

Aid for Trade: Cool Aid or Kool-Aid?¹

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Revised 28 September 2007

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1. Introduction

“Aid for Trade,” the catch-all term describing North-South financial support to (1) realize gains from trade reform and (2) alleviate its adverse effects, has entered center stage in the behind-the-scenes negotiations to finalize Doha. Delays, scaling back of expectations, lack of substance on special and differential treatment, disappointment on implementation of the Uruguay Round agreement, unfulfilled promises on cotton and duty-free, quota-free treatment for LDCs, and particularly the mounting empirical evidence on welfare losses in many LDCs from likely Doha packages point towards the potentially critical role an Aid for Trade deal might play in efforts to revitalize the Doha process.

¹ Kool-Aid is a flavoured drink associated with the mass suicide of cult followers of Jim Jones of the People’s Temple in Guyana in 1978 by imbibing a similar drink laced with cyanide. The expression has come to mean “Whatever they tell you, don’t believe too strongly.”

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This paper critically examines the issues at hand. First, what is the promise of Aid for Trade? Generally, the benefits of an Aid for Trade program can be categorized under (1) and (2) above. Under (1), funds would be employed to help developing countries generate supply-side responses, as, for example, tariff removal on agricultural products in the developed world might not trigger a strong export response given large shares of small-scale farming and a general lack of infrastructure. Furthermore, developed countries increasingly tighten borders through the application of (sanitary and phytosanitary) standards, which poor countries are often unable to comply with, even if only for the thin web of legal and technical know-how. Under (2), funds would be allocated to *micro* trade adjustment assistance, designed to help developing countries cope with undesirable outcomes in particular industries due to the reallocation effects of trade liberalization. *Macro* adjustment assistance could include compensation for preference erosion and lost tariff-revenue, where the latter can play a substantial role in small developing countries budgetary plans. To some extent, therefore, the debate presents a reversal of the adage “trade, not aid”, recognising that there is a need for assistance to enable developing countries to expand and diversify their trade in a manner that deepens the development impact. Put another way: in this view, aid can help develop trade, so that eventually trade can replace aid.

However, despite a general agreement that these are important issues for all developing countries, there is no agreement on the relative importance of (1), essentially infrastructure development aid, versus (2), representing a focus on management of adverse shocks. Equally important, no agreements exist on organization, collection and disbursement of funds. Who would be eligible, what activities would be covered, and how donor activities would be coordinated are only some of the many unanswered questions. Moreover, World Bank and IMF have indicated that they are willing to help, suggesting that borrowing, with its attendant specialised advice, may also be seen as a form of aid for trade, if not “aid” in the narrower sense of official development assistance (ODA). Critics have pointed out that increases in developing countries’ liabilities to gain access to funds originally designed to aid trade reform adjustment would be tantamount to pulling the rug out from underneath. Furthermore, some see a risk that such borrowing could further limit development policy space through loan conditionalities. In addition, if funds are approved on a case-by-case basis, negotiations over trade reform “gains” would essentially stretch into the indefinite future. Inevitably, the question also arises as to what extent aid for trade would be in addition to existing aid commitments or merely a re-direction of existing funding towards trade and related activities, which may be a lower development priority in some countries. Given this long list of unanswered questions, and some bad experiences of recent trade reforms, developing countries have looked with some suspicion at the proposals, regarding aid for trade more as Kool-Aid, rather than cool aid!

The paper is structured as follows. Section 2 delves deeper into definitions of Aid for Trade and discusses its role and place within multilateral institutions during recent years. Section 3 examines the need for aid for trade. Section 4 reviews recent development in WTO negotiations, followed in section 5 by a discussion of private sector issues. The paper closes with conclusions.

2. What is “Aid for Trade”?

a. Definition

Much has been written about aid for trade in recent years by the international organizations, but there is still some confusion about what is covered and it may be useful in the first instance to clarify the kinds of needs that are being discussed without entering into the more controversial issues about whether these needs should be met by external assistance, and, if so, by whom and how. In a recent paper for the IMF Executive Board, a World Bank-IMF staff paper (World Bank and IMF, 2007) comments that donors each use their own definitions, and that infrastructure may be used for trade and for other purposes.

In a 2006 paper to the Development Committee, the World Bank (2006a) suggested that an “all encompassing definition (in terms of objectives), for example, would cover:

- trade and regulations;
- trade development activities;
- support to address supply-side constraints (infrastructure);
- support for micro-economic adjustment (worker training, social safety nets, targeted subsidies);
- support for a macroeconomic adjustment (preference erosion, fiscal revenue losses, impact of changes in the prices);
- commodity price stabilisation.”

The OECD, which has historically been the most important coordinator of official development assistance through its Development Assistance Committee (DAC) and has been working with the WTO since early 2006 on a database on trade-related aid activities, takes the view that trade-related technical assistance and capacity building, together with trade-related infrastructure are clearly covered by the definition of aid for trade (OECD, 2006). Within the category of trade-related infrastructure, OECD includes transport and storage, communications, and energy, even though some infrastructure projects are not used exclusively for trade. In the monitoring system, building productive capacities is also included as a separate item, covering sectoral support for: banking and financial services; business and other services; agriculture, forestry and fishing; industry and mining; and tourism. However, OECD notes that there is some disagreement on the extent to which aid for trade should cover building productive capacity. It is even more categorical that aid for trade should not cover adjustment related expenditure such as social safety nets, balance of payments support, or compensation for the potential costs of multilateral liberalization, such as preference erosion or reduction in government revenue – categories which it labels as macro-economic and micro-economic adjustments. It simply notes that the international financial institutions, such as the World Bank and the IMF have been supporting developing countries' adjustment efforts arising from a host of factors, including trade reforms, and will continue to do so. It should also be noted that OECD includes only *concessional* lending, thus excluding much trade-related lending by the international financial institutions (IFIs) and regional development banks, thus

understating the trade-related lending of these institutions (World Bank and IMF, *op. cit.*). On the other hand, the World Bank also uses a narrower definition of concessional lending, excluding all investments that improve the productivity of tradable sectors, counting only that portion of a project that focuses on trade (*idem*).

A breakdown of concessional aid, as defined by OECD, showing that it totals around 40 per cent of all ODA is shown in Table 1.

Table 1. Breakdown of Concessional Aid for Trade (US\$bn. at 2004 constant prices and exchange rates)

Trade related commitments for:	2001	2002	2003	2004	2005
Trade policy and regulations	0.9	0.8	1.0	0.8	0.9
Infrastructure	9.8	9.4	9.7	13.7	12.1
Productive capacity building	9.3	7.4	9.2	9.6	9.5
Structural adjustment	4.8	5.9	6.4	5.2	3.5
Total aid for trade	24.9	23.5	26.3	29.3	26.0
Memo item:					
Aid for trade/sector allocable ODA%	46.0%	42.1 %	40.9%	40.8%	36.5%

Note: Sector allocable ODA includes general budget support and excludes food aid and other commodity assistance, debt relief, humanitarian aid, administrative costs, support to NGOs, refugees in donor countries, and imputed student costs.

Source: OECD (2007).

In terms of instruments, the World Bank (2006a) notes that aid from trade can be delivered through the: technical assistance and capacity building (including support from trade diagnostics); project financing; and policy lending (including support for adjustment, loss of tariff revenue, reduced exports resulting from preference erosion, or institutional reform). Thus, the Bank clearly considers that aid for trade might be delivered through both grants as well as concessional and non-concessional loans.

Finally, Nielson (2005), a World Bank staff member, notes that countries suffering adjustment shocks from trade liberalization, including the Doha round, need to be assured of transition support from the international community. She says that first step is identifying the countries affected, and goes on to point out the Bank and the IMF plan to assess the nature and magnitude of adjustment needs of countries that present a *prima facie* case that they face significant adjustment shocks. She says that the group is likely to include, for example, countries negatively affected by the end of the textile quotas and by preference erosion, net food importing countries, and countries undertaking major programmes of trade reform. Among the factors that would need to be taken into account are: the possibility of offsetting lost tariff revenue through customs reform and more efficient collection of tariffs; the extent to which existing preferences were used; the extent of liberalization undertaken by trading partners on products subject to preferences; and the characteristics of affected industries and groups. While this list is useful, it is not necessarily comprehensive, and might usefully have included the need for balance of payments support, as it is common in a trade reform for imports to increase quickly while

it takes time to develop an export response. Indeed, this has been the main rationale for structural adjustment lending in the past.

b. Perspective on Aid for Trade

The issue of aid for trade has come to the surface as a major issue in the current WTO negotiations for a number of reasons. First, a number of studies have indicated that the proposals that currently on the table in the WTO negotiations may have a negative impact on a number of developing countries. Taken together with new information about the costs of implementing the Uruguay Round Agreement, as well as a series of studies highlighting the negative effect of some trade reforms of the last 10 to 15 years in a number of developing countries, especially in Africa, these new estimates of the impact of further trade reforms under the WTO have caused some trepidation amongst developing countries (see later). Second, developing countries have also expressed concern about the implementation of the Uruguay Round Agreement, claiming that promises of gains to developing countries have not been fulfilled. Third, while in the past developing countries were able to benefit from special and differential treatment that allowed them considerable flexibility in applying WTO rules, this flexibility seems to be being reduced, and developed countries now seem to regard special and differential treatment merely as a transitional device to allow developing countries time to apply the same rules as developed WTO members.

