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Coping with Trade Reforms:
A Developing-Country Perspective
on the WTO Industrial Tariff Negotiations

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Coping with Trade Reforms: A Developing-Country Perspective on the WTO Industrial Tariff Negotiations

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OVERVIEW CHAPTER

(Advance Copy)

Introduction

The trade negotiations launched at the World Trade Organization (WTO) ministerial meeting in Doha in November 2001, which aimed at further liberalization of trade in goods and services, hold out hopes for potentially important gains for developing countries in terms of improved access to overseas markets. Many of these countries are expected to undertake further liberalization commitments and this could bring them even further gains, at least in the longer term. The standard argument is that trade liberalization improves efficiency in the allocation of scarce resources in an economy, enhances economic welfare and contributes to economic growth (see, for example, Sachs and Warner, 1995). However, this relationship between openness and growth is essentially based on empirical evidence; no formal linkage has been established in economic theory. Some economists have criticized the econometric evidence, and emphasize the importance of governance rather than openness per se (Rodrik, 1999). There may also be an economic case, based on externalities, for long-term intervention, where the social benefits of intervention (e.g. in terms of environment and health) outweigh the costs.

While there might well be long-term gains from liberalization, liberalizing economies are, nevertheless, likely to face short- to medium-term adjustment costs. This is because, as economies open up, imports use existing channels while new exports often come from different sectors that have to gear up production and find new markets. The structural unemployment that occurs as this transition takes place is, perhaps, the major social cost of adjusting to trade reforms. Unfortunately, most developing countries do not have well-developed social safety nets, such as unemployment benefits, retraining programmes and portable pensions, to address these problems. Other areas of adjustment to be addressed include: the need to replace tariff revenues as a major source of government funding as protection is reduced; tackling the likely loss of preferences in overseas markets as MFN rates are lowered under multilateral liberalization; and intrasectoral and intersectoral reallocation of resources in response to changes in the levels of protection.

To gauge the possible developmental implications of the current WTO trade negotiations, it is important to examine the various proposals and attempt to assess to assess their likely economic impact. Part I provides a quantitative analysis of the various proposals being considered in the WTO negotiations launched at Doha in November 2001, as well as a review of other studies of adjustment to trade reform. Part II examines the experiences of a number of countries at different levels of development and across various regions to try to ascertain the impact of their trade reforms and the factors that contributed to the outcomes. Most of these country studies were commissioned under a project funded by the United Kingdom's Department for International Development (DFID), and supplemented by studies under UNCTAD's own work programme.

It is hoped that the study will be useful in helping governments decide on the most beneficial approaches to the WTO negotiations on further liberalization of trade in goods and services, and to design policies that will enable them to withstand changes in trade policy that might be expected to result from the negotiations in order to achieve a development-friendly outcome. their likely economic impact.

Part I: Quantitative assessment and literature review

What are the numbers?

Chapter 1, Now What?, by Santiago Fernandez de Cordoba (UNCTAD) and David Vanzetti (UNCTAD and the Australian National University) reviews key features of the main proposals that have been tabled in the WTO Negotiating Group on Non-Agricultural Market Access, and attempts a quantitative assessment of the likely economic impacts of those proposals.

The main focus of discussion in chapter 1 is a formula-based approach to tariff reductions, a major distinction being between variations on formulae, which compress high rates more than proportionately (extensions of the "Swiss" formulae used in the Tokyo Round), and a uniform cut approach, differentiated by developed and developing countries, with the added element of capping rates (e.g. at three times the national average to eliminate tariff peaks). Other key elements include: the possibility for the complete elimination of tariffs in some sectors considered to be of export interest to the developing countries, exclusion of the LDCs from any commitment to cut tariffs, the possibility of reduced commitments by countries that have recently acceded to the WTO, and the extension of binding commitments (i.e. making legal commitments not to increase tariff rates for specific products).

All of the approaches could be applied in a more, or less, ambitious manner, that is, using an approach intended to achieve a greater or lesser degree of liberalization. Using a global CGE model, the Global Trade Analysis Project (GTAP) model, to assess the economic impact of the proposals, the authors conclude that the level of ambition is, to some extent, more important than the particular formula. In general, they show that the more ambitious approaches would offer developing countries greater welfare, output, employment and trade gains, but that they would also lead to increased imports and revenue losses. Approaches based on Swiss-type formulae tend to be more complex and less transparent than a linear approach supplemented by the capping of tariff peaks, and, as the authors say, "appear to contribute little to the outcome".

All the proposals would remove some of the latitude in the use of tariffs for development purposes. The more ambitious proposals could also squeeze out the "water in the tariff", gap between legally bound and applied rates came about largely because of autonomous reforms under World Bank and IMF programmes. A number of developed countries have been pressing for an approach that would reduce or eliminate this gap, since they expect no direct trade effects from reductions that leave the bound rates above the applied rates.

