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**MAJOR ISSUES AND CHALLENGES OF THE  
NEW WTO WORK PROGRAM  
FOR IDB MEMBER COUNTRIES**

**By**

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## Abbreviations and Acronyms

AEDCs	Agricultural Exporter Developing Countries
AMS	Aggregate Measurement of Support
AoA	Agreement on Agriculture
DSB	Dispute Settlement Body
DSU	Dispute Settlement Understanding
ENT	Economic Needs Test
EU	European Union
FDI	Foreign Direct Investment
FIDCs	Food Import Dependent Countries
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GM	Gray-area Measure
GMO	Genetically Modified Organisms
GSP	Generalized System of Preferences
IDB	Islamic Development Bank
ILO	International Labor Organization
IT	Information Technology
LDCs	Least Developed Countries
MFA	Multifiber Arrangement
MFN	Most Favored Nation
MRAs	Mutual Recognition Agreements
NTBs	Non Tariff Barriers
ODA	Overseas Development Assistance
OECD	Organization for Economic Cooperation and Development
OIE	Office of International Epizootic
R&D	Research and Development
SDT	Special and Differential Treatment
SPS	Sanitary and Phytosanitary Measures
SSG	Special Safeguard Provisions
STE	State Trading Enterprises
TRIPS	Trade Related Intellectual Property Rights
TRQs	Tariff Rate Quotas
TSE	Total Support Estimate
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization



## PREFACE

After the WTO Ministerial Conference, held at Doha, Qatar, in November 2001, it is realized that the developing countries, including the Islamic Development Bank (IDB) member countries, are likely to face new challenges emerging from the new WTO Work Program. In particular, the member countries are likely to be more concerned with the hardships of non-implementation of the existing WTO arrangements, the elaboration of the objectives and timetable for the current negotiations on agriculture, services and market access. Consequently, there is a view that the IDB member countries would be facing more international uncertainties and difficulties in integrating their economies with the global economy.

The IDB is aware of the complexities and challenges of the WTO agreements and is thus endeavouring to provide various forms of assistance to its member countries to enable them to reap full benefits from these agreements. The underlying theme of IDB's efforts to promote economic co-operation among member countries is based on strengthening the trade ties through its various programmes. The bank is also endeavouring to support various WTO-related technical assistance programmes in member countries. The assistance provided by the bank has so far been designed to create awareness amongst IDB member countries of the provisions of agreements and the procedures of the WTO to enhance their negotiating skills so as to accede to the WTO on the best possible terms.

The bank also aims to assist its member countries in fulfilling their membership obligations in the WTO, introducing policy and institutional reforms that will enhance their competitiveness and capacity to benefit from the various agreements, and formulate and defend their position on items in the built-in agenda and new issues that may emerge in the WTO that respond to their individual and collective interests.

The Doha Ministerial Declaration clearly reveals that there are three areas which are of utmost importance for the IDB member countries i.e. negotiations on Agriculture, Services and Market Access for non-agricultural products. The study presents a strategy that IDB member countries may adopt in the course of negotiations on these three main areas.

## EXECUTIVE SUMMARY

1. Doha Declaration extends the negotiations to access the markets in agriculture, industrial and services sectors through reduction in both tariff as well as non-tariff barriers, and tariff peaks and escalation. It also includes competition policy and foreign direct investment, transparency in government procurement, trade facilitation and the environment. The Doha Declaration allows special and differential treatment for developing countries and hopes that negotiations are effective and enable the developing countries to meet their needs especially the rural development and the food security. The importance of the technical assistance to poor members has also been recognized so that they are properly integrated into the trading system and participate fully in the negotiations. The post-Doha 'round' of negotiations is to be completed by 2005 and the ministerial conference in 2003 will take stock of the situation.

2. Since IDB member countries are labour surplus, heavily dependent on the agriculture sector and have limited domestic markets, liberalisation efforts would go a long way towards realization of their growth potential. However, they must watch out their interests rather carefully in view of the misuse of the safeguard measures, incorporation of environment and labour standards, and non-implementation of special provisions for developing and least developed countries.

3. The share of industrial tariff lines subject to bound tariffs has increased from 78 percent to 99 percent in case of developed countries and from 21 to 73 percent in case of developing countries. The simple post-Uruguay Round average bound tariff on textiles and clothing are significantly higher than for the entire merchandise trade. Besides, contingent protection instruments, particularly anti-dumping measures, are currently being used more frequently.

4. While IDB member countries must reduce the level of tariffs to expose their economic activities to international competition, they need market access; currently their products face many obstacles in entering the markets of rich countries. In addition to extremely high tariffs and other protection measures, tariff escalation remains an important obstacle for developing countries to enter into the industrial exports. Rich countries need to do more to reduce trade distorting subsidies and dismantle their existing barriers on competitive exports from developing countries. Since most of the developing countries including the IDB member countries have been taking measures to liberalize trade unilaterally outside the WTO framework, they need to be given credit for the unilateral tariff reduction. The ground rules for the current tariff negotiations may allow developing countries longer period than provided to developed countries either on overall basis or in respect of particular products.

5. The IDB member countries amongst themselves or with other developing economies may negotiate industrial tariffs on an MFN basis on products traded between them. This would go a long way towards liberalisation of trade and improvement in their welfare levels. At the same time, they may take a joint stand relating to anti-dumping, environments, labour standards and other safeguard measures.

6. The IDB member countries bound their tariffs at levels significantly higher than the applied rates and as such bound rates may not result in any reduction in the applied rates. Therefore, it may be argued that market access negotiations would have to provide for possibilities of reductions in both the bound as well as applied rates.

7. The Doha Ministerial Conference calls for removal of all the non-tariff barriers on industrial products as they are least transparent and have major distortionary impact. However, frequent use of anti-dumping rules has constrained the liberalisation attempts. The developing countries are concerned over the new issues such as environments and labour standards.

8. IDB member countries may agree to reduce the bound rates and where they do not have comparative advantage to steep fall in tariff cuts both in the bound and applied rates; negotiate the conversion of all specific tariffs into ad-valorem tariffs; strive to seek substantial reductions in peak rates; and seek due allowance for the autonomous liberalization and flexibility in "staging" of tariff reductions. IDB member countries may press for international financing for training of public officials, screening industrial countries' trade policies, and building a network with other developing countries with the aim of jointly presenting cases.

9. The market access is provided through replacing the non-tariff with tariffs and reducing the tariff rates even further on agricultural products. However, tariff rates continue to be rather high compared to the industrial products. Moreover, the use of specific import duties raise the import duties in ad-valorem term that ranges from around 22% to 90%. Most of the IDB member countries have bound only a small proportion of the lines in their tariff schedules and have bound their tariffs at substantially higher rates than they apply.

10. Reform of the regime governing tariff rate quotas is extremely important in gaining market access. The reform options need to revolve around the abolition of TRQs accompanied with very substantial tariff cuts and the expansion of quotas with effective limits placed on within-quota rates.

11. The aggregate measurement of support (AMS) is relatively low for most developing countries. It is less than one percent of agricultural produce in most of the developing economies and in some countries it is even negative. On the other

hand, in EU and Japan, it is 22.9 and 32.5 percent of agricultural output. While AMS has been reduced, the overall level of subsidization of agriculture has increased in the developed countries as a result of reinstrumentation of support from measures subject to reduction commitments to those not subject to such commitments. Consequently, the total support estimate (TSE) of the countries belonging to OECD rose from US\$ 308 billion in the period 1986-1988 to US\$ 361 billion in 1999.

12. As of February 2001, 25 member countries are allowed to use the subsidy and Indonesia is the only IDB member country on the list. This is partly because many developing countries are incapable of financing export subsidies. The absence of internationally agreed rules governing the use of export credits, export credit guarantees and insurance programmes has enabled some countries to circumvent and reduce the value of export subsidy reduction commitments.

13. The developing countries do not consider state trading as a major impediment to more 'open' trading in agricultural markets. The STEs in future will need to be seen to be open with regard to their pricing policies, and to 'share' markets with private traders. It would be unfortunate if future negotiations led to provisions being incorporated in international trade law that hindered the ability of STEs to operate effectively in developing countries.

14. The existing Special and Differential Treatments (SDTs) are only "best endeavour" clauses and do not amount to anything. Since they are non-enforceable, they cannot be demanded as rights. There are scores of more such ineffective clauses in the WTO, which were put in during the Uruguay Round negotiations, to assure the poor countries that their interests would be treated differentially. Unfortunately, ever since the WTO came into being, there has not been a single instance when any SDT (except time frame was actually used by a poor country or a concession granted by a rich country).

15. The Sanitary and Phytosanitary (SPS) Agreement includes obligations that SPS measures be based on principles of international science and risk assessments of harm in order to minimize trade distortions. A central problem in the SPS framework concerns the lack of balanced considerations of dynamic benefits to economic development and trade under conditions in which acceptable risk is not set at zero tolerance levels. When combined with the lack of progress on harmonization of standards and escape clauses for setting regulation to meet national needs, developing country exporters are at a clear disadvantage.

16. IDB member countries may support proposals for a substantial reduction in applied tariffs using a harmonization formula that would reduce tariff peaks, expansion of TRQs and limitations placed on within-quota rates should be linked to the reform of quota administration favouring the auction system, application of

Special Safeguards is discriminatory, because they are not generally available to developing country governments.

17. IDB member countries should support the total abolition of export subsidies, and the regulation of export credits to ensure that they do not contain hidden subsidies. If the maintenance of an aggregate measure of support is non-negotiable as the focus of support reduction, then the argument for the developing countries to be able to apply an aggregate *de minimis* (as opposed to commodity specific) exemption becomes tenable. This should be negotiated as a concession to developing countries only, and a case made for an expansion of the *de minimis* exemptions to say, 15%.

18. There should be greater transparency in STE operations. Developing countries should exempt from any restrictions on STE activities that might reduce their bargaining power in international markets. Reinforcing existing levels of flexibility for both developing and least developed countries with respect to implementation of any new provisions; this will include maintaining measures which are currently temporary, as well as defining exemptions regarding the extent and timing of any changes to existing policies. Improved adherence to the principles contained in the relevant Ministerial Decisions, particularly with respect to technical assistance.

19. The efficient provision of services is basic to the efficiency of the commodity producing sectors. The countries where the quality of services is poor and are priced high, they would not be able to compete against imported products especially when the tariff rates go down. Poor-quality, high-priced services not only affect the current operations of manufacturers but also discourage future investment by locals and foreigners by lowering the profitability of such investment. This may be one major factor constraining the flow of FDIs to developing countries despite access to cheap labour.

20. International trade in services is estimated to be more than US\$1000 billion a year and accounts for over 20% of all the international trade. It is growing at a rapid rate; during the 1990s, the annual growth rate of trade in overall services was 12% and in telecommunications, financial, professional and business services it averaged 16%.

21. The fundamental objective of the GATS is fair trade in services under nondiscriminatory and transparent conditions. It seeks freer, if not completely free trade in services and aims to achieve nondiscriminatory trade through progressive liberalization and increased coverage of sectors in the schedules of commitments. GATS preserve the right of governments to regulate their service sectors, but at the same time it gives foreign suppliers certain rights. Where governments have not made a specific commitment, they have to adhere to the non-discrimination

principle and ensure transparency and where specific commitments have been made, they are bound to give market access and national treatment to foreign service suppliers under the conditions described in their schedules of commitments. The GATS deals extensively with rights of service suppliers in the markets of other members and as such have significant implications for investment flows and the movement of personnel across borders.

22. Trade in services can be rather helpful to IDB member countries because of the expansion in market, better returns to R&D and technological spill-overs. So far the developed countries have largely benefited from GATS commitments. The barriers to services provided by the IDB member countries include price based measures: entry and exit taxes and visa fees for the movement of natural persons; discriminatory airline landing fee, port taxes, licensing fees; tariffs on goods in which services are embodied or goods that are necessary input in the production of services; subsidies granted in developed countries including for high technology sectors as well as horizontal subsidies and investment incentives that can have a trade distorting impact on services exports from developing countries; technological standard and licensing, the licensing of commercial services and standard setting have been used to restrict entry into the industry and discriminatory access to information channels and distribution networks.

23. The next phase of bargaining in the multi trade negotiations in services will focus strongly on insurance services, professional services, telecommunication services, financial services and Maritime services. Negotiations in the insurance sector would revolve around loosening regulatory constraints including the abolition of monopolies and tax discrimination particularly, cross border supply of re-insurance; full rights to establish subsidiaries or branches; liberalisation of equity participation; elimination of monopolies and exclusive service providers; temporary entry conditions to be permitted for professional level personnel of the foreign firms; national treatment condition for insurance business related to state bodies and with respect to capital, solvency, reserve, tax and other financial conditions; transparency in the introduction of new regulations, in the requirements for license applications and in the provision of information to consumers; and establishment of independent regulatory authorities.

24. Typical barriers affecting the professional services relate to entry in the profession; segmentation of activities; professional monopolies; advertising; solicitation of new clients and prohibitions on foreign firms forming companies; use of international or foreign names; partnerships; hiring of local staff; equity or management control participation; and cross border supply.

25. The GATS telecom commitments most commonly list limitations on the number of suppliers, restrictions on type of legal entity and participation of foreign

capital. Most frequently the limits are associated with commercial presence for basic telecom services. There are significant differences between levels of commitments of developed and developing countries, with the latter having imposed more limitations on telecom service suppliers.

26. The negotiations on financial services will focus on improved international cooperation on agreed standards including methods of supervision; elimination of nationality-based restrictions on market access; and full national treatment for foreign-based financial service providers.

27. In maritime services sector negotiations would relate to auxiliary services. There may be a debate as to whether the 'three pillar' approach of transport, auxiliary and port facilities, should have a fourth pillar added for multi-modal operations involving an over-lap with land transport features and requiring additional commitments on horizontal aspects such as investments. The operators of integrated multi modal services need access to the ports, their transport connections, to customer's agents or customer premises and to be able to do marketing and advertising for new customers.

28. While the IDB member countries have potential to export services they are constrained by human resource development and technological capacity; upgrading of all the telecommunications infrastructure; a coherent pro-competitive regulatory framework for goods and services; government support to help service firms particularly SMEs to improve the quality of the service they provide; an increase in the financial capacity of service firms; promotion of their exports; use of new business technologies such as creation of alliances and networking; and presence in major markets and the capacity to exploit the opportunities offered by regional markets.

29. There is considerable discrimination against foreign suppliers in national procurement markets as the margin of preferences range from 13 to 50 percent for leading OECD nations across a wide range of government purchases. It suggests that there is considerable scope for expanding competition in national procurement markets.

## CHAPTER 1

### THE DOHA WTO MINISTERIAL CONFERENCE

#### I. INTRODUCTION

The WTO Fourth Ministerial Conference (Doha Conference) held in November 2001 in Doha, Qatar, was a major milestone towards liberalization of trade in goods and services. It calls for implementing the WTO agenda and sets the stage for the commencement of negotiations on new liberalization commitments.<sup>1</sup> Besides, it includes launching of a new global trade negotiations and a work program relating to environment, Trade Related Intellectual Property Rights (TRIPS) and access to medicines and Public Health. While Doha negotiations would help in further liberalisation of trade in goods and services, the efforts of developing world for the development round of trade negotiations have met with only limited success.<sup>2</sup> Nevertheless, developing countries have been successful in creating a new negotiating dynamics at the ministerial conference by demanding and playing an important role in shaping its outcome.

The post-Doha 'round' of negotiations is to be completed by 2005 and the ministerial conference in 2003 will take stock of the situation. The post-Doha negotiations need to be viewed in the context that:

- Free trade leads to higher economic growth due to specialisation in accordance with comparative advantage. Since tariffs, discriminatory regulations and lengthy trade procedures hamper the trade and result in lower growth, trade liberalization would help in an increase in welfare levels;<sup>3</sup>
- There has been sharper reduction in poverty and core labour standards have improved in the countries which have pursued pro-trade policies; and
- While removal of restrictive trade regimes eventually lead to higher level of welfare, loss of output and employment in the short run cannot be ruled out.

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<sup>1</sup> The new liberalization commitments relate to telecommunications, financial services, energy, audio visual, and express delivery.

<sup>2</sup> The development agenda included moving forward on global cooperation to expand trade outside the WTO, enacting new policies in high-income countries to provide aid for trade and adopting more trade reforms in developing countries [World Trade Organization, (2002a)].

