Rethinking World Trade Negotiations

Kevin P. Gallagher

At present, the negotiations for the Doha round are in jeopardy to be put on hold until at least 2009. A two-year break in negotiations is not necessarily damaging to the talks as long as nations use the time to rethink trade liberalization. By reintroducing development to the Doha round, the possible subsequent reforms could be a way forward in making trade work for the poor.

Though Uruguay Round negotiations were completed in 1994 and culminated in the establishment of the World Trade Organization (WTO) in 1995, developing countries balked when the industrialized world proposed another round of global trade talks in 2001, citing the shortcomings of the previous round. Indeed, they accepted new negotiations only on the condition that development issues form the centerpiece of the negotiations.

The initial fanfares sounded promising. At the 2003 Cancun Ministerial meeting of the WTO, Eveline Herfkens, former World Bank executive director and current executive coordinator for the United Nations' Millennium Development Goals, asserted that "[a] pro-poor Doha Round could increase global income by as much as $520 billion and lift an additional 144 million people out of poverty."[i] Yet new projections, from the same sources, now estimate potential welfare gains at just $287 billion in the year 2015—just a third of the level two years ago. Projections of gains for developing countries have dropped to $90 billion—0.8 percent of GDP, while their share of global gains has fallen from 60 percent to just 31 percent.[ii] The primary reason for this enourmous decrease in projected gains is due to changes in the database used for trade model simulations. Such sensitivity to updating the base year by merely a few years commends to read any such "promises" from models with the utmost care. In any case, it is of grave concern given that the current negotiations are billed as the "development round" of global trade talks.[iii]

Table 1. Revised Estimates of Doha Benefits

	World	Developing countries	(Poverty)
Year	*Benefits ($USb)*	*Benefits ($USb)*	*Million persons ($2/day)*
2003	832	539	144
2005	287	90	66

Source: See endnote II

Furthermore, these estimates presume a scenario of "full" global trade liberalization. In other words, the models assume that all tariffs and subsidies are completely eliminated in the world economy, a certainly unrealistic scenario for the current round. To reflect more accurately the state of the present negotiations, the new reports include projections for a "likely Doha scenario" of partial liberalization.[iv] Such "likely" Doha benefits predicted by the models are shown in Table 2, with global gains for 2015 at just $96 billion, of which only $16 billion would accrue to the developing world—representing a meager 0.16 per cent of GDP. In per capita terms, that amounts to $3.13, or less than a penny per day per capita for those living in developing countries. Thus, assuming for the arguments sake that the models' assumptions are valid abstractions of economic reality, and such "gains" in fact materialize, developing countries' cut would be close to negligible relative to, say, export revenues.

Although agriculture has received most of the attention in the negotiations, developing country gains from "likely" agricultural reforms amount to less than 0.1 percent of GDP—just $9 billion. Likely gains from northern subsidy reduction are projected at barely $1 billion.[v] Only a few developing countries are among the recipients, as half of all the benefits to developing countries are expected to flow to Argentina, Brazil (which stands to receive 23 percent of the developing country benefit), China, India, Mexico, Thailand, Turkey, and Vietnam.[vi]

Table 2. Benefits of "likely" Doha Round scenario

	Beneficiary region		
	High-income	Developing	World
Total amounts, billions of dollars	80	16	96
Per capita, dollars per person	$79.04	$3.13	$15.67
Percentage of GDP	0.24%	0.16%	0.23%

Source: See endnote II.

Another area of negotiation in the Doha Round is services negotiations. Services trade has been growing faster than goods trade since the 1980s. Developed countries are pushing developing countries to open up their services markets—especially in the financial and telecommunications sectors—in exchange for market access in agriculture. Modeling services liberalization is in its infancy,[vii] but projections confirm the distribution of gains from goods market liberalization. Like the estimates in goods trade, services trade liberalization is expected to yield relatively small benefits, the majority of which would go to developed countries. Under a full liberalization scenario, the total benefit for the world would be $53 billion. Only 34 percent of those benefits would go to the developing world, amounting to a one-time increase of 0.31 percent of GDP, or roughly a penny per day per capita. A more likely scenario of partial liberalization—50 percent reduction in services trade barriers–would yield only $6.9 billion for the developing world, or 29 percent of the total benefits, which amount to much less than a penny per day for one year. Importantly, and analog to merchandise trade liberalization, most of the gains would accrue to large, semi-industrialized countries such as India, South Africa, and China.

The World Bank created extensions for their models in order to estimate the extent to which the Doha round will lift the world's poor over global poverty lines. Like projected welfare gains, the poverty projections are now smaller. The Cancún projection cited by Herfkens of 144 million people has now been revised downward to 66 million under the complete liberalization scenario.

The "likely" Doha scenario would bring the number to just 6.2 million people lifted above the $2 per day poverty line and 2.5 million people lifted above the $1 per day level of extreme poverty.