The analysis by Fernandez de Córdoba and Vanzetti, which covers all the sectors but is more detailed in its treatment of industrial tariffs, estimates global annual welfare gains from liberalization to be in the order of $90 billion to $200 billion – similar in order of magnitude to a number of other, more conservative studies, including those of the World Bank. While these results seem impressive, the percentage changes in aggregate welfare and trade are relatively minor – in many cases, less than 1 per cent. However, crucially, these modest results in the aggregate conceal potentially important sectoral variations; while the exports and production of some sectors are likely to expand considerably, other sectors are likely to suffer large contractions of output and employment as imports increase.[1] Among the more significant increases would be the output of services. If the tariff cuts are large enough to significantly reduce applied rates in developing countries, as in the so-called free-trade scenario, there will be a big shift to services. The most significant increases in absolute terms are estimated to occur in China.

Perhaps of greater interest are the substantial negative changes in sectoral employment. In percentage terms, the largest falls in employment over the partial liberalization scenarios fall under an ambitious application of a Swiss-type formula in sectors such as motor vehicles for the Rest of South Asia (i.e. other than India) (-36 per cent) and non-ferrous metals for India (-24 per cent). Under a more moderate scenario, in the leather sector, there is a loss of skilled and unskilled employment of over 30 per cent in Japan and nearly 21 per cent in Canada, while in developing countries, the losses tend to be less than 10 per cent. These provide an indication of the structural adjustment that would be needed.

The high adjustment costs associated with these estimated changes are one of the reasons for the hesitation of some developing countries to take on board some of the more ambitious liberalization proposals. Temporary unemployment of labour and capital can have a significant negative effect on output and welfare. On the other hand, if the reforms lead to a greater use of previously unemployed labour, the welfare gains would be significant, perhaps as much as the gains from using resources

[1] Output and employment seem to increase with the level of ambition, but less so with the degree of harmonization.

more efficiently. However, as discussed in the next section, there is relatively little documented evidence concerning the scale and nature of these costs or of the adjustment process of local economies in the aftermath of trade liberalization, despite some 15 years of unilateral reforms in developing and transitional economies. For informed policy-making, governments need a better understanding of the costs to their economies following changes in their tariffs.

Comment by Joe Francois

Professor Joe Francois of the Tinbergen Institute, in commenting on the chapter by Fernandez de Cordoba and Vanzetti, draws attention to the fact that all the formulas yield larger cuts in percentage terms for developed countries, and larger cuts in absolute terms for developing countries (at least under the ambitious scenarios). He says that the modelling results, in common with all recent CGE studies of the Doha negotiations, produce the strongest export gains from a reduction in average tariffs across developing countries. He also argues: “A message between the lines… is that tariff preferences may be a second order economic issue, despite its high profile as a political one.” The overall effect of tariff reductions by OECD countries would be a net expansion of exports by LDCs (many of whom are in the sub-Saharan Africa aggregate in the model). Discussing problems with the administration of preferences, he concludes that, “because of limitations placed on trade preferences, NAMA negotiations matter even more for developing countries than if preferences worked better.” He suggests that this points to even deeper gains to developing countries from tariff reductions by the OECD countries.

Experiences of adjustment to trade reform: a review of the literature

There have been a number of studies of adjustment costs and even some prior reviews of other studies, as discussed in Chapter 2 by Fernandez de Cordoba, Laird, Maur and Serena. While the various studies take different views of the nature of adjustment costs, and use different methodologies, many have concluded that the gains from trade liberalization are often less than the adjustment costs, particularly in the presence of rigid labour markets. The difference in treatment of social and private adjustment costs helps to explain some of the variations in the findings of some empirical studies, and highlights the importance of being prepared to face the adjustment process.

An important issue raised in the literature is that adjustment occurs not just due to changes in trade policy at home (or abroad), but also from a wide range of factors, such as technological change, changes in demand/tastes, changes in national law, weather/natural phenomena and political (in)stability, or as a result of international agreements, including trade agreements. There is no agreement in the literature as to whether it is feasible or desirable to try to separate the causes of adjustment costs: the key is to put in place policies and institutions that facilitate structural adjustment, whatever the source. The emphasis on labour market issues (structural unemployment) highlights the major social concern of trade reforms, and clearly needs to be addressed with social safety nets and programmes for re-insertion into the labour force if workers are to be persuaded of the long-term benefits from the reforms. One implication of the main body of studies is that the phasing-in of liberalization is strongly recommended.

Part II - Country case studies: experiences of trade reforms and adjustment

The case studies

Developing countries have undergone major trade reforms in the last 10 to15 years, often under World Bank/IMF lending programmes, RTAs (mainly in the 1990s), commitments undertaken in various Uruguay Round agreements, and as part of preparations for accession to the WTO.[2] With some important exceptions for sensitive products, tariffs are now low to moderate in most countries, and the main question being asked in Part II of this book is how these countries fared under the reform process. We are also interested in the explanations for their performance. If they fared well, what were the factors that contributed to a successful outcome? If they faced problems, why and what could they or others have done to obtain a successful outcome?