<sup>3</sup> It is estimated that abolishing all trade barriers could increase global income by US \$2.8 trillion and lift 320 million people out of poverty by 2015. If all subsidies to agriculture in OECD countries are removed, it could return to developing and least-developed countries- the poorest of the poor-three times more than all the overseas development assistance (ODA) they currently receive. Complete liberalization in all sectors – agriculture, services and manufactures would benefit these countries by almost eight times ODA [World Trade Organization (2002b)].



Even though Islamic Development Bank (IDB) Member countries have made significant progress towards liberalizing their economies<sup>4</sup>, there is still a need to liberalise their economies further. Despite the fact that restructuring has resulted in closure of large number of firms and industries in which they did not have comparative advantage and consequently growth of the manufacturing sector has slowed down, the overall GDP growth rate of IDB member countries has remained somewhat constant. A further liberalisation can strengthen their growth prospects through an orderly elimination of high tariffs, tariff peaks, tariff escalation and elimination of non-tariff barriers.

The IDB member countries, in general, have large agriculture sector. The manufacturing sector that has grown at a rapid rate, has two main characteristics. Firstly, since it has grown behind steep tariff walls, it is quite inefficient. Secondly, it concentrates on a few products including textiles, leather and food products. Therefore, while on the one hand, IDB member countries have to lower their tariff rates to expose their producers to competition, they have to ensure that their exports do not face restrictions which distort the comparative advantage. Accordingly, they must ensure the success of liberalization policies in general and towards agriculture in particular. This is all the more important in the context that IDB member countries are labour surplus, heavily dependent on the agriculture sector and have limited domestic markets. Moreover, IDB member countries can carve out a large market share in the services sector in view of the cheap labour force equipped with human resource development. However, they have to watch out their interests rather carefully in view of the misuse of safeguard measures, incorporation of environment and labour standards, and non-implementation of special provisions for developing and least developed countries. The IDB countries, individually or collectively, must exert the pressure to safeguard their interests in view of the fact that WTO is a member-driven organization, which functions on the principle of consensus.

The present study takes three main issues on which post-Doha negotiations are to be held, viz. market access, the agreement on agriculture and the agreement on services sector. Plan of the study is as follows. After this introductory section the key issues, commitments and obligations of the IDB member countries in the WTO regime relating to Doha Declaration are reviewed in section II. Market access issues and how IDB member countries can maximize their welfare through proper negotiations are discussed in Chapter 2. The Agreement on Agriculture, main issues and the possibilities of maximizing IDB member countries' trade through reduction in subsidies and import barriers are analysed in Chapter 3. The

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<sup>4</sup> Trade openness is measured as the ratio of imports and exports to GDP. Among IDB member countries it has increased from 44.3 percent in 1990 to 61.5 percent in 2000; see appendix table A5.

significance of services sector in the economies of IDB member countries, the GATS agreement, main issues and strategies for IDB countries for their resolution are analysed in Chapter 4. Major conclusions of the study are summarized in Chapter 5. The Annexure presents the IDB member countries who are members of the WTO.

## **II. THE DOHA AGENDA AND DECLARATION**

The agenda for Doha Ministerial conference included agriculture, services, investment and competition rules, trade facilitation, anti-dumping and anti-subsidy rules, dispute settlements, environment, labour and the development issues of the developing countries. The six issues identified for discussion included: agriculture, implementation, Trade Related Intellectual Property Rights (TRIPS) and public health, environment, WTO rules, and the Singapore issues. The complexity of the issues and already established positions of developed and developing countries led to fierce negotiations. Besides existing North South divide, major stumbling blocks in launching the new round were the differences even among the Quad countries (the US, the EU, Japan and Canada) defending their respective interests. The EU's non-acquiescence on environment and agricultural subsidies (a major impediment to launch a new round at Seattle) and US's non-acceptance to discuss the antidumping and countervailing measures along with market access for developing countries made the negotiations more complex and thorny. Nevertheless, work program that is spelt out in two declarations, main declaration and one on TRIPS and public health, and one decision on implementation, i.e. developing countries' difficulties in implementing current WTO agreements, have been approved. The main ministerial declaration includes elaboration of objectives and timetables for the current negotiations in agriculture and services, negotiations on a range of issues such as industrial tariffs, trade and investment, trade and competition policy, some aspects of trade and the environment, etc. Negotiations under the work programme are to be concluded not later than 1<sup>st</sup> January 2005 but negotiations on improving and clarifying the Dispute Settlement Understanding must be concluded by the end of May 2003. Other elements of the work programme are to be concluded by the end of 2002 or by the next Ministerial Conference. The conferences have to take place at least once every two years. The declaration in TRIPS and public health spells out the recognition of flexibilities in the agreement to deal with health problems. It also sets out specific tasks for the WTO TRIPS Council. The main category of new issues being pushed into the WTO agenda includes international investment rules, competition policy, transparency in government procurement, global coherence, trade facilitation, industrial tariffs and environment.

Developing countries are frustrated over the outcome of Doha and feel that trade agenda of the commercial interests of the developed world has been taken up

while their agenda has been excluded. They have been calling for fairer existing trade agreements in view of the fact that their development efforts have been undermined by agreements on agriculture, textiles, intellectual property rights, investment measures and anti-dumping. They required action in the following four key areas:

- **Agriculture:** For nearly 50 developing economies agriculture accounts for over one third of export earnings and for nearly 40 of them it represents over half. Yet massive agricultural support in the developed countries undercuts the developing countries and forces even the most efficient producers out of markets where they would otherwise be earning foreign exchange. A key element of development agenda was to reduce substantially such support and eliminate the specific export subsidies. Besides average Organization for Economic Cooperation and Development (OECD) bound tariff rate for agricultural products is four times that of industrial products. This has affected badly the developing world especially the rural poor.
- **Textiles and clothing:** This is the largest export earner for many developing countries, and the negotiations must ensure that the sector is "integrated" as planned for 1 January 2005. Given the back-loading of this agreement, with the bulk of changes substantively improving exports prospects of developing countries being left until the final year, there is every reason to be extremely vigilant.
- **Tariff peaks:** Despite low average non-agricultural tariffs, the products in which developing countries are globally competitive continue to attract relatively high tariffs.
- **Tariff escalation:** Tariff escalation is a tilt against the value-added chain. If developing countries are ever to diversify their economies away from the dependence on a few primary products for most of their foreign exchange earnings, such escalation must be eliminated.

The Doha Declaration provides the mandate for negotiations on various subjects, including the issues related to the implementation of the present agreements, new commitments on services and agreements to go into new areas such as TRIPS, environments, etc. It emphasizes tariff-cutting negotiations including reduction or elimination of tariff peaks, high tariffs and tariff escalation and removal of non-tariff barriers on products of export interest to developing countries. It was agreed at Doha that the international trade should continue to be governed by multilaterally agreed rules and craft better WTO rules by revising some of the existing ones. The debate on the 'implementation issues' has led to the

conclusion that several WTO agreements need to be adjusted to better reflect particular interests and concerns of both the developing and the developed world.

The Doha Declaration extends the negotiations for liberalizing access to markets. The negotiations on agriculture and services, which began in 2000, are now moving into a higher gear. Negotiations have begun on market access for industrial products, including textiles and clothing, covering both tariffs and non-tariff barriers, and tariff peaks and escalation. The agenda also covers a range of "new issues", which include competition policy and foreign direct investment, transparency in government procurement, trade facilitation and the environment. Important decision on these issues will have to be taken at the WTO's next Ministerial meeting, to be held in Mexico in the second half of 2003.

The negotiations on agriculture started in early 2000 and a large number of proposals were submitted by 121 governments by November 2001. As per Doha Declaration, agriculture is now part of the single undertaking in which all the related negotiations relating to market access; export subsidies; and domestic support are supposed to be completed by January 1, 2005.

The Doha Declaration allows Special and Differential Treatment (SDT) for developing countries and hopes that negotiations are effective and enable the developing countries to meet their needs especially the rural development and the food security. The non-trade concerns, such as environment protection, food security and rural development were also noted. The WTO agreement gives developing countries longer time period for implementing the agreements to increase the trading opportunities for the developing countries and SDT provisions are to be reviewed and strengthened to make them more precise.

The Services negotiations officially started in early 2000 under the Council for Trade in Services. The Council initiated the negotiating guidelines and procedures in March 2001. The Doha Declaration reaffirmed the negotiating guidelines and procedures and established the timetable and the deadline for the conclusion of negotiations as part of the single undertaking that has to be finished by January 1, 2005.

At Doha, ministers recognized the importance of the technical assistance and placed emphasis on helping poor members to integrate into the trading system and participate fully in the negotiations.<sup>5</sup> The redesigned integrated framework will also help Least Developed Countries (LDCs) mainstream trade into their national development plan and strategy for poverty reduction.

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<sup>5</sup> Members have acted decisively by approving an increased secretariat budget for 2002 and pledging 30 million Swiss Francs to a new Global Trust Fund for technical assistance.

## CHAPTER 2

### MARKET ACCESS ISSUES AND IDB MEMBER COUNTRIES

The IDB member countries, most of which are developing countries, have developed their manufacturing industries behind steep tariffs and non-tariff barriers and following the trade liberalisation their economies especially the manufacturing sector needs to be restructured. While specialisation in accordance with the static comparative advantage requires that both the tariffs and non-tariff barriers are removed, in the presence of divergence in the long and short run comparative advantage, protection to domestic industry is necessary for realising the long run comparative advantage. Out of the two instruments of protection, i.e., tariffs and non-tariffs, the former is preferred because it is less distortionary and more transparent.

Since tariffs do distort the comparative advantage<sup>6</sup>, reduction and elimination of tariffs has been the centre of trade negotiations since the inception of General Agreement on Trade and Tariff (GATT) and continue to be an important subject in the subsequent multilateral trade negotiations. During the Uruguay Round, tariff negotiations constituted a central issue; tariff negotiations were held on the basis of Most Favoured Nation (MFN) principles<sup>7</sup>. These MFN rates were bound and could be increased only through negotiations under Article XXVIII of GATT and therefore, provide a secure and stable market access. Nevertheless, there are significant tariff peaks<sup>8</sup> on products such as textiles, clothing and leather products. Besides, contingent protection instruments, particularly anti-dumping measures, are currently being used more frequently. The number of anti-dumping investigations has increased sharply since the Uruguay Round agreements were signed. They have more than doubled from 156 in 1995 to 340 in 1999 [Bacchetta and Bora (2001)]. High tariff bounds, tariff escalation and safeguard measures indicate the heavy odds against exports of IDB member countries.

The comparison of average applied and bound rates in pre-Uruguay with post-Uruguay round outlined in Table 1 is quite revealing. The applied rate of tariffs of the industrial countries has increased from 2.6 to 4.0 percent and bound rate from 3.7 to 4.7 percent (see Tables 1 and 2). That liberalization attempts have resulted in higher tariff rates is quite disturbing. Probably, this reflects the

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<sup>6</sup> The non-tariff barriers are more distortionary and as such GATT and WTO called for their elimination prior to reduction in tariffs. Most of the non-tariff barriers have already been removed.

<sup>7</sup> MFN requires that tariff rates negotiated between particular trading partners are available to all members of the WTO.

<sup>8</sup> High tariffs and tariff peaks are generally in the areas that are of export interest to developing countries and it includes textiles and clothing, footwear, and agriculture. The impact of tariffication of agricultural nontariff barriers (NTBs) in the Uruguay Round in some cases has resulted into even more restrictive trade regimes.

tariffication of the non-tariff barriers and as such it is hardly helpful in trade promotion. While applied rate of developing economies has declined somewhat, the bound rate has gone up.

**Table 1**  
**Pre-Uruguay Round Applied and Bound Rates**  
**of Industrial and Developing Economies by Major Product Group** (percent)

Product Group	Industrial Economies		Developing Economies	
	Applied	Bound	Applied	Bound
1. Agriculture, excluding fish	5.2	7.2	18.6	19.9
2. Fish and fish products	4.2	4.9	8.6	25.9
3. Petroleum	0.7	0.9	7.9	8.4
4. Wood, pulp, paper, and furniture	0.5	0.9	8.9	10.3
5. Textiles and clothing	8.4	11.0	21.2	25.5
6. Leather, rubber, and footwear	5.5	6.5	14.9	15.4
7. Metals	0.9	1.6	10.8	10.4
8. Chemical and photographic supplies	2.2	3.6	12.4	16.8
9. Transport equipment	4.2	5.6	19.9	13.2
10. Non-electrical machinery	1.1	1.9	13.5	14.5
11. Electrical machinery	2.3	3.7	14.6	17.2
12. Mineral products; precious stones and metals	0.7	1.0	7.8	8.1
13. Manufactures, not elsewhere specified	1.4	2.0	12.1	9.2
All Industrial goods	2.5	3.5	13.3	13.3
All merchandise trade	2.6	3.7	13.3	13.0

*Source:* Finger, Ingco, and Reincke (1996).

**Table 2**  
**Post-Uruguay Round Import-Weighted Applied and Bound Tariff Rates** (percent)

Country Group or Region	Applied Tariff rate	Bound Tariff Rate
Industrial economies	4.0	4.7
Developing economies	13.1	20.8
Latin America and the Caribbean	10.1	18.6
East Asia and Pacific	9.8	16.6
South Asia	27.7	56.1
Other Europe and Central Asia	9.6	14.9
Middle East and North Africa	14.4	26.8
Sub-Saharan Africa	16.5	19.8

*Sources:* Hockman, Bernard et al (2002).

Tariff escalation is quite harmful to the industrialization process of the developing economies. Reduction in tariffs on raw materials by the developed countries results in higher levels of effective protection on finished and semi-finished products and thus making it even more difficult for the developing economies to export the manufactured products to industrial countries. Table 3 shows quite clearly the tariff escalation in the industrial and tropical products [For details, see Michalopoulos (1999)].

**Table 3**  
**Tariff Escalation on Products Imported by**  
**Industrial Economies from Developing Economies**

Product	Post-Uruguay Round bound tariff (percent)		
	All industrial Products (excluding petroleum)	All tropical products	Natural resource-based products
Total	4.3	1.9	2.7
Raw materials	0.8	0.0	2.0
Semi-manufactures	2.8	3.5	2.0
Finished products	6.2	2.6	5.9

Source: GATT (1994)

#### *Doha-Declaration and Market Access*

The Doha Ministerial Declaration<sup>9</sup> follows almost the same formulation as in the declaration to launch Uruguay Round in 1986. It envisions reduction or elimination of industrial tariffs as well as an attack on tariff peaks, tariff escalations and non-tariff barriers in particular on products of interest to developing countries. These are expected to help in the growth of trade which provides opportunities to the IDB member countries to alleviate poverty through trade liberalisation. While they must reduce the level of tariffs to expose their economic activities to international competition, they need market access; currently their products face many obstacles in entering the markets of rich countries. Rich countries need to do more to reduce trade distorting subsidies and dismantle their existing barriers on competitive exports from developing countries. The important issues in this regard are:

- Textiles and clothing is the largest export earner for many developing countries, and the negotiations must ensure that the sector is integrated as planned for 1 January 2005. Given the back-loading of this agreement there is every reason to be extremely vigilant.

<sup>9</sup> This is referred to in para 16 of the declaration.

- **Agricultural support** by the developed countries undercuts the developing countries and forces even the most efficient producers out of markets where they would otherwise be earning foreign exchange. Two key elements are to reduce substantially such support and the average OECD bound tariff rate for agricultural products is four times that of industrial products.
- **Tariff peaks** negotiations have to be high on the agenda. Despite low average non-agricultural tariffs, the products in which developing countries are globally competitive continue to attract relatively high tariffs.
- **Tariff escalation** tilts the incentives against the development of indigenous processing/transformation and movement up the value-added chain. For diversification of economies and trade such escalation must be eliminated.
- **Specific Taxes** generally are high. These need to be converted into ad-valorem rate. To start with, each member state should provide information on the ad-valorem incidence of the specific taxes.
- **Anti-dumping duties, technical standards and sanitary and phytosanitary (SPS) requirements** restrict trade and the possibility that the contingent protection measures may be justified on the grounds of environmental protection and labour standards is of great concern to developing world. Since developing countries generally have lower labour and environmental standards than developed countries, these would be detrimental to export and development interests of developing economies [Krueger (1999)].