In this context then, many WTO Members feel that providing some form of support to the developing countries could help overcome their fears about the possible negative impact of the current negotiations. This was one of the preoccupations in February 2005 G-8 Finance Ministers called on the World Bank and the IMF to develop proposals for additional assistance to countries to ease adjustment to trade liberalization and to increase the capacity to take advantage of more open markets. Within the WTO, the issue came to a head at the Ministerial Meeting in Hong Kong in 2005, when it was decided to establish a task force to look at the issue of aid for trade, as discussed later.

c. Linkage to the MDGs and Financing for Development

The United Nations Millennium Declaration of 2000 highlighted the importance of the “open, equitable, rule-based, predictable and non-discriminatory multilateral trading and financial system” for meeting the objectives on development and poverty eradication, and expressed concern “about the obstacles developing countries face in mobilizing the resources needed to finance their sustained development.” Among other points, the declaration also undertook to address the special needs of the LDCs, including through duty- and quota-free access for essentially all their exports, and also to deal comprehensively and effectively with the debt problems of the low- and middle-income countries. These concerns and other development concerns were encapsulated in the Millennium Development Goal 8, namely to “Develop a Global Partnership for Development”.

Subsequently, the Monterrey Consensus adopted at the International Conference on Financing for Development in March 2002 built on the Millennium Declaration and explicitly laid out a new framework of mutual obligations and mutual accountability between developed and developing countries. While all parties agreed on the importance of the “ownership” of developing countries of their national development strategies, and urged the governments of developing countries to redouble their efforts to increase the resources spent on development and ensure that they are used effectively, the High-Level Panel on Financing for Development, convened by the UN Secretary-General under the chairmanship of the former President of Mexico, Ernesto Zedillo, concluded in its report that even assuming developing countries adopted sound policies and maximized the use of domestic resources, an additional \$50 billion a year in aid would likely be needed, as a minimum, in order to meet the Millennium Development Goals. (UN GA document A/55/1000). The Monterrey Consensus covered the main areas of Financing for Development, namely:

- Mobilizing domestic financial resources for development.
- Mobilizing international resources for development: foreign direct investment and other private flows.
- International Trade as an engine for development.
- Increasing international financial and technical cooperation for development.
- External Debt.
- Addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development.

Thus, the issues of trade, aid, financing for development and debt relief were all seen by the United Nations as inter-linked elements of the same programme to tackle the issues of development and poverty reduction, and the Doha Ministerial Declaration of November 2001 was welcomed by the Secretary-General of the United Nations as contributing to Goal 8 of the MDGs.³

Later, the UN Millennium Project Task Force on Trade (2005) made a case for a multilateral trading system that was more supportive of economic growth and poverty alleviation in developing countries, and, to this end, put forward a set of goals to be accomplished by the ongoing Doha Round as well as longer term objectives for the trading system. The report went on to note that the multilateral system was unbalanced against the interests of developing countries, and suggested greater opening of markets by developed countries as one step to address this imbalance. The Task Force recommended the use of official development assistance to support poor countries “in generating the sources of revenue needed to compensate for losses incurred as a result of lowering import duties, in building the human and physical infrastructure they need to benefit from increased market opportunities, and in adjusting to erosions of existing trade preferences stemming from multilateral negotiations.”

³ “Implementation of the United Nations Millennium Declaration”, Report of the Secretary-General (UN GA document A/58/323 of 2 September 2003).

Moreover, the report said that if trade were to contribute to economic growth, expanded trade, and poverty reduction, it must be coordinated with other policies at both the national and international levels. “At the national level, policy coherence means the adoption of sound complementary policies by national governments to manage liberalization, as well as ensuring that trade policymaking is appropriately informed by expertise across a range of policy areas. At the international level, coherence calls for a significant ramping up of ‘aid for trade’ by the development community (to negotiate, assess, and implement WTO agreements and to design and implement adjustment policies) and for a clear and realistic view of the WTO’s role in technical assistance. This assistance for increasingly deeper capacity building must be additional to, and not at the expense of, development aid. Trade liberalization requires international negotiations and international assistance, but its benefits and challenges remain”

Formally, the Task Force recommended that a temporary aid for trade fund “commensurate with the size of the task, or significantly ramped-up contributions through such existing channels such as the Integrated Framework” be set up to support countries in addressing adjustment costs associated with the implementation of a “Doha reform agenda.” The Task Force report specifically recommended that such funding should be additional to current aid flows, and “could be financed out of the tariff revenue that is presently collected by OECD and higher income developing countries on imports that will be subject to Doha reduction commitments”. A priority task for the development and trade communities would be the identification of new and existing channels through which this additional funding could most efficiently be made available for relevant, targeted projects in developing countries.

In summary, the UN Millennium Project Task Force on Trade highlighted the need for additional aid for trade capacity building, to build human and physical infrastructure, to address adjustment costs, to offset tariff revenue losses, and to offset the erosion of preferences, and it suggested that new channels would be needed for this purpose.

d. Linkage to the Integrated Framework (IF)

The Integrated Framework for Trade-related Technical Assistance (IF) may also be seen in the context of aid for trade. The IF brings together the IMF, the ITC, UNCTAD, UNDP, the World Bank and the WTO as well as bilateral donors to assist the least-developed countries (LDCs). It has two objectives: integrating trade into national development plans as poverty reduction strategies; and to assist in the co-ordinated delivery of trade-related technical assistance responses to needs identified by the LDCs. In the first stage, a diagnostic trade integration study specifies the main elements of the policy framework for national trade integration, and an action matrix maps out the delivery of trade-related assistance, while identifying trade-related investment needs.

Experience with the IF has highlighted a number of problems: weak in-country capacity, lack of systematic follow-up at the country level, insufficient and uncertain financing, and variable donor responses to priorities identified in the diagnostic trade

integration study. Recent enhancements, adopted by the Steering Committee on the recommendation of a Task Force on 1 May 2007, are intended to address some of these problems. These include: increased resources, strengthened in-country structures, strengthened governance, improved links to donor process, multi-year programmes of technical assistance and capacity building. These improvements suggest that the enhanced IF should be able to address most aid for trade needs of the beneficiary countries, but much depends on a willingness on donors to make funds available.

Despite the problems, the IF has produced some positive results for beneficiary countries, and is now being seen as a potential model for the delivery of aid for trade. Some of the key elements of the IF are also regarded as important to include in any new initiative on aid for trade: in-country ownership, donor coordination, and mainstreaming trade into national development strategies. The World Bank and the IMF had recommended an extension of the programme to other low-income countries, but this was strongly opposed by the LDCs, which fear a dilution of resources available to them, and, in the end, this proposal was not recommended. However, it was felt that a similar mechanism could be of value in addressing their needs.

e. Linkage to special and differential treatment and the current WTO negotiations

To some extent, the issue of aid for trade has arisen because developing countries have lost the flexibilities available as special and differential (S&D) treatment under the GATT system and that have diminished under the WTO. Moreover, analyses of the current WTO negotiations suggest that, despite extensive discussions on S&D treatment, new concrete actions seem unlikely to emerge, new commitments are likely to be required of developing countries, and estimates suggest that developing countries will have to face a number of adjustments in their economies as a result of terms of trade, preference and revenue losses.

This situation is symptomatic of an ongoing internal conflict in dealing with developing countries within the multilateral trading system, with non-discrimination as a core principle. This is manifest in the fact that the rules have had to be modified several times over the years to handle development issues. The original GATT was not conceived as a development institution, but as part of the International Trade Organisation (ITO) to be established under the Havana Charter of 1947. After the failure to have the ITO ratified, it became necessary to introduce special provisions to deal with development issues by amending the GATT, such as Article XVIII on Balance of Payments, Article XXVIII *bis* that provided flexibility in tariff negotiations for developing countries to assist their economic development. Part IV of the GATT (1964) recognised the special needs of developing countries in the trading system, but much of the language was in “best endeavours” terms. The Enabling Clause (1979) provided legal cover for the Generalised System of Preferences (GSP), for regional arrangements among developing countries, and for special treatment in favour of the least-developed countries.

As a result of these modifications to the GATT rules, there was little pressure on the developing countries prior to the Uruguay Round to make burdensome commitments, but this changed in the Uruguay Round. Partly under pressure from the developed countries, partly because of their own reforms, and partly as a result of some disillusionment about the value of S&D, developing countries participated actively in the Uruguay Round, making some important concessions on market opening and accepting a wide range of obligations. While they did not have to cut tariffs to the same extent as developed countries and were given longer to implement their commitments, the value of the preferences they received was reduced and they had to accept all WTO Agreements under what was known as a “Single Undertaking.” In recognition of special difficulties in implementation of some of the agreements and associated adjustment costs, some new S&D provisions were introduced, targeted at the least-developed countries (LDCs), the net food importing developing countries (NFIDCs), and Annex VII Countries (defined as those with a per capita income less than \$1,000). In various agreements, provisions were added that developing countries had to take special account of the needs of developing countries in the application of the particular agreement – although, as noted, many such provisions took the form of “best endeavours”, rather than firm legal commitments.