Obviously, economic growth depends on many factors, some of which are related to demand conditions in the rest of the world. It is therefore difficult to attribute the variations in growth entirely to the reforms. Moreover, the range of possible explanations is so great in relation to the availability of data, that obtaining a more precise explanation and identifying the role of specific factors by econometric means is practically impossible. The purpose of the case studies, then, was to try to apply a standard approach, using descriptive statistics and local knowledge to try to distinguish the important elements – positive and negative – in each case.

The *Bangladesh* study, by Narun Rahman, a private consultant, notes that "over the last three decades, Bangladesh has come a long way in the evolution of its economic and policy orientation, from a highly interventionist regime with widespread control on trade, the exchange rate and investment, to a substantially liberalized economic framework." The study gives details of the changes in policy in Bangladesh, which seem to have gathered momentum since 1991, and then goes on to discuss their economic impact. The results appear to be mixed: "an improved, but not strong enough growth performance; expansion of trade, but without meaningful diversification; reduction in poverty, but an increase in inequality." The share of manufacturing in exports increased from 77 per cent in 1990 to 92 per cent in 2003. The textiles and clothing sector, particularly low-end readymade garments, accounts for over 80 per cent of total merchandise exports, while the shares of agricultural raw materials and food have fallen drastically. The number of workers employed in the readymade garments sector has increased almost tenfold over the past 15 years, but the overall employment rate has fallen both in relative and absolute terms. As an LDC, Bangladesh benefits from preferential treatment in Europe, but there are significant limitations on its preferential access to the United States. Overall revenue receipts of the Government have risen in recent years, due to increased imports and improved revenue collection. During the 1990s Bangladesh succeeded in reducing the aggregate level of poverty, but the evidence in the study suggests that income inequality has increased. In the WTO context, the elimination of textiles and clothing quotas at the end of 2004 is expected to pose some challenges for Bangladesh, as competition, particularly from China, intensifies, while preference erosion will increase pressure on domestic firms to become more competitive. WTO rules may also have implications for the ability of the country to enter new dynamic sectors of world trade (e.g. pharmaceuticals, leather goods, information and communications technology (ICT) products and ICT-enabled services, agro and marine products, and niche items of interest to expatriate Bangladeshi and other South Asian nationals).

The *Brazil* study, by Professor Lia Valls Pereira of the Fundaçao Getulio Vargas in Rio de Janeiro, notes that, after more than two decades of restrictive trade policies, in the early 1990s Brazil started to implement a comprehensive plan of economic reforms including a stabilization programme and other initiatives to modernize and increase the efficiency of the public sector. Under the first broad trade reform in 1990, most quantitative controls were eliminated and tariffs were significantly reduced. Brazil was also a founder member of the Southern Common Market (MERCOSUR), established in 1991. The financial crisis of 1998 featured an overvalued exchange rate and increasing deficits in the trade balance, leading to growing protectionist sentiments and a partial reversal of trade liberalization. The devaluation of the Brazilian currency in 1999, however, alleviated the protectionist pressures.

The post-liberalization period in Brazil has been characterized by relatively low rates of growth (2.4 per cent in the 1990s, compared with the world rate of 3.8 per cent), although trade generally increased after trade liberalization. An overvalued exchange rate explains the trade deficit and the persistent growth of imports until 1999, while the freeing of the exchange rate in 1999 led to the growth of exports and the decline of imports, resulting in a trade surplus. There is evidence that total factor productivity increased across most sectors, but there seems to be no agreement about the specific impact of trade liberalization on this increase. Unemployment rose from 5.7 per cent in 1992 to 7.9 per cent in 1999. Job losses in the manufacturing sector, although this was partly due to competition and to "increases in productivity through the adoption of new technologies and/or greater management efficiency (a non-reversible trend)". There is some evidence that part of the newly unemployed were absorbed by the informal market, where low earnings predominate. Uneven income distribution and the lack of opportunities, especially in education, are still the main factors that explain the poverty in Brazil, and there is no clear-cut evidence of the impact of trade liberalization on them.

The *Bulgarian* study, by Victor Ognivtsev of UNCTAD, notes that Bulgaria has undergone 15 years of profound reforms in the process of its transition to a market economy, and in pursuing its main current strategic goal: to accede to the EU by 1 January 2007. Before 1989, Bulgaria's trade was mainly directed to countries of the Council for Mutual Economic Assistance (CMEA), and was in some sense "centrally planned". After the collapse of the Soviet bloc, trade became "market-driven". Liberalization of Bulgaria's trade regime, in particular through RTAs, has been much faster for industrial products, while trade in agricultural products has been only partially liberalized. Export growth has been one of the main contributors to the growth of GDP in the last few years, with the EU now accounting for 52.4 per cent of Bulgaria's total trade, compared with 38.5 per cent in 1995. The recovery of the economy after 1997 has been accompanied by persistent current-account and trade deficits, financed mainly by foreign direct investment (FDI). The EU accession process is helping to improve the competitiveness of the economy by increasing regional trade, encouraging FDI and providing additional funding for social safety measures. However, Bulgaria still faces a high and persistent level of unemployment, and poverty indicators have deteriorated.