## 2.1 FEATURES OF TARIFF NEGOTIATIONS

While tariff negotiations have been at the heart of most multilateral trade rounds, there are various approaches to tariff negotiations. The choice of the negotiating techniques is vital because each technique would yield different qualitative and quantitative results. Which technique may be used depends on the objectives of a nation or group of nations. Some of the techniques of tariff negotiations are:

- (i) **Linear Tariff Reduction Formula:** This technique was applied in the Kennedy Round and broadly consists of an across-the-board reduction of all rates in the tariff schedules by a specific and equal percentage. While this technique lowers average rate of duties, it does not affect the structure of tariffs and, hence, imbalance in duties continues to prevail.
- (ii) **Harmonization Formula:** This formula was adopted during the Tokyo Round. This technique implies cutting high rates by a greater percentage than the lower tariffs. It helps in realization of both the objectives of lowering as well as rationalizing the tariff rate structure. This formula by



definition contributes to harmonization of tariffs. Nevertheless, tariffs are slashed across the board irrespective of the products. Accordingly, if certain industries need to be protected, this formula needs to be avoided.

- (iii) Offer-Request Formula: This technique implies exchange of concessions on a product by product basis. The negotiations under this formula are conducted on reciprocal basis but any reduction achieved is applicable to all the members through the MFN provision of the GATT.
- (iv) Zero-for-Zero Formula: This approach implies zero-for-zero tariffs on a selected group of products between the interested parties but the MFN provisions of the GATT apply. So far, the sectors covered under this technique include pharmaceuticals, medical, agricultural and construction component, etc.

## 2.2 RATIONALE FOR TARIFF REDUCTION AND MAIN TARIFF ISSUES IN THE POST-DOHA SCENARIO

The post-Doha industrial tariff negotiations are prompted by three main considerations: Firstly, the increasing trend towards regionalism results in preferential trade amongst a few countries resulting in discriminatory trade treatment for the countries that are not parties to the regional arrangements. Tariff negotiations on multilateral basis resulting in an MFN-based tariff cuts would reduce chances of such discrimination. Second, the developed countries that follow protectionist policies in the field of agriculture argue that if liberalization is confined to agriculture sector only and no liberalization takes place in the industrial sector, the results of tariff negotiations would be lopsided. Third, industrial tariff negotiations have the potential to boost intra-regional trade among developing countries, should such negotiations lead to tariff cuts on MFN basis. The main tariff issues in the post-Doha scenario are examined in the following.

### (i) Tariff peaks and escalation

Problems of frequency, high tariffs and tariff escalation remain wide spread for developing countries even after the Uruguay Round. A significant proportion of the tariff of Quad countries (USA, EU, Canada and Japan) continues to exceed the level of 12% ad-valorem even after full implementation of the Uruguay Round and GSP rates are taken into account (see Table 4). One fifth of the tariff peaks of the United States, about 30% of those of Japan and the EU and about one seventh of those of Canada exceed 30%. Peak tariffs affect both agricultural and industrial products but more significantly the former products.<sup>10</sup>

<sup>10</sup> Out of the total LDC exports of US\$22.7 billion in 1999, US\$17 billion went to the Quad economies. For example, more than 25 percent of their total exports are potentially affected by tariff peaks in Canada and 14 percent in the United States.

The main problems occur for major staple foods such as rice, sugar, milk products and meat; fruit, vegetables, fish etc; food industry products; textiles and clothing; footwear, leather and travel goods; automotive products; consumer electronics and watches. Peak tariffs are for the time being accumulated with the continued application of stringent textiles and clothing quotas by three of the most developed markets (USA, EU and Canada) as well as severe import restrictions maintained for reasons of plant and animal health. In addition to extremely high tariffs and other protection measures, tariff escalation remains an important obstacle for developing countries to enter into the industrial exports. This is particularly pronounced in the sectors which are of direct export interest to developing countries including the IDB member countries.

**Table 4**  
**Developed Countries: Frequency of Post-Uruguay**  
**Round Tariff Peaks in the Industrial Sector by Product Groups**

(Percentage of tariff lines within each group with duties above 12 percent ad-valorem)

Product Group	United States	Canada	European Union	Japan
Leather & leather products	12	4	0	22
Textiles	21	45	1	1
Clothing	44	93	0	0
Footwear	42	67	0	71
Glass products	10	5	0	0
Vehicles	4	1	8	0

Source: UNCTAD Trade and Development Report 1999.

The problem of peak tariffs occurs in six sectors: (a) major agricultural staple food products; (b) fruit, vegetable, fish etc; food industry; (d) textile & clothing; (e) foot wear, leather and travel goods; (f) automotive sector and a few other transport and high technology goods.

- (i) Major agricultural food and commodities: The most important areas with the high frequency and the highest rates are the major agricultural staple foods, in particular, wheat, sugar, milk, butter, cheese and cereal as well as tobacco products. Removal of quantitative restrictions, levies and other non-tariff barriers and replacing them with tariffs on these products have resulted in extremely high rates exceeding in most cases 30% and reaching upto 900%.

- (ii) Fruit, vegetables, fish etc: In these areas, tariff peaks are generally lower than in the above mentioned major food sectors but nonetheless very common. In most cases peak duties for major fruit, vegetables and fish range from 12 to 30%. This is frequently the case for oranges and citrus fruit, pineapples, apples, grapes and tomatoes in the high season. Special national features include the prohibitive tariffs for the above quota imports bananas into the EU; dried beans and peas into Japan; and groundnuts into the United States.
- (iii) Food Industry: The food industry is a major area where tariff protection is widespread and high in the major developed countries markets even after the implementation of the Uruguay Round concessions. Tariff peaks and a range of additional measures extend far beyond the initial processing stages in a large variety of industries. The EU's food industry accounts for about 30% of all tariff peaks ranging (with some exceptions) from 12% to 100%. There are several cases of additional duties to compensate processing industries for higher prices of agricultural inputs. Examples of products subject to particularly high rates include cereals and sugar based products, fruit preparation and canned fruit juices. Similarly, the food industry accounts for one sixth of all tariff peaks in the United States and these also fall mainly into 12% to 100% range. The United States also applies a wide system of combined MFN tariff quota rates in this area particularly with additional safeguard duties.
- (iv) Textile & Clothing: In the major textile importing countries like the US, EU and Canada large proportions of clothing and textile imports are subject to high tariffs. Most tariff peaks are in the 12-32% range. These high tariffs are also combined with quantitative restrictions at present.
- (v) Footwear, Leather and Travel goods: Footwear of various types is still protected by high tariffs in most developed countries. Post Uruguay Round MFN rates are close to 160% in Japan, 37.5-58% in the US and 18% in Canada. MFN duties remain relevant, as General System of Preferences (GSP) benefits are limited in this sector.<sup>11</sup>
- (vi) Automotive sector, transport equipment and electronics: With the exception of Japan and the Republic of Korea, level of protection for one or the other branch of the transport industry is rather high. In the developed countries MFN tariff protection is more selectively applied in the automotive and transport sector. In addition various developed

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<sup>11</sup> In the US and Canada most foot wear and leather products are excluded from coverage of the scheme so that MFN tariffs apply fully to developing countries.

countries apply high tariffs on TV receivers, TV picture tubes and some other high technology products.

**(ii) Negotiations amongst Developing Countries**

The negotiations in the various Rounds of GATT have been either amongst the developed countries or between the developing and the developed countries. By negotiating reduction in tariffs on the products of their export interests, developed countries under GATT have gained significantly. On the other hand, participation of the developing countries in trade negotiations has been minimal and there have hardly been any such negotiations amongst the developing economies. The trade amongst developing countries has increased significantly but the trade would have been significantly higher if tariffs were cut on the products of their export interest. Negotiations on industrial tariffs amongst developing countries would go a long way in the promotion of trade in goods and services. It would help in increasing significantly the share of trade amongst developing countries as a proportion of their total trade.

The new market opportunities that have been created by liberalization measures in developing countries including the IDB member countries should now encourage enterprises in these countries to give equal, if not greater importance, to trade among themselves. Hence, the market access negotiations among developing countries including the IDB member countries will have particular significance in the context of IDB's objective of promoting intra-trade among its member countries. Accordingly, the IDB member countries amongst themselves or with other developing countries may negotiate industrial tariffs on an MFN basis on products that are traded or have a potential of trading between them. This would go a long way towards liberalization of trade and improvement in the welfare levels. At the same time, they may take a joint stand relating to anti-dumping, environments, labour standards and other safeguard measures to protect their export interest.

**(iii) Loss of Revenue Resulting from Tariff Reduction**

One important element in the reduction of tariffs that need to be seriously considered is fall in public revenues; custom revenues constitute a significant proportion of public revenues of the IDB member countries and most of these face fiscal problems. Therefore, IDB members must approach tariff negotiations in such a manner that it minimizes revenue loss. In this case, the choice of technique and modality of negotiations would be of paramount importance. It would be noted that in case of formula approach duties are cut across the board implying that reductions have to be made in the duties which are protective as well as those which are of purely revenue in nature. On the other hand, the product-by-product approach allows reductions to protective duties and spares cuts in duties which are

non-protective in nature. In any case, these countries may impose higher sales taxes to recoup the revenue losses.

**(iv) Scope for Negotiations: Bound and Applied Rates**

An important issue in the industrial tariff negotiations is whether such negotiations should cover bound rate only or both the bound and the applied rate. In case of developed countries major proportion of their tariffs are bound and the bound rates broadly conform to their applied rates. Therefore, reduction in bound rates would automatically result in reductions in the applied rates resulting in improvement in the market access. The situation in respect of the IDB member countries is, however, different. During the Uruguay Round many of these countries bound their tariffs at levels significantly higher than the applied rates. In some cases "ceiling bindings" were given i.e. they agreed not to increase any of the duties in their tariff schedules above the ceiling rates. In such countries a reduction in bound rates may not result in any reduction in the applied rates as the reduced bound rates still remain higher than the applied rates. Such reduced bound rates would nevertheless improve predictability of market access; exporting firms are reassured that the existing applied rates would not be increased beyond the bound rates. However, reduction in bound rates would not constitute any improvement of market access unless applied rates are reduced simultaneously. Therefore, it may be argued that market access negotiations would have to provide for possibilities of reductions in both the bound as well as applied rates.

**(v) Credit for Autonomous Liberalization**

While developed countries have generally reduced their tariffs in the context of multilateral trade negotiations, most of the developing countries including the IDB member countries have been taking measures to liberalize trade unilaterally outside the WTO framework. As the lower rates resulting from such reductions benefit the exports of developed countries, the credit should be given for the unilateral tariff reduction. It may be done by providing greater flexibility in the choice of "base tariffs" that are to be used as the basis for reductions. Countries are generally given choice to use the tariff rates applicable in the preceding 2-3 years as basis for negotiations.

**(vi) Relative Reciprocity in Negotiations between Developed and Developing Countries**

Another significant aspect of tariff negotiations is to ensure that the rules relating to relative "reciprocity" as embodied in part IV of GATT and the "General Enabling Clause" are fully respected in the negotiations between developed and developing countries. In particular, the ground rules adopted for conduct of negotiations need to be such that the extent of liberalizing the developing

economies should be in accordance with their level of development, trade, economic situation, and national policy objectives. The ground rules should further recognize that the developing countries may have the option to reduce duties on selected tariff headings and, if necessary, exclude certain sectors and sub-sectors from the liberalization process. It should also be open to them to offer tariff bindings at rates which are higher than the reduced rates.

**(vii) Staging of Tariff Reductions:**

The reductions agreed in the multilateral trade negotiations in the past have been staging over a period of time. The tariff cuts agreed in Uruguay Round were implemented in equal stages from January 1, 1995 to January 1, 2000. For some of the products, however, which were considered import sensitive, longer implementation period of 8-10 years were negotiated. The ground rules for the current tariff negotiations may allow developing countries longer period than provided to developed countries either on overall basis or in respect of particular products.

**2.3 NON-TARIFF MEASURES**

The Doha Ministerial Conference rightly calls for removal of all the non-tariff barriers on industrial products as they are least transparent and have major distortionary impact. Important non-tariff barriers on the export interest to developing countries including IDB member countries are:

- Use of licensing procedures particularly automatic licensing procedures;
- Technical regulations applicable to such products as electric machinery, chemicals and pharmaceutical products;
- Contingency protection measures such as safeguards and anti-dumping countervailing measures; and
- Quantitative restrictions on imports particularly those which apply to Textiles and Clothing sector.

With the adoption of various WTO agreements, legal framework now exists for ensuring that non-tariff measures such as licensing and technical barriers to trade do not constitute unnecessary inhibiting effect on trade. Moreover, where a country considers that measures taken by another country are inconsistent with the provisions of the relevant agreements, the matter could be challenged. The fact that disputes procedure move forward automatically make it a little difficult for larger countries to put pressure on smaller countries into giving up their legal complaints. However, most of the clauses in the Dispute Settlement Understanding (DSU) regarding developing countries have proved to be more declarative than operative. For example, Article 21.7, mandates that when a matter is raised by a developing

country, the Dispute Settlement Body (DSB) is to consider what further action might be appropriate. However, this provision has not been used by any developing country for various reasons but particularly due to lack of expertise and resources.<sup>12</sup> Besides even though Article 22 calls for financial compensation to the complaining party by the country which has been found to be in violation of the rules, it has rarely been done.

Even if a developing country obtains a clear legal ruling that an industrial country has violated its legal obligations, the developing country has no effective way to enforce the ruling. The only enforcement sanction provided by the WTO dispute settlement procedure is trade retaliation—the imposition of discriminatory trade sanctions by the complaining country against the trade of the defendant country. However, trade retaliation by smaller developing countries simply does not inflict any significant harm on larger industrial countries. In this regard, the proposal by Pauwelyn (2000) that “coupled with countermeasures, a broad scheme of compensation—additional market access offered by the losing party to WTO members—would provide genuine leverage to induce compliance, a move beneficial to all WTO members, and not just ‘compensation’ to the one or few that brought the case” should be seriously considered.

### *Environment*

It was agreed in Doha to launch negotiations on certain aspects of environmental policy particularly the relationship between environmental agreements and WTO rules. Even if environmental concerns are quite legitimate, their trade impact is inequitable between North and South. Therefore, it will be quite difficult to agree on an agenda on trade and environment. Poor countries need to be given the economic and environmental space to fulfill their development aspirations and as such impact of environment on income generation through trade liberalization must be examined. The distributional effects of trade liberalization will be crucial for understanding their potential environmental effects; it is important to have a good understanding of the effects on environmental degradation of both trade liberalization and trade distortions. Solutions to the trade and environment debate must be sought outside the WTO. Environmental and development objectives should be achieved through supportive measures and international cooperation, as well as through better coordination at the national and multilateral levels. It seems premature to engage in negotiations on trade and environment.

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<sup>12</sup> The expertise required is in the fields of checking arguments, issues, and possibilities and comparing experiences and results; exploring new legal as well as economic arguments; and, domestically, building up an efficient and transparent liaison between the state and industry in order to obtain up-to-date information on trade problems in which developing countries have a stake.

## *Labour Standards*

As regards concerns for the labour standards of the developed world, IDB members have to use a positive approach towards labour rights. While it is wrong to call for the WTO to displace the ILO in protecting workers, it would be equally wrong to ignore the legitimate economic, social, and political imperatives that call for improved dialogue, better coordination, and mutually supportive policies and institutions in the international community. A new context for improved coordination and exchange is needed.

It needs to be underscored that the proposals relating to environment and labour standard focus on accommodating measures that restrict trade as opposed to measures that promote trade [Jha and Vossenaar (2001)]. Therefore, such measures must not be on the WTO agenda.

