promised 'special and differential' treatment to developing countries; and, more fundamentally, perceptions that some of the rules of the game constrain national efforts to increase economic growth. Table 4 provides a subjective 'birds-eye view' of the development and implementation dimensions of major WTO disciplines.

Table 4: Development Dimensions of Major WTO Rules and Disciplines

Agreement on:	Encourages moves towards good policy?	Significant direct implementation costs?	Significant corollary investment required (indirect costs)?
Transparency	Yes	No	No
Tariff reductions	Yes	No	No
Tariff binding	Yes	No	No
Customs valuation	?	Yes	Yes
Classification (HS)	Yes	Yes	No
Production subsidies	?	No	No
Export subsidies	?	No	No
Quotas	Yes	No	No
Balance of payments	No	No	No
Antidumping	No	Yes	No
Countervail	No	Yes	No
Emergency protection	?	Yes	No
GATS	Yes	No	Yes
TRIPS	?	Yes	Yes
Technical barriers	Yes	Yes	Yes
SPS measures	Yes	Yes	Yes
Agriculture	Yes	No	No
Import licensing	Yes	No	No
Rules of origin	Yes	Yes	No
State trading	Yes	No	No
Regional integration	Yes	No	No
Textiles & clothing	Yes	Yes	No

Note: See Hoekman and Kostecki (2001) for a motivation of the normative assessments; McCulloch, Winters and Cirera (2001) for an analysis of the likely poverty impact of WTO rules.
Source: Hoekman (2002a).

Post-Uruguay Round research—in particular Finger and Schuler (2000)—revealed that the costs associated with complying with certain WTO disciplines—e.g., on customs valuation—can be significant. This is not so much because of the rules themselves, but because of the ancillary investments that are required to allow the rule to be applied. As mentioned, because WTO rules are often based on those prevailing in OECD countries, implementation costs are asymmetrically distributed. This does not necessarily imply that WTO rules are bad from a development perspective—but making them work in low-income countries may require wholesale reform and strengthening of a variety of institutions. The resources required for implementation, if substantial, might be better used for alternative purposes (Finger and Schuler, 2000). This is an important point, one that has yet to be fully internalized by many WTO members. Dealing with this and identifying beneficial issue linkages requires much greater participation and ownership of agreements. Indeed, this a key dimension of the political economy challenge confronting governments—ensuring that there are stakeholders that support the process.

4.1 Towards Greater Ownership: Participation and Transparency

The Uruguay Round marked a change in the attitudes of many developing countries regarding the trading system. From being largely uninvolved and reactive, many became active participants in the negotiating process (Tussie and Lengyel, 2002). This did not prevent many countries from being confronted with what they came to regard as bad outcomes. Participation is not enough; to be effective it requires a clear understanding of national objectives and priorities, and how multilateral agreements can help achieve them.

In many regulatory areas, the trial and error experience—the assessments of the real-world impacts of alternative policy options—that can inform the design of multilateral rules that support development does not exist (Finger, 2001). This lack of experience makes it difficult to establish lines of communication between policymakers and domestic constituents that have interests that can be pursued through multilateral talks—be it domestic reform or policy changes in partner countries to enhance market access. Industrialized country policymakers are generally well informed (lobbied) by domestic interest groups. Most developing countries have much weaker linkages with stakeholders, impeding their ability to build the political support needed for welfare-improving reforms.

Greater 'ownership' of the WTO requires that multilateral agreements be seen as helpful in order to attain national objectives. Getting it right in a technocratic sense is not sufficient; there must be strong local support for what is (being) negotiated. As interests will differ and often will be inconsistent, mechanisms to allow the resulting distributional conflicts to be resolved in a transparent fashion are needed (Rodrik, 2002). This is not straightforward to achieve, given that trade policy is inherently a nontransparent redistributive policy instrument, and is often used for that reason. A vital element in promoting better policies is transparency and access to information. Much of the focus of attention in this regard has been on enhancing the transparency of WTO operations and improving access to—and dissemination of—WTO databases, reports and information. While this is important—for example, better access to data underlying WTO trade policy reviews and public access to databases on tariff bindings would help think tanks, firms and NGOs engage in the domestic policy formation process (Francois, 2001)—it is necessary that the required analysis is done by stakeholders. It is a truism that to reduce protection and resist protectionist pressures those that lose (pay) need to be aware of the costs of such policies if they are to defend their interests.