Nevertheless, the Uruguay Round represented a step towards a single-tier system of rights and obligations. S&D treatment started to be seen more as a transitional set of measures to allow developing countries to take on the same level of obligations as the developed countries. And, as is discussed below, the cost and administrative difficulties in implementing these commitments were greater than anticipated, while many of the promised gains did not materialize (Laird, Safadi and Turinni, 2005). Finally, estimates in a number of studies at UNCTAD and the World Bank showed a remaining bias in protection against developing country exports, with higher tariffs and more non-tariff barriers (NTBs) facing their key products. (The same point was made by the UN Millennium Project Task Force on Trade, *op. cit.*).

The package of decisions at the WTO Ministerial Conference in Doha at the end of 2005 appeared to address these issues, in particular the main Ministerial Declaration that seeks “to place the needs and interests [of the developing countries] at the heart of the [WTO] Work Programme...” Positive efforts were to be made “to ensure that developing countries, and especially the least-developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development”. Indeed, the declaration contains many references to taking account of the needs and interest of the developing countries, and their need for technical assistance to allow for their full participation in the work programme. There was also to be an examination of the provisions relating to special and differential (S&D) treatment for developing countries “with a view to strengthening them and making them more precise, effective and operational.”

While it is difficult at this stage to discuss the outcome of the current negotiations, the general shape of the deal is now clear. Various studies estimate that the global welfare gains amounts to less than 0.5 per cent of GDP (Viborny, 2007; Laird and Fernández de Córdoba, 2006). The analysis behind these various estimates suggests that the use of

approaches being used in agriculture may well exclude deep cuts in intervention in areas of interest to developing countries, while in non-agricultural products developing countries will be required to make the greater reductions in tariffs. The analyses tend to be pessimistic about the likelihood of any significant liberalization in the area of services, where previous estimates project global gains in excess of \$300 billion, much accruing to the developing countries, mainly associated with liberalization under Mode 4 Winters, *et al.*, 2003). Despite the modest overall gains, which would be shared by the developing countries as a group, it is expected that in the short term there would be wide variations in the estimated impact of the proposals across countries and across sectors. For example, Fernández de Córdoba and Vanzetti (2006) show potential employment losses of more than 30 per cent in some developing country sectors, while Viborny (*op. cit.*) suggests welfare losses for Sub-Saharan Africa (other than South Africa) unless 100 per cent duty-free, quota-free access for LDCs is allowed.

Various quantitative studies show several potential losses to sub-sets of developing countries, notably LDCs, Sub-Saharan Africa (excluding South Africa) and ACP countries (which are, to some degree, overlapping sets). These results from: terms of trade losses, as food prices are expected to rise (studies cited in Viborny, 2007; Fernández de Córdoba, 2006), losses of preferences (Alexandraki and Lankes, 2004; Lippoldt and Kowalski, 2005; Low et al. 2005 and 2006), and loss of tariff revenues (Fernández de Córdoba, 2006; Elborgh-Woytek *et al.*, 2006; Kowalski, 2005). While none of these studies show up large losses overall, they note that there is considerable variation that could cause problems in some instances. In his study for OECD, Kowalski (*op. cit.*) argues that the “mixed evidence calls for an assessment in advance of which countries may be particularly vulnerable to tariff cuts agreed in the DDA negotiations. Also, revenue concerns should be included in any special and differential treatment provisions to help disadvantaged developing countries adjust to the changes, whether in the form of extended implementation periods or coordinated financial assistance to help them overcome financial, technical or capacity constraints.”

Most of these analyses have been well publicised for some time, and the concerns being raised by development economists in various international institutions may have been a factor when, at the Hong Kong Ministerial Declaration of 18 December 2005, Ministers reaffirmed that provisions for special and differential (S&D) treatment were an integral part of the WTO Agreements and renewed their determination to fulfil the mandate contained in the Doha Ministerial Declaration as well as the later Decision of the WTO’s General Council on 1 August 2004 (the so-called “July package”) that all S&D treatment provisions be reviewed with a view to strengthening them and making them more precise, effective and operational. The Ministers also adopted a limited package for LDCs (Annex F of the Hong Kong Declaration), including the adoption of five specific proposals for LDCs, as well as proposals on TRIPS and public health, the extension of the TRIPS transition period for LDCs, and an enhanced integrated framework (IF). Developed countries (and those developing countries that considered themselves able) accepted a commitment to grant duty-free, quota-free (DFQF) treatment of imports from all LDCs that extends DFQF treatment to all LDCs for at least 97 per cent of products by 2008 - or “no later than the start of the implementation period” – which in fact puts off

the implementation until the conclusion of the negotiations. On services, it was decided that the LDCs would not be expected to undertake new commitments, paralleling the draft text on non-agricultural market access (NAMA), while there was a “best endeavours” agreement to give priority to the sectors and modes of supply of export interest to LDCs, particularly in Mode 4 (temporary movement of labour).

Nevertheless, the fulfilment of the development promise of the Doha negotiations seems to be rather modest, with some mixed improvements in market access, while S&D treatment does not seem as if it will stave off some potentially acute adjustments in some sectors in some developing countries. Much of the discussion of S&D has resulted in compartmentalizing the issue and shunting discussion off to specialised committees where little has been achieved. Nor has there been much progress in attempting to operationalize the provisions by turning them into binding legal language. In the end, a number of developing countries will face some difficult adjustment as a result of the current WTO negotiations, despite the modest overall result and the accumulation of words on S&D treatment.

In concluding the discussion of S&D treatment, it should be noted that the idea of helping developing countries cope with these kinds of economic adjustments has not typically been part of the thinking within the GATT or the WTO. In an analysis of the various provisions on S&D treatment in 2001, the WTO Secretariat identified some 145 provisions spread across the different Multilateral Agreements on Trade in Goods; the General Agreement on Trade in Services; The Agreement on Trade-Related Aspects of Intellectual Property; the Understanding on Rules and Procedures Governing the Settlement of Disputes; and various Ministerial Decisions.⁴ The Secretariat laid out the following six-fold typology for S&D treatment: (i) provisions aimed at increasing trade opportunities; (ii) provisions under which WTO Members should safeguard the interests of developing country Members; (iii) flexibility of commitments, of action, and use of policy instruments; (iv) transitional time periods; (v) technical assistance; and (vi) provisions relating to least-developed country Members. Of these, the only provision that specifically involves funding is that on technical assistance, but in the WTO this has been confined to assisting developing countries to meet their legal obligations, for example, by advising them on how to draft the legal instruments to put their commitments into force in their countries.

The UN Millennium Project Task Force on Trade made a direct link between these adjustment issues, S&D treatment and mandatory commitments on technical and financial assistance. It said “while it is clear that developing countries benefit from freer trade, it is equally clear that their capacity to do so is different from that of developed countries. Developing countries generally have a more limited ability to take advantage of new opportunities and to bear adjustment costs. Special and differential treatment makes sense and should be made more effective and operational.” The Task Force did not argue for permanent deviations from rules on traditional trade policies, suggesting that the factors which guided S&D treatment should include: “the extent to which the rules are related to trade (market access), the extent to which they are in line with broader

⁴ WTO document WT/COMTD/W/77/Rev. 1 of 21 September 2001.

development priorities, the costs of implementation, and the relative costs to others of non-implementation.” The Task Force then went on to argue that assessments of costs and benefits would vary by issue and the level of development of the country concerned, concluding; “Where the costs are high and the trade and development benefits minimal, the issue should not be included in the WTO. Where the costs are high and development benefits only a longer term priority, there is a strong case for extensive—but not eternal—flexibility. Where development benefits are greater or more immediate, a model that calibrates commitments with assistance and gives greater flexibility to countries to determine appropriate implementation periods is appropriate. Where WTO rules promise real and short-term trade and development benefits, concrete technical and financial assistance should be assured—say, through mandatory commitments subject to review and linked to implementation requirements of developing countries.”

3. The need for Aid for Trade

a. Developing countries experiences with trade reforms

The developing countries have been expressing their concerns about trade policy changes following adverse experiences in unilateral reforms, mostly under Bank/Fund programmes, as well as the high costs of implementation of the WTO Agreement. While there have been useful gains in a number of countries, there have also been some serious negative effects, especially in Africa. And, while lessons have been learned, there is still much that can go wrong.

Typically, reform programmes supported by the World Bank and the IMF have followed a standard pattern of eliminating non-tariff barriers, followed by rationalisation and progressive reduction of tariffs to moderate or low levels. But, case studies show that “despite years of experience with reform programmes, there is no recipe for monotonically increasing levels of welfare; reforms are tools/instruments, and serious mistakes are still being made with regard to timing, sequencing, implementation and inclusion of all relevant essential elements” (Laird and Fernández de Córdoba, 2006). These case studies - which show reduced rates of growth and important negative effects on unemployment after reforms, often continuing for a number of years - suggest that little account seems to have been taken of adjustment costs in the design of liberalization programmes, other than to provide balance-of-payments support as countries undertake reforms, while waiting for a supply response that did not always develop, and there was little use of proactive support policies to overcome market failures or kick-start a supply response, for example, using industrial policies such as the promotion of cluster groups, etc, that were a key part of policies in successful economies like Ireland, the Republic of Korea and Singapore. These findings suggest a need for caution in asking countries to embark on ambitious reform programmes, since reform-minded governments could risk being replaced by others that take a more protectionist stance, which would result in reforms being stalled, if not reversed.