### **2.4 NEGOTIATING STRATEGY FOR MARKET ACCESS**

Techniques and modalities that are adopted in industrial tariff negotiations have significant bearing on the outcome. A variety of techniques and modalities evolved during the eight rounds of trade negotiations which took place under the auspices of GATT have been enumerated above. The IDB member countries have to adopt an approach that results in securing maximum reductions on products which they export. As regards their commitment to reduce the import duties, they may use product by product approach. Such products that relate to industries in which the country does not have the long run comparative advantage they may agree on steep cuts while the other industries where long run comparative advantage exists but producers have become lethargic due to heavy protection, they may reduce the duties to ensure exposure to competition without jeopardizing the industrial growth. With a view to ensuring the maximum advantage, following elements may be kept in view:

- Preceding the industrial tariff negotiations it is necessary to agree on the ground rules that would be followed in the conduct of tariff negotiations. Such ground rules would need to ensure that different needs and objectives of the participating countries are adequately taken into account. In other words, ground rules must accommodate the special needs and interests of developing and the least developed countries' participants as ordained in Article XVIII and part IV of GATT;
- IDB member countries determine the extent to which they are willing to liberalise their own economies to win tariff reductions and removal of other barriers with a view to having access to the markets of their trading partners;



- IDB member countries may agree to reduce the bound rates and where they do not have comparative advantage to steep fall in tariff cuts both in bound and applied rates;
- IDB member countries should ask for conversion of all specific tariffs into ad-valorem tariffs;
- IDB member countries should strive to seek substantial reductions in peak MFN tariffs which apply to products of export interest to them e.g. textiles, leather products, footwear, etc and, if feasible, aim at elimination of all other MFN rates of tariffs and tariff escalations in sectors where they exist;
- IDB member countries ought to seek due allowance for the autonomous liberalization these countries may have undertaken. One way of ensuring credit for the autonomous liberalization is to have greater flexibility in the choice of "base tariffs" to be used as a basis for tariff cuts as a result of the industrial tariff negotiations;
- IDB member countries must seek flexibility in "staging" of tariff reductions. The ground rules for the negotiations should provide the developing countries including the IDB member countries longer period than that provided to developed countries for staging of tariff reductions; and
- IDB member countries may press for international financing for training public officials, screening industrial countries' trade policies, and building a network with other developing countries with the aim of jointly presenting cases that could help address some of these problems.

### CHAPTER 3

#### AGREEMENT ON AGRICULTURE AND IDB MEMBER COUNTRIES

Because of domestic support, high tariffs and non-tariff barriers and subsidies to exports, the agriculture sector of developing economies has suffered the most. The basic objective of the Agreement on Agriculture (AoA) is to remove the distortions and ensure that countries specialize in accordance with their comparative advantage and improve predictability and security for importing and exporting countries. The Doha Declaration reconfirms the long term objectives of AoA and lays down the time table for subsequent negotiations on reduction in tariffs and quota restrictions to ensure effective market access; reduction and eventual elimination of all types of export subsidies; and substantial reduction of domestic support which distorts the comparative advantage.

The Doha declaration calls for completion of negotiations by January 1, 2005 and allows for special and differential treatment for the developing countries in terms of new commitments as well as relevant new or revised rules and disciplines. It calls upon the WTO members to exercise restraint in challenging measures notified under the green box by developing countries to promote rural development and address food security concerns. The declaration also notes the possible negative effects of reform programme on least developed and net food-importing developing countries and includes various decisions relating to food aid, technical and financial assistance for improved agriculture productivity and infrastructure; and financing normal level of imports of basic foodstuffs. It also instituted a follow up mechanism for review of progress in implementation.

The IDB member countries face different challenges in their agricultural sector. Most of them with relatively low protection of agriculture face major challenges in expanding their agricultural exports due to the presence of high tariff and the subsidies provided by the developed world to their agriculture sector. Removal of the subsidies is expected to raise world prices which would create opportunities for exporters, but the adjustment problems for importers. Therefore, any negotiations must take into consideration the concerns of importing IDB member countries. These countries would seek to obtain an increased amount of food aid to compensate for the increased cost on the food imports.

The mandate for negotiations on agriculture derives from article XX of the AoA stipulating that new negotiations to continue the reform process are to be initiated by 1 January 2000 taking into account:

- The experience with respect to the implementation of the reduction of commitments;

- The effects of reduction commitments on world trade in agriculture;
- Non-trade concerns, special and differential treatment for developing country members and the objective system; and
- Any further commitments necessary to achieve the long term objective of a substantial progressive reduction in support and protection.

The market access is provided by replacing the non-tariff with tariffs and reducing the tariff rates even further.<sup>13</sup> However, in case the quotas continue for certain products, the quantities imported prior to the agreement cannot be reduced. Moreover, through a system of "tariff-quotas", further quantities of the product are allowed *albeit* at higher tariffs. The products whose non-tariff restrictions have been converted to tariffs, special emergency actions, i.e. safeguards, are allowed with a view to preventing swiftly falling prices or surges in imports from hurting their farmers.<sup>14</sup>

Doha declaration calls of effective implementation of the AoA by both the developed and developing economies in accordance with the agreement.<sup>15</sup> The Doha declaration sets a new mandate by making the objectives more explicit, building on the work so far done and by setting deadlines.<sup>16</sup> Because views and interest of each of the member countries differ, the negotiations are going to be long drawn; each country's commitments would vary depending on the outcome of negotiations.

### 3.1 MAJOR ISSUES IN TRADE IN AGRICULTURE

#### (i) Tariffs

Despite the AoA agreement the tariff rates on agricultural products continue to be rather high. In the 23 major industrialized countries tariff rate on agricultural products is 6.4 percent [see Wilson (2002)]. While this tariff rate is much lower than that of the developing countries (18.1%), it is relatively high compared to a number of industrial products where it has been reduced to zero percent. Moreover, this is an underestimate in view to the lingering quota and tariff-quota restrictions. As pointed out earlier, the developed countries use specific

<sup>13</sup> In developed countries, the production-weighted average nominal rate of protection for agriculture is estimated at 33 percent, as compared with 2 percent for manufacturing industries [Anderson (1999)].

<sup>14</sup> Agreement specifies when and how these emergency actions can be introduced e.g. they cannot be applied for tariff-quota imports.

<sup>15</sup> It may be reiterated that the developed countries were to cut the tariffs by an average of 36 percent, in equal steps over six years, while developing countries were to make 24 percent cuts over ten years period.

<sup>16</sup> The key dates for AoA are (i) Formulas and other "modalities" for countries' (ii) commitments: by 31 March 2003 (iii) Countries' comprehensive draft commitments: by 5<sup>th</sup> Ministerial Conference, 2003 (in Mexico) (iv) Stock taking: 5<sup>th</sup> Ministerial Conference, 2003 (in Mexico) (v) Deadline: by 1<sup>st</sup> January 2005, part of single undertaking.

import duties as well and in general their ad-valorem effect ranges from around 22% to 90%. Since non-advalorem tariffs, by definition, weigh more heavily against low priced agricultural exports from the developing countries, there is an urgent need for resolving these issues.

Table 5 exhibits simple averages for applied and bound tariffs as well as for differences between the two for different developing country income groups and regions. It needs to be underlined that the pattern of both the average bound and the applied tariffs in manufactures tend to vary inversely with per capita income, i.e., the poorer the country, the higher the tariffs. This holds for all sectors and groups with the exception of applied tariffs in agriculture, where there is little difference between the average for the high income and middle-income countries. Similarly, the average differences in the margins between applied and bound tariffs tend to be highest in the low-income countries and lowest in the highest income one.

**Table 5**  
**Tariff Averages**

	(Percent)								
	BOUND			APPLIED			MARGIN		
	M	A	T	M	A	T	M	A	T
42 developing countries	42	59	49	17	21	19	23	34	30
High income (4)	17	29	20	5	20	8	12	10	12
Middle Income (23)	34	48	39	16	18	17	18	30	22
Low Income (15)	64	86	75	24	27	25	38	52	50
Latin America and the Caribbean (13)	33	40	38	13	14	13	21	26	25
Asia and Pacific (12)	34	49	37	19	26	21	14	18	16
Sub-Sahara Africa (12)	63	84	74	20	19	20	39	59	54
Europe, Middle-East And North Africa (5)	37	70	46	21	29	23	16	41	23

Explanations:

M: Manufactures

A: Agriculture

T: Total; for all products

Source: Mchalopoulos, C. (1999).

Most of the IDB member countries have bound only a small proportion of the lines in their tariff schedules and have bound their tariffs at substantially higher rates than they apply. Tariffs of IDB member countries on import of agricultural products are rather high. Nevertheless there is a great variability amongst the IDB member countries. Since several IDB member countries chose to set fixed bound tariff ceilings that do not decline over the years, they have significant room to

maneuver. Since there are large differences between bound and applied rates in the IDB member countries, these countries may negotiate to reduce bound rates against concessions by the developed world (see Table 6).

**Table 6**  
**Selected IDB Member Countries Tariffs**

							(Percent)
Country	Year	Bound	Applied	SD	CV	Margin	% Unbound
Bangladesh	1996	84.0	29.0	15.0	0.5	54	-
Benin	1998	114.0	13.0	6.4	0.49	101	-
Cameroon	1994	80.0	21.0	4.7	0.2	59	-
Egypt	1993	48.0	32.0	16.2	0.5	15	-
Indonesia	1999	38.0	10.0	-	-	29	6
Malaysia	1996	19.0	9.0	14.4	1.7	10	21
Morocco	1995	42.0	25.0	13.1	0.5	17	0
Pakistan	1996	68.0	68.0	16.3	0.2	0	70
Senegal	1989	17.0	12.0	-	-	5	42
Tunisia	1995	69.0	31.0	7.5	0.2	38	47
Turkey	1995	30.0	11.0	4.8	0.4	19	55
Uganda	1996	62.0	17.0	4.7	0.3	45	75
Average		55.92	23.17				

**Explanation:**

**Bound** - Simple average bound rate at the end of implementation of URA on 01 January 2005.

**Applied** - Simple average applied rate

**SD** - Standard Deviation for Applied Tariff Lines

**CV** - Coefficient of Variation: SD divided by the Applied tariff

**% Unbound** - Proportion of total tariff lines unbound

**Margin** - Difference between the average bound and applied rates

**Source:** Michalopoulos, (1999).

It is rather surprising that bound rates of a large number of IDB member countries having comparative advantage in agriculture are rather high. Not only that, even the average applied tariffs on agricultural products in general are higher than tariffs for the manufactures. Moreover, the standard deviation is higher for agricultural products than for industrial products, indicating that the differences between the tariffs on different agricultural products are significantly higher than the differences between the tariffs on different industrial products<sup>17</sup> (see Table 7). IDB member countries may reduce these bounds significantly in exchange for concessions on their exports.

<sup>17</sup> Standard deviation is the indicator of the dispersion of tariffs. The dispersion of tariff indicates the dimension of a country's schedule. The higher the dispersion of tariffs, the higher the cost of tariff protection in terms of economic welfare.

The preceding discussion shows quite clearly that tariffs on agriculture sector of both the developed and developing countries are rather high. The developing countries having comparative advantage not only have relatively higher tariffs, the tariffs on agriculture are higher compared to manufacturing. They must reduce their bound and applied rates and negotiate concessions against them.

**Table 7**  
**Selected IDB Member Countries Tariff Rates by Sector**

						(Percent)
Country	Sector	Bound	Applied	SD	CV	Margin
Bangladesh	Agriculture	84	30	14.5	0.5	54
	Manufactures	84	27	14.9	0.6	56
Benin	Agriculture	79	-	-	-	-
	Manufactures	119	-	-	-	-
Cameroon	Agriculture	80	23	4.9	0.2	57
	Manufactures	79	20	4.6	0.2	59
Egypt	Agriculture	92	34	24.6	0.7	58
	Manufactures	33	31	13.5	0.4	1
Indonesia	Agriculture	47	9	24.3	2.8	39
	Manufactures	37	10	15.7	1.6	27
Malaysia	Agriculture	17	5	8.3	1.7	12
	Manufactures	20	9	14.9	1.6	10
Morocco	Agriculture	44	29	13.8	0.5	16
	Manufactures	42	24	12.9	0.5	18
Pakistan	Agriculture	101	71	16.6	0.2	30
	Manufactures	51	67	16.2	0.2	-16
Senegal	Agriculture	30	0	0	**	30
	Manufactures	12	13	-	-	0
Tunisia	Agriculture	115	35	7.4	0.2	80
	Manufactures	49	30	7.5	0.3	19
Turkey	Agriculture	53	18	10.1	0.6	35
	Manufactures	21	8	3.1	0.4	12
Uganda	Agriculture	61	23	5.6	0.2	38
	Manufactures	63	15	4.4	0.3	48

**Explanation:**

\*\* not applicable

Bound Simple average bound rate at the end of implementation of URA on 01 January 2005.

Applied Simple average applied rate

SD Standard Deviation for Applied Tariff Lines

CV Coefficient of Variation: SD divided by the Applied tariff

Margin Difference between the average bound and applied rates

Source: Michalopoulos, (1999).

**(ii) Non-Tariff barriers**

Where tariffs were the only form of protection for agricultural products, they were bound to a maximum level under WTO. However, for a number of

products, market-access restrictions involved non-tariff barriers, a "tariffication" package was agreed which provided for the replacement of agriculture-specific non-tariff measures with a tariff which afforded an equivalent level of protection. The tariffs resulting from the tariffication process are rather high. Following the AoA, there is now a prohibition on agriculture-specific non-tariff measures, and the tariffs on virtually all agricultural products traded internationally are bound in the WTO. Developing countries may apply ceiling bindings for most commodities instead of using tariffication formula and primary agricultural products, which are important in traditional diets, are exempt subject to very strict criteria.

### **(iii) Further Liberalization Plus Tariff Harmonization**

Agricultural Exporter Developing Countries (AEDCs) have a strong interest in further liberalisation and tariff harmonization approach because their principal concern is market access. The erosion of preferential access and GSP margins heightens the concerns of such countries. They want more effective tariff reductions and rationalization of the anomalies within AoA. Similarly, the tariff peaks, another major issue for developing country exporters, and a formula of tariff cuts that facilitate a degree of tariff harmonization is necessary.

### **(iv) Tariff Rate Quotas (TRQs)**

Reform of the regime governing tariff rate quotas is extremely important in gaining market access. The reform options need to revolve around the abolition of TRQs accompanied with very substantial tariff cuts and the expansion of quotas with effective limits placed on within-quota rates. Modifications to the tariff rate quota system ranging from substantial increases in the quantities subject to lower rates to elimination of tariff rate quotas as well as possible disciplines on tariff quota administration are required. Substantial tariff cuts and the removal of tariff peaks and wedges need to be negotiated for an effective access to developed country markets. Abolition of TRQs is a potential mechanism for bypassing developed country protectionism.

### **(v) Domestic Support**

The AoA distinguishes between support programs that stimulate production directly and those that are considered to have no direct effect. Domestic policies that do have a direct effect on production and trade have to be cut back. Developed countries have agreed to reduce the total aggregate measure of support by 20 percent over six years period starting in 1995, while the developing countries cuts are targeted at 13 percent reduction during the 10 years period.<sup>18</sup> Domestic

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<sup>18</sup> The AoA classifies countries into four groups: (1) those with AMS in an acceptable range (Green Box), (2) those who have high AMS but have agreed to reduce (Amber Box), (3) those with AMS beyond the range of (2)

support such as production subsidies are more common among developing countries and are often market distorting. Due to their variety and complexity, it is difficult to establish common measures of support.

Governments in most developing countries subsidize agricultural inputs, including fertilizer, irrigation, seeds, electricity and credit to partly mitigate the bias against agriculture caused by export taxation and industry policy. This form of support appears to be largely for reasons of administrative convenience and also because reduced input costs enable farmers to produce at prices that are constrained by social objectives. A number of developing countries concerned about ensuring access to basic food by a growing population have typically used consumption subsidies to keep food prices down. A wide array of domestic support arrangements at present continue to feature in the agricultural policies of many developing countries.

#### **(vi) Green Box**

Some forms of support that are exempt from any reductions include a range of government services (such as research, training, infrastructure services, stockholding for food security objectives and domestic food aid), decoupled direct payments (such as decoupled income support, income insurance, disaster relief and regional assistance programs), support through investment aids, payments under environmental programs and payments under regional assistance programs. These exemptions are sometimes called 'green box' exemptions. Measures involving direct payments under production limiting arrangements that conform to certain criteria are also exempt and are sometimes called 'blue box' exemptions.

#### **(vii) De-minimis Provision**

Another special provision is *de minimis* provision. Under this, countries are allowed to provide non-exempt domestic support up to a given percentage of the value of total production, without such support being subject to reduction commitments. For developed countries, the percentage agreed was 5 percent of commodity specific support and also 5 percent of non commodity specific support. Government outlays on domestic producer support in developing countries have tended to be below the *de minimis* level because of budgetary pressures.