Even if the requisite analysis is undertaken and is reflected in domestic policy debates and the formulation of national positions, a precondition for defending these interests is effective representation in Geneva. Many low-income countries do not have a presence at the WTO, impeding active engagement in negotiations. Indeed, many have yet to become a member. Although options have been identified to expand representation in Geneva at relatively low cost—for example, Blackhurst, Lyakurwa and Oyejide (2000) propose transferring national representatives from UN bodies to Geneva and more intense cooperation among members of regional integration arrangements—there is limited expertise available in most countries. A case can be made that funding should be made available to allow low-income countries to hire experts to assist governments to undertake the required analyses (Winters, 2001). Such advice and expertise needs to be available on a long-term basis to policymakers on a country-by-country basis. Given that there are dozens of countries requiring assistance (the LDC group alone already numbers 49), the needs in this area are significant.

Another constraint is that countries may find it difficult to engage effectively even if they have a presence (have representation). Traditionally, contentious issues on which deals must be struck are thrashed out in so-called Green room meetings, comprising the major OECD members and a small number of developing countries. At the Seattle ministerial meeting many developing countries that were excluded from critical Green room meetings felt that they were not being informed of developments or granted the opportunity to defend their views. In Doha, a 'Committee of the Whole' approach was followed, under which all interested WTO members were invited to participate in plenary meetings, as well as in six working groups dealing with the major outstanding issues whose chair persons reported regularly the committee of the whole (heads of delegations). This 'hub-and-spoke' system worked reasonably well and was a major improvement over Seattle. However, this approach is not possible on a day-to-day basis, i.e., does not resolve the Geneva representation issue.

Proposals have been made periodically to replace the informal Green room process with a formal mechanism that allows all countries to be represented—e.g., a formal, non-decision-taking Consultative Board with rotating membership that would operate in instances where Green Room meetings cannot accommodate all WTO members (Blackhurst, 2001). The objective of the Board would be to put forward (non-binding) recommendations to the entire membership. To date, no progress in this direction has proven possible in the WTO.

One important positive development in this area has been increased cooperation among developing countries—and cooperation between like-minded developing and developed countries—to submit joint positions and proposals. Such agenda setting coalitions are one way of overcoming some of the constraints noted above.

4.2 The Regulatory Agenda and Issue Linkage

A lesson from the Uruguay Round is that multilateral efforts to harmonize regulatory policies should be scrutinized carefully. Another lesson is that the WTO is not necessarily the right focal point for harmonization efforts. There are many organizations and bodies that seek to determine good practices and establish international norms for regulatory policies. Examples are international product standards set by the International Organization for Standardization, phytosanitary norms established by the Codex Alimentarius Commission, financial standards created under auspices of the Bank for International Settlements and good practices in customs clearance defined by the World Customs Organization. In all these cases the norms concerned are not arrived at through a negotiating process where market access is made conditional on the adoption of specific norm. Instead, cooperation is driven by the self-interest of countries, and implementation is gradual, depending on national circumstances and capacity, assisted by the relevant international institutions as well as bilateral donors. There is generally no binding dispute settlement mechanism or threat of sanction for non-implementation. The latter factor is of course a major reason why sectoral interest groups propose regulatory standards for inclusion in the WTO. However, there is a great danger in overloading the institution and reducing its legitimacy and support by using it as an enforcement agency for voluntary, 'good practice' norms developed by other technical and specialized bodies.

As mentioned, one reason regulatory issues are put on the agenda is that this allows cross-issue linkages in WTO negotiations. While this increases the potential gains from negotiation (see Hoekman and Kostecki 2001 for a guide to the literature), a necessary condition for this is that the implications of alternative deals are understood, and that trade is an appropriate instrument of enforcement. When it comes to 'new' issues on which developing countries have little experience, it may be difficult to determine whether a 'grand bargain' will have a net positive social payoff. This is a major reason why developing country negotiators have often been risk averse in GATT/WTO negotiations and sought to avoid issue linkage. At the same time, lack of information and good analysis can also result in missed opportunities to use linkage to achieve better policies at home or in trading partners—ignorance discourages actions that may be beneficial. Determining the expected cost-benefit ratio of proposed agreements is therefore important. So is assessing whether it makes sense to use trade as an enforcement device—something that depends on how 'trade-related' an issue is.

