The Right to Trade

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Stiglitz helped create a new branch of economics, 'The Economics of Information', exploring the consequences of information asymmetries and pioneering such pivotal concepts as adverse selection and moral hazard. His work has helped explain the circumstances in which markets do not work well, and how selective government intervention can improve their performance.

At Columbia, Stiglitz co-chairs the Committee on Global Thought and is co-founder and co-president of the Initiative for Policy Dialogue. He is also president of the International Economic Association, co-chair of the Commission on the Measurement of Economic Performance and Social Progress and chair of the Commission of Experts of the President of the United Nations General Assembly on Reforms of the International Monetary and Financial System.

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Contents

Abbreviations and acronyms

AGOA	African Growth and Opportunity Act
EBA	Everything but Arms
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNI	gross national income
GTF	Global Trade Facility
IFIs	international financial institutions
LDC	least-developed country
NGO	non-governmental organisation
ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
TRIPS	Trade Related Aspects of Intellectual Property Rights
UNCTAD	UN Conference on Trade and Development
WTO	World Trade Organization

Summary

The link between aid and trade has been an important nexus in the global development framework since the World Trade Organization (WTO) launched its 'aid for trade' initiative at the 2005 Ministerial in Hong Kong.

Proponents of aid for trade declared at the time that its purpose was to recognise the disadvantage of developing countries participating in the global trading system, and to bolster the effectiveness of aid disbursements.

Yet aid for trade was also a creature of pragmatic politics. The trade community was motivated to give alms to the poor countries, which felt duped by the undelivered promises of the Doha Development Agenda. After the walkout in Cancun, aid for trade was a libation intended to induce developing countries back to the negotiating table. At the same time, the aid community was seeking a bulwark against growing criticism that development assistance was ineffective. By linking development aid with trade outcomes, donors and recipients could point to long-term poverty-reduction impacts of their projects.

Seven years later, aid for trade has become a fixture in the development landscape, accounting for no less than 25 per cent of total official development aid (ODA) (OECD and WTO 2011). Aid for trade is being positioned as a building block in the future development agenda beyond the 2015 expiry of the Millennium Development Goals.

This book analyses whether aid for trade has delivered on its promise. Has it delivered incremental resources to developing countries? Has it been a complement to pro-development liberalisation, unlocking genuine progress in multilateral trade reform? And has the focus on trade made aid more effective? As we show, considerable doubt remains on each of these questions. The aid for trade initiative may well be primarily a reallocation rather than an increase in assistance, and constitute a relabelling rather than a fundamental reform of the global trade and development framework.

This book also considers alternative means to improve trade outcomes for developing countries. We propose that a 'right to trade' and a 'right to development' be enshrined within the WTO's dispute settlement system. These rights would give developing countries increased opportunity within current and future trade agreements to expand their trade and safeguard their development.

In addition, we propose that aid for trade funds should be consolidated into a more coherent and predictable framework. Dedicated funds should be committed by rich countries to a Global Trade Facility and dispersed through a transparent and competitive process.

Together these proposals would go some way to creating a genuinely pro-development trade liberalisation agenda, giving developing countries greater scope to eliminate the international trade barriers and domestic capacity constraints that limit their ability to pursue export-led development pathways.

Chapter 1

Introduction

The World Trade Organization's 'aid for trade' initiative was launched at the 2005 Ministerial in Hong Kong to recognise the disadvantage of developing countries participating in the global trading system, and bolster the development dividend of the flailing Doha Round. Seven years since the birth of the aid for trade initiative, huge resources have been mobilised. Fully 25 per cent of total ODA is now channelled, or at least labelled, as aid for trade (OECD and WTO 2011). Yet questions remain as to whether the coming together of aid and trade has delivered on the promise of additional resources for developing countries. If aid for trade has not been truly incremental to existing aid commitments, there is the further question: has the changed focus made aid more or less effective, resulting in stronger growth or reduced poverty?

Perhaps the greater concern is that aid for trade was initially offered as a complement to additional market access to be provided through the Doha Development Agenda – it was supposed to enhance, rather than replace, pro-development liberalisation on the part of the advanced countries. Unfortunately, as advanced countries' commitment to Doha has faded, aid for trade is beginning to seem more like a pecuniary payoff for undelivered promises.

This book outlines an alternative path for aid for trade as part of a pro-development, multilateral liberalisation agenda. First, the World Trade Organization would enshrine a 'right to trade' and a 'right to development' operational within the dispute settlement system. This right would give developing countries legal recourse against advanced countries whose policies materially impact the development of poor countries by restricting their ability to trade. Second, dedicated funds committed by rich countries to a Global Trade Facility would be administered by the UN Conference on Trade and Development (UNCTAD) and dispersed through a transparent and competitive process based on need and impact.

Chapter 2

From 'Trade Not Aid' to 'Aid for Trade'

The institutions of the modern multilateral trading system were established at a time of relative, albeit far from uniform, consensus about the relationship between trade liberalisation and development. Tariff reduction was widely understood to have a clear and positive effect on trade flows. Trade flows were deemed to be positively associated with economic growth. And trade-induced growth was believed to enhance general welfare. Armed with these supposed certainties, developed and developing countries were emboldened to embrace the liberalisation of global trade. The Uruguay Round was struck and the World Trade Organization was born.