Further reduction in AMS, elimination of the *de minimis* level for member countries with high AMS, allowing developing countries to recalculate their AMS or raising their *de minimis* level to 2.0-2.5% and correcting or clarifying the methodological problems in the calculations of AMS in a manner favourable to

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(Red Box)-forbidden, and (4) those who are exempt from the general rule, but with payment associated with acreage or animal numbers [Wilson (2002)].



developing countries. Since developing countries have been used to provide only small subsidies, the measure is discriminatory against developing economies.

#### (viii) Aggregate Measurement of Support (AMS)

The aggregate measurement of support (AMS) is the level of domestic support that is subject to reduction commitments. In general, for developing countries it is far lower than most of the developed countries. However, the AMS levels are not a consistent measure of market distorting domestic arrangements.

The aggregate measurement of support tends to be relatively low for most developing countries. It is less than one percent of agricultural produce in most of the developing economies and in some countries it is even negative. On the other hand, in the EU and Japan, it is 22.9 and 32.5 percent respectively of agricultural output (see Table 8). An important issue is whether the nature of the domestic support provided distorts agricultural incentives in these countries. Typically, product specific support in developing countries is not evenly distributed across all agricultural commodities. Instead, developing countries tend to target their support to only a subset of commodities, with adverse implications for the allocation of resources within agriculture. In countries where price support is provided, it tends to be allocated to traditional crops such as rice and sugar.

While AMS has been reduced, the overall level of subsidization of agriculture has increased in the developed countries as a result of re-instrumentation of support from measures subject to reduction commitments to those not subject to such commitments. Consequently, the total support estimate (TSE) of the countries belonging to OECD rose from US\$ 308 billion in the period 1986-1988 to US\$ 361 billion in 1999.

Lack of financial resources limits developing countries' ability to subsidize their agriculture sector and, therefore, they suffer from an inherent disadvantage compared to the developed countries. AoA institutionalizes the disparity by allowing developed countries to maintain 80 percent of their base-level AMS, while prohibiting the developing countries from going beyond the *de minimis* level of 10 percent set for them.

#### (ix) Export Subsidies

The Agreement on Agriculture requires members to notify the WTO of their intent to use export subsidies. As of February 2001, 25 member countries are allowed to use the subsidy. They are mainly middle to high-income countries, and Indonesia is the only IDB member country on the list. This is partly because many developing countries are incapable of financing export subsidies. While IDB member countries may call for total prohibition of export subsidies, the following three issues need to be resolved.

**Table 8**  
**Aggregate Measurement of Support in Selected Economies**

		Aggregate measurement of support	Share of gross agricultural product
		US \$ m	%
<b>Developing Economies</b>			
Argentina	1995-96	122.8	0.6
Botswana	1995-96	0.0	0.0
Brazil	1996-97	371.2	0.7
Colombia	1996	4.0	0.03
Egypt	1997	0.0	0.0
India	1995-96	-23.8	-31.1
Fiji	1997	0.0	0.0
Mexico	1995	0.5	0.002
Namibia	1996-97	0.0	0.0
Pakistan	1996-97	-56.9	-0.03
Paraguay	1996	0.0	0.0
Philippines	1997	27.1	0.2
South Africa	1996	451.1	8.2
Sri Lanka	1996	0.0	0.0
Thailand	1996	513.2	2.5
Tunisia	1997	Na	1.7
Uruguay	1997	9.0	0.4
Venezuela	1996	331.3	12.3
Zambia	1996	0.0	0.0
Zimbabwe	1996	0.0	0.0
<b>Developed Economies</b>			
Australia	1997-98	89.4	0.5
European Union	1995-96	61309.1	22.9
Japan	1996	30547.7	32.5
United States	1997	6238.4	3.1

na Not available

**Source:** Freeman et. al; (2000) "The Impact of Agricultural Trade Liberalization in Developing Countries". ABARE Research Report 2000.

- (a) The maintenance of food aid and the need to clarify entitlements regarding compensation for additional food insecurity arising from the removal of subsidies on food exports;
- (b) Exemptions from any possible restrictions on the use of export taxes;
- (c) The maintenance of existing exemptions under the Special and Differential Treatment (SDT).

The absence of internationally agreed rules governing the use of export credits, export credit guarantees and insurance programmes has enabled some countries to circumvent and reduce the value of export subsidy reduction commitments. Developing countries also point out that the use of a roll-

over facility, permissible in the past, allowed members to carry forward unused subsidy.

To the extent that export subsidies are further reduced and exports credit rationalized, food import dependent countries (FIDCs) require concrete assurances in terms of more substantial guarantees regarding food aid commitments as well as other forms of financial and technical assistance. The rationalization of export marketing in this way may well be in their long term interests in terms of more stable and predictable international markets, but the cooperation in their removal could be made conditional on strengthening the operational implications of the Ministerial Decision on LDCs.

**(x) State Trading**

From the developing country perspective, state trading is not considered a major impediment to more 'open' trading in agricultural markets. However, the issue is likely to be dominated by the interest of a small number of developed countries agricultural exporters. In this context STEs in future should be more open with regard to their pricing policies, and share markets with private traders. Governments in many developing countries have already adopted this course, and there is no reason why social objectives cannot be met, and economies of scale realized, when STEs are working hand in hand with a regulated private sector.

It would be unfortunate if future negotiations led to provisions being incorporated in international trade law that hindered the ability of STEs to operate effectively in developing countries. As a matter of fact, in the absence of state trading, there is not a level playing field; most international agricultural markets are dominated by a small number of very large corporations. Such legislations could mean that developing countries lose the ability to achieve the very credible social objectives for which STEs have been typically designed.

**(xi) Special and Differential Treatment (SDT) Measures**

The existing SDTs are only "best endeavour" clauses and do not amount to anything. Since they are non-enforceable, they cannot be demanded as rights. There are scores of more such ineffective clauses in the WTO, which were put in during the Uruguay Round negotiations, to assure the poor countries that their interests would be treated differentially. Unfortunately, ever since the WTO came into being, there has not been a single instance when any SDT (except for a time frame actually used by a poor country or a concession granted by a rich country). Therefore, as a counter tactic in the hectic pre-Doha negotiations, the poor countries submitted a demand asking for a stand-alone agreement on SDTs, as it is a cross cutting issue.

**(xii) Food Security**

There is a need to take into account the “multi-functionality” of agriculture in future reductions in agricultural support and protection since the positive externalities arising from agricultural activity should be balanced against the envisaged allocative efficiency arising from agricultural trade liberalization. Consideration of concrete measures that could be put in place to deal with the problem of inadequate food production and the negative effects of the reform programme on them is necessary. A special ministerial decision sets out objectives, and certain measures, for the provision of food aid and aid for agricultural development. It also refers to the possibility of assistance from the International Monetary Fund and the World Bank to finance commercial food imports.

**(xiii) Sanitary and Phytosanitary Standards (SPS)**

Debate over sanitary and phytosanitary standards, although not directly part of the negotiations on agriculture, provides part of the subtext for discussion on liberalization in the overall sector. Majority of submissions to the WTO have centered on developing countries and the SPS, although it is clear that there is no unified position of the middle income or least developed countries. A number of proposals under discussion refer to equivalence and harmonization of standards and article 4 of the SPS Agreement. From developing country perspectives, concerns about harmonization center largely on problems in access to information and lack of participation in international standard-setting activities. Standards developed by the International Plant Protection Convention, and International Office of Epizootics (OIE) can facilitate harmonization. However, limited resources in developing countries preclude their access and active engagement in their development.

It is difficult for most developing countries to have their standards accepted as “equivalent” by developed countries. Mutual Recognition Agreements (MRAs) are not feasible given the lack of modern facilities to test and certify in many countries. Even under conditions of technological parity between trading partners, such as the U.S., Europe and Japan, there is little evidence that MRAs will facilitate trade. Failure to recognize equivalence of measures is a major problem confronting developing countries.

The requirements on the application of science and risk assessment in decision-making have also been addressed in proposals by developing countries to the agriculture negotiations. The SPS Agreement includes obligations that SPS measures be based on principles of international science and risk assessments of harm in order to minimize trade distortions. A central problem in the SPS framework concerns the lack of balanced considerations of dynamic benefits to economic development and trade under conditions in which acceptable risk is not

set at zero tolerance levels. When combined with the lack of progress on harmonization of standards and escape clauses for setting regulation to meet national needs, developing country exporters are at a clear disadvantage.

Special and Differential Treatment (SDT) for developing countries is referenced in Article 10 of the SPS Agreement. Some WTO members have suggested that SDT should include mandatory provision of technical assistance or that longer phase in periods be allowed for developing countries to implement obligations under the SPS agreement. It is doubtful, however, that a focus on the expansion of SDT is in the long-term interests of developing countries, especially the least developed in Asia and Africa. Integration into the WTO system requires a focus on the tools to implement commitments and exercise rights, not a process of SDT that provides an easy way to postpone necessary action on technical assistance.

Finally, the debate over genetically modified organisms (GMO) in agriculture is also of particular relevance to developing countries in the current negotiations. The adoption of technology to expand agricultural production should be of central concern to both net food importers, as well as exporters. The benefits of adoption of GMO techniques based on experience and technology in use in the U.S., Canada, Europe, and other developed countries is clear. The problem in today's international trading system includes a lack of consensus on the basic elements of a regulatory approach, and a system suited to GM crops and byproducts, the costs and benefits of labeling programs, and whether WTO disciplines remain uncertain. Proposals in the agriculture negotiations have addressed GMO and related labeling protocols, including submission by Korea, Japan, Europe and other WTO members. Egypt has banned imports of tuna canned in oil based on perceptions of risk related to GM modified soybeans. Thailand has registered complains arguing that the tuna is not prepared with GM soybeans. A certification program may provide a means to settle the dispute. Whether consensus on labeling, harmonized conformity assessment mechanisms or the need for regulation in this area at all can be achieved within the context of WTO negotiations is not certain.

#### **4.2 NEGOTIATING STRATEGY FOR AGRICULTURE**

Since IDB member countries, in general, are agrarian economies, they have keen interest in negotiations on the agriculture sector. There are three main areas of negotiation. Firstly, tariffs, which could affect the price of imported food (with differential effects on consumers and producers) and also government revenues. Second, domestic subsidies, which could alter the feasibility of policies to enhance the labour entitlements (e.g. import credits or market development). Third, export subsidies, which could affect the feasibility of transfer and safety net

policies that use imported food, since cuts will tend to increase 'commercial' import prices may reduce the availability of food. Keeping these three main areas of negotiation in view, the following points would be helpful in promotion of trade in agriculture that benefit IDB member countries:

- IDB member countries may support proposals for a substantial reduction in applied tariffs using a harmonization formula that reduces tariff peaks. The current formula that allows tariff cuts to be concentrated on 'non-sensitive' products should be abandoned with the opportunity for such selective use of tariff cuts reduced. In addition any tariff reduction formula should incorporate a mechanism for reducing tariff escalation by linking tariff levels in primary commodities to those affecting their processed form.
- All LDCs be given the same level of entry into the developed countries markets as currently enjoyed by African, Caribbean and Pacific (ACP) countries, i.e., agricultural exports from LDCs should have tariff-free access to developed country markets.
- The expansion of TRQs and limitations placed on within-quota rates should be linked to the reform of quota administration favouring the auction system, and stricter monitoring of quota.
- The application of Special Safeguards is discriminatory, because they are not generally available to developing country governments. From the perspective of IDB countries they should be either broadened in scope to make them available to all markets, or abolished altogether.
- IDB countries should negotiate the phasing out of Special Safeguard Provisions (SSGs). Appropriate negotiating stances for developing countries in this respect could focus on a choice of two strategies, viz., to support the application of stricter disciplines but only in the case of food commodities; or to support such measures across the board but argue for exemptions under expanded Special and Differential provisions for developing countries.
- Even where the short-term effects of a blue box abolition and a more restrictive green box are negative for the group of countries, the longer term effects could be positive. It is probably in the long term interests of the great majority of IDB member countries for the blue/green provisions to be restricted as much as possible.
- A number of mediating factors which can impact on long run outcomes include transmission elasticities with respect to international and domestic prices, and the ability of domestic producers to respond to changed price signals may be taken.

- Greater discipline regarding domestic subsidies, providing that adequate arrangements are made to compensate for the potential of relatively higher import prices, particularly through related flows of financial and technical assistance.
- IDB member countries that export in competition with developed countries are disadvantaged by the latter's use of domestic subsidies. They are constrained by lack of financial resources. Therefore, there should be greater flexibility extended to developing countries in meeting subsidy reductions.
- There is a conflict of interest for those that are food importers because lower export subsidies lead to higher import prices in many cases. Any short term disadvantage, however, should be outweighed by longer term advantage of a more level playing field in international markets.
- It is necessary for IDB member countries to strengthen their options to use support measures in the future, through the negotiation of greater flexibility for themselves. Level-playing field is necessary not only with respect to reducing the current bias of the trading system, but also one that addresses the structural disadvantages that developing countries face in the international trading environment.
- If the lower reduction commitments provided for in the SDT are of no great value to most developing countries, it is of considerable importance that the concessions which excluded export marketing subsidies from the prohibited list should be maintained and strengthened.
- IDB member countries should give support for the total abolition of export subsidies, and the regulation of export credits to ensure that they do not contain hidden subsidies.
- If the maintenance of an aggregate measure of support is non-negotiable as the focus of support reduction, then the argument for the developing countries to be able to apply an aggregate *de minimis* (as opposed to commodity specific) exemption becomes tenable. This should be negotiated as a concession to developing countries only, and a case made for an expansion of the *de minimis* exemptions to say, 15%.
- Support for further cuts in domestic support levels should be made conditional on the opportunity to re-submit in the case of those developing countries that have submitted a zero AMS where it should be negative. In addition, negative AMS calculations to be interpreted as negatives which can be reduced towards zero without penalty.

- Input and transport subsidies should be included as green box exemptions only for developing countries.
- There should be greater transparency in STE operations. Developing countries should exempt from any restrictions on STE activities that might reduce their bargaining power in international markets.
- Reinforcing existing levels of flexibility for both developing and least developed countries with respect to implementation of any new provisions; this will include maintaining measures which are currently temporary, as well as defining exemptions regarding the extent and timing of any changes to existing policies.
- Improved adherence to the principles contained in the relevant Ministerial Decisions, particularly with respect to technical assistance. Included in the latter will be support in facilitating developing countries submissions in conformity with their best interests.
- Short-term obligations to maintain food aid commitments in the context of rising international prices of food commodities. Given that food aid is traditionally sourced through domestic surpluses in the exporting countries, the availability of supplies will fall as prices increase. There is a need, therefore, to strengthen existing funds to facilitate this provisioning.



## CHAPTER 4

### TRADE IN SERVICES

The efficient provision of services is basic to the efficiency of the commodity producing sectors. This is because they account for 10-20 percent of production costs in addition to all the costs of trading such as communications, transport, trade finance and insurance, and distribution services [Hodge and Nordas, (1999)]. The countries where the quality of services is poor and are priced high may well have negative effective rates of protection for most of the manufacturing sector. This has become all the more important in view of the falling rates of tariffs.

Poor-quality, high-priced services not only affect the current operations of manufacturers but also discourage future investment by locals and foreigners by lowering the profitability of such investment. This may be one major factor constraining the flow of FDIs to developing countries despite access to cheap labour. The liberalization programmes for sectors such as financial services, telecommunications, transport and professional services whether the sector is predominantly owned by the private sector or by the Government, would go a long way towards improvement of the services and the commodity producing sectors.

International trade in services is estimated to be more than US\$1000 billion a year and accounts for over 20% of all the international trade. It is growing at a rapid rate; during the 1990s, the annual growth rate of trade in overall services is 12% and in telecommunications, financial, professional and business services, it has averaged 16%.

The services sector accounts for a large proportion of GDP in the IDB member countries. In most IDB member countries its contribution falls in the range between 45% and 60% which is average for middle income countries and ranges between 33% in the case of Kyrghistan to 71% for Jordan. Nevertheless, the quality of services has to be improved significantly and cost of provision reduced substantially, if the IDB member countries have to carve out a major share in the trade in services.