In the *India* study, Dr Veena Jha of the DFID-UNCTAD India project in New Delhi explains that India has been engaged in a wide-ranging economic reform programme since the early 1990s. It began with progressive liberalization in areas such as the exchange rate regime, foreign investment and industrial policy. This was followed by autonomous trade liberalization measures included the reduction of trade restrictions, the abolition of import licensing, and the rationalization and reduction of import tariffs, which were reduced from almost 50 per cent in 1990 to 26 per cent in 2003 (and reportedly have been further reduced to 17–18 per cent). There has been a rapid rise in the use of anti-dumping measures and safeguards. India has further liberalized on a regional basis as a party to the Bangkok Agreement, the South Asian Preferential Trade Agreement, the Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation agreement and the Indian Ocean Rim Agreement for Regional Cooperation.

Economic growth surged after liberalization was introduced, averaging 6 per cent in the 1990s. Poverty indicators have also improved, but inter-state and regional disparities have widened. Both exports and imports have grown significantly – by almost 50 per cent between 1998 and 2003 – and they have become increasingly diversified. The current account has moved into surplus. However, employment trends following liberalization have been mixed. There has been a rise in the overall level of unemployment (from 6 per cent in 1993/94 to an average of 7.3 per cent in the period 1999–2003), mainly in agriculture and in the informal sector.

Dr Jha concludes that India's gradual approach to liberalization has helped to spread adjustment costs and to ensure better preparedness among industries. In particular, the sequencing of reforms, whereby fiscal, monetary and investment reforms preceded trade liberalization, may explain India's positive experience with adjustment. The services sector holds significant promise for growth and should be a focus of WTO negotiations. Regional cooperation could facilitate better market access, build competitiveness and help reduce non-tariff barriers. Losses of tariff revenue need to be offset by other forms of taxation.

The *Jamaica* study, by Professor Michael Witter of the University of the West Indies in Kingston, mentions that, under several waves of reforms that began as early as 1982, the average tariff was reduced from 25 per cent in 1989 to 8.9 per cent in 2002, while the tariff structure has been rationalized and almost all import licensing and quota requirements have been abolished. In the 1990s, trade liberalization was given a further boost with "the reform of the common external tariff of the CARICOM, the pressure to comply with the WTO's international trade regime, the restructuring of trade relations with Europe that is embodied in the Cotonou Agreement (…) and commitments taken in the context of the process to establish a Free Trade Area of the Americas (FTAA).” Other important reforms implemented in the period include fiscal reforms, financial liberalization and the elimination of exchange rate controls, and divestment of public enterprises.

Despite the reforms, GDP growth in last two decades has been very slow: per capita GDP has grown on average by 0.5 per cent a year, partly as a result of the financial crisis of the mid-1990s and the consequent monetary tightening, and partly due to the negative international economic conditions for bauxite/alumina and the tourism sector. Overall, “the evidence indicates that trade liberalization led to the decline of manufacturing for the domestic market, and to an increase in apparel exports from the free zones, but there was an overall decline in the contribution of the manufacturing sector to GDP.” Unemployment rate fell from 27.4 per cent in 1980 to 15 per cent in 2001, but this was mainly due to the slowing of the rate of growth of the labour force, while outward migration rose to over 20,000 per year, mostly skilled workers.

In the *Malawi* study, Dr Kennedy Mbekeani of the Botswana Institute of Development Policy observes that prior to the trade liberalization programme that began in 1988, Malawi had maintained a restrictive and complex trade and exchange rate regime based on discretionary allocation of foreign exchange, non-tariff barriers (NTBs), high tariffs, restrictive licensing requirements and surrender requirements on imports and exports. Malawi’s trade reform process consisted of: the elimination of NTBs, the consolidation of its tariff structure, a reduction of tariff protection, and the liberalization of its export regime. Malawi substantially rationalized its tariff structure by lowering and harmonizing duty rates. As Dr Mbekeani notes: “By mid-1999, Malawi’s liberalization programme had produced one of the most liberal and transparent regimes in Africa.” Externally, Malawi enjoys preferential market access to the EU market through the Cotonou Agreement and the “Everything-but-Arms”(EBA) Initiative, and to the United States market through the African Growth and Opportunity Act (AGOA). Malawi is also a member of two regional agreements: the Common Market for Eastern and Southern Africa (COMESA) and the Southern Africa Development Community (SADC).