The Uruguay Round was by far the most ambitious trade liberalisation in history. After effectively sitting out the first four decades of multilateral trade negotiations, developing countries' participation in the Uruguay Round led them to accept substantial liberalisation of their trade regimes. It covered tariff and non-tariff barriers in industrial and agricultural goods and extended multilateral rules to new areas, including services and intellectual property. International organisations including the World Bank and the Organisation for Economic Co-operation and Development (OECD) strongly supported the round. They published estimates of large projected welfare gains in the order of US$200–US$500 billion per year. A large share of these gains, it was argued, would accrue to the poorest countries and, on that basis, the international financial institutions (IFIs) urged developing countries to sign up.[1]

Almost as soon as the ink dried on the Uruguay deal, it became clear that the agreement was unbalanced. The final terms reflected, in large part, the priorities of the advanced countries. Market access gains were concentrated in areas of interest to developed countries including services, intellectual property and advanced manufacturing. Far less progress was made in areas of interest to the poor countries such as agriculture (including subsidies to agriculture) and textiles. The effect was to concentrate tariff reductions on products exported by the rich countries. Laird (2002) estimated that after the implementation of the Uruguay Round Commitments, the average OECD tariff

on imports from developing countries was four times higher than on imports originating in the OECD.[2] Developed countries had also maintained non-tariff barriers and other protectionism including agricultural subsidies and phytosanitary conditions, which effectively limited the competitiveness of farmers and some other producers in poor countries.[3]

Even where the exchange of market access had been *de jure* reciprocal, it was *de facto* unbalanced. Exporters in rich countries were able to quickly take advantage of greater market access, but the poor countries found their ability to export to rich countries was limited by a range of constraints including non-tariff barriers, weak infrastructure and supply constraints.

To make the 'Uruguay hangover' worse for developing countries, they rapidly realised that as well as receiving only a small share of the gains from the Uruguay Round,[4] they were now subject to a remarkable range of additional obligations and responsibilities. Finger and Schuler (2000) estimated the implementation costs of just three areas (customs valuation, Trade Related Aspects of Intellectual Property Rights [TRIPS] and sanitary/phytosanitary measures) would cost each developing country around US$150 million – a huge sum for many least-developed countries. Overall the agreement was not only unbalanced, it was unjust. Some estimates suggested the 48 least-developed countries had actually lost a total of US$600 million a year as a result of the Uruguay Round (around 5 per cent of their gross domestic product [GDP]).

There was increasing concern too about the high developmental and health costs of some of the obligations undertaken under the Uruguay Round and the Financial Services Agreement. For instance, access to lifesaving generic medicines was restricted; countries' health budgets were hit badly and/or access to life-saving medicines was diminished; and newly flourishing generic drug companies in developing countries saw their prospects wane. Local financial firms found it difficult to compete with large multinationals, and local small businesses often seemed unable to gain access to credit from these multinationals. A growing body of literature suggested that financial market liberalisation (as pushed by the Financial Services Agreement) did not promote growth, but did enhance instability (Detragiache et al. 2008).

Even after the results of the Uruguay Round were clear, the international financial institutions continued to advise the developing countries that liberalisation was in their best interests. Developing countries were encouraged to address their concerns

through a fresh round of liberalisation. The acting European Trade Commissioner, Sir Leon Brittan, said 'the only way to address the issue is through a new round of negotiations. Indeed, I would ask all WTO members, including developing countries, whether they are entirely happy with the present trading system. If the answer is no, it is clear that the only way of improving upon that system is in a new round' (see Stiglitz and Charlton 2005: 39, and the references cited there). The answer to the problems of liberalisation was more liberalisation. But developing countries' experiences had made them wary of a repeat of the unfairness of Uruguay. Fresh from what they felt was a betrayal,[5] developing countries were cautious about signing up to another round. The first attempt to establish a new round of trade talks in 1999 in Seattle was a debacle. Sceptical developing countries torpedoed the meeting. Outside on the streets some 40,000 people protested the injustices of the global trading system.[6]

To restart trade talks, in 2001 at Doha the advanced countries made a string of promises to put the poor at the centre of the new round – even naming the talks the Doha Development Agenda. The Ministerial Declaration acknowledged the unfairness of the past and promised to 'place (the developing countries') needs and interests at the heart of the work program' for the new round. These assurances soothed the concerns of many developing countries. Ever hopeful, they signed up to a new round.

The goodwill lasted less than two years.[7] When developing countries walked out of the 2003 meeting in Cancun, the Doha Round stumbled into a deadlock from which it never recovered. By July 2005, the negotiations had reached an impasse. Recognising the crisis, WTO Director-General, Pascal Lamy, made a decision to suspend negotiations. The stalling of the Doha Round and the implacable sense that the world trading system was manifestly unfair to developing countries led the WTO, its members and civil society to search for alternative avenues to promote trade, bring development closer to the centre of the WTO's work programme and mollify the concerns of developing countries. In this context, aid for trade – an obvious carrot for the developing countries – was an idea whose time had come.