The GATS consists of a framework which lays down a set of general principles for trade in services. The basic principles which apply to trade in goods also apply to trade in services, but they have been modified to take into account the special characteristics of trade in services. GATS requires countries to apply MFN treatment by not discriminating between service products and service providers of different countries and allows a transitional period of 10 years (upto January 1, 2005) during which the country rules are made consistent with the MFN principles. The Agreement also incorporates the national treatment principle which stipulates

that countries should not treat foreign service products and service providers less favourably than their own service products and service providers. The GATS, however, does not as in the case of trade in goods impose this as an obligation to be applied across-the-board in all service sectors but requires countries to indicate in their schedules of concessions the sectors and the conditions subject to which such treatment would be extended.

The preceding discussion brings quite clearly that the fundamental objective of the GATS is fair trade in services under nondiscriminatory and transparent conditions. It seeks freer, if not completely free, trade in services and seeks to achieve nondiscriminatory trade through progressive liberalization and increased coverage of sectors in the schedules of commitments. GATS preserves the right of governments to regulate their service sectors, but at the same time it gives foreign suppliers certain rights. Where governments have not made a specific commitment, they have to adhere to the non-discrimination principle and ensure transparency and where specific commitments have been made, they are bound to give market access and national treatment to foreign service suppliers under the conditions described in their schedules of commitments. The GATS deals extensively with rights of service suppliers in the markets of other members and as such have significant implications for investment flows and the movement of personnel across borders.

GATS Article XIX.I stipulates negotiations to “achieve a progressively higher level of liberalization on mutually advantageous basis” and aim at “securing an overall balance of rights and obligations” among participating countries. GATS Article XIX.I further provides for successive rounds of negotiations for progressively higher level of liberalization in the trade in services. Pursuant to this particular GATS provision, starting point for the new round of GATS negotiations is the 1997 financial services deal in the WTO; over 100 WTO member countries had made commitments and some 70 countries had improved the commitments they had made at the end of Uruguay Round relating to the financial services and fairly significant results were achieved

The Services negotiations officially started in early 2000 under the Council for Trade in Services. The Council initiated the negotiating guidelines and procedures in March 2001. The Doha Declaration reaffirmed the negotiating guidelines and procedures and established the timetable and the deadline for the conclusion of negotiations as part of the single undertaking that has to be finished by January 1, 2005.

GATS applies to both the private sector enterprises and the companies owned or controlled by Government if they supply services on a commercial basis. The obligations under GATS may broadly be divided into two categories, general

obligations which are applied to all service sectors; and conditional obligations applicable to sectors covered by commitments specified in the national schedules.

The supply of services is envisaged under four different modes:

- Cross border supply – a non-resident service supplier supplying services across borders in a member's territory.
- Consumption abroad – the freedom for a member's residents to purchase services in the territory of another member.
- Commercial presence – the opportunity for foreign service suppliers to establish and expand a commercial presence in a member's territory.
- Presence of natural persons – entry and temporary stay in a member's territory of foreign individuals in order to supply a service.

The choice of mode of supply is determined by technical feasibility on the one hand and barriers to trade that exist across each mode on the other [Hoekman and Mattoo (2000), UNCTAD (1995)]. Services in trade may be liberalised through reduction of regulatory barriers to market access and discriminatory national treatment across all four modes of supply.

IDB member countries have comparative advantage in the services and can export a broad range of services. At present, however, the most significant export is tourism accounting for a large proportion of total export revenues among poorer countries [Karsenty (2000)]. The other areas of potential comparative advantage include exports of energy, labor-intensive sectors such as construction etc. However, trade has been limited by trade barriers, including the reluctance of most countries to extend the visas to the less-skilled occupations for delivery of a service [UNCTAD (2000)]. Information technology-related services such as back-office processing and call centers have opened new vistas where services can be provided without any movement of persons. Obviously, success of IT exports depends on improvements in communications and transport services.

Trade in services can be rather helpful to IDB member countries because of the three main factors. Firstly, there are economies of scale in provision of services and firms are able to reduce unit costs. Besides, trade in services provides differentiated services which add value for consumers [Krugman (1996)]. Second, because of economies of scale in research and development (R&D), an expanding market may increase the incentive for those activities, enhancing long-run growth rates [Grossman and Helpman (1991)]. Third, learning is enhanced through technological spillovers in exporting. Trade also increases the extent of competition in the market, which lowers the market power of existing firms and brings down their price-cost markups. This is particularly important in such

services where, typically, large-scale economies exist, severely limiting competition in small economies.

The sector specific commitments so far made under GATS cover commercial presence and there is very little on measures regulating movement of natural persons as service suppliers. This lack of access creates a major imbalance in the trade in services. Horizontal commitments made by 92 WTO member countries refer to movement of natural persons in only (i) Intra corporate transferees; (ii) Business visitors; and (iii) Independent professionals including those providing services under services contract. These are the developed countries that have largely benefited from GATS commitments. The restrictions on movement of technicians and businesspersons from developing countries including the IDB member countries prevent them from participating in a variety of activities that are essential to the penetration of world markets for services. The other barriers faced by service suppliers from developing countries including the IDB member countries are:

- (i) Prohibition of foreign access to service markets which are reserved for domestic suppliers: nationality, residency or visa requirements can prohibit or limit the movement of natural persons;
- (ii) Price based measures: entry and exit taxes and visa fees for the movement of natural persons;
- (iii) Discriminatory airline landing fee, port taxes, licensing fees;
- (iv) Tariffs on goods in which services are embodied or goods that are necessary input in the production of services (films, television programmes, computer soft-wares on disc, telecommunication equipments, etc);
- (v) Subsidies granted in developed countries including for high technology sectors as well as horizontal subsidies and investment incentives that can have a trade distorting impact on services exports from developing countries;
- (vi) Technological standard and licensing, the licensing of commercial services and standard setting have been used to restrict entry into the industry.
- (vii) Discriminatory access to information channels and distribution networks: for example, suppliers of the telecommunications network may discriminate by excluding certain users, charging higher fees or imposing restrictions on attaching equipment;
- (viii) Lack of transparency in government measures and practices of mega firms and other major barriers to market access for developing countries;

- (ix) The growing importance of financing in winning projects in export market and difficulties developing countries face in trying to tap international financial markets;
- (x) Lack of access to procurement orders of the governments of the developed countries.

## **5.1 OPENING OF VARIOUS SERVICES SECTORS BY IDB MEMBER COUNTRIES**

While results in the insurance sector were rather patchy, banking and securities sectors took much of the limelight in 1997 Financial Services negotiations in the WTO. It is being visualized that the next phase of bargaining in the multilateral trade negotiations on services will focus strongly on insurance services, financial services, professional services, telecommunication services and maritime services.

### **(i) Insurance Services**

The insurance business is undoubtedly a big business. Expenditure on insurance premium is typically between 5 and 12% of GDP in the OECD countries and even in some of the developing countries the ratios are equally high. The OECD estimates that total gross premium in OECD member states amounts to over US\$ 2.2 trillion split equally between life and non-life cover. The US alone accounts for nearly US\$ 1 trillion in gross premium with Japan at about one third of that level.

### **Starting Point for the Current Services Tasks**

The starting point for the ensuing round of GATS negotiations are the results of the 1997 financial services deal in the WTO. Consequently, more than 100 WTO member countries made commitments in the financial services including the insurance sector. Moreover, as many as 70 countries improved the commitments they had made at the end of Uruguay Round.

While fairly significant results were achieved as a result of 1997 services deal, results in the insurance sector were rather patchy. Most of the bargaining had concentrated on four areas:

- In terms of cross-border supply, the emphasis was on re-insurance and provision of maritime, aviation and transport (MAT) insurance which entails international risks and can often only be met in certain international markets.
- Regarding the equity participation, there have been fierce negotiations. While US and European negotiators pushed for 100% equity participation, many developing countries refused to bind any commitments beyond 49%.

- Regarding the right to establish branches of foreign firms, very little progress was seen.
- With respect to the “grandfathering” of existing investments, the outcome was least encouraging.

Notwithstanding the nature of 1997 deal on financial services, it would be wrong to assume that the sole targets in the next GATS Round in the Insurance Sector will be developing countries. In fact, in some developed countries insurance markets are characterized by market access barriers as is evident from the following:

- in some OECD countries, the state itself is a provider of insurance services and is often in monopoly position.
- restrictions in some developed countries on concluding group insurance contracts with non-established insurance.
- specific licensing requirements and documentation for the establishment of branches or agencies for foreign insurers.
- sundry legal provisions which discriminate against foreign insurers.

#### Elements of GATS Negotiations on Insurance

Following elements are most likely to form a core of their demands in the course of negotiations on insurance under the GATS process:

- full commitments to loosen regulatory constraints including the abolition of monopolies and tax discrimination particularly, cross border supply of re-insurance.
- full rights to establish subsidiaries or branches.
- equity participation to be liberalized.
- elimination of monopolies and exclusive service providers
- temporary entry conditions to be permitted for professional level personnel of the foreign firms.
- national treatment condition for insurance business related to state bodies and with respect to capital, solvency, reserve, tax and other financial conditions.
- transparency in the introduction of new regulations, in the requirements for license applications and in the provision of information to consumers.
- establishment of independent regulatory authority.

While some IDB member countries may have a large and well structured insurance sector, smaller developing countries are still struggling to create a well functioning insurance sector. In liberalizing markets, the latter countries face the near certainty of insolvencies among domestic suppliers in the insurance sector.

Experience suggests that in the past small markets have opened up without adequate regulation in place only to find new foreign entrants arriving with inappropriate services and products with them. This kind of experience understandably breeds suspicion of the GATS process among the developing countries.

In fact, imprudent and hasty opening of insurance sector to foreign competition may lead to an uneven playing field for the domestic suppliers in the IDB member countries. This would, perhaps, suggest that the developing countries (including the IDB members) whose insurance sector is still at an "infant" stage and where there is no credible regulatory apparatus in place, may wish to follow a gradual market opening approach as ordained in Article XIX of GATS. This, however, may not be construed as an argument against the long-term benefits of the opening of insurance services to foreign competition. The point being made is that a developing country ought to be first ready in terms of restructuring of its indigenous insurance sector before embracing the full-scale liberalization.

#### **(ii) Financial Services**

Financial services play a rather crucial role in the growth process. The liberalization process in services has so far mainly focused on this sector. With a view to further liberalizing the financial services, key objective of the negotiations currently underway is to obtain sufficient number of market access commitments. Many WTO member countries have a wide array of restrictions on both the cross border transactions and the participation of foreign financial institutions in local financial markets. The most common types of market access barriers on financial services are the type of legal entities allowed; participation of foreign capital; the number of suppliers in the market; and the value of transactions or assets. Accordingly, current negotiations on financial services would focus on:

- improved international cooperation on agreed standards including methods of supervision.
- elimination of nationality-based restrictions on market access.
- full national treatment for foreign-based financial service providers.

With a view to achieving the ultimate objective of open international trade and competition in financial services, both the developing as well as developed countries will have to reform their domestic regulations. Moreover, the financial authorities will need to expand international cooperation on issues related to the prudential supervision of financial institutions under their jurisdiction. In general, the challenge of regulatory reform is to shift the nature of regulations from a system under which the financial authorities exercise supervision by authorizing specific types of transactions by financial institutions to a system under which they

exercise supervision by monitoring the overall financial condition of financial institutions.

Progress on the liberalization of trade in financial services would depend on a deeper understanding of the domestic advantages of liberalization by both the developed and developing countries. Some of the important advantages include:

- improved access by national firms to international capital markets, thus reducing their cost of capital and expanding their potential pool of capital;
- improved rates of return on funds invested by pension funds, thus reducing future claims on government funding;
- diversification of risk insured by domestic insurance carriers;
- promoting inward investment; and
- promoting overall economic efficiency.

The IDB member countries will have to take into account the imperatives of their domestic financial sector before agreeing to any further market access commitments. In this context, it may be noted that notion of progressive liberalization is one of the basic tenets of the GATS Article XIX which provides that liberalization takes place with due respect for national policy objectives and Member's development levels both overall and in individual sectors. The IDB member countries have, thus, the flexibility for opening fewer sectors, liberalizing fewer types of transactions and progressively provide market access in line with their development situation.

### **(iii) Professional Services**

The professional services comprise of accountants, architects, engineers and lawyers. These services are generally regulated by the State, though in some jurisdictions by the professional association with or without a specific Government mandate. The main thrust of the regulation is to provide protection to consumer and to counter where possible the asymmetry of information between professions and the general public. Typical barriers affecting the professional services are:

- Entry in the profession;
- The segmentation of activities;
- Professional monopolies;
- Advertising;
- Solicitation of new clients and prohibitions on foreign firms forming companies;



- Use of international or foreign names;
- Partnerships;
- Hiring of local staff;
- Equity or management control participation; and
- Cross border supply.

The most significant issue in respect of professional services is the widespread nature of local qualifications and licensing requirements both for individual practitioners as well as conditions for ownership and management of firms. Similarly, the lack of mutual recognition of qualifications is the most common barriers for the movement of natural persons to supply professional services.

#### (iv) Telecom Services

Telecommunications are the most vital infrastructure in promoting growth and development. With the advent of electronic commerce and the digital economy it has assumed even greater significance. There is a high degree of synergy in this sector between national and multilateral initiatives and that may generate a positive atmosphere for the GATS negotiations; additional market-opening commitments would go a long way in the growth process. That there is very little likelihood of tussle between North and South in this area and that in a large number of IDB member countries telecommunications has already been opened, is quite encouraging.

The GATS sets out rules that govern measures affecting the telecommunication services. The "Reference Paper" of April 1996 sets out the regulatory framework, the purpose of which is to ensure that there is fair and technology neutral competition after liberalization of telecom services. It consists of set of principles, covering such matters as the competition, safeguards, interconnection guarantees, transparent licensing procedures and the independence of regulators. It also includes pricing mechanisms such as 'cost-oriented rates' and connection 'charges that reflect cost' and it bans 'anti-competitive cross subsidization'. Majority of signatories to the WTO's Telecom Agreement have inserted additional commitments and the remainder are expected to do so in the current round of services negotiations.

Two main objectives of telecommunications negotiations are: (a) securing new telecommunications commitments from the governments that currently have none; and (b) obtaining improvements from those with commitments already in their schedules. As regards new commitments, government will be able to commit

on blueprints for future reforms by specifying phase-in dates for various reforms in the GATS schedules. The main challenge would be that commitments are in line with national decisions on the breadth and sequencing of reforms.

Main issues in areas of telecommunications relate to the measures restricting foreign equating participation and the number of providers permitted to supply a particular type of service; gaps in commitments created by sequencing on national telecommunications liberalization; phase-in dates inscribed by governments in schedules regarding the staged implementation of reforms; and modes of supply.

The GATS telecom commitments most commonly list limitations on the number of suppliers, restrictions on type of legal entity and participation of foreign capital. Most frequently the limits are associated with commercial presence for basic telecom services. Whereas it is difficult to quantify the extent of barriers by the developed and developing countries, there are significant differences between levels of commitments of developed and developing countries, with the latter having imposed more limitations on telecom service suppliers.

#### **(v) Maritime Transport Services**

Even though liberalisation in maritime transport services has been a special concern in Uruguay Round, very few countries have shown willingness to make commitments and those too with strong limitations. Negotiations in this sector relate to the three "pillars", viz., international shipping, auxiliary maritime services; and access to and use of port facilities. It needs to be underscored that this sector, though an integral part of GATS, is not subject to MFN rule. The existing market access and national treatment commitments are essentially the unilateral commitments.

International shipping is relatively more open sector. However, there are three main areas where foreign firms face some restrictions. Firstly, the Cabotage which is most protected but has been excluded from the scope of WTO negotiations. Second, there are also restrictions on auxiliary services and port services which are public monopolies and are only gradually being privatized. Third, in the multi-modal transport, the foreign firms frequently encounter difficulties in establishing their transport operations.

Whereas developed countries have not yet a negotiating strategy for maritime services, it seems likely that they will seek significant liberalization commitments for auxiliary services. There may be a debate as to whether the 'three-pillar' approach of transport, auxiliary and port facilities, should have a fourth pillar added for multi-modal operations involving an over-lap with land transport features and requiring additional commitments on horizontal aspects such

as investments. The operators of integrated multi-modal services need access to the ports, their transport connections, to customer's agents or customer premises and to be able to do marketing and advertising for new customers.