Malawi’s post-liberalization economic performance has been disappointing. Growth had reached as high as 15 per cent in 1994, but thereafter it began to fall steadily. By 2001, growth was below 2 per cent, and in 2002 the economy shrunk even further. The manufacturing sector shrank by 30 per cent between 1989 and 1998, and by 11.4 per cent in 2002 alone. Other contributory factors, included macroeconomic instability, weak infrastructure and poor institutions. The main obstacles are transport costs (due to Malawi being a landlocked economy with a poor road infrastructure) and supply-side constraints. The author notes that Malawi's main exports, including tobacco, face high tariffs in key export markets (products and markets not covered by the EBA or AGOA). In the WTO negotiations on further liberalization of trade in goods and services, the “biggest challenge for Malawi is how firms will adjust to global competition.” Preference erosion may also be a problem. Limited technical capacity implies that Malawi cannot participate effectively in the WTO processes.

The *Philippines* study by Dr Ramon Clarete, a private consultant from Manila, notes that the Philippines has implemented various unilateral trade reform programmes since 1981. The reforms gradually lowered nominal and weighted average tariff rates, and simplified the tariff structure. Throughout the reforms, there were temporary periods of reversals: for instance, the Government raised the tariff rates in 1998 and 1999 in response to difficulties caused by the Asian financial crisis. More recently, in 2003, there has been another increase in tariff protection for selected industries (steel, sugar, polymers).

Since 1990, in the wake of the Asian crisis, aggregate exports have expanded dramatically, overtaking aggregate imports. However, growth has occurred in only a few sectors (manufacturing, machinery and transportation equipment), while in others (raw materials, animal and vegetable oils) it has remained stagnant or even declined. Per capita income has not changed, and there is mixed evidence as to whether the reforms have improved income distribution or alleviated poverty. This unsatisfactory economic performance can be attributed mainly to macroeconomic instability (economic contraction in 1985, the Asian financial crisis in 1997-1998), natural disasters (El Niño-induced drought in 1997) and poor economic institutions (high transaction costs, lack of property rights, high logistical costs). Even if market access is facilitated through unilateral or negotiated trade liberalization, the Philippines may not be able to avail fully of the new access opportunities because of high transaction costs that dampen the country's competitiveness. Dr Clarete argues that investment has been slow to react to new export opportunities because of a poor investment climate and the relative difficulty of enforcing property rights.

The *Zambia* study by Dr Manenga Ndulo and Mr Dale Mudenda of the University of Zambia in Lusaka, highlights the fact that the Zambian economy is heavily dependent on the production of a single commodity: copper. In 1974 the price of copper plunged by 40 per cent, and thereafter continued to remain weak and unstable. Zambia has experienced two major episodes of reforms, first in 1985–1987 and the second since 1991. Key reforms, besides trade liberalization, included privatisation of the State-owned firms, liberalization of agricultural input markets and marketing, public sector reform, financial sector liberalization and the removal of exchange rate controls.

In general, trade liberalization has failed to contribute to substantial economic growth, and GDP per capita continues to decline. On the one hand, the reforms have stabilized the macroeconomic situation and boosted competition and efficiency. On the other hand, reforms have entailed significant adjustment costs and have failed to help the development process. The import-competing industrial sectors suffered heavy losses.after liberalization, and their contribution to GDP fell by 50 per cent. Formal employment as a share of the total labour force fell from 23 per cent in 1981–1990 to 8.3 per cent in 2003. Thus, recent trade liberalization and the associated adjustment measures have resulted in a fall in employment levels in Zambia by over 50 per cent. Moreover, most of the development indicators have worsened. Due to the HIV/AIDS pandemic, life expectancy has declined; and due to the deterioration of the economy and rising levels of poverty, education indicators have also worsened. The authors' analysis is that the implementation of the reforms was too rapid, unsequenced and often without, the support of the stakeholders, and that there were serious. limitations in administrative capacity.

Comments by Messerlin and Tussie

In addition to the country studies, at the request of DFID, Professor Patrick Messerlin of the Institut d'Etudes Politiques de Paris (Sciences-Po) and Professor Diana Tussie of the Facultad Latinoamericana de Ciencias Sociales (FLACSO) of Buenos Aires were asked to comment on the country studies. They provided valuable advice to the project and also to the authors of the individual country studies. Their observations are also included in this book.

Professor Patrick Messerlin while acknowledging that average tariffs have fallen, says that trade liberalization in most developing countries has substantially consisted of reducing protection imposed on goods that are not produced (or produced in small quantities) at home. A consequence is that resources are likely to move only slowly out of the traditional sectors and towards new activities. He suggests there may even be an increase in resource misallocation from uneven liberalization. In Professor Messerlin's view, it is therefore difficult to expect a boost to economic growth and a noticeable move to diversification, which is why the disappointing economic performance from such liberalization is not surprising.