2.1 Questioning the benefits of liberalisation

At the same time that developing countries began to fear that the trading system was unbalanced, they also began to more critically question the benefits of trade liberalisation. This provided a second impetus for aid for trade.

The welfare impacts of free trade were formalised in modern economics by Paul Samuelson (1938).[8] However, the underlying assumptions that yield this conclusion are highly restrictive and often fail to reflect many of the relevant characteristics of developing economies.[9] Moreover, neither Samuelson nor subsequent analyses provided a strong analytic basis for the notion that trade liberalisation would lead either to stronger development or faster growth. Nonetheless during the 1980s, neoliberal policy prescriptions based on the positive welfare impacts of trade liberalisation gained support among the international financial institutions.

Import substitution policies and managed trading regimes fell out of favour and developing countries were encouraged to rely more on market mechanisms.[10] Developing countries were told they must reduce their own tariffs if they were to reap the benefits of engagement in the global economy. Influenced by advice from the international financial institutions and cajoled by aid conditionality, whereby aid was extended on the condition of trade liberalisation, many developing countries shifted their strategy to participate more actively with the WTO.

In the last decade, there has been a significant reappraisal of the Washington consensus, and especially the relationship between trade liberalisation and economic development (Chang 2002). Although some research in the 1990s appeared to confirm that trade liberalisation promoted economic growth, several subsequent studies cast doubt on these results on the basis that the key 'openness' variables employed in earlier empirical studies poorly reflected trade liberalisation (Rodriguez and Rodrik 2000). Recently, successive studies have emphasised the heterogeneity in developing countries' experience with liberalisation and economic growth. For instance, Wacziarg and Welch (2008) found that roughly half of the countries in their survey experienced zero or even negative changes in growth post-liberalisation. Other studies have questioned the direction of causation – it may be possible that rather than being caused by liberalisation, successful development leads to integration into the global economy.[11] Estevadeordal and Taylor (2008) agree that most of the prior literature is weak, but find some support for positive effects on growth of liberalising intermediate goods and imported capital tariffs.

While there remains controversy about the relationship between trade liberalisation and growth, what is clear is that the simple and clear link asserted by liberalisation advocates has not been verified by the data. It may be that under certain circumstances

(for instance, when the economy is fully employed and when financial markets work well – circumstances applicable in few least developing countries) trade liberalisation, at least of intermediate goods, could enhance growth. Trade liberalisation might lead to growth when accompanied by certain other policies. However, trade liberalisation, as practiced, has often had adverse effects on growth, for reasons that are explained shortly below.

If there are strong doubts about the relationship between trade liberalisation and growth,[12] there is even less consensus on the causal link between liberalisation and poverty. The evidence is at best weak (see: Bannister and Thugge 2001; Winters et al. 2004) with many studies finding that trade liberalisation, even when it is associated with economic growth, also leads to an increase in inequality (World Bank 2005; Topalova 2010).

Earlier theoretical literature had explained why results suggesting that trade liberalisation might not lead to an increase in well-being should not have come as a surprise. Dasgupta and Stiglitz (1977) and Newbery and Stiglitz (1984) had noted that trade liberalisation increased risk, so much so that everyone could be worse off. These concerns were especially relevant in developing countries, where risk markets were imperfect. Second, the process of adjustment to liberalisation was costly. Neoclassical theory (upon which most of the pro-liberalisation analyses were based) simply presumed that workers would move from inefficient protected sectors to efficient unprotected sectors, without cost. What often happened in reality was that they moved from inefficient protected sectors into unemployment. Output decreased rather than increased. It should have been obvious that the neoclassical model did not describe economies in which there were, even before liberalisation, high levels of unemployment. In these cases, trade liberalisation simply added to the ranks of the unemployed. Again, this was a concern especially in developing countries, where financial markets often didn't work well and where there was a scarcity of entrepreneurship. It was harder to create new jobs than to destroy old jobs. Moreover, trade liberalisation took away one of the most important sources of government revenue. Most countries found it difficult to replace tariffs, say with a value-added tax (VAT) (Aizenman and Jinjarak 2009). The constraints in government revenues forced cutbacks in investments in education and infrastructure, thereby impairing development.

At first, the impacts on inequality came as a surprise, since the conventional model (the Samuelson-Stolper theorem)[13] predicted an increase in unskilled wages in developing countries.

However, three factors contributed to the increase in inequality typically associated with liberalisation:

i As we have already noted, it often was done in a way that resulted in increased unemployment. This had adverse effects directly on poverty and inequality (in particular, since it is typically those at the bottom who suffer the most from unemployment [Furman and Stiglitz 1998]). But it also has an indirect effect: higher unemployment puts downward pressure on wages.

ii. Liberalisation was often asymmetric, with capital and goods liberalisation outpacing labour market liberalisation.[14] This adversely affected workers' bargaining position, and put pressure on governments to cut taxes on capital and, correspondingly, programmes for those who were less mobile – unskilled workers. Thus before taxes and transfers, income became more unequal, and after taxes and transfers it was even worse.

iii. The unskilled didn't benefit from the creation of new export jobs, and they were often in agriculture, which could be hurt by subsidised agriculture exports from developed countries.[15]