Moreover, it should be emphasized that such poverty-alleviation calculations, just as the welfare gains previously discussed, depend crucially on assumptions made by the modelers. Both welfare gains and poverty reduction in the models rest on the assumption that tariff reductions reduce prices, so that, *given income at a full employment level*, people can afford to buy more—welfare increases—and more people can buy just enough not to be counted any longer as poor, decreasing poverty. It is worth emphasizing: Even benefits as puny as a penny per day per capita for the South and 2.5 million people helped out of extreme poverty are build upon the assumptions that (a) increased trade openness does not lead to unemployment due to displacement, (b) producers in developing countries are competitive, and (c) their governments are able to replace all lost tariff revenues with consumption taxes.[viii] If the projected gains for developing countries are so small, and rest on dubious assumptions, it makes sense to ask who really bears the costs of trade liberalization.

Key among the costs of liberalization are those associated with adjustment, which take the form of tariff revenue losses and job losses. The standard models—including the World Bank's—make the assumption that nations' fiscal balances are fixed—in other words, any losses in tariff revenue are offset by lump-sum taxes. In the real world, however, such taxation schemes are difficult to pass and face stiff resistance.[ix] Total tariff losses for developing countries under non-agricultural market access, WTO-lingo for manufactured goods, could be $63.4 billion, or almost four times the level of benefits.[x] As most developing countries rely on tariffs for more than one quarter of their tax revenue, consequences can be drastic, both for anti-poverty as well as industrialization programs. Much discussed "Aid-for-trade" programs are supposed to be stepped up in order to enable adjustment. The risk of limiting policy space and increasing aid dependency, however, appears to outweigh any potential benefits.

Although net benefits for many countries are projected to be positive, they would result from significant structural changes *away* from knowledge-based assets and back toward primary commodities and low-technology manufacturing. Primary commodities are experiencing a temporary upswing in prices, but the long-term trends are not encouraging. According to the Food and Agriculture Organization, the price of non-energy commodities have declined by 30 percent between 1980 and 2005, and they are likely to continue to do so in the future. What's more, the terms of trade—the average prices of agricultural commodities sold by developing countries relative to the price of manufactured goods purchased from developed countries—have fallen by close to 70 percent during the period between 1961 to 2001.[xi]

When commodity prices go down again, there may not be much industry left to pick up the slack since almost all of the projected employment increases would be in the agriculture or apparel industries. Hard-hit would be manufacturing industries such as machinery, non-ferrous metals, electronics, and motor vehicles. For Brazil and Argentina, this would translate into job losses in cities and expansion in the countryside. In Asia, there would be a movement of people out of higher technology manufacturing and into apparel jobs. Both adjustments underscore the slide in wages and level of technological sophistication that would occur under a liberalization scenario that does not devote significant attention to paying adjustment costs.

To put development back into the Doha Round the following five steps will be essential:

1. The United States and Europe should agree to honor WTO rulings that have deemed their subsidies for cotton and sugar to be in violation of existing trade rules that forbid exporting products at prices lower than what it cost to make them. This would give a tangible boost to farmers in West Africa and Latin America and send a strong signal to developing countries that developed nations are willing to honor the rules of the WTO.

2. Western nations should take commodities issues seriously. The proposal by many African nations to tame global businesses that demand unfair prices for resources used in farm production and reap billions in profits on the sale of final products. African nations made numerous proposals during the round to this end, specifically to make room for international supply management schemes to raise prices and to curb the oligopolistic behavior of large foreign commodity firms but were ignored by the developed nations.

3. Negotiators should recognize the long-standing WTO principle of "special and differentiated treatment" for poorer nations. Developed nations should roll back patent laws that impede poorer nations from manufacturing cheaper generic drugs, and they should allow poorer countries to exempt staples of their local economy such as corn, rice and wheat from deregulation.[xii]

4. International financial institutions should fund adjustment. For the measures that are agreed upon, international institutions such as the International Monetary Fund (IMF) and World Bank should step in and help developing nations cover the costs of adjustment such as tariff losses and job retraining until the proper policies can be put in place on the ground. The IMF's Trade Integration Mechanism is already in place for such a task but is not ambitious enough and should not come with additional conditionality. The IMF plan also leaves little room for incorporating costs of adjustment and the Fund is often criticized for tying further reforms to their policies.[xiii]

5. There should be a moratorium on regional and bilateral trade deals. These deals exploit the asymmetric nature of bargaining power between developed and developing nations, divert trade away from nations with true comparative advantage, and curtail the ability of developing countries to deploy effective policies for development.