Regulatory policy areas where WTO negotiations have been proposed for some time include industrial, investment, competition, trade facilitation and public procurement policies. In Doha, it was agreed that negotiations on the last four of these so-called Singapore issues "will take place after the Fifth Session of the Ministerial Conference on the basis of a decision to be taken, by explicit consensus, at that Session on the modalities of negotiations." Discussions on industrial policy are ongoing in the context of implementation and 'special and differential treatment' concerns. The WTO already imposes a number of disciplines, including on subsidies and local content policies. These have implications for the design of export processing zones and other export incentive schemes, and governments need to ensure that WTO rules in these areas do not restrict their ability to pursue good policies. The basic question as far as the four Singapore issues are concerned is similar: whether and how multilateral disciplines could help promote the adoption of good policy in each area. While space constraints prevent discussion of the substantive issues that arise,[9] a key factor determining the development-relevance of agreements will be the extent to which policies of trading partners that are harmful to poor countries are addressed—e.g., OECD antitrust exemptions for export cartels and investment incentives. The less this is the case, the weaker the rationale for using the WTO as opposed to other non-binding fora as a vehicle for multilateral cooperation. Many question whether multilateral disciplines on issues such as investment or competition will address development priorities. Simply participating in discussions and negotiations on such issues requires the use of scarce administrative resources, and therefore has a potentially high opportunity cost (Winters, 2002). If the primary reason to negotiate

[9] For a discussion of these issues, see Hoekman and Kostecki (2001) and the references cited there.

on such policies is for purposes of issue linkage, efforts may be better directed at other areas—starting with market access.

4.3 Implementation of Agreements

Even if WTO agreements have strong support ('ownership') in developing countries, implementation may be costly. Doing more to assess the impacts of agreements *ex ante*, including a costing out of investment requirements, would help avoid difficulties *ex post*. The challenge here is to allow for development concerns to be taken into account in instances where resource constraints prevent effective implementation of WTO agreements that were deemed at the time of negotiation to be beneficial.[10] What is required is a type of safeguard mechanism that allows implementation problems to be considered in the context of a nation's overall development strategy.

The approach that is currently pursued in the WTO with respect to implementation problems is primarily agreement-specific, generally involving requests for extension of transition periods in relevant WTO bodies. This approach does not allow for an assessment of needs in the context of the overall development strategy of the countries concerned and does nothing to place trade issues in the context of the country assistance strategies of international financial institutions and bilateral donor assistance agencies.

One option could be to make transition periods a function of national circumstances. This is already done to some extent—the WTO makes a distinction between least developed and other developing countries and grants the former longer transition periods and greater 'special and differential' treatment. This is rather arbitrary in that it ignores differences across countries. A better approach would to link implementation of resource-intensive agreements to the provision of development assistance, and adopt an arbitration approach to implementation disputes that involve low-income countries. Such arbitration could be based on an independent 'implementation assessment' at the request of governments who have been unable to meet WTO norms. This would involve a determination of what is required to implement the agreement(s) in a way that makes sense from an economic perspective (including a costing out of necessary ancillary reforms and investments), the time frame that would be required given sequencing considerations and institutional capacity, and an assessment of the adequacy of the financial assistance that has been offered by donors.[11] The assessment, which would need to be transparent and objective, might be undertaken by a panel of development experts in consultation with

[10] It should be emphasized that the focus of what follows is on agreements that were deemed to be desirable cannot be implemented as envisaged due to a lack of resources or absence of complementary reforms and institutional strengthening. Agreements that can be implemented 'by decree' —e.g., changes in tariffs or reductions in subsidies—would not eligible for the approach described. There the need is to ensure that commitments are welfare improving in the course of negotiations.

[11] Such assessments could be informed by national development frameworks such as the Poverty Reduction Strategy Paper (PRSP) in the case of low-income economies, as these establish development priorities on a country-by-country basis (see www.worldbank.org for a description of the PRSP process). For LDCs, the priorities identified in Integrated framework diagnostic studies could be a benchmark (see below).

national economic policymakers, reporting to the WTO Committee on Trade and Development.