The reappraisal of the main tenets of the Washington consensus in economic literature was an inevitable consequence of the mixed experience among the developing countries that had embraced trade liberalisation. Many countries that had, according to the neoliberal prescription, done the 'right things' (that is, not only had liberalised, but followed other policy dictates of the Washington-based international institutions) subsequently stagnated. And many countries that had not followed the Washington consensus had achieved considerable success. Rodrik (2001) argued that the three primary models of successful development in the twentieth century all relied on managed trade regimes: import substitution, as practised by a number of countries in the 1960s; outward-orientated industrialisation, as practiced in East Asia in the 1980s; and the state-directed capitalism of China in the 1990s. Chang (2002) showed that almost all of today's rich countries used tariff protection and subsidies to develop their industries, and 'Britain and the USA, the two countries that are supposed to have reached the summit of the world economy through their free-market, free-trade policy, are actually the ones that had most aggressively used protection and subsidies'.[16]

The ultimate refutation of the trade-not-aid mentality came with the introduction of highly favourable market access preferences for least-developed countries, including the EU's Everything but Arms initiative (EBA) and the United States' African Growth and Opportunity Act (AGOA). These initiatives, though a positive and important step, have had limited impact on beneficiary countries' exports. Sub-Saharan Africa's share of world exports decreased dramatically between 1980 and 2006, falling from 3.9 per cent to 1.9 per cent. African least-developed countries (LDCs) did even worse, seeing their average share fall from 0.06 per cent to 0.02 per cent over the same period. Multilateral tariffs, it turned out, were not the binding constraint on the ability of these countries to trade. Their capacity to export was hindered by a range of non-tariff trade costs and barriers, as well as supply constraints.

These three factors – the historical unfairness of previous trade agreements; the high adjustment costs and disappointing results from trade liberalisation; and the broader reappraisal of the relationship between trade, trade liberalisation and development – changed developing countries' approach to multilateral trade liberalisation and their engagement with the WTO. If the gains from trade were not automatic, as the Washington consensus had implied, and the relationships were complex and contingent and the outcomes were heterogeneous, developing countries would (and should) be significantly less sanguine about further trade liberalisation.

At the 2003 WTO meeting in Cancun, UNCTAD Secretary-General, Rubens Ricupero, spoke for many when he acknowledged the shifting mood: 'Trade liberalization is no panacea for developing countries. For many of them, it involves considerable adjustment and social costs. There is a need for synergy and proper sequencing – between the capacities of the developing countries, the level of obligations they are to take on, the cost of implementation, and the adequacy of financial and technical resources available to them' (Ricupero 2003: 3).

2.2 Birth of aid for trade

Aid for trade was born in this context. Once the developing countries began to lose faith in the prospects for multilateral liberalisation, the rich countries had to put something else on the table. Aid for trade was a salvo. Some saw it as a recognition that previous agreements had been unfair, others said it was recognition that developing countries faced adjustment costs

associated with trade liberalisation, others still saw it as a means to increase the benefits of market access. It was all of these things, but the fundamental driver of the aid for trade initiative was that the trading system was in crisis. If the developing countries walked away from the round, the WTO's agenda for expanding trade would grind to a halt.

In early 2005 at the International Monetary Fund (IMF)–World Bank spring meeting, the Development Committee put aid for trade firmly on its agenda and resolved 'to work with others to develop proposals to help developing countries adjust to and take advantage of the round, for consideration by our next meeting' (International Monetary Fund and World Bank 2005: 2). A few weeks later at the Gleneagles G8 meeting in May, Heads of Government committed 'to increase our help to developing countries to build the physical, human and institutional capacity to trade, including trade facilitation measures',[17] and called 'on the IFIs to submit proposals to the annual meetings for additional assistance to countries to develop their capacity to trade and ease adjustment in their economies'.[18]

By late 2005 the WTO had rallied behind the proposal. At the WTO Ministerial Conference in Hong Kong in December 2005, the 'Aid for Trade Initiative' was officially launched. The Hong Kong Ministerial Declaration reflected the interests and objectives of both the WTO and donors: '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'.[19] Shortly thereafter, aid for trade moved toward the centre of the WTO's work programme. Director-General, Pascal Lamy, said in 2006: 'We cannot ignore the costs of adjustment, particularly for the developing countries, and the problems that can arise with the opening up of markets. These adjustments must not be relegated to the future: they must be an integral part of the opening-up agenda. We must create a new "Geneva consensus": a new basis for the opening up of trade that takes into account the resultant cost of adjustment' (Lamy 2006).

It is noteworthy that Lamy emphasised only the adjustment costs. The term 'adjustment costs' suggested that the costs were a short-term problem: they didn't recognise that trade liberalisation might actually impede longer-term development. Advocates of trade liberalisation never fully understood that even in equilibrium, trade liberalisation might have adverse effects, and especially so if it was pursued in an asymmetric way.