Obtaining an improved export and growth performance as a result of trade reforms has proved elusive. For example, as the World Bank (2006b) recently noted, while tariff and non-tariff barriers have been reduced, “... export performance...has been

highly varied. While most regions diversified their exports, Africa largely failed to do so, and competitiveness eroded for many African countries, which contributed to their increased marginalization in global trade. Thus, despite the efficiency gains from trade, Bank support has not been sufficient to help place many of its poorest clients on a path toward sustained growth.” In its own evaluation of some 15 years of trade-related lending, the Independent Evaluation Group (IEG) of the World Bank (*op. cit.*) found that the Bank had underestimated the complexity of complementary reforms in the investment climate, paid inadequate attention to external factors, and gave insufficient attention to analyzing the poverty-distributional outcomes. “While economic growth often improved after liberalization, it could not always be attributed to an improved export supply response, but rather to more general efficiency gains brought about by removing trade-related distortions.” Among the key findings, the IEG recommended that the Bank be more systematic about assessing (*ex ante*) possible trade-related poverty-distributional outcomes in both economic and sector work and in lending operations.

This recent research on trade reforms has some important implications for the kinds of support that might be offered under the aid for trade initiative, in particular, raising concerns about the kind of conditions that might be attached to such support. It highlights that there is no easy one-size-fits-all approach, and the need to take account of initial conditions in individual countries. As noted, the World Bank has emphasized the need for *ex ante* evaluations of the poverty impact of lending programmes. It has also suggested the need for a more systematic program of research on micro-level adjustment to trade policies, looking at firms, households, and individuals. It has suggested the need for greater sharing of country experiences, as well as the need to revisit the balance between the global and country agendas and to strengthen operational links on trade issues.

After nearly a decade of running down its trade-related activities, since 2001 the Bank has reappraised its trade activities and intensified their focus on the global trading system and on the use of trade-related research, advocacy, capacity building, and mainstreaming of trade in Bank operations. On the lending side, attention has shifted to trade facilitation (both physical infrastructure and institutions). This shift in Bank trade-related activities demonstrates an important shift away from the narrower vision that had been characterised as the “Washington consensus.” Again, this is a pointer to take into account in the design of aid for trade support programmes.

b. Costs of adjustment

A number of studies of adjustment costs were recently reviewed by Fernández de Córdoba *et al.* (2006). While the various studies take different views of the nature of adjustment costs, and use different methodologies, many have concluded that the gains from trade liberalization are often less than the adjustment costs, particularly in the presence of rigid labour markets. The difference in treatment of social and private adjustment costs helps to explain some of the variations in the findings of some empirical studies.

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

c. Costs of implementation of commitments

There has been no attempt at this time to try to estimate what it might cost to implement the kind of programme now taking shape in the course of the WTO negotiations, even on the most limited basis of legal and procedural changes that might derive from fulfilling new legal commitments. However, a limited study was carried out by Finger and Schuler (1999) of the costs of meeting the Uruguay Round obligations in the areas of import licensing procedures, customs valuation, technical, sanitary and phytosanitary standards (SPS), and intellectual property law. As Finger and Schuler point out, implementing such reforms are investment decisions in that implementation required the purchase of equipment, training people, establishing systems of checks and balances, etc.

As an illustration of the amount of money involved, Finger and Schuler showed that, to gain acceptance for its meat, vegetables and fruits in industrial country markets, Argentina spent over \$80 million to achieve higher levels of plant and animal sanitation. Hungary spent over \$40 million to upgrade the level of sanitation of its slaughterhouses alone. Mexico spent over \$30 million to upgrade intellectual property laws and enforcement. As Finger and Schuler argue, "those figures, for just three of the six Uruguay Round Agreements that involve restructuring of domestic regulations, come to \$130 million" which they state is more than the annual development budget for seven of the twelve least developed countries for which they were able to identify that part of the budget.

While it is indisputable that many LDC institutions are weak, and would benefit from strengthening and reform, the question arises whether spending scarce resources on these items is the highest development priority, especially in countries with a high incidence of disease and many other basic needs. But, unlike previous rounds of trade negotiations which allowed participants to opt out of certain agreements, the Uruguay Round eliminated this option with its "Single Undertaking" committing all members to all part of the agreement. As Finger and Schuler point out, World Trade Organization (WTO) obligations reflect little awareness of development problems and little

appreciation of the capacities of the LDCs to carry out the functions that SPS, customs valuation, intellectual property, etc. regulations address. Moreover, because of their limited capacity to participate in the Uruguay Round negotiations, the WTO process has generated no sense of "ownership" among the developing countries of the reforms to which they became committed.

d. Addressing supply-side and institutional constraints

For LDCs and many other developing countries that are beneficiaries of special preferences such as those available under the Cotonou Agreement, the Caribbean Basin Initiative, AGOA, and so on, the trade issue is not market access, but that of building supply capacities and being able to compete on world markets. There is considerable evidence from UNCTAD's various Least Developed Countries Reports about weaknesses in production capacities, which are also applicable in many other developing countries – see, for example, the UNCTAD LDC reports for 2004 and 2006.

Of the various factors that make up the weaknesses on the supply-side, a number of studies highlight transport infrastructures as particularly important role at the early stage of the export sector development (Fugazza, 2004; Limão and Venables, 2001). Fugazza comments that "African countries could do much to lift their supply capacity by investing in transport infrastructure" and notes that "the fact that this sort of investment has not occurred in a significant manner in the last two decades could explain the very low upward mobility of African countries in export performance".

Among other constraints commented on by Fugazza (2004) is the high cost of capital. Typically, in many developing countries, interest rates are in the order of 20-30 per cent, a major burden for small and medium-size enterprises that do not have access to international financial markets. To overcome this obstacle, a number of countries have implemented various schemes to reduce the costs of capital to small and medium-size enterprises. These range from large operations such as Brazil's Banco Nacional de Desenvolvimento (BNDES) to Bangladesh's Grameen Bank and other micro-financing schemes. Various Ex-Im banks have also played a role in export finance and insurance.

Aid for trade could well be directed specifically at some of these supply-side issues. For example, donors have tended to neglect large-scale infrastructure projects in recent years, but the evidence suggests that this is an area where they need to re-direct their attention, especially since the returns tend to be long-term, reducing the likelihood of attracting private capital. In the same way, a coordinated approach - by donors, the IFIs and regional banks - could do much to tackle the issue of the high-cost of finance by supporting local development banks to fill in the weaknesses in private sector financing at the early stages of development.

Foreign direct investment (FDI) can also help overcome weaknesses in domestic capital markets, but perhaps more important is that FDI can bring in new technologies and increase productivity, contributing positively to export performance, as has been

argued in a number of UNCTAD's World Investment Reports.⁵ The availability of finance and of FDI may also be crucial in order to achieve and maintain competitiveness by using best practice techniques and technology, for example, having flexible and efficient production lines, as well as training workers and middle and upper managers.

The ability to attract FDI is often influenced by factors such as political stability, the availability of an educated labour force, a stable and reliable legal framework for business, and other governance factors. It is often argued that these factors are more important than specific fiscal investment incentives in attracting FDI (or stimulating domestic investment for that matter). Investment in education, also stressed in WEF (2006), has been crucial in the success of East Asian countries and Eastern European countries.

Studies that emphasize the role of incentives refer to the broad institutional and policy framework (see, for example, Easterly, 2001), rather than specific fiscal incentives, such as tax breaks, whose role has been downplayed by various international organisations such as UNIDO and the World Bank, although they may have been a factor in the initial phase of attracting FDI in a number of countries.

Of course, the specific factors that need to be addressed in any individual country can vary widely, and solutions need to be tailored to each country's own needs. Some of these issues are for governments, while others need attention from the private sector itself. Many issues may be best tackled within the context of a public-private partnership, with business and government working together to achieve sustainable development.

e. Building export competitiveness

The World Bank identified the failure to produce an export supply response in reforming countries as a key weakness, consequently giving competitiveness high priority in the context of aid for trade in a recent paper for the Executive Directors of the Fund (World Bank and IMF, 2007). The emphasis on competitiveness is not new to the Bank, having been the subject of its concerns for many years (see, for instance, Harberger, 1988; Keesing and Singer, 1990).

Being internationally competitive refers to the ability of a country or firm to offer its products abroad at a price below or near the price asked by rivals abroad – necessarily without risking its survival through ruinous competition. Thus, revenues have to cover costs and provide a mark-up (or profit) that can be distributed to shareholders or, alternatively, can be retained in order to finance future investments. Improving competitiveness implies reducing unit costs relative to competitors in foreign markets, which can be achieved through a variety of means.

⁵ However, it has also been argued in UNCTAD's Trade and Development Reports and its Africa Report that there is a need to look beyond the rate of growth of exports in assessing the development impact of FDI, and it is important to establish a strong regulatory framework.