The IDB member countries will have a positive interest in the provision and efficiency of port services for the sake of their own merchandise trade as well as earning revenues from servicing fleets of trading partners. They will have to prepare a position on the multi-modal dimension in the context of ongoing negotiations on services.

#### **4.2 SUPPLY CONSTRAINTS TO PROVISION OF SERVICES**

While most developing countries including the IDB member countries face market access barriers to the developed countries markets, these countries face major supply constraints and do not satisfy the pre-conditions for building a competitive services sector. These pre-conditions include:

- (a) Human resource development and technological capacity-building to ensure that professional and quality standards are met;
- (b) Upgrading of all the telecommunications infrastructure;
- (c) A Coherent pro-competitive regulatory framework for goods and services;
- (d) Government support to help service firms particularly SMEs to improve the quality of the service they provide;
- (e) An increase in the financial capacity of service firms;
- (f) Promotion of their exports;
- (g) Use of new business technologies such as creation of alliances and networking; and
- (h) A presence in major markets and the capacity to exploit the opportunities offered by regional markets.

#### **4.3 CHALLENGES FOR IDB COUNTRIES**

IDB member countries are finding themselves engaged in increasingly complex negotiations on services, which are going beyond sector-specific liberalization of market access and national treatment. The majority of developing and least developed countries have already liberalized their services sectors. However, to ensure that trade is taking place in a fair and competitive environment, other multilateral measures may be necessary for disciplining anti-competitive practices in tourist-originating countries. These countries can expect to find themselves under pressure to liberalize in many sub-sectors of energy services, and it may be necessary to gain a better understanding of the implications and opportunities of the liberalization of energy markets for energy-producing countries.

A further concern for many countries is the potential social loss from reform.

- Low-income households lose access to necessary services once cross-subsidization is removed and commercial concerns focus on profitable segments of the market. Subsidization of such groups can still occur under a reformed regulatory regime but through different mechanisms, such as a nondiscriminatory levy on all providers in the industry, proceeds from which are distributed directly to the households requiring assistance (Bergman and others 1998).
- Regulatory reform provides the additional benefit of facilitating price reductions that allow larger numbers of low income households to demand such services and that raise the real income of those households that are already making use of the services (Hodge 2000).
- The most distinguishing characteristic of services transactions is that their production and consumption occur simultaneously, often requiring direct contact between producers and consumers.

There is considerable discrimination against foreign suppliers in national procurement markets as the margin of preferences ranges from 13 to 50 percent for leading OECD nations across a wide range of government purchases [Francois, Nelson, and Palmetier (1997)]. It suggests that there is considerable scope for expanding competition in national procurement markets. In general, there are five forms of discrimination against foreign suppliers:

- Policies that directly or indirectly reduce the number of bidders (referred to here as entry discrimination);
- Establishing a “price preference” for domestic bidders by adding a specified percentage to foreign firms’ actual bids before they are compared with domestic firms’ actual bids is an example of price discrimination;
- Policies to reduce price competition for domestic bidders (price discrimination);
- A limited tender that deliberately involves few, or no, foreign firms is an example of entry discrimination; and
- Discrimination that increases the costs of foreign bidders (cost discrimination).

#### **4.4 NEGOTIATING STRATEGY FOR TRADE IN SERVICES**

Since there is a large scope in the long run to export services and at the same time to protect their infant service activities, the IDB member countries have to negotiate hard in the GATS negotiations. Following need to be considered:

- Maintaining the present architecture of GATS intact;
- Clarifying the existing commitments through establishing the mechanism to undertake a comprehensive country-by-country review/ assessment of the schedule of commitments to identify pattern of bound commitments, the most important barriers/limitations/ restrictions to clarify the extent of market access and national treatment and to see whether commitments meet the obligations contained in GATS Article IV and Mode 4;
- Ensuring full transparency in respect to measures affecting supply of services including immigration legislation and labour market regime;
- Operationalizing GATS Article IV and XIX through commercially meaningful commitments on movement of natural persons and capacity building measures, focusing on sectors of actual potential interest to IDB member countries such as construction, engineering, medical and tourism services;
- Achieving symmetry between capital and labour to ensure efficiency and economic welfare benefits through revision of the Annex on Movement of Natural Persons;
- Strengthening provisions on business practices/anti-competitive behaviour;
- Providing initiative on GATS Article VI which would give primacy to particular policy objectives, equity, distributional issues;
- Achieving liberalization in sectors where such liberalization can contribute to sustainable development;
- Recognition of autonomous liberalization in terms of receiving the credit for it;
- To ensure that the results of the current services negotiations in all services related areas are completed in the same timeframe to ensure balanced results; and
- Negotiations would focus on selected sectors or all sectors in principle. While the Doha Ministerial Declaration clearly states that no service sector would be excluded from the services negotiations, some proposals advanced by the developed WTO member countries refer to "sectoral" negotiating modalities particularly for services which have intermediate function, which would imply priority attention being given to financial and telecommunications services.
- Removal of immigration-related regulations governing entry and stay of services providers; regulations concerning recognition of qualifications, work experience, and training; differential treatment of domestic and foreign services personnel; and regulations on other modes of supply, particularly on commercial presence.

- Inadequacy of regulatory mechanisms for dealing with asymmetric information is a problem which has received relatively less attention. For instance, in professional services, low standards and disparities in domestic training and examinations can become a major impediment to obtaining foreign recognition.

Besides the above negotiating priorities, the IDB member countries ought to ensure that the results of the current services negotiations in all services related areas are completed in the same timeframe to ensure balanced results. Another equally significant issue for the IDB member countries is whether negotiations would focus on selected sectors or all sectors in principle. While the Doha Ministerial Declaration clearly states that no service sector would be excluded from the services negotiations, some proposals advanced by the developed WTO member countries refer to "sectoral" negotiating modalities particularly for services which have intermediate function, which would imply priority attention being given to financial and telecommunications services. Moreover, it should be noted that the pre-requisite to obtaining results in the current Round would be identification of national interests by the IDB member countries. Therefore, mechanisms to ensure cooperation between government, private sector and academia in these countries would be crucial in this respect.

In order to ensure balanced results of the services negotiations, the IDB member countries would need to give serious consideration as to what kind of mechanisms or combination of mechanisms should be used for achieving the aim of progressive liberalization e.g. request/offer, qualitative and quantitative formula approach resulting in minimum access commitments, model schedules (as in maritime, transport and telecommunication), pre-commitment to future liberalization, zero-for-zero initiative etc. In principle, the request/offer approach would result in a more gradual liberalization. The question is whether adopting formula approach (as was previously done in the case of negotiations on financial and telecommunication services) could be in the best interest of IDB member countries and how to undertake an evaluation of the impact of formula approach. Formula approach, in effect, could mean a negative list approach implicitly. IDB member countries would need to consider seriously the impact of formula approach as in the case of negotiations on financial services many developing countries decided not to apply the formula approach. On the other hand, the formula approach could have a liberalizing impact on Mode 4 in a selective number of categories of natural persons.

## CHAPTER 5

### CONCLUSIONS AND POLICY IMPLICATIONS

Main conclusions of the study are summarized below:

1. IDB member countries should determine the extent to which they are willing to liberalise their own economies to win tariff reductions and removal of other barriers with a view to have access to the markets of their trading partners.
2. IDB member countries ought to seek due allowance for the autonomous liberalization these countries may have undertaken. One way of ensuring credit for the autonomous liberalization is to have greater flexibility in the choice of "base tariffs" to be used as a basis for tariff cuts as a result of the industrial tariff negotiations.
3. IDB member countries must seek flexibility in "staging" of tariff reductions. The ground rules for the negotiations should provide the developing countries, including the IDB member countries, longer period than that provided to developed countries for staging of tariff reductions.
4. The IDB member countries have to adopt an approach that results in securing maximum reductions on products which they export. Preceding the industrial tariff negotiations it would be necessary for the IDB member countries to agree on the ground rules that would be followed in the conduct of tariff negotiations. IDB member countries may agree to reduce the bound rates and where they do not have comparative advantage to steep fall in tariff cuts both in bound and applied rates.
5. IDB member countries should ask for conversion of all specific tariffs into ad-valorem tariffs.
6. AEDCs have a strong interest in further liberalisation and tariff harmonization approach because their principal concern is market access. Similarly, the tariff peaks, another major issue for developing country exporters, and a formula of tariff cuts that facilitate a degree of tariff harmonization is necessary.
7. Reform of the regime governing tariff rate quotas is extremely important in gaining market access. Modifications to the tariff rate quota system ranging from substantial increases in the quantities subject to lower rates to elimination of tariff rate quotas as well as possible disciplines on tariff quota administration are required. Substantial tariff cuts and the removal of tariff peaks and wedges need to be negotiated for an effective access to developed country markets. Abolition of TRQs is a potential mechanism for bypassing developed country protectionism.

8. To gain better market access, IDB member countries should seek substantial reductions in peak MFN tariffs, which apply to products of exports interest to them, for instance, textiles, leather products, footwear, etc. IDB member countries must seek flexibility in staging of tariff reductions. The ground rules for the negotiations should provide that the member countries would be allowed longer period than that provided to the developed countries for staging of tariff reductions. IDB member countries should also ensure that tariff reductions are both in 'Bound Rates' and 'Applied Rates'.
9. It is necessary for IDB member countries to strengthen their options to use support measures in the future, through the negotiation of greater flexibility for themselves. Level-playing field is necessary not only with respect to reducing the current bias of the trading system, but also one that addresses the structural disadvantages that developing countries face in the international trading environment.
10. IDB member countries may support proposals for a substantial reduction in applied tariffs using a harmonization formula that would reduce tariff peaks. In addition any tariff reduction formula should incorporate a mechanism for reducing tariff escalation by linking tariff levels in primary commodities to those affecting their processed form.
11. IDB member countries that export in competition with developed countries are disadvantaged by the latter's use of domestic subsidies. Input and transport subsidies should be included as green box exemptions only for developing countries. Moreover, developing countries are constrained by lack of financial resources and, therefore, there should be greater flexibility extended to developing countries in meeting subsidy reductions.
12. There is a conflict of interest for those that are food importers because lower export subsidies lead to higher import prices in many cases. Any short term disadvantage, however, should be outweighed by longer term advantage of a more level playing field in international markets.
13. A number of IDB member countries are net agricultural exporters. Trade liberalization is expected to benefit these net exporter countries, particularly those that are highly open to trade. Many IDB member countries agricultural exports have penetrated the regional market, and hence domestic policies in its regional partners will be an issue of priority. The IDB member countries that are net agricultural importing countries should be more cautious about trade reforms whose benefits and costs are mixed.
14. Most of the IDB member countries in general did not participate fully in the negotiations. Though special and differential treatment has enabled them to



avoid major changes so far, it would not be advisable to rely more on these in the further negotiations. It would be safer for development interests to be fully integrated into the broader discussions of subsidies and tariff reduction.

15. IDB member countries have comparative advantage in the services and can export a broad range of services. Trade in services can be rather helpful to IDB member countries because of the expansion in market, better returns to R&D and technological spill-overs. Besides, trade in services provides differentiated services which add value for consumers.
16. Developed countries are expected to seek significant liberalization commitments for auxiliary services in the maritime services. The IDB member countries will have a positive interest in the provision and efficiency of port services for the sake of their own merchandise trade as well as earning revenues from servicing fleets of trading partners.
17. Since there is a large scope in the long run to export services and at the same time to protect their infant services activities, the IDB member countries have to negotiate hard in the GATS negotiations.
18. In order to ensure balanced results of the services negotiations, the IDB member countries would need to give serious consideration as to what kind of mechanisms or combination of mechanisms should be used for achieving the aim of progressive liberalization.
19. Because of the concern that their infant domestic service industries might be stifled by an influx of established firms, IDB member countries are likely to remain cautious participants in multilateral negotiations on services. The main benefits from a multinational agreement, however, would come from fostering the liberalisation of domestic markets. Simply permitting foreign firms into an uncompetitive market produces relatively limited benefits. This is because the main benefits of liberalisation come from increased domestic efficiency and the consequent income flows, and not from greater access to other countries' markets. To the extent that the GATS does not advance domestic liberalisation its impact will be muted.
20. Developed country commitments on the cross-border supply of labour intensive services may increase developing country export opportunities. Business services, which are intensive in skill and labour rather than capital, are activities in which developing countries have actual or potential comparative advantage.

21. In addition to unilateral liberalisation, the developing countries service industries could involve capital and technical support for modernising business structures and gathering information on export markets. Foreign investment can also contribute to development by enhancing local skills, injecting capital, technology and management techniques, and improving efficiency.
22. Technical assistance for programmes in trade in services is available from the WTO, as part of the GATS, and a number of UN organisations. Bilateral and plurilateral aid programmes also support the enhancement of developing countries' trade in services (e.g. the Lome Convention). Properly structured regional trade agreements which liberalise trade in services can also help to foster local suppliers.

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## Glossary of Trade-Related Terms

**ACP:** African, Caribbean, and Pacific countries, a group of mostly former European colonies.

**Aggregate measure of support** Measure of the total support given to an activity as a result of policies such as production subsidies and market price support policies. Used in the WTO Agreement on Agriculture.

**Applied Rate** is the rate which is actually applicable.

**Bound Rate:** Implies the rate which has been entered into the WTO member countries schedules of commitments.

**Ceiling Binding:** Often used to describe a situation where there is a large difference between the tariff that is actually applied and the level at which the tariff is bound in GATT (the "ceiling").

**Competition policy:** Legislation and regulations designed to protect and stimulate competition in markets by outlawing anticompetitive business practices such as cartels, market sharing, or price fixing.

**Countervailing duty:** Duty levied on imports of goods that have benefited from production or export subsidies. The duty is intended to offset the effect of the subsidy.

**Dispute Settlement Body:** WTO body that is responsible for dealing with disputes between WTO members. Consists of all WTO members meeting together to consider the reports of dispute settlement panels and the Appellate Body.

**Dumping:** A form of price discrimination by which the export price of the product exported from one country to another is less than the comparable price in the ordinary course of trade, that is, including transport and related costs-for the like product when destined for consumption in the exporting country (GATT Art. VI). Also defined as sales below the estimated cost of production. The margin of dumping is the difference between the two prices.

**Economic needs test:** Measure requiring a demonstration that an import (of goods but more usually natural service providers) cannot be satisfied by local producers or service providers.

**Effective rate of protection:** A measure of the protection afforded by an import restriction calculated as a percentage of the value added in the product concerned. Takes into account the protection on output and the cost-raising effects of protection on inputs.

**Formula approach:** Method of negotiating down tariffs or other barriers to trade by applying a general rule (formula). For example, a rule specifying that all tariffs are to be cut to a certain fraction of their initial level, or that an agreement should cover a certain proportion of economic activity (sectors).

**Free on Board (f.o.b.):** The price of a traded good including its value and the costs associated with loading it on a ship or an aircraft, but excluding international transportation (freight) costs, insurance, and payments for other services involved in moving the good to the point of final consumption.

**Free-trade area:** A group of countries in which the tariffs and other barriers are eliminated on substantially all trade between them. Each member maintains its own external trade policy against non-members. Also called free trade agreement or free trade arrangement. Contrasts with custom union.

**GATT:** General Agreement on Tariffs and Trade. Major Articles:

1. General MFN requirement.
2. Tariff schedules (bindings).
3. National treatment.
4. Freedom of transit of goods.
5. Allows antidumping and countervailing duties. Superseded by the GATT 1994 Agreement on Antidumping, and the Agreement on Subsidies and Countervailing Measures.
6. Requires that valuation of goods for customs purposes be based on actual value. Superseded by the GATT 1994 Agreement on the Implementation of Article VII.
7. Requires that fees connected with import and export formalities be cost-based.
8. Reaffirms MFN for labeling requirements and calls for cooperation to prevent abuse of trade names.
9. Obligation to publish trade laws and regulations: complemented by the WTO's Trade Policy Review Mechanism and numerous notification requirements in specific WTO agreements.
10. Requires the general elimination of quantitative restrictions.
11. Permits trade restrictions if necessary to safeguard the balance of payments.
12. Requires that quotas be administered in a non-discriminatory manner.
13. Established GATT 1947 rules on subsidies. Complemented by the WTO Agreement on Subsidies and Countervailing Measures.