Yet even if liberalisation did not have these adverse effects, and even if the multilateral trade agreements (the Uruguay Round in particular) had been 'fairer', there would be a need for aid for trade. Symmetric agreements can have asymmetric effects, as we have already noted, because of the asymmetries of different countries. (That was part of the rationale for special and differential treatment.) Market failures are especially pervasive in developing countries and there is, accordingly, need for government interventions. Trade requires resources – infrastructure and finance – that developing countries often cannot provide on their own. Aid for trade can be seen in part as filling in these lacunae.[20]

2.3 Questioning the effectiveness of aid

Aid for trade was born at least in part as a result of a crisis in the global trading system. But it would not have got off the ground with the support of the trade community alone. Aid for trade received additional impetus from the aid and development communities, which were faced with a parallel series of challenges to significantly scale-up disbursements and to demonstrate the effectiveness of development programmes. At the United Nations Millennium Summit in 2000, world leaders came together around eight goals for the poorest countries, which came to be referred to as the Millennium Development Goals. Two years later at the financing for development conference at Monterrey in Mexico, leaders recognised 'dramatic shortfalls in resources required' to achieve these goals.[21] In subsequent years, major advanced economies made significant commitments to increase their aid budgets. Several major countries committed to a collective foreign aid target of 0.7 per cent of Gross National Product (GNP) by 2015, these targets have not for the most part been reached.[22]

At the same time the aid community faced a challenge to its legitimacy from those who questioned the benefits of aid. In the last two decades, researchers have scrutinised the conditions under which aid is effective. William Easterly argued that the US$568 billion spent on aid to Africa over the last 40 years has not lifted average African incomes.[23] Other recent cross-country analyses also conclude that the relationship between aid and development is weak and often ambiguous (Rajan and Subramanian 2008; Easterly et al. 2003; Hubbard and Duggan 2009). Clemens et al. (2012: 590) do find that it is 'plausible […] that aid causes some degree of growth in recipient countries, although the magnitude of this relationship is modest, varies

greatly across recipients and diminishes at high levels of aid'. In a recent meta-analysis of the literature, Doucouliagos and Paldam (2011) conclude that the overall finding on 'aid ineffectiveness' has not been overturned, though there are some results suggesting certain components of aid *may* be effective.

It is perhaps not surprising that the links between aid and development are often difficult to discern. Aid has frequently been provided for with non-economic objectives, such as emergency assistance following disaster relief, or for political or geostrategic reasons. During the Cold War, billions of dollars of aid supported corrupt and tyrannical dictators such as Joseph Mobutu of Zaire (now the Democratic Republic of the Congo) and Jean-Bédel Bokassa of the Central African Republic. Many well-intentioned aid projects were rendered ineffective through poor conception and execution, or fettered by tenuous and sometimes counterproductive conditionality. In other cases, aid may have had a negative effect on growth through 'Dutch Disease' effects – where inflows of capital reduce the competitiveness of the export sector through the appreciation of exchange rates.

Moreover, because the effects of aid (such as education) often take years to be realised, it is hard to assess with contemporaneous data the effects of aid. More generally, the cross-section 'aid and growth' literature is bedevilled by all the econometric problems associated with the 'trade and growth' literature, to which we referred earlier. The effectiveness of aid clearly depended on circumstances.[24]

Critiques of the impact of aid have become more vociferous as the global campaigns to increase aid have gained momentum. Policy-makers and researchers have responded, both in a commitment to make aid more effective and in analyses to enhance understanding of what is required to do so. At Monterrey donors wanted to know that aid would be used as effectively as possible before they agreed to increase their ODA budgets.

In 2003 aid officials and representatives met in Rome for the High-Level Forum on Harmonization, where donor agencies committed to work with developing countries to better co-ordinate their activities. Two years later, the Paris Declaration on Aid Effectiveness was endorsed – a comprehensive attempt to establish principles to improve the effectiveness of aid.

Aid for trade has been a beneficiary of these trends. It has been presented as an effective channel through which significantly increased aid can be disbursed. At the same time linking aid to trade has enabled the development community to point to

longer-term impacts of assistance programmes on growth and economic development.[25] This became especially relevant as many in the development community shifted attention away from just poverty to growth, in the belief that it was only or mainly through growth that there would be long-term, sustainable reductions in poverty.

Moreover, if aid for trade did enhance trade, then a stronger case could be made that it was in the self-interest of the developed countries to provide such assistance. Exporters in developed countries knew that their exports could only increase with the enhanced trading capacity of developing countries.[26]

Chapter 3

Has Bringing Aid and Trade Together Helped?

The concurrent challenges facing the aid and trade communities led to a marriage of convenience from which aid for trade ensued. As the development promises of the Doha Round crumbled, the trade community had an urgent need to mollify developing countries by demonstrating a tangible development agenda. At the same time, the aid community of multilateral institutions, bilateral donors and non-governmental organisations (NGOs) were caught between the challenge to ramp up their disbursements to absorb growing national ODA commitments and increasingly strident critiques of the effectiveness of existing aid programmes. 'Aid for trade' enabled the trade and aid communities to leverage one another. The World Trade Organization could point to significant development-focused activity. The aid community accessed an expanded mandate to invest growing aid resources in productive capacity.

That aid for trade was an expedient product of circumstance is neither especially surprising, nor necessarily concerning – many positive initiatives have been born of pragmatism. As we wrote (Stiglitz and Charlton 2006), aid for trade had the potential to complement trade liberalisation and increase the ability of developing countries to take advantage of market access opportunities delivered through multilateral trade negotiations.