Kevin P. Gallagher is an assistant professor of international relations at Boston University and Senior Researcher at the Global Development and Environment Institute, Tufts University. He is the co-author of the recent book The Enclave Economy: Foreign Investment and Sustainable Development in Mexico's Silicon Valley, editor of Putting Development First: The Importance of Policy Space in the WTO and IFIs, and author of Free Trade and the Environment: Mexico, NAFTA, and Beyond.

i "A Doha Scorecard: Will Rich Countries Once Again Leave Developing Countries as Beggars at the Feast?" Speech by Eveline Herfkens, Cancun 2003.
ii All projections of the benefits of the Doha Round in this paper are from the following: Kym Anderson and William Martin, eds., Agriculture Trade Reform and the Doha Development Agenda (Washington DC: World Bank, 2005), Tables 10, 12.14; Kym Anderson, William Martin, and Dominique van der Mensbrugghe, "Global Impacts of the Doha Scenarios on Poverty," in T. W. Hertel and L. A. Winters, eds., Putting Development Back into the Doha Agenda: Poverty Impacts of a WTO Agreement (Washington DC: World Bank, 2005), Chapter 17. For a critical review of these estimates see Frank Ackerman, "The Shrinking Gains from Trade: A Critical Assessment of the Doha Projections" (Working Paper 05-06 Global Development and Environment Institute, Tufts University, Medford, 2005).
iii The changes in estimates from 2003 to 2005 are due the fact that much trade liberalization has occurred since the last time estimates were generated. Specifically, the World Bank updated their "base year" from 1997 to 2001, bringing China's accession to the WTO, the European Union's expansion and the expiration of the Multi-Fiber Agreement into the picture.
iv The "likely" scenario, according to these models, involves agricultural tariff rate reductions in developed countries of 45, 70, and 75 percent within three bands of existing tariffs, and reductions in developing countries of 35, 40, 50, and 60 percent within four bands of tariffs. The least developed countries are not required to make any reductions in agricultural tariffs. For nonagricultural tariff bindings the scenario calls for 50 percent cuts in developed countries, 33 percent in developing countries, and zero in the least developed countries.
v New research by the Carnegie Endowment for International Peace using similar modeling exercises puts the potential gains to developing countries at $21.5 billion. See Sandra Polaski, "Winners and Losers: Impact of the Doha Round on Developing Countries" (Washington, DC: Carnegie Endowment for International Peace, 2006), Figures 3.1-3.8.
vi Kym Anderson, William Martin, and Dominique van der Mensbrugghe, "Global Impacts of the Doha Scenarios on Poverty," in T. W. Hertel and L. A. Winters, eds., Putting Development Back into the Doha Agenda: Poverty Impacts of a WTO Agreement (Washington DC: World Bank, 2005), Chapter 17.
vii The World Bank also put together models for services trade benefits but ended up deeming them too "highly speculative" to publish in their Doha Round publications. See Hertel, T.W. and R Kenney (2005). "What's at Stake? The Relative Importance of Import Barriers, Export Subsidies and Domestic Support." Kym Anderson and William Martin, eds., Agriculture Trade Reform and the Doha Development Agenda (Washington DC: World Bank). Not only is trade in services difficult to quantify, but the benefits of removing trade barriers have to be extrapolated for modeling purposes, since "tariffs" in the sector do not exist. "Barriers" to cross-border exchange reside more in the form of domestic investment rules and restrictions on entry into markets in a nation's service sector. For estimates of services benefits, see Joseph Francois, Hans van Meijl, and Frank van Tongeren, "Trade Liberalization and Developing Countries Under the Doha Round" (Tinbergen Institute Discussion Paper 2003-060/2 Rotterdam and Amsterdam: Tinbergen Institute, 2003), Table 4.4.
viii See Ackerman (2005), cited in footnote 2, and Taylor, L. and R. von Arnim (2006), "Modelling the Impact of Trade Liberalisation: A Critique of Computable General Equilibrium Models," Oxfam International Research Report, for a comprehensive critique of such modeling strategies. (a) refers to the assumption of full employment, (b) to unusually high trade elasticities assumed in "standard" and World Bank trade model simulations, and (c) to the assumption of fixed budget deficits discussed further below.
ix For example, Mexico was not able to pass a tax increase during the entire six-year term of President Vicente Fox.
x "Likely" benefits from Anderson (2005). Tariff losses from Santiago Fernandez De Cordoba and David Vanzetti, "Now What? Searching for a Solution in WTO Industrial Tariff Negotiations," in Coping with Trade Reforms, ed. Sam Laird and Santiago Fernandez De Cordoba (Hampshire: Pagrave MacMillian, 2006), Table 11.
xi Food and Agriculture Organization, The State of Agricultural Commodities Markets 2004 (Rome, FAO, 2004), 75; World Bank, "Primary Commodity Prices" in the 2006 World Development Indicators, http://devdata.worldbank.org/wdi2006/contents/Section6.htm, Table 6.5.
xii Gibbon, Peter. (2007), "Africa, Tropical Commodity Policy and the WTO Doha Round," Development Policy Review, 25(1), 43-70.
xiii See for example Joseph Stiglitz , Globalization and Its Discontents (New York: Norton, 2002).