First, productivity increases lower unit costs. If a hundred workers produce two hundred units of output instead of one hundred, and do so at unchanged wages (and other variable costs), costs per unit decrease by 50%. From the supply-side productivity increases can be fostered through implementation of policies such as building quality institutions, improving transport and market infrastructure, providing healthcare, higher education and training and supporting technology diffusion, innovation and business sophistication. These ideas underlie the position of the World Economic Forum (WEF)'s World Competitiveness Report which states that "... we understand national competitiveness as the set of factors, policies and institutions that determine the level of productivity of a country. Raising productivity – meaning better use of available factors and resources – is the driving force behind the rates of return on investment, which in turn determine the aggregate growth rates of an economy" (WEF, 2006).

However, generating (export) growth through *indirect* market-oriented supply-side policies and institution building does not stand out as a development success story – in sharp contrast to export-led growth of developing countries with managed exchange rates. A competitive real exchange rate *directly* decreases the relative price of a country's exports in markets abroad, and allows still uncompetitive industries to gain market shares and develop brands. Exports, in turn, are relatively high productivity goods, and a rise in the share of such traded goods in output increases overall productivity. A managed real exchange rate increases exports, generates productivity growth and thus facilitates positive feedback to competitiveness. The fundamental insight goes back to Verdoorn (1949) and Kaldor (1978), who discussed the strong positive relationship between manufacturing output growth and productivity. Frenkel and Taylor (2006) analyze the relationship in an open economy setting, and Frenkel (2007) elaborates on monetary policy issues associated with exchange rate targeting. The importance of getting the real exchange rate right has also been stressed by Harberger (1988), Thomas and Nash (1990). Laird and Messerlin (2003) show that for a sample of Asian and Latin American countries a one percentage point decrease in the real exchange rate index (REER) led to a 0.46 percentage point increase in the index of exports.

Obviously, an exchange rate policy is determined by national monetary authorities and as such is subject neither to multilateral trade agreements nor to a potential deal on aid for trade. However, a variety of *direct* measures, targeted by aid for trade, can be seen as complementary to an exchange rate policy. Examples are the establishment of export processing zones or industrial parks as well as cluster group formation. Export subsidies and State-trading enterprises (STE) can further improve a country's competitiveness.

The World Bank has as well emphasized the importance of the import regime as a factor in export performance, e.g. in relation to trade procedures or duty drawbacks. However, the issue is much broader in that there is a general link between import and export regimes, first propounded in 1932 by Abba Lerner who showed that import taxes also worked through the economy to implicitly tax exports (the so-called Lerner Equivalence theorem). This is one of the central ideas behind reform programmes that emphasize the elimination of non-tariff barriers and reduction of tariff rates. However, as

we have seen, liberalizing import regimes does not produce an immediate response in terms of overall economic growth or in export performance, as discussed previously.

The beneficial effects of reforms need time to manifest and there often are negative effects in the short to medium term that require resources to manage. Unfortunately, some of the reform packages seem to have underestimated the length of time and overestimated the capacity of developing economies to adjust, as in Africa, while other packages have included conditions that have exacerbated the situation, for example, in the Asian crisis of 1997-98.

4. Developments in the WTO

a. The Hong Kong Ministerial Declaration

In response to the concerns of the developing countries about the costs of implementation and possible negative impact of the current WTO negotiations, WTO Members at the Hong Kong Ministerial Conference of the WTO in December 2005 invited the WTO Director-General “to create a task force that shall provide recommendations on how to operationalize Aid for Trade” and to make recommendations on how Aid for Trade might contribute most effectively to the development dimension of the current WTO negotiations. The DG was also invited to consult with Members as well as with the IMF and World Bank, relevant international organisations and the regional development banks on “appropriate mechanisms to secure additional financial resources for Aid for Trade, where appropriate through grants and concessional loans.” The HK Declaration (paragraph 57) also stated that “Aid for Trade should aim to help developing countries, particularly LDCs, to build the supply-side capacity and trade-related infrastructure that they need to assist them to implement and benefit from WTO Agreements and more broadly to expand their trade. Aid for Trade cannot be a substitute for the development benefits that will result from a successful conclusion to the DDA, particularly on market access. However, it can be a valuable complement to the DDA.”

In a related decision, the WTO Ministers in Hong Kong welcomed the establishment of a Task Force by the Integrated Framework (IF) Working Group, endorsed by the IF Steering Committee (IFSC), to make recommendations for an enhanced IF (finally adopted on 1 May 2007), including: how to provide increased, predictable, and additional funding on a multi-year basis; how to strengthen the IF in-country, including through mainstreaming trade into national development plans and poverty reduction strategies; more effective follow-up to diagnostic trade integration studies and implementation of action matrices; and achieving greater and more effective coordination amongst donors and IF stakeholders, including beneficiaries; and how to improve the IF decision-making and management structure to ensure effective and timely delivery of the increased financial resources and programmes.

Following the Hong Kong meeting of the WTO, the WTO Secretariat prepared a concept note on Aid for Trade, which also linked the enhanced IF to aid for trade (WTO, 2006a). The paper noted that “by the end of the Round, there will need to be evidence that ‘secure’, ‘additional’ and ‘predictable’ Aid-for-Trade is being provided.” Then paper expected that “appropriate mechanisms to guarantee this” would be expected to emerge from a consultative process. It also noted that “at a minimum, developing countries and LDCs will expect evidence that substantial fresh money is being made available. They expect Aid-for-Trade to go well beyond the scope of the IF, and help them to cover the costs of implementing WTO Agreements, macroeconomic adjustment, training and institution-building, and supply-side capacity and infrastructure.” The paper also commented that statements made by donors at the Hong Kong meeting suggested that they were supportive of these expectations,⁶ and that it seemed that “the amount of new money they are prepared to commit to Aid-for-Trade is potentially much larger than for the IF.” The paper singled out trade facilitation as an area where aid for trade could make an important contribution.

The paper pointed out that both the IMF/World Bank Development Committee and the OECD DAC favoured the improvement of existing mechanisms rather than the creation of new ones to handle aid for trade.

As far as the WTO’s own role was concerned, the WTO paper suggested that this was one of advocacy, encouraging agencies and donors to increase the resources for aid for trade on favourable terms. It also said it would encourage trade ministries in developing countries and LDCs to work domestically for trade to receive a higher profile in the process of attracting and allocating ODA at the national level. It acknowledged that it would need to work with multilateral, regional and bilateral donors under the coherence mandate to increase flows of technical and financial assistance to trade through existing channels.

The WTO also proposed to work with OECD on data on bilateral aid for trade flows as well as asking the World Bank, the IMF and regional development banks for data on their aid for trade activities.

⁶ According to the WTO paper, Japan announced spending on trade, production and distribution infrastructure of \$10 billion over three years, the U.S. announced Aid-for-Trade grants of \$2.7 billion a year by 2010, and the E.U. and its member states announced trade-related spending of €2 billion per year (up by 600 million) by 2010. Calculations on which G-7 Finance Ministers based their statement of support in early-December 2005 involved doubling Aid-for-Trade by 2010 to \$12 billion a year, with an additional \$2 billion a year for "trade policy, regulation and development" (policy formulation, implementing trade agreements, export promotion, and standards) and an additional \$4 billion a year for supply-side capacity and infrastructure. The separate component of adjustment assistance is tied more directly to the results of the Doha Round than other forms of Aid-for-Trade – whether the amount needed will exceed the resources available through existing programmes, notably the IMF’s Trade Integration Mechanism, will have to be assessed at a later stage.

b. Submissions by WTO Members and international agencies

As well as the various financial institutions, a number of other international delegations and WTO Members responded to the Concept Note and provided inputs to the Task Force. These are all available on the WTO web-site under two document series: WT/AFT/* and WT/COMTD/AFT/*.

The WTO Secretariat has also produced a compilation of contributions from inter-governmental organizations (other than OECD) to the Task Force (WTO, 2006c). This includes:

- An overview of the current scope and content of the aid for trade programmes of the various institutions.
- An assessment of outstanding, important trade-related needs that are not currently being met.
- The extent to which trade, as a vehicle to promote growth, development and poverty reduction, has been adequately addressed in countries' development plans and poverty reduction strategies.
- How trade-related needs and priorities should be identified.
- The adequacy of the existing system of delivery mechanisms for aid for trade, and what options might exist to address any gaps.
- The need to strengthen monitoring and evaluation, and how this should be done.
- The role of the private sector in identifying needs and implementing responses.
- How aid for trade should reinforce the principles of aid effectiveness of coherence

The responses to these questions are taken up in the report of the Task Force (below).

A useful comparison table of the various recommendations, proposals and views on aid for trade by a number of WTO Members, international Organizations, NGOs and individual authors has also been compiled by the International Centre for Trade and Sustainable Development (ICTSD, 2006). A number of groups that are major beneficiaries of aid for trade made substantive contributions, for example, Benin on behalf of the African Group (WTO, 2006d), Zambia on behalf of the LDCs (WTO, 2006e) and Mauritius on behalf of the ACP Group (WTO, 2006f). The major developed country donors do not appear to have made any written contribution on the general issue, although the EU did make a submission on engaging the private sector on aid for trade.