A mechanism of this kind could help foster greater policy 'coherence' by providing a vehicle to discuss how WTO disciplines requiring the investment of scarce resources can be implemented consistently with a country's development strategy.[12] The objective would not be to allow for open-ended opt-outs and to avoid situations where implementation periods are repeatedly pushed back following requests for extension. The approach would generate information on the constraints that prevail, and the adequacy of the assistance that has been provided or offered. By providing a forum for the development and trade communities to interact on implementation issues, it could help both developing and donor countries improve internal policy coherence.

4.4 Enforcement of Agreements

Issues relating to the cost of satisfying WTO rules and non-fulfillment of assistance commitments by trading partners are only one part of the implementation agenda. Another concerns enforcement of rights and obligations. Low-income countries may have difficulty doing so through the WTO dispute settlement system.[13] Political realities—e.g., threats of cross-issue linkages and retaliation outside the WTO—may constrain the ability (willingness) of governments to assist national firms defend their WTO rights. Poor countries may also find it more difficult to determine when trading partners use WTO-illegal policies to harm their interests, and often will find it hard to credibly threaten retaliation.

Various suggestions have been made to deal with this potential problem. One is to reduce the burden for individual countries to take action by establishing an independent Special Prosecutor or Advocate. This entity could be granted the mandate to identify potential WTO violations on behalf of developing countries. Such outsourcing of 'discovery' could help leverage the activities of the Advisory Centre for WTO Law—which started to provide legal counseling services to developing countries in late 2001[14]—by addressing both the resource constraints and the incentive problems (fear of cross-issue linkage) that may impede developing country governments from pursuing cases. Although limited to a transparency function, this can lead to significant moral pressure to bring measures into conformity with the WTO.[15]

[12] See also Prowse (2002).
[13] For an in-depth discussion, see Hoekman and Mavroidis (2000).
[14] It does so at below-market rates, based on donor provided resources (see www.acwl.ch).
[15] Historically, this 'Dracula principle' (Bhagwati 1988) has been an important factor in inducing WTO members to abide by the rules of the game.

5. PREFERENCES AND REGIONAL INTEGRATION

Unilateral actions by industrialized countries can improve the 'terms of trade' of low-income economies—through duty-free and nontariff barrier free access to markets and elimination of aspects of investment, competition and related policy regimes that are detrimental to developing countries. For many products exported by low-income countries, tariffs in high-income countries are zero as a result of GSP schemes. However, trade preferences for developing countries tend to be limited for tariff peak items as these are by definition 'sensitive' products that are often excluded or subject to some type of quantitative limitation.

The decision by the EU in 2001 to grant LDCs duty- and quota-free access for all products has changed matters. Full elimination of market access barriers can help boost investment incentives and expand trade-related employment. Emulation by all OECD countries of the EU initiative would therefore be beneficial to these countries—potentially increasing LDC exports by over 10 percent.[16] As LDCs account for only 0.5% of world trade, offering these countries duty free access will have only a very limited effect on total imports into OECD nations—suggesting that adjustment pressures will be small. Of course, preferential access for LDCs will have detrimental trade diversion effects for other low-income countries, although the very small share of the world market that is held by LDCs suggests such effects will be small in relation to total non-LDC exports. It is also the case that because LDCs have no market power in negotiating down foreign trade barriers—where tariff peaks can be over 100 percent—they cannot play the WTO reciprocity game.[17]

A major issue for the WTO that is created by preferences is the fear of preference erosion—an opposition to MFN liberalization by OECD countries because it will reduce the value of the preferential access that has been granted. The validity of this fear depends on the value of existing preferences. A case can be made that this is low, given that sectoral or product-specific exceptions and limitations, the threat of antidumping and safeguard actions, restrictive rules of origin and product standards may effectively nullify duty-free access. Liberal rules of origin are critical for preferences to be meaningful. Rules of origin are generally recognized to be a major factor reducing the value of preferences. Brenton and Manchin (2002) demonstrate that EU rules of origin are so restrictive as to induce between 35 and 45 percent of Central and East European exports of clothing—which in principle have complete duty-free access to the EU—to enter the EU under a special customs regime, so-called outward processing. This allows them to avoid documenting that rules of origin have been met, because the regime applies to products that use EU inputs. Similarly, Mattoo, Roy and Subramanian (2002) conclude that restrictive rules of origin greatly reduce the benefits for recipient countries resulting from the US African Growth and Opportunity Act.