14. Requires that state trading enterprises follow MFN.
15. Allows developing countries to restrict trade to promote infant industries and to protect the balance-of-payments (imposing weaker conditionality than Article XII).
16. Allows for emergency action to restrict imports of particular products if these cause serious injury to the domestic industry. Complemented by the WTO Agreement on Safeguards.
17. General exceptions provision - allows trade restrictions if necessary to attain non-economic objectives (health, safety).
18. Allows trade to be restricted if necessary for national security reasons.
19. Requires consultations between parties involved in trade disputes.
20. GATT's main dispute settlement provision, providing for violation and non-violation complaints. Complemented by the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes.
21. Sets out the conditions under which the formation of free trade areas or customs unions is permitted.
22. Allows for renegotiation of tariff concessions.
23. Calls for periodic rounds of negotiations to reduce tariffs.
24. Allows for accession

**Part IV:** Calls for more favourable and differential treatment of developing countries. Entered into force in June 1966.

**GATS:** General Agreement on Trade in Services Major Articles:

1. Definition. Trade in services covers all four modes of supply.
2. MFN obligation. Option to invoke exemptions on a one-time basis.
3. Notification and publication. Obligation to create an enquiry point.
4. Increasing participation of developing countries. High income countries to take measures to facilitate trade of developing nations.
5. Economic integration. Allows for free trade and similar agreements.
6. Allows for domestic regulation. Requirements concerning the design and implementation of service sector regulation, including in particular qualification requirements.
7. Recognition of qualification, standards and certification of suppliers.
8. Monopolies and exclusive suppliers. Requires that such entities abide by MFN and specific commitments (Articles XVI and XVII) and do not abuse their dominant position.

9. **Business practices.** Recognition that business practices may restrict trade. Call for consultations between members on request.
10. **General exceptions.** Allows measures to achieve non-economic objectives.
11. **Market access.** Defines a set of policies that may only be used to restrict market access for a scheduled sector if they are listed in a member's specific commitments.
12. **National treatment.** Applies in a sector if a commitment to that effect is made and no limitations or exceptions are listed in a member's schedule.
13. **Calls for successive negotiations to expand coverage of specific commitments (Articles XVI and XVII).**

**Generalized System of Preferences (GSP):** The GSP is a system through which industrialized high-income countries grant preferential access to their markets to developing countries. Also called Generalized System of Trade Preferences.

**Gray-area measure:** Measure whose conformity with contractual obligations is unclear: for example, voluntary export restraints under pre-WTO rules of the GATT.

**Intra-industry trade:** Trade in which a country both exports and imports goods that are classified to be in the same industry.

**Least developed country (LDC):** A country that satisfies a number of criteria established by the United Nations that together imply a very low level of economic development. As of 2002, the UN had classified 49 countries in the LDC group. Used in the WTO Subsidies Agreement, where LDCs are granted differential treatment.

**Market access:** Refers to the conditions under which imports compete with domestically produced substitutes. These are determined by the extent to which foreign goods are confronted with tariffs, discriminatory taxes, and other regulations.

**Mode of supply** Term used in the GATS context to identify how a service is provided by a supplier to a buyer.

**Most favored nation (MFN) principle:** MFN is the "normal", non-discriminatory tariff charged on imports of a good. In commercial diplomacy, exporters seek MFN treatment, that is, the promise that they will be treated as well as the most favored exporter. Called normal trade relations in the United States.

**Multifiber Arrangement (MFA):** "Arrangement Regarding International Trade in Textiles." Negotiated as a temporary exception to the GATT in 1973. Regulates trade in certain textile products between signatories by means of negotiated



bilateral quotas. Superseded by the WTO Agreement on Textiles and Clothing in 1995, which specifies that all quotas are to be abolished by 2005.

**Mutual recognition:** The acceptance by one country of another country's certification that a product has satisfied a product standard. Often based on formal agreements between countries if the standards are mandatory.

**Nominal rate of protection:** The proportion by which the (tariff-inclusive) internal price of an import exceeds the border or world price.

**Non-tariff barrier (NTB):** A catch all phrase describing barriers to international trade other than the tariffs - for example, quotas, licensing, or voluntary export restraints.

**Producer subsidy equivalent:** A measure of the aggregate value of the gross transfers from consumers and taxpayers to farmers due to policy measures. Also called producer support estimate.

**Quad:** Refers to the participants in the Quadilateral meetings - that is, Canada, the European Union, Japan, and the United States.

**Quantitative restriction or quota:** Measure restricting the quantity of a good imported (or exported). Quantitative restrictions include quotas, nonautomatic licensing, mixing regulations, voluntary export restraints, and prohibitions or embargoes.

**Quota rent:** The economic rent received by the holder of a right to import under a quota. Equals the domestic price of the imported goods, net of any tariff, minus the world price, times the quantity of imports.

**Sanitary and Phytosanitary (SPS):** measure A technical requirement specifying criteria to ensure food safety and animal and plant health. Many international SPS standards are set by the FAO/WHO. See also Codex Alimentarius Commission.

**Special and differential treatment:** The principle in WTO that developing countries be accorded special privileges, either exempting them from some WTO rules or granting them preferential treatment in the application of WTO rules.

**Special safeguard:** In the WTO agreement on Agriculture, a protectionist measure that can be triggered automatically by a decline in prices or an increase in imports.

**State Trading:** Trade by a government agency or enterprise or by an enterprise to which the government has granted exclusive or special privileges in respect of international trade. State trading does not necessarily involve a monopoly or quantitative restriction of trade and does not require state ownership (GATT Art. XVII).

**Subsidy:** Assistance granted by government to the production, manufacture, or export of specific goods, and taking the form either of direct payments, such as grants or loans, or of measures having equivalent effect, such as guarantees, operational or support services or facilities, and fiscal incentives.

**Tariff binding:** In GATT context, commitment by countries not to raise particular tariff items above a specific or bound level. Also referred to as ceiling bindings. The so-called schedule of tariff concessions of each WTO member is annexed to its protocol of accession.

**Tariff equivalent:** Measure of the protective effect of an NTB – the tariff that would have the exact same effect on imports as the NTB.

**Tariff escalation:** occurs if the tariff increases as a good becomes more processed. Escalation discourages imports of more processed varieties of the good (discouraging foreign processing activity) and offers domestic processors positive levels of effective protection. For example, low duties on tomatoes, higher duties on tomato paste, and yet higher duties on tomato ketchup.

**Tariff peaks:** Tariffs that are particularly high, often defined as rates that exceed 15 percent or the average nominal tariff by a factor of more than three.

**Tariff rate quota (TRQ):** Measure under which a good is subject to a MFN tariff, but a certain quantity (the “quota”) is admitted at a lower, sometimes zero, tariff. TRQs are mainly applied to agricultural trade and can be seasonal.

**Tariffication:** Procedure of converting NTBs into their tariff equivalents. In the Uruguay Round, all industrial countries’ agricultural NTBs were tariffed and bound.

**Terms of trade:** The price of a country’s exports relative to the price of its imports.

**Trade-related Investment Measure:** Policy used by governments to influence the operations of foreign investors by establishing specific performance standard relating to trade. Examples are export performance requirements and local content rules (mandating that investors use a certain proportion of domestic inputs in their production).

**TRIPs:** Trade-related intellectual property rights. In WTO, used as an acronym for the Agreement on Trade-Related Aspects of Intellectual Property Rights.

IDB MEMBER COUNTRIES OF THE WTO (1 JANUARY, 2002)

1.	<b>BAHRAIN, KINGDOM OF</b>	1 JANUARY 1995
2.	<b>BANGLADESH</b>	1 JANUARY 1995
3.	<b>BENIN</b>	22 FEBRUARY 1996
4.	<b>BRUNEI</b>	1 JANUARY 1995
5.	<b>BURKINA FASO BURUNDI</b>	23 JULY 1995
6.	<b>CAMEROON</b>	13 DECEMBER 1995
7.	<b>CHAD</b>	19 OCTOBER 1996
8.	<b>CÔTE D'IVOIRE</b>	1 JANUARY 1995
9.	<b>DJIBOUTI</b>	31 MAY 1995
10.	<b>EGYPT</b>	30 JUNE 1995
11.	<b>GABON</b>	1 JANUARY 1995
12.	<b>THE GAMBIA</b>	23 OCTOBER 1996
13.	<b>GUINEA-BISSAU</b>	31 MAY 1995
14.	<b>GUINEA</b>	25 OCTOBER 1995
15.	<b>INDONESIA</b>	1 JANUARY 1995
16.	<b>JORDAN</b>	11 APRIL 2000
17.	<b>KUWAIT</b>	1 JANUARY 1995
18.	<b>KYRGYZ REPUBLIC</b>	20 DECEMBER 1998
19.	<b>MALAYSIA</b>	1 JANUARY 1995
20.	<b>MALDIVES</b>	31 MAY 1995
21.	<b>MALI</b>	31 MAY 1995
22.	<b>MAURITANIA</b>	31 MAY 1995
23.	<b>MOROCCO</b>	1 JANUARY 1995
24.	<b>MOZAMBIQUE</b>	26 AUGUST 1995
25.	<b>NIGER</b>	13 DECEMBER 1996
26.	<b>OMAN</b>	9 NOVEMBER 2000
27.	<b>PAKISTAN</b>	1 JANUARY 1995
28.	<b>QATAR</b>	13 JANUARY 1996
39.	<b>SENEGAL</b>	1 JANUARY 1995
30.	<b>SIERRA LEONE</b>	23 JULY 1995
31.	<b>SURINAME</b>	1 JANUARY 1995
32.	<b>TOGO</b>	31 MAY 1995
33.	<b>TUNISIA</b>	29 MARCH 1995
34.	<b>TURKEY</b>	26 MARCH 1995
35.	<b>UGANDA</b>	1 JANUARY 1995
36.	<b>UNITED ARAB EMIRATES</b>	10 APRIL 1996

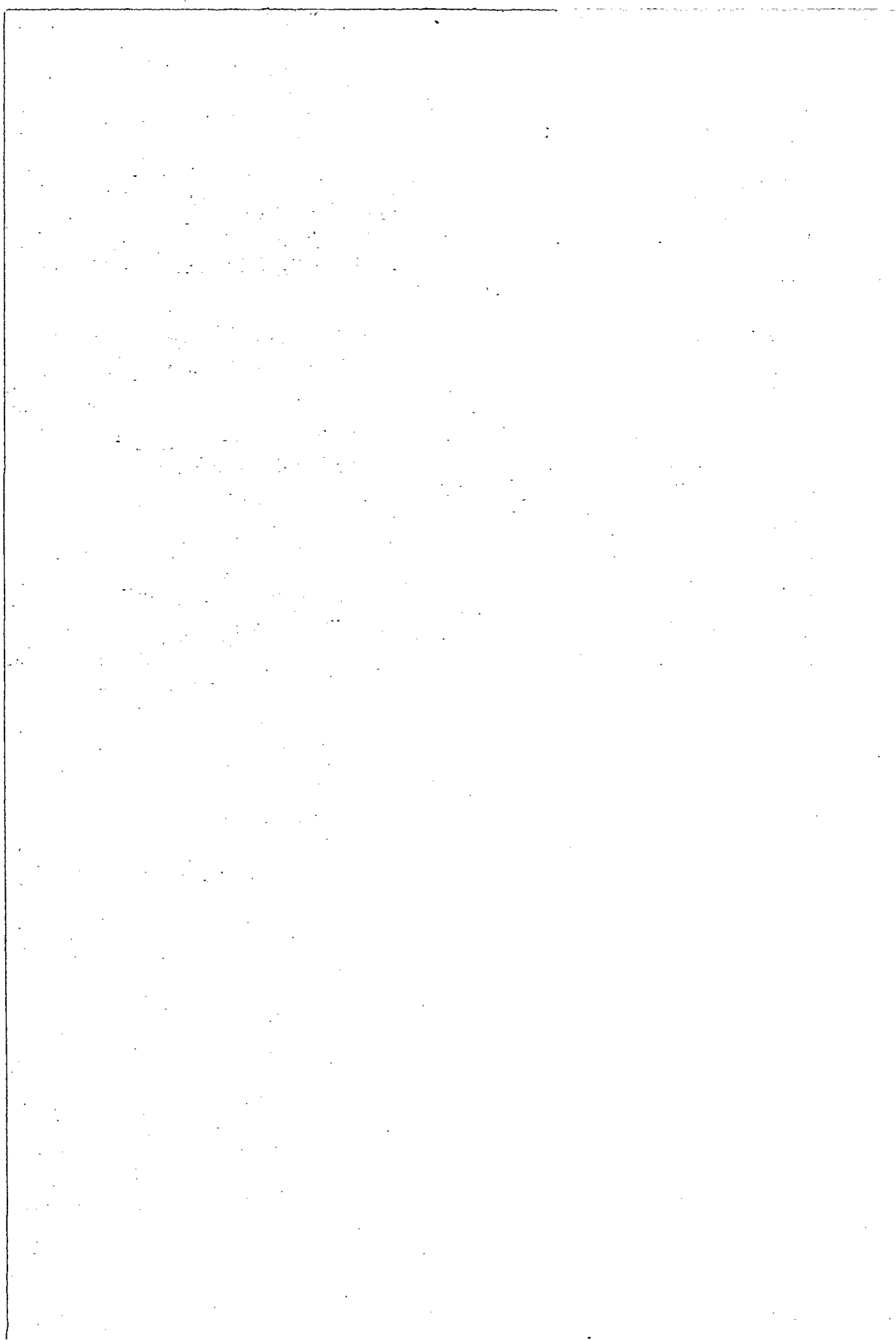
## **About the Authors**

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Prior to his appointment as Director, PIDE, Dr. Kemal served the Government of Pakistan as Chief Economist, Member of the Planning Commission and Joint Economic Advisor, Ministry of Finance.

Dr. Kemal is co-author/co-editor of seven books. He has about 148 research articles on a range of issues, such as international trade, macroeconomic policies, agriculture taxation, environment, poverty, etc., published in various national and international journals and books.

**Mr. Mumtaz Malik** is currently a Joint Secretary, Ministry of Finance, Government of Pakistan. He worked as WTO expert with the Islamic Development Bank from February 99 to November, 2001. He also worked as Economic Counselor (WTO) at the Permanent Mission of Pakistan, Geneva from August 1995 to December, 1998.



# ISLAMIC DEVELOPMENT BANK

## Establishment of the Bank

The Islamic Development Bank is an international financial institution established in pursuance of the Declaration of Intent issued by a Conference of Finance Ministers of Muslim Countries held in Jeddah in Dhul Qadah 1393H, corresponding to December 1973. The Inaugural Meeting of the Board of Governors took place in Rajab 1395H, corresponding to July 1975, and the Bank formally opened on the 15<sup>th</sup> Shawal 1395H, corresponding to 20<sup>th</sup> October 1975.

## Purpose

The purpose of the Bank is to foster the economic development and social progress of member countries and Muslim communities individually as well as jointly in accordance with the principles of *Shari'ah*.

## Functions

The functions of the Bank are to participate in equity capital and grant loans for productive projects and enterprises besides providing financial assistance to member countries in other forms for economic and social development. The Bank is also required to establish and operate special funds for specific purposes including a fund for assistance to Muslim communities in non-member countries, in addition to setting up trust funds.

The Bank is authorized to accept deposits and to raise funds in any other manner. It is also charged with the responsibility of assisting in the promotion of foreign trade, especially in capital goods, among member countries, providing technical assistance to member countries, extending training facilities for personnel engaged in development activities and undertaking research for enabling the economic, financial and banking activities in Muslim countries to conform to the *Shari'ah*.

## Membership

The present membership of the Bank consists of 54 countries. The basic condition for membership is that the prospective member country should be a member of the Organization of the Islamic Conference and be willing to accept such terms and conditions as may be decided upon by the Board of Governors.

## Head Office

The Bank's principle office is in Jeddah in the Kingdom of Saudi Arabia and the Bank is authorized to establish agencies or branch offices elsewhere.

## Financial Year

The Bank's financial year is the lunar Hijra Year

## Language

The official language of the Bank is Arabic, but English and French are additionally used as working languages.

**ISLAMIC DEVELOPMENT BANK**

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