As discussed earlier in the paper, the IFIs tend to take a fairly wide view of the needs that might be covered by aid for trade, and they also view their lending activities as covered by the definition, not merely official development assistance. They also consider that there is no need for any new body to administer aid for trade, thereby opposing the proposal by Stiglitz and Charlton (2006) for a stand-alone Global Trade Facility. In their

submissions to the aid for trade Task Force, the African Development Bank and the LDC Group seemed to support the establishment of a special trade funding facility. However, this was not supported by other developing countries. The ACP group, however, suggested that the current IF model was a good framework with respect to governance structure, involvement of relevant agencies and management of funds. Alternatively, it suggested that it might be possible to consolidate existing multilateral TCB trust funds, modelled on that of the Global Environment Facility. UNCTAD said that, if the global facility were not to be established, then an option might be the establishment of consolidated mechanism funding -- a sort of umbrella facility of aid for trade funding mechanisms, which would regroup existing, separate funding mechanisms to provide a coordinated response to country-specific needs and requests for aid for trade. This would function like a door conference, but on less of an *ad hoc* basis than the current mechanism. UNCTAD suggested that it would be desirable to have a clear division of labour between the funding agencies and mechanisms on the one hand, and implementing agencies, on the other.

OECD would exclude aid for trade from covering macro-economic or micro-economic adjustments, such as social safety nets, balance of payments support for compensation for potential costs from multilateral liberalization, such as preference erosion or a reduction in government revenue (OECD, 2006). It would appear that OECD is arguing that these kinds of adjustments should not be on the aid for trade agenda, but not that they are undeserving of support, and it notes that the World Bank and the IMF have been supporting developing countries' adjustment efforts arising from a host of factors, including trade reforms, and will continue to do so. In seeking to exclude these broader kinds of adjustments from the aid for trade agenda, OECD seems to be divided from the large majority of other agencies and WTO Members that made submissions to the aid for trade Task Force perhaps reflecting its own historical concern with ODA, rather than assistance in the broader sense.

The majority of submissions emphasized the need for "additionality". The ACP group, and Oxfam argued that aid for trade support should be primarily in the form of grants. The Inter-American Development Bank also suggested that the resources should be predictable, long-term and grant-based money. Oxfam also added that aid for trade should be free of economic conditions.

Most submissions emphasized the importance of country ownership and suggested that needs assessment should be country-driven. Several submissions stressed the need for a diagnostic study to determine the needs and priorities of individual countries.

The majority of submissions suggested the need for a monitoring mechanism on the delivery and effectiveness of aid from trade. Several submissions suggested that such a mechanism should be housed within the WTO. However, the African Development Bank suggested the need to establish a monitoring body, consisting of the WTO, multilateral development banks, NGOs, and civil society, similar to the Africa Partnership Forum.

A number of submissions referred to a role for the private sector. For example, the submissions referred to: the need for public-private partnerships; the need for the private sector to have a role in determining the development needs of the country, including private sector projects as potential beneficiaries, for example, in the context of enterprise development; the need to focus on private sector development by facilitating the improvement of the business environment for exporters; a potential role for the private sector in providing expertise and financing, coordinating with other donors. Thus, the private sector was seen both as a beneficiary of aid for trade as well as a contributor in public-private partnerships.

c. The WTO Task Force on Aid for Trade

The Task Force, chaired by Ambassador Mia Horn Af Rantzien of Sweden, reported back to the WTO in July 2006, setting out a detailed course of action for Aid for Trade, with guidelines on funding, identifying recipients' priorities, needs assessment and monitoring (WTO, 2006b). This report was adopted by the WTO General Council in October 2006. The Task Force did not recommend a new agency to administer Aid for Trade, but stressed the need for a better coordination mechanism at the national, regional and multilateral levels. The WTO Director-General has also stressed the WTO's role in "promoting coherence" through monitoring aid for trade.

The Task Force considered that aid for trade was about "assisting developing countries to increase exports of goods and services, to integrate into the multilateral trading system, and to benefit from liberalized trade and increased market access." The Task Force believed that effective aid for trade would "enhance growth prospects and reduce poverty in developing countries, as well as complement multilateral trade reforms and distribute the global benefits more equitably across and within developing countries."

The Task Force also set the general framework for the discussion by making it clear at the beginning of its report that "additional, predictable, sustainable and effective financing is fundamental for fulfilling the Aid-for-Trade mandate". And it also recalled that "substantial additional targeted resources for trade-related programmes and projects" had been pledged at the WTO's Hong Kong Ministerial Conference "and against the background of the broader international commitment at the UN's Monterrey Conference and the G8 Summits in Gleneagles and St. Petersburg to significantly scale up development assistance by 2010." Importantly, the Task Force considered that, in order to measure "additionality" and the adequacy of funding available, it would be necessary to take stock of what is being done today, and this led to the specific proposal to review the scope of the Joint WTO/OECD Database in the light of the Task Force's definition, and to update the information on the basis of needs and responses by both providers and recipients of aid for trade. This would also be important for a monitoring and evaluating mechanism that the Task Force considers to be essential in building confidence that increased aid for trade will be delivered and effectively used. It also notes that all the providers of aid for trade and the recipient countries have the responsibility to report on progress and results.

Concerning the scope of aid for trade, the Task Force said that it should be defined in a way that is “both broad enough to reflect the diverse trade needs identified by countries, and clear enough to establish a border between Aid for Trade and other development assistance of which it is a part.” It went on to list the following categories, based on the Joint WTO/OECD Database:

- Trade policy and regulations, including the training of trade officials, analysis of proposals and positions and their impact, support for national stakeholders to articulate commercial interest and identify trade-offs, dispute issues, institutional and technical support to facilitate implementation of trade agreements and to adapt to and comply with rules and standards.
- Trade development, including investment promotion, analysis and institutional support for trade in services, business support services and institutions, public-private sector networking, e-commerce, trade finance, trade promotion, market analysis and development.
- Trade-related infrastructure
- Building productive capacity
- Trade-related adjustment
- Other trade-related needs

This is a very broad definition that could likely cover all potential trade and trade-related needs, which, given the inclusion of the category “other trade-related needs,” hardly establishes a border between aid for trade and other development assistance, as was the stated intention of the Task Force.

Two other parts of the report by the Task Force deserve mentioning. The first is a list of what the Task Force considered to be the major challenges remaining in integrating trade into development strategies. These include:

- Low attention to trade as a tool of development in recipient countries and in donor agencies.
- Insufficient trade mainstreaming in national development strategies and PRSPs.
- Lack of private-sector involvement in identifying trade needs.
- Limited absorptive capacity in recipient countries.
- Inadequate linking mechanisms and lack of predictability in donor response to trade priorities identified at the national and regional levels.
- Lack of coordination and coherence in donors' trade-related responses.
- Slow, duplicative and bureaucratic processes in the assessment and delivery of trade assistance, including burdensome parallel structures within recipient countries.
- Lack of data on, and analysis of, trade policies and their impact on development, lack of easily-available information on existing Aid-for-Trade instruments.

- Ineffective monitoring of trade-related country policies and donor activities; absence of rigorous, independent project and programme evaluation and impact assessment.
- Limited support for regional, sub-regional and cross-border trade-related programmes and projects.
- Inadequate support to address the adjustment costs of trade liberalization.
- Insufficient resources for infrastructure and productive capacity building.
- Uneven country coverage.

The second element worth reporting is what the Task Force considers to be the objectives of aid for trade. These are:

- To enable developing countries, particularly LDCs, to use trade more effectively to promote growth, development and poverty reduction, and to achieve their development objectives, including the Millennium Development Goals (MDGs).
- To help developing countries, particularly LDCs, to build supply-side capacity and trade-related infrastructure in order to facilitate their access to markets and to export more.
- To help facilitate, implement, and adjust to trade reform and liberalization.
- To assist regional integration.
- To assist smooth integration into the world trading system
- To assist in implementation of trade agreements.

The report goes on to say that aid for trade should be guided by the Paris declaration on aid effectiveness, applicable to donors, agencies and beneficiaries, including key principles such as country ownership, mutual accountability, aligning aid to national development strategies, effective donor coordination, harmonization of donor procedures, use of programme-based aid modalities, managing for results, transparency, and predictable, multi-year commitments. The report states that there is a need to strengthen the demand side, through a commitment to country ownership and country-driven approaches, such as in setting priorities. It states that donors should give more attention to trade issues in the aid programming and strengthened their trade expertise both in the field and at headquarters. It also makes the point that greater donor and agency coordination and harmonization of procedures are critical. It suggests the need to better match the demand and response sides of the aid equation, for example through a "National Aid-for- Trade Committee", which would include recipient countries, donors, and other relevant stakeholders, such as the private sector, under the leadership of relevant ministries. He report emphasizes the need for greater coordination between donors and the main international agencies delivering aid for trade. It also suggests that technical cooperation among developing countries is a valuable tool to deliver effective results because of their common experience and understanding of the challenges they face. These points are extensively elaborated in the report and included in an extensive list of specific recommendations.

In relation to the WTO negotiations, the Task Force considered that aid for trade was a complement to, not a substitute for, the Doha Round, but was not conditional upon its success. It noted that aid for trade was important in its own right, and should assist developing countries to benefit from increased trade opportunities multilaterally (both from previous rounds and from the anticipated results of the current WTO negotiations), regionally, bilaterally and unilaterally. The Task Force therefore recommended that aid for trade should be operationalized as soon as possible.. It argued that increasing trade opportunities for developing countries, in particular the LDCs, remained the most important contribution that the WTO could make to development, but it also noted that a successful conclusion of the negotiations would increase the need for assistance to implement new agreements (e.g., Trade Facilitation), to ease adjustment costs, and to make use of new market access.