[16] Ianchovichina, Mattoo and Olarreaga (2000); UNCTAD (2001).

[17] The best policy would be to remove all barriers on products in which developing countries have a comparative advantage on a nondiscriminatory basis. As mentioned previously, this is unlikely to be feasible on a unilateral basis, given that a number of low-income countries are significant exporters—it will need to be pursued on a reciprocal basis in the WTO.

The downsides of preferential trade are well known. They are uncertain, subject to unilateral change or withdrawal, and can give rise to serious trade diversion. Similar problems as far as excluded countries are concerned are raised by preferential trade agreements. For the 'non- or less-preferred'—those without GSP or better status—the challenge is to reduce discrimination and the global welfare reducing trade diversion associated with preferential trade. The same is true for regional preferences. Regional integration agreements are a more permanent feature of the trade policy landscape. As argued in World Bank (2000), North-South RIAs can be particularly beneficial to developing countries if these are associated with additional development assistance that aims at improving trade capacity and related institutions, have very few (ideally no) exemptions in terms of product coverage, and include trade in services. While RIAs presumably are on net positive for members—otherwise, why join?—the problem is that they can easily be detrimental to excluded countries, giving rise to adverse terms of trade effects as well as so-called investment diversion. A major function of the WTO in this regard is to provide a mechanism to ensure that such effects are attenuated through periodic rounds of liberalization of trade in both goods and services.

5. MULTILATERAL CO-OPERATION: 'AID FOR TRADE'

A precondition for domestic 'ownership' of trade policy reforms is that there are constituencies that have an incentive to see specific reforms and commitments implemented and enforced. Support for country-specific efforts to identify reform priorities and infrastructure needs (both software and hardware) is an important dimension of this, as is identification of policy options and their distributional and growth impact, and, critically, mobilization of finance to address the priority bottlenecks to trade and employment expansion. Numerous trade-related challenges confront many developing countries. Examples include meeting export market product standards, protecting intellectual property, regulating service industries, improving trade logistics and customs clearance, and, upgrading transport, communications and other basic infrastructure services. All of these policy areas are important elements of the overall investment climate and determinants of trade capacity. In all such areas external development assistance can do much to help address priority needs.

As illustrated by Table 6, there are potentially many issues on the trade capacity agenda and many agencies that can provide assistance. What is needed are concerted efforts to mobilize additional financial and technical assistance ('aid for trade'), channeled through development institutions, specialized bodies and the private sector. A pre-condition for this to occur is that demandeur countries place trade-related assistance high on their agendas. The development assistance agenda spans much more than trade, implying that a first step is to establish that trade is a priority. Whether building trade capacity rather than investing in other areas—such as health or education—is appropriate is a policy decision. The challenge for national policymakers is to identify the areas where the net social return to domestic action is highest; the challenge for the development community is to assist countries to do this and to provide support in the areas that are identified.

Table 6: Elements of the Global Trade Architecture for Development

Issues	**Multilateral cooperation**			**Unilateral actions**	
	WTO	**North-South RIAs**	**Specialized bodies**	**DC**	**IC**
Market access	A	A	S	A	A, S
Rule making					
Trade-related policies	A	A	S	A	A, S
Non-trade policies		A	A, S	A	A, S
Supply-side initiatives					
Trade capacity development		S	S		S
Institutional reform/strengthening:					
Customs		S	A, S	A	S
Tax administration		S	A, S	A	S
Standards, certification		S	A, S	A	S
Intellectual property		S	A, S	A	S

Enforcement of agreements	A	A	S	A	A, S
Services:					
Infrastructure upgrading		S	A, S	A	S
Regulatory development		S	A, S	A	S
Design of economic policies		S	S	A	A
Social policy; redistribution		S	S	A	A

Notes: RIA: regional integration agreement; A — issue is a responsibility of a government or in the mandate of an international organization; S — support can be (is) provided by relevant entity to developing countries; DC: developing countries; IC: industrialized countries.
Source: Hoekman (2002a).