Yet from the start there were immediate fears that aid for trade was merely a semantic façade. After all, the concept of aid programmes focused on trade was not new. The International Trade Information Centre was established in 1964 under the General Agreement on Tariffs and Trade (GATT) to provide trade-related assistance. In the post-Uruguay era, trade-related assistance was stepped up through the Integrated Framework (IF) for Trade-Related Technical Assistance to Least-Developed Countries established in 1997 and the Joint Integrated Technical Assistance Program (JITAP) for Africa established in 1998. More broadly, to the extent that aid for trade covers wider assistance to developing countries to develop their supply-side capacity, much development aid over the last 20 years – including assistance in developing infrastructure and institutions and other support for integration into the global economy – has been trade-related.

Simply renaming this assistance 'aid for trade' would not deliver incremental benefit.[27] There were many warnings at the time of the launch of aid for trade that it would only be beneficial if it was additional, predictable and responsive to the needs of recipient countries (including the private sector), and increased the coherence of poverty-reduction assistance. Without these qualities, aid for trade would be little more than a repackaging of existing commitments – another *legerdemain* on the part of the rich countries.

Evaluating the impact of aid for trade involves two questions. First, have aid for trade projects been effective at promoting trade and development? This is the question that most of the analysis of aid for trade has focused on, and is relevant to the design and delivery of aid programmes. But this question goes to whether aid for trade is a good way to deploy bilateral development assistance, not whether it is the best way. The second question poses a tougher test: has the emergence of aid for trade increased the overall effectiveness of global aid programmes? This question incorporates issues of additionality and opportunity costs in overall development assistance.

3.1 Have aid for trade programmes helped to promote trade and development?

One would have hoped that aid for trade would have begun with an analysis of the major impediments facing developing countries with respect to trade, and then systematically gone about reducing those impediments. That kind of systematic analysis has not, for the most part, occurred. Had it occurred, it would have been realised that there are policies (such as escalating tariffs [see Stiglitz and Charlton 2005] of the advanced industrial countries) that impede developing countries' trade and development and which could be easily altered, in some cases with net positive benefits to the developed countries. It would have been realised too that the absence of small business finance has been a major supply constraint, and again there are low-cost policies and programmes that might have facilitated the flow of credit to local small enterprises.[28] Finally, a major barrier to trade (supply constraint) is lack of infrastructure.

Nonetheless, we believe that trade-related programmes funded by bilateral donors *can* be effective. Indeed it is possible that aid for trade, by being more focused on removing supply constraints on trade, could have leveraged effects on growth.[29] Several studies have demonstrated that aid spent on promoting trade is positively associated with global trade, particularly in poor

countries with weak infrastructure (Portugal-Perez and Wilson 2012).

Trade facilitation projects in particular have demonstrated considerable benefits. Trade facilitation covers a range of behind-the-border actions including institutional and regulatory reform, infrastructure, and customs and port efficiency. The total value of trade facilitation funding has increased considerably in recent years. Funding by the World Bank has risen five-fold in the last seven years and trade facilitation projects make up around half of all trade-related development assistance. Helble, Mann and Wilson (2011) used 16 years of trade and aid data for 40 donor countries to analyse the impact of trade facilitation on trade. Their results suggest that a 1 per cent increase in aid for trade facilitation is associated with about US$290 million of additional exports from the recipient countries.

3.2 Has the emergence of aid for trade increased the overall effectiveness of aid?

The key problem in evaluating the 'aid for trade initiative' is that it is difficult to ascertain the counterfactual, i.e. what would have happened in its absence? Without evidence of additionality and a clear distinction between projects that would have occurred anyway under development programmes, it is challenging to assess whether the initiative has delivered *incremental* benefits to developing countries.

The promise of aid for trade was that it would prove to be more than new nomenclature. When UNCTAD Secretary-General, Rubens Ricupero, called for aid for trade at the 2003 Cancun WTO meeting, he specified that trade assistance must be additional, 'developing countries need aid for trade, and such aid must not come at the expense of aid for development'. The WTO Ministerial Declaration in Hong Kong also called for 'appropriate mechanisms to secure *additional* financial resources for Aid for Trade' [emphasis added] (WTO 2005).

However, in the seven years since the initiative was launched, there has been scant evidence that aid for trade has been additional. Certainly the volume of aid for trade has increased. According to the OECD and WTO's 2011 review, *Aid for Trade at a Glance*, aid for trade commitments reached US$40 billion in 2009, a 60 per cent increase over the decade. The report claims that much of this increase is incremental to regular development assistance. But these claims are not fully convincing. While the OECD and WTO have invested significant resources in

building an inventory of information on aid for trade flows, there remains no comprehensive analysis of aid for trade quality or its effectiveness (either in its direct mission of promoting trade or its more fundamental goals of promoting growth and poverty reduction) or the extent to which it represents additionality. For the most part, the measurement and evaluation framework relies on self-assessment. As donors provide their own financial and other reporting, there is little independent verification of additionality or impact.