Finally, the Task Force urged WTO Members to implement its recommendations expeditiously. It suggested a key role for the WTO Director-General in following up on the recommendations of the Task Force, including by pursuing his mandate to consult on "appropriate mechanisms to secure additional financial resources for Aid for Trade" so that the mandate in the Hong Kong Declaration could be implemented in a holistic manner. Among these recommendations for follow-up, it suggested that he establish an *ad hoc* consultative group to take forward the practical follow-up of these recommendations, and invited him to convene an initial review of Aid for Trade, with the participation of all relevant stakeholders. It also suggested that the WTO Secretariat conduct an assessment of associated Aid-for-Trade needs in developing countries, particularly those most affected, including LDCs, and of how aid for trade could contribute to the development dimension of the Doha negotiations.

d. Follow-up actions on Task Force recommendations.

A general review of Aid for Trade is scheduled for November 2007, preceded by three regional reviews covering Latin America, Asia and Africa, that began in September 2007.

At the WTO General Council meeting in December 2006, the Director-General said that the proposal from monitoring and evaluation at three levels: global monitoring carried out by the OECD-DAC; donor monitoring, in the form of self-evaluations; and in country assessments, done by the recipients. He suggested that these inputs should be addressed in periodic reviews in the Committee on Trade and Development (CTD), in order to give all members an opportunity to discuss the findings and express their views, with the aim of bringing the findings together in an annual report on aid for trade.

At the first session of the CTD on aid for trade, the chairman said that the CTD could play a key role in moving from the policy discussion phase to the implementation phase. To launch the process, the OECD-DAC Secretariat had asked to give a preliminary global perspective on ODA flows related to trade, trying its existing Creditor Reporting System (CRS). The CTD was also planning to invite multilateral and bilateral agencies to share the results of their own self-evaluations.

Also at the first session of the CTD on aid and trade, a representative of the OECD made a presentation, saying that, using the current CRS categories, statistics show that of the period 2002 to 2005 commitments to trade development assistance with just over \$2 billion, productive capacity building assistance of a role \$9 billion, infrastructure or work \$11 billion and general budget support averaged \$5 billion. He also observed that commitments which had been made since the Monterrey Financing for Development Conference in 2002 called for an additional US\$50 billion of ODA from 2004 to 2010. This included the doubling of aid for Africa from US\$25 to US\$50 billion. He noted that these commitments had been reaffirmed by a meeting of the G8 development ministers in Berlin and included the Hong Kong Aid for Trade pledges and the Gleneagles commitments. He also noted that the international community was still undertaking a big debt relief effort which explained the slight projected increases in ODA for 2007 and 2008. However, for the years 2009 and 2010, there would need to be a very sharp scaling up of aid if the objectives that had been fixed so far were to be met. This had to be seen in the light of a fall in ODA of 5 per cent in 2006. Excluding debt relief, ODA had fallen by 1.8 per cent. A substantial annual increase in ODA was needed. Finally, he noted that Aid for Trade, using the definition in the Task Force report, amounted to 26 per cent of total ODA. Forty-one per cent of ODA was spent in social and administrative infrastructure, including education, health and governance. He observed that these categories were not irrelevant to Aid for Trade, since any country which wanted to diversify its economy and its exports would have to pay attention to its human resources base. This should not be ignored when carrying out the Aid for Trade monitoring.

The CTD also held an aid for trade meeting in April 2007 to provide information on trade finance for developing countries. Senior representatives of the Asian Development Bank, the European Bank for Reconstruction and Development, the Inter-American Development Bank and the IFC made presentations. It was stated that the international financial institutions (IFIs) were running a global network of Trade Finance Facilitation Programmes (TFFP) that were acknowledged to fit well with the aid for trade initiative. The TFFPs did not require further administrative structures; they were demand-driven, with demand outweighing supply; donor funding also existed, but needed to be topped up to boost the supply of trade finance; TFFPs provide "global coverage" to small and medium-size enterprises (SMEs) and small banks from all around the world, without regional exclusion; the leverage of such programmes is very high on trade flows (\$4 of trade "produced" for \$1 dollar of guarantee); TFFPs benefit small private sector players which would not have a chance to trade without these programmes; finally, technical assistance was also provided by all IFIs (at donor cost) since the ultimate objective was to allow developing countries to handle their own trade financing.

5. Private sector issues

As noted earlier, the role of the private sector was raised by the WTO Secretariat in its survey of activities by international organizations. The respondents generally said that it was important to take account of the views of the private sector in designing aid for trade programmes. The WTO/UNCTAD International Trade Centre (ITC), for example, said that: "Most of the benefits of development derive directly from the activities of the

private sector, including the largest and the very smallest enterprises and local non-profit agencies. The private sector should have an equal, if not even a pre-eminent role, in determining the development needs of a country.For reasons of sustainability also, private interests must be invoked since it is they which principally drive the development process, with or without donor support.”

This centrality of the private sector was also highlighted by Brewster and Njinkeu (2006), who noted that there had been little success in creating an environment conducive to private sector development in developing countries and LDCs. They noted that the cost of doing business in these countries was still high due to inadequate physical infrastructure or poor access to credit, investment capital and banking services. In these countries, the overwhelming majority of private business units were micro, small or medium-sized enterprises, coexisting with a formal sector. These enterprises were often too small to achieve not all division of labour and internal specialisation in their business operations. Brewster and Njinkeu said that ground-based resources were not traditionally used for financing capital investment for the private sector. They suggested that it would be more likely that aid for trade grant resources could be used as seed money to attract the participation of commercial banks in economic activities, for example, by softening the terms and conditions for accessing resources that might otherwise be available only on commercial terms. Their assessment of this need seems to contradict the statements made by the regional banks at the meeting of the WTO CTD (above) on the availability of trade finance, but it is consistent with the findings of Laird and Fernández de Córdoba (2006).

UNCTAD saw the private sector as both a beneficiary of aid for trade as well as a contributor in public-private partnerships, and, it said, enterprise development should accordingly be a key component of aid for trade. In this, it emphasized trade facilitation, where the private sector, as the main direct beneficiary, could act as a partner of the government agency in the design and implementing of solutions to simplification. “The trading community and the providers of trade support services can improve their commercial practices and thereby contribute to lower transaction costs and times.The private sector has shown initiative in relevant, if infrequent, cases where their contribution, both financial and in kind, has helped to develop advanced systems and train government officials in the use of modern trade-monitoring management techniques.”

As mentioned earlier, the EU also made a submission on how to engage the private sector on aid for trade. It said that the private sector could try to add additional value by creating innovative business solutions for specific trade constraints in developing countries and thus transferring technology and know how. The private sector could also help by identifying constraints to trade development, having first-hand knowledge about the constraints facing trade development. It suggested that the role of the private sector could take different forms such as an advisory role, participation in the management of activities for trade and private sector development, the development of action plans, or more directly creating public private partnerships to supply specific services or to deliver goods and services to the government or other companies. A very

important topic that could be addressed in this context would be the involvement of the private sector in developing regulations and operational support for backbone support services (financial services, transport services, customs and port functioning, utilities). Specifically, the following actions could be considered:

- Governments should include the private sector in their trade policy processes and actively involve them in trade diagnostics work, design, implementation and monitoring of Aid-for-Trade actions. Where the appropriate institutional mechanisms are lacking, they should be created, building on what is already there.
- Private sector organizations, such as chambers of commerce and branch organizations, in developing countries should be supported, for instance through training, studies, seminars, to enable the private sector to participate in the trade policy process and the development and implementation of Aid-for-Trade plans.
- Donors should use donor groups on private sector development to promote and coordinate support for trade.
- Public Private Partnerships should be considered as a delivery mechanism for TRA.
- At the global and regional level, associations of the private sector should be involved in the Aid-for-Trade debate, for instance through inviting them to events on Aid for Trade. They could then encourage their members to play a more active role in developing countries, including through providing know-how, training and advice.

In a submission to the Task Force, Zambia, on behalf of the LDC Group, also made a submission concerning the role of the private sector in aid for trade (WTO, 2006k). Zambia argued that Value Chain Analysis was one of the tools that could be used to effectively pin point the needs and gaps on which aid for trade projects could focus so as to deliver maximum value for the least possible cost in LDCs and other developing countries. It suggested that Value Chain Analysis could help:

- To increase the competitiveness of the private sector and expansion of exports
- Enhance productivity and value addition.
- Identify, cost and propose measures needed to minimize impediments and improve the environment for both public and private investment.
- Promote better understanding of the characteristics and inefficiencies of specific value chain.
- Strengthen linkages along the primary-to-finished goods supply chain.
- Identify new market opportunities and measures of ensuring sustainability.
- Identify interventions concerning policy, institutional and administrative reforms as well as physical infrastructure needs with the greatest impact on efficiency along the value chains.

The use of value chain analysis in relation to aid for trade was also suggested by Brewster and Njinkeu (*op. cit.*) and Wilska and von Bonsdorff (2006).

Clearly there are a number of issues related to aid for trade that can usefully be addressed as a cooperative effort by government and business. Such partnership efforts can be used to identify problems and possible solutions, and such public/private sectors partnerships seem to have been important in a number of countries, such as Ireland, Mauritius and Singapore.