In considering the policy implications, Professor Messerlin believes that special and differential treatment (SDT) has not worked well because key sectors for developing countries – shoes, clothing and agriculture – were excluded from SDT. However, he accepts that the poorest countries still need preferential access to rich countries, which could do much more, including opening their farm and clothing markets and simplifying their rules of origin. The poorest countries could also gain from other developing-country markets. He proposes that cuts of high tariffs by developing countries be compensated by finance from the rich countries for transport infrastructure and to make up for revenue losses.

Professor Messerlin suggests that the full benefits from trade liberalization are likely to require complementary domestic reforms, and that there are many instruments for development purposes at their disposal (production and consumption subsidies, or taxes on goods, services and factors of production) that can better achieve the desired objectives at a much lower cost than trade barriers. He argues that, in services, introducing economically sound and politically acceptable special and differential treatment will be no easy task. Attention should be on regulatory creativity focusing on a well-defined cluster of services, such as those related to trade facilitation, which might afford the largest net benefits.

Professor Diana Tussie notes that, after decades of highly interventionist trade regimes, all eight countries covered by this project initiated major trade reforms, leading to increased trade openness; they also signed various forms of trade agreements with country neighbours and/or other trade partners. Since the trade reforms were usually part of much broader policy reforms, it is difficult to disentangle the effects of the different policy changes.

With some exceptions, the results of the reforms have been disappointing with respect to growth rates and social indicators, especially employment. Preferential access to major markets was important for Bangladesh and Bulgaria, especially in textiles and clothing (assisted by FDI), and contributed significantly to their overall economic and export growth. However, Malawi and Zambia were unable to take advantage of similar preferential access because of their extremely limited supply response capacity. Further liberalization under the WTO will pose additional challenges as it will erode preferential access for the African countries and Jamaica. In Brazil, growth rates fell below those of the 1960s and 1970s, but the main problems seem to lie in domestic policies – exchange rates, public debt, high interest rates, and difficulties in implementing all the economic reforms. Professor Tussie observes that, by contrast, Indian economic growth in the past decade has been impressive, although there is disagreement about how much of this can be attributed to the trade reforms. She concludes that the incidence of poverty is so dramatic in India and Brazil that trade alone cannot provide a way out; improvements in income distribution will be necessary to achieve poverty reduction.

Overall assessment from the country studies

From the case studies, it is clear that one size does not fit all: in the design of programmes it is necessary to take account of the level of development, the quality of institutions, resource endowments and the availability of resources to support reforms. Despite years of experience with reform programmes, there is no recipe for monotonically increasing levels of welfare; reforms are tools/instruments, and serious mistakes are still being made with regard to timing, sequencing, implementation and inclusion of all relevant essential elements.

Little account seems to have been taken of adjustment costs in the design of liberalization programmes, other than to provide balance-of-payments support as countries undertake reforms, while waiting for a supply response that does not always arrive. Yet proactive support seem to run afoul of ideological stances (e.g. "if there is a problem, not enough has been done" - and not that the programme has design flaws). Moreover, the possibility of using policy tools, such as subsidies, to overcome market failures are increasingly running up against limitations imposed by expanding WTO rules. Overall, there is need for caution in asking countries to embark on ambitious reform programmes, since reform-minded governments could risk being replaced by others that take a more protectionist stance, which would result in reforms being stalled, if not reversed.

A number of specific points deserve mention:

- The countries in the study embarked on a process of switching from import-substituting industrialization towards more open economies. Import liberalization, initially brought a more rapid growth of imports than exports, and, in the majority of cases in the study, this had severe negative effects on domestic production and employment in import-competing sectors. In some cases, these negative effects have persisted for a number of years. Most countries had difficulties in generating a supply response in terms of alternative production processes and exports, but this seems to have been less of a problem for the larger countries, as noted below.