Assistance is now being provided to LDCs under the auspices of the Integrated Framework (IF) for trade-related technical assistance, a joint effort of six international agencies (IMF, ITC, UNCTAD, UNDP, World Bank and WTO), bilateral donors and LDC governments to do this. The aim of the IF is to work with LDCs to undertake diagnostic studies to identify barriers to integration, assist countries determine if and how trade issues should be integrated into the national development strategy and then provide a mechanism through which donors and agencies follow-up with trade-related technical and financial assistance to address the priority areas for action that are identified. Complementary mechanisms to identify trade-related assistance priorities include the Poverty Reduction Strategy paper in non-LDCs, regional integration arrangements, the African Union, and NEPAD. Given the Monterrey commitment to expand development assistance resources should be available—what is needed is to channel some of those additional resources to address trade capacity constraints.

Capacity building should extend to support of analytical and operational research at the country level, aimed at mobilizing constituencies that have an interest in domestic policy reform and using multilateral initiatives to pursue this. Capacity-building programs to assist national stakeholders define trade policy reform priorities and objectives must be country-driven and target think tanks, key NGOs, parliaments and the private sector, as well as government officials. External policy advice and diagnostic studies can help in this process, but what matters fundamentally is active engagement in the policy formulation process by national stakeholders outside the public sector.

6. CONCLUSION

In concluding, it is useful to summarize some of the negative aspects of the current international architecture for developing countries:

- The prevailing pattern of protection in the world today is biased against the poor in that barriers are highest on goods produced by poor people—agriculture and unskilled labor-intensive manufactures and services (World Bank, 2001);
- Interest groups are increasingly seeking to use trade as a tool to enforce rules for non-trade policies;
- Capacity constraints—both at home and in the WTO—impede developing countries from defining priorities and ensuring that WTO agenda items and multilateral rules reflect their interests;
- Given that negotiation and implementation of agreements can be costly, there is a danger of 'resource diversion' away from development priorities as the negotiating agenda expands;
- There is an excessive reliance on litigation to enforce agreements, enhancing fears of engagement and accepting to discuss new issue areas.

From a development perspective, a strong case can be made that the focus in the WTO should primarily be on market access liberalization in both industrialized *and* developing countries for goods and services. Much remains to be done, not only in reducing tariffs, but in dealing with nontariff measures such as antidumping, restrictive product standards, in liberalizing trade in services and disciplining the use of agricultural support policies. Elimination of industrial tariffs by OECD countries before a specific date, a major reduction in agricultural tariff peaks and escalation through the use of a formula of some type, a deadline for the phase-out and banning of export subsidies, and a significant expansion of service sector commitments, including mode 4 service supply opportunities would do much to eliminate the 'development credibility' deficit of the WTO.

Strong resistance by lobbies in OECD countries against liberalization of agriculture and labor-intensive manufactures implies that active use of the engine of reciprocity will be needed. Given the relatively high barriers to trade in goods *and* services in developing countries, they have a lot to bring to the table in a mercantilist sense. Indeed, there should be more than enough to 'trade' in the market access areas. An implication is that negotiations on issues such as investment and competition may not be necessary in terms of making progress on market access and should be considered on their own merits. Flexibility will be needed in setting rules in such areas if WTO members move down this path. If multilateral obligations are to assist in, and not detract from, the realization of development objectives they must be 'owned' by stakeholders in developing countries. For the development community this implies priority should be given to strengthening the capacity to identify national priorities and to analyze the costs and benefits of proposed agreements in light of those priorities.

Of fundamental importance is to improve domestic policies, strengthen institutions and enhance domestic supply side trade capacity to benefit from improved market access. The latter has numerous dimensions—many of which play a major role in defining the investment climate. Most of the policy agenda associated with trade capacity enhancement is domestic—it is up to civil societies and governments to define beneficial policy changes and to set priorities in the context of an overall development strategy and to allocate scarce resources accordingly. These are not negotiating issues and require action outside the WTO framework. However, they do have an important bearing on the political economy dynamics of the WTO. Without a clear sense that industries, farmers, and communities will benefit from further rule making and liberalization—which requires trade capacity—there will be little support for making the additional commitments that are needed in their own right and for reciprocity reasons. Building trade capacity demands resources. The payoff for building trade capacity rather than using resources elsewhere is an investment decision, not a given. If deemed a priority, the focus of policymakers and civil society should be to ensure that this is reflected in national development strategies and as well as donor and agency country assistance strategies.

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