6. Conclusions

There is now widespread acceptance of the need for aid for trade which could make a useful contribution to achieving the MDGs, in particular under Goal 8. This derives in part of the role that trade can play in economic development, as well as the growing appreciation that this is not an autonomous process, but needs a pro-active support, and that, badly managed, trade reforms can cause considerable damage.

However, the discussions that have taken place on aid for trade in the last few years have thrown up a number of questions that need a response to allow the international community to move on the issue. The key questions seem to be the following (from the WTO Secretariat's Concept Paper of January 2006). How much new money is to be made available (without cutting into other official development assistance)? What is the nature of the money - grants or loans? And, what policy conditionality is likely to be attached to its disbursement? To these questions might be added: What will be covered by aid for trade? Who will be eligible? How will the aid be administered? Who will oversee aid for trade activities? And, finally, what is the link, if any, with the WTO negotiations?

As far as new funding is concerned, this was promised at recent G8 meetings and was confirmed most recently in the G8 Trade Declaration at Heiligendamm in 2007, which stated: "Building up on the G8 Summits in Gleneagles and St. Petersburg and the recommendations of the WTO task force on Aid for Trade we urge all donors to improve quality and quantity of the means available by 2010 and encourage partner countries to include the Aft agenda in their poverty reduction and national development strategies."

World Bank papers seems somewhat sceptical of the feasibility of attracting additional funds for aid from trade, as, in practice, aid allocation decisions by donors is likely to be done in the general context, and increasing aid for trade is likely to require some trade-offs. As noted by the representative of the OECD at the recent meeting of the WTO's CTD, there have been slight projected increases in ODA for 2007 and 2008 while the international community was continuing to make an effort on debt relief, but for 2009 and 2010, there would need to be a very sharp scaling up of aid if the objectives that had been fixed so far were to be met.

On the nature of the assistance, most of those engaged in the debate – and certainly the IFIs - seem to think that the concept refers to both grants and loans. (The IFI papers refer to "concessional" loans, but in World Bank and IMF, 2007, it is noted that this would exclude much of the trade-related lending by the World Bank and regional development banks). However, in so far as the main monitoring exercise is concerned,

whereby OECD-DAC is providing data to the WTO, this only refers to grants and lending with a high grant component (such is International Development Association, IDA, lending). On the other hand, the questions also arises whether other forms of assistance – in kind, rather than cash – should be considered as aid for trade for example, technical assistance provided from the regular budgets of the international organizations or assistance by means such as opening markets (including through preferences), withdrawal of domestic support and export subsidies in areas of export interest to developing countries, and other forms of special and differential treatment.

With respect to what conditions might be attached to such aid, a question of considerable importance is the extent to which new conditions would be attached. Will there be conditionality as well as “additionality”? Stiglitz suggests that aid for trade should not be subject to the usual macro-economic or political conditionality. And, as discussed in the paper, the idea that aid for trade would come with strings attached raises some concerns among developing countries, some of which have had unfortunate experiences with reforms under Bank-Fund lending programmes.

The next question is what kind of activities would be covered by aid for trade. Most international organizations and NGOs seem to take a fairly wide view of the issue, but OECD seems to be opposed to at least narrowly defined ODA to help countries cope with the major macroeconomic and microeconomic adjustments associated with trade reforms, although it sees the World Bank and the IMF continuing their supporting role for these kinds of adjustment. The IMF and the OECD tend to be dismissive of the importance of preference and tariff revenue losses, including calculations by the World Bank and UNCTAD, but they acknowledge that these losses could cause problems in some instances. There have also been a number of studies on the effectiveness of supports for some types of activities, such as trade-related physical infrastructure, especially in Sub-Saharan Africa, and other forms of trade facilitation. ITC, UNIDO, the LDC Group and others also perceive a role for the private sector in identifying the nature of the constraints to building supply capacities and export competitiveness, and access by SMEs to financial services have been identified as a market failure in many developing countries. At least part of the hand-wringing seems to be an ethical issue relating to what burden should be borne by the country affected (government, citizens, private sector, etc) and where there is a moral obligation to help. However, while this might seem alien to some international organizations, the notion of compensation between states for certain trade policy changes is an integral part of WTO law in relation to the withdrawal of tariff concessions, in RTAs, etc., and may be awarded in dispute settlement (Page, 2007). Compensatory mechanisms are also well known in some systems, for example, in European agricultural policy. Bhagwati has also argued that developing countries need aid for trade for import adjustment programmes, as assistance to offset tariff revenue losses and as a “buy out” to offset their opposition to MFN tariff reductions because of potential preference losses.⁷

⁷ Financial Times, 26 September 2005. Letter to the Editor: “World Bank Funds should be used to lubricate trade liberalization by developing countries.”

A closely related issue is the extent to which aid for trade would be targeted to specific projects or provided as general budget support. By its nature, one might expect that aid for trade would be targeted at specific, trade-related projects. But are such projects always the developing countries' highest priority? For example, if a developing country had an incidence of 30% of AIDS, as is the case in some African countries, then spending money on health programmes might be seen as a higher priority than spending money, for example, on an improved customs valuation system in order to comply with WTO obligations. A number of donors have tended to favour general budget support, allowing the developing countries to determine their own needs and priorities, but an aid for trade programme may tie them to much more specific projects.

As to which countries would be eligible to receive aid for trade, it is clear that donors now consider LDCs to be the major countries deserving of aid for trade, and aid budgets now reflect this fact. Today, this means that other low-income countries are receiving proportionately less aid than before. Yet many of these countries have a very high proportion of the world's poor. If present trends continue, however, these countries may expect to have to rely to an increasing extent on other forms of assistance, especially assistance targeted to specific projects favouring the poor or other particular interests of donors.

The question also arises how aid for trade will be administered? Stiglitz has suggested a stand-alone Global Trade Facility - not as a stand-alone fund, but as a special facility, like the Global Environment Facility - but this seems to have garnered only limited support. As noted in the paper, UNCTAD has proposed that, if a global facility were not to be established, an option might be the establishment of consolidated mechanism for funding, regrouping existing, separate funding mechanisms to provide a coordinated response to country-specific needs and requests for aid for trade. The IMF, which established its Trade Integration Mechanism (TIM) partly to anticipate adjustment problems, and the World Bank consider that existing mechanism are adequate to meet foreseeable needs, a position which has been criticized by the LDCs, and others. The Task Force did not recommend any specific mechanism, but was critical of existing mechanisms.

Certainly, there is a need for better coordination of donor activities, and, despite its hesitant start and limited resources, the IF model - for all its faults - seems to be regarded as a suitable framework with respect to governance structure, involvement of relevant agencies and management of funds. One advantage of the IF is that it places considerable emphasis on integrating trade-related lending into wider Poverty Reduction Strategy Programmes (PRSPs). This may be one way of ensuring that aid for trade is given appropriate treatment in terms of each beneficiary country's own development priorities, also ensuring ownership of the programme. However, the LDCs have successfully opposed the extension of the IF to other low-income countries, so it seems that a parallel structure, identical or very similar to the IF - perhaps even with identical membership - would be needed to deal with countries other than the LDCs. This may be an advantage since, as Stiglitz points out, the IF itself has extremely limited resources,

that do not come close to meeting the needs that have been identified in the various analyses of situations that would merit aid for trade.

It would seem that, at the political level, oversight of aid for trade has *de facto* already been devolved to the WTO, which has established a monitoring and annual review mechanism, going beyond the advocacy role which it suggested in its own submission to the Task Force, and despite the proposals of the African Development Bank that a monitoring mechanism be established similar to the African Partnership Forum, as noted earlier. The Director-General has also suggested that the Trade Policy Review Mechanism be used to scrutinise the success of aid for trade programmes. However, the WTO has relatively limited experience of aid for trade in the wider sense, being mainly concerned with technical assistance related to implementation of WTO legal obligations. On the other hand, the WTO Secretariat has been providing logistical support for the IF, and if the IF or a similar mechanism were to be used as the main means of administering aid for trade, then it would be difficult to argue against a similarly limited supporting role. At the same time, this does not, nor could not, require other agencies to abrogate their responsibilities for their own activities and to carry out their own evaluations.

Finally, what is or should be the link, if any, between aid for trade and the WTO negotiations? It has been argued that aid for trade should play a complementary role to trade reforms and to a successful conclusion of the Doha negotiations, and it should not become a substitute for these. Certainly, at present, aid for trade is not an integral part of the WTO negotiations (e.g., through the Single Undertaking), although there is some recognition of the need for technical assistance for implementing the results of the negotiations, and it seems unnecessary and undesirable to wait till the completion of the negotiations to think through how this would be operationalized. However, in the WTO context, there is no general linkage between the overall economic impact of the negotiations and aid for trade, despite the unfortunate experiences of trade reforms in some developing countries. Yet, as Nielson (*op. cit.*) from the World Bank argued, countries suffering adjustment shocks from trade liberalization, including the Doha round, need to be assured of transition support from the international community. In this sense, the WTO seems to be set on repeating the process at the end of the Uruguay Round of agreeing on a deal without any attempt to assess either the costs of implementation in advance or how it will be paid for. Kool-Aid, anyone?

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