Indeed, there is no clear framework for how additionality is measured. Many of the commitments made by governments in the last decade have been opaque and the amounts are re-announced several times in successive packages. Worse, the line between more general aid for development and aid for trade is arbitrary (how close to a port does a road need to be in order to be aid for trade?). This blurring of categories means that it is easy for donor countries to count development projects as aid for trade projects (Page 2007).

Since most countries have not reached their commitment to reach 0.7 per cent of GDP in aid, it is hard to see aid for trade as additional. It is certainly not additional to what they had previously promised to deliver.

If aid for trade is not additional to existing aid commitments, then donors must answer some fundamental questions about its purpose and utility. Development assistance reclassified as aid for trade obviously cannot fulfil the compensation motive arising from the unfairness of the Uruguay Round. And developing countries will hardly feel better about the collapse of the Doha Round knowing that assistance that they would have otherwise been receiving is now labelled aid for trade.

Assessments of the effectiveness of aid for trade have been equally problematic. External measurement of the results of aid for trade is challenging. Many projects do not have defined baselines against which impacts can be assessed.[30] There is only a weak framework to evaluate the impact of aid for trade projects and programmes on welfare, growth and inequality.

Indeed, despite evidence of success in case studies in specific areas, structural features of aid for trade as it has emerged give cause for doubts about its *overall* effectiveness. The model of bilateral disbursement (which has been de facto adopted by donor countries) has meant that aid for trade comes with all the challenges of traditional development aid. Priorities may be skewed toward the interests of preferences of donors, and there

may be limited country ownership and a range of explicit or implicit conditions.

Earlier, we argued that if aid for trade has not resulted in additional resources, then it certainly can't perform the role intended as providing partial compensation for the unbalanced nature of the trade agenda or the failure of developed countries to live up to their promises that the Doha Round would be a Development Round. Yet developing countries might be even more concerned: if aid for trade is less effective at poverty reduction than unrestrained aid, then the aid for trade movement could have been counterproductive, at least as far as that critical goal is concerned.[31] If aid for trade has not lead to more assistance, then it may create a high opportunity cost. By imposing an additional constraint on the way aid money is spent, aid for trade has the potential to have a negative impact on developing countries.

Chapter 4

A Proposal to Support Pro-development Trade Liberalisation

Aid for trade has failed to live up to its promise of additional, predictable and effective finance to support developing countries' integration into the global economy. More importantly, aid for trade may not be addressing the fundamental concerns with the global trading system and aid system that gave rise to it, and instead has become a means for both the aid and trade communities to paper over their weaknesses without doing much for the fundamental concerns of poor countries.

This book proposes a novel approach to aid for trade that would go some way to address the underlying unfairness of the global trading system and deficiencies in aid arrangements. Our proposal is to make aid and trade liberalisation work for poor countries and tied directly to specific development objectives.

4.1 The 'right to trade'

There are significant parts of industrial countries' trade policy that materially restrain the development of poor people and constrain the ability of developing countries to participate in international trade. In fact, perversely, the global trading system is still stacked against the poorest – the areas of trade where barriers are the highest (agriculture, textiles etc.) are also the areas of most importance to developing countries. As a consequence, as we have noted, the average tariff in OECD countries on imports from other OECD countries is significantly lower than imports from non-OECD countries. For example, import tax collected by the US from the imports originating in Bangladesh and Cambodia amounted to US$1 billion in 2008, which is more than the total amount collected on imports from the United Kingdom and France (Centre for Global Development 2010). In addition, it is not just the average level of tariffs that matter; it is their structure. Escalating tariffs are an impediment to development. And perhaps even more important than tariffs are the non-tariff barriers faced by developing-country exporters.[32]

Aid for trade cannot be a substitute for removing these inequities – it must be a complement rather than a replacement for fundamental change to the trading system. This was recognised

in 2005 in the Hong Kong Ministerial Declaration 'Aid for Trade cannot be a substitute for the development benefits that will result from a successful conclusion to the [Doha Development Agenda] DDA, particularly on market access. However, it can be a valuable complement to the DDA' (WTO 2005).

As the development promise of the Doha Round has faded away – only to be replaced by concerns that what remains may even have an adverse effect on some of the poorest countries – it has become clear that there is no imminent prospect of a pro-development reform to the trading system through formal rounds of multilateral liberalisation. Instead, it is imperative to install alternative mechanisms to rebalance the global trading system and make trade work for poor people. To achieve this, we propose that members of the World Trade Organization should adopt a general 'right to trade' and a 'right to development' operating within the dispute settlement body.

Article 20 of the GATT provides for certain exceptions to the applicability of trade commitments, e.g. for matters of national security, health and the environment. So too, TRIPS included a provision for compulsory licences for health – the breadth of that provision was a major subject of controversy prior to the Cancun meeting. The Shrimps-Turtle case provided an important set of exceptions in the enforcement of import restrictions (based on technology) on the basis of the environment.[33]

We have seen that trade liberalisation (especially if the rules are unbalanced and there is insufficient accompanying support) may not lead to growth; but worse, trade agreements and the obligations they impose may impair development, e.g. through the inability to develop new industries or through devastating effects on existing industries, through the inability to acquire technology and knowledge, or through impacts on public health or public budgets.