- Several studies have emphasized the importance of a stable macroeconomic environment as one conducive to growth and facilitating reforms by creating new jobs for those displaced from import-competing industries that have seen protection reduced.
- Several studies point to the importance of the real effective exchange rate (REER), that is, relative movements of prices at home and abroad, adjusted by the nominal exchange rate. If the REER is allowed to appreciate, export competitiveness is reduced. Some countries, with high rates of inflation, have used exchange rate policy to help control domestic inflation, but with negative consequences for domestic production and exports, unless productivity can be increased more rapidly than in other countries.
- Overall income growth does not necessarily lead to a more even distribution of income.
- Countries that opened up first to investment,[5] or obtained significant FDI inflows received a boost to economic growth that created new jobs for those displaced under import liberalization.
- The studies do not explore in detail conditions for investment, but the conditions appear to include exchange rate liberalization, macroeconomic stability, and some trade liberalization in the form of easing of import restrictions (including licensing, tariff reductions or waivers for investment goods, and duty waiver or drawback schemes for imported materials and components for finished goods for re-export).
- Other studies point to the importance of political stability, good institutions and labour supply. These conditions have generally been present in the countries covered in the case studies.
- The functioning of capital markets is very important, especially for SMEs that cannot easily tap international capital markets when domestic borrowing rates are high, as in many countries studied here. (Some form of development bank, such as Brazil's BNDES that borrows at sovereign rates and re-lends with a margin to cover costs, may be an important option worth considering).
- The trade reforms usually proceeded with the reduction and elimination of non-tariff measures, followed by the rationalization of tariff structures and reduced tariff rates. In some cases, the new tariff structures are still characterized by tariff escalation – adoption of a uniform tariff structure was not observed in the countries under study – and tariff peaks remain in sensitive areas. In the first phase, when non-tariff measures were reduced, tariff revenues increased in some cases, but fell as tariffs were later reduced.
- In the case of Bulgaria, where reforms proceeded relatively quickly, partly because of preparations for accession to the WTO as well as for eventual EU accession, considerable financial support was provided by the EU. World Bank/IMF programmes provided considerably lower levels of budgetary support, but it was, nonetheless, very important.
- The larger countries in the study (Brazil, India and the Philippines) had a number of options for diversification into alternative lines of production, and were able to develop some intra-industry trade. In the smaller countries, it was more difficult to

[5] This was the case of India (see study) and, reportedly, of China (not covered here).

develop alternatives, for example, in Zambia or in Malawi where some the textiles industry practically disappeared.

- Several studies point to the importance of institutions as a key factor in explaining performance, In general, the larger countries had better institutions to cope with reforms, but they are still lagging behind the industrialized countries. Labour market rigidities tend to encourage the growth of the informal sector.
- The larger countries became important users of administrative protection, in particular, anti-dumping measures, as they liberalized.
- Several studies have underlined the need for complementary domestic policies, including industrial, educational, labour and social policies.
- Brazil and India had some positive support policies, including subsidies, but in most of the countries studied, such positive policies were lacking. The reasons are not given, but this could be related to the lack of funding.
- None of the countries studied report the use of policies such as those adopted by Ireland, the Republic of Korea and Singapore (not covered here) to encourage certain industries or to facilitate cluster group formation, though the Philippines study mentions the importance of export processing zones.
- The importance of physical infrastructure, especially in the transport area, is noted in a number of cases. This is particularly important in Africa, where two landlocked countries are examined. Complementary action on competition policy in the transport sector is signalled in Zambia.
- The reduction of preferences, as most favoured nation (MFN) rates are being reduced, seems to be an issue for the ACP countries, and is highlighted in the Jamaica study. The issue is also important for other, including Bangladesh, Malawi and Zambia.
- Regional trade agreements, partly to negotiate improved access to foreign markets, have played an important role in further liberalization following autonomous reforms, and, particularly in the case of Bulgaria, in modifying a number of "behind-the-border" measures.
- The studies highlight the importance of involving stakeholders to gain public support for reform programmes. Such involvement creates a sense of ownership of the reforms, as well as a belief that the reforms are intended to increase efficiency and competitiveness, and could help overcome existing difficulties (such as hyperinflation in Brazil in the early 1990s).
- Supply-side elements have been important. However, in a number of sectors, tariff peaks and escalation have made it harder for developing countries to expand into areas where they have a comparative advantage when import-competing sectors face the challenge of increased competition under liberalization programmes. In addition, where markets have been opened up, additional problems of entry have occurred; for example, because of sanitary and phytosanitary (SPS) standards and technical barriers to trade, or developing countries have been unable to capture the gains from trade because of the control of marketing channels by a few large intermediaries.

How can the WTO processes help?

The study suggests that the trade negotiations launched at the WTO ministerial meeting in Doha in November 2001 present both challenges and opportunities with respect to adjustment by both the developed and developing countries. There are challenges in that the more ambitious scenarios seem to offer greater export possibilities and welfare gains, but they also imply increased imports, greater intersectoral shifts in production and employment, and further losses of tariff revenue. On the other hand, the negotiations also offer opportunities to correct imbalances that have resulted from the uneven evolution of rules and the removal of measures in previous negotiations; these have left both a systemic bias in the multilateral trading system as well as higher barriers against developing countries' key exports.

In the past the GATT moved faster on areas that were relatively easy to tackle. It liberalized areas of export interest to the developed countries and tightened rules or the application of rules on subsidies, balance-of-payments (BOP) measures, infant-industry support, trade-related aspects of intellectual property rights (TRIPS) and trade-related investment measures (TRIMs), while providing lacunae or exemptions of one form or another on agriculture, and textiles and clothing. It also made the provision of differential and more favourable treatment for developing countries into "best endeavour" clauses.

By creating new opportunities for developing countries ahead of any new commitments that they may have to undertake, the economies of these countries should start to attract new investment and generate a supply-side response that should help them cope with the expected negative effects of the challenges posed by WTO negotiations, whether through their own liberalization or the loss of preferences.

The developing countries need to be provided with flexible timetables for the implementation of new commitments. Pushing too hard, too fast could generate the kind of negative effects that have been identified in a number of countries from prior episodes of liberalization. Any backlash from such effects could have negative consequences for longer term liberalization.

Among the issues to be addressed are the provision of:

- Improved access for developing countries' key exports of agricultural goods, manufactures and services.
- Policy space for developing countries, consistent with received economic views on the importance of externalities, and taking account of market imperfections.
- Realistic time frames, and financial and technical support for implementation of any new commitments, and support for structural adjustment. Ideally, such assistance should be provided by the donor community, especially to the highly indebted countries, perhaps with technical support from the international financial institutions in their respective areas of expertise under the coherence arrangements, and without further conditionalities.
- Compensation for losses due to preference erosion, similar to that available within the EU's Common Agricultural Policy (CAP) compensatory payments scheme
- Assistance and adequate time for developing countries to restructure their fiscal systems to offset revenue losses where tariffs are reduced as a result of new commitments.
- Special and differential treatment, including less than full reciprocity, in all areas of the negotiations, as identified in the Doha Ministerial Declaration.

These issues need to be resolved prior to the conclusion of multilateral negotiations (or indeed any reform programme), in keeping with normal business practice that proposals should be costed, and implementations realistically programmed, with provision made for financing. The failure to take account of similar issues, and the consequent unexpected and often high costs, may well have led to the disillusion with the outcome of the Uruguay Round and to the failed WTO meeting in Seattle. Although it may take longer to strike a deal that takes account of such issues, such a deal would be more likely to retain the confidence in the multilateral system of all the WTO Members.

Conclusions

After the extensive reforms of the last 10 to 15 years, developing countries face additional adjustments following WTO negotiations. These adjustments, positive and negative, will result from their own liberalization affecting sectoral production and employment as well as aggregate revenues, and from changes in access to overseas markets. The adjustments will be positive as barriers are brought down and negative as preference margins are eroded. All this has implications for their human development.

Preliminary analysis from case studies and reviews of other experiences suggest that it would be desirable to anticipate such adjustment in a number of ways: by encouraging domestic and foreign investment, including through legislation and institutions that are business-friendly; by developing capital markets to provide access to finance, especially by SMEs, by providing social safety nets, introducing labour retraining, and extending other skills-oriented education programmes; providing or improving physical infrastructure, especially in the transport sector; trade facilitation; debureaucratization; helping developing countries meet SPS/TBT standards, which at present constitute barriers in major markets; and encouraging cluster group formation.

The international financial institutions, with their considerable technical expertise in a wide range of projects, can play an important role in helping developing countries to implement or extend programmes in many of the ways outlined; they have already indicated their willingness to help (e.g. the IMF’s Trade Integration Mechanism). However, the donor community can also play an important role, particularly where the affected countries are already heavily indebted.

The WTO process can also help by providing for anticipated liberalization in areas where the developing countries have comparative a advantage. This would help create jobs ahead of job losses in sectors that are likely to suffer from increased competition as their own barriers are lowered. The WTO could also usefully address systemic and rules-related issues with the aim of allowing policy space for development purposes. This was partly envisaged in the original GATT, but it seems that such options, including the use of support policies in the presence of externalities, are being closed off to developing countries.

One last comment. It is clear that newly open economies invariably face adjustment problems (WTO, 2004:20). Although largely overlooked in the past, it is now more widely recognized that short- to medium-term adjustment assistance to trade shocks is indispensable to facilitate acceptance of freer trade. In the absence of any adjustment assistance or social safety nets, trade liberalization may be resisted or even reversed.

The multilateral trade agreements of the GATT/WTO were traditionally silent on the issue of adjustment, leaving this entirely up to national policies to address, with or without the support of the Bretton Woods institutions in the case of the developing countries. An international consensus appears to be emerging on this issue, and on building supply-side capacity, under the rubric of "aid for trade". However, if this approach is to influence attitudes towards multilateral trade negotiations, there may be a need for a more formal organic link within the WTO itself, creating rights and obligations in relation to adjustment that go beyond the "coherence mandate" covering cooperation between the WTO and the Bretton Woods institutions.

This is especially important for developing countries, most of which lack adjustment assistance instruments to be able to withstand increased import competition; they would require substantial international support in this regard. Some recent initiatives address this issue: a temporary "aid for trade fund" was proposed by the UN Millennium Project's Task Force on Trade in its Report on Trade For Development, 2005, while Mandelson, the EU Trade Commissioner, proposed on 4 February 2005 the establishment of a special Trade Adjustment Fund to "help the poor to trade more effectively and ease the social costs of adjustment". The new challenge for the multilateral trading system would be to design efficient adjustment mechanisms, ensure their funding and find ways to effectively integrate them into the negotiating outcomes.

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