The 'right to development' would limit the applicability of WTO obligations when the enforcement of such obligations would have a significant adverse effect on development.[34]

Faizel Ismail has suggested the adoption of such a right to development for the least-developed countries:

> ….a mechanism should be established in the WTO in the course of the Doha negotiations that provides small, weak, and vulnerable economies with 'flexibility' to avoid implementation of a specific discipline, if such non-implementation is properly justified for development interests (Ismail 2006: 64).

We would argue, however, that such a right be extended not just to the most vulnerable economies, but to any of the least developed.

The 'right to development' is, in a sense, a right not to be harmed by the imposition of trade rules. It recognises that in the formulation of the trade rules, the voices and concerns of the least-developed countries were not given sufficient weight; that provisions on special and differential treatment were not adequately 'hard wired' into the international trading system; that development itself is a complex matter; and that trade ministers have neither necessarily the competence nor interests to design a global trading system that promotes development. Rather than specifying a long list of ways in which developing countries might be adversely affected, and how developed countries might offset these adverse effects (e.g. through aid for trade), it enunciates a broad *enforceable* principle, the details of which would have to be fleshed out in the WTO dispute resolution process.[35]

We argue further that if, as advocates of trade liberalisation claim, trade is good for growth and development (with its strongest advocates claiming that it is necessary and almost sufficient), then actions taken by developed countries to impede trade are, themselves, a violation of the 'right to development'. A corollary, then, of the right to development within the international trade regime is the 'right to trade'.

The right to trade would give developing countries the ability to bring an action against any advanced country where three conditions are satisfied:

i. a specific group of poor people within a developing country (or the country or group of countries as a whole) can be identified as being significantly and directly affected by a specific trade or trade-relate policy (or policies) of an advanced country;

ii. the effect of the policy acts to materially impede the economic development of those poor people (or the country or group of countries as a whole); and

iii. the impediment operates by restricting the ability of the people (or the country or group of countries as a whole) to trade, or gain the benefits of trade.

This right would enable any developing country to bring an action against an advanced country on the basis that a specific policy materially impedes the development of an identified community in a poor country by restricting its ability to trade.

4.1.1 Remedies

Subject to appropriate safeguards, this right would transcend existing agreements and apply to all trade-related policies of advanced country member states. A developing country (or countries) bringing successful actions under the right to trade could access a range of remedies:

- Elimination or change to the offending policy as a result of mediation between the advanced country and the developing country.
- A range of bilateral sanctions including an increase in tariffs against the advanced country (a remedy that would be available to all affected developing countries). This right to sanction would be tradeable (see Stiglitz and Charlton 2005). Rather than merely raise tariffs, sanctions should also be able to include suspension of other WTO commitments of interest to advanced countries, including the TRIPS agreement.
- Compensation from the offending advanced country or support from a multilateral aid for trade fund (outlined in the next section).

Any dispute between a rich and a poor country is never a fair fight. Setting aside the differences in their ability to bring suit, even when a developing country prevails, enforcement is difficult. Existing remedies under the WTO dispute settlement system suffer from a range of asymmetries, which weaken the position of poor and small countries and often make those remedies ineffective. For example, raising tariffs against the larger country can be counterproductive if the bigger country represents a large share of imports. The effect on the bigger country may be small, while the population of the small country may face higher prices on imported goods. That is why it is important that the sanctions be 'tradeable' and that they include the suspension of other WTO commitments.

4.1.2 Who can bring an action?

Poor countries may furthermore find themselves subject to coercion, as the larger countries make implied threats to reduce aid or other benefits. This will reduce the likelihood that actions will be brought, eviscerating the force of the 'right to trade'. To address this problem, we propose three alternative mechanisms:

i. Developing countries should be able to club together to impose joint sanctions, where they are mutually affected

by a developed country policy.[36] Also, developing countries should have recourse to funds (described further in the following section) to support themselves in the action and provide compensation for any reduction in aid or other losses resulting from retaliation by the developed country.

ii. Bilateral investment agreements have recognised the right of private parties to initiate actions against states, when they are harmed. The private parties that bring suit under investment agreements are corporations. The rights of poor people should be equally enshrined under the law. Indeed, the rule of law is supposed to be directed at protecting those who otherwise could not fend for themselves. Any group of poor individuals harmed by a trade policy of another country should therefore have the right to bring a case before the WTO.

iii. There should exist an office ('Defender of the Right to Trade'), potentially located within UNCTAD, that would have the right to bring suit against any country seen as violating the right to trade as defined above.

4.1.3 Breadth and specificity of the right to trade

Most advanced industrial countries have, effectively, recognised the right to trade on the part of least-developed countries. They have recognised that opening up their markets to these countries would have little impact on their own economies (indeed, to the extent that trade restrictions are distortionary, benefiting producers at the expense of consumers, overall welfare would probably increase), but could be of enormous benefit to the least-developed countries. That is why Europe adopted its EBA initiative and the US similarly passed AGOA. However, the implementation of the principle has fallen far short of the aspiration, partly as a result of non-tariff barriers (like rules of origin and phytosanitary conditions).

In a sense, the proposed right to trade does nothing more than formalise the obligations that developed countries have already broadly taken upon themselves, helping immunise trade ministries from the pressures that are brought by special interests within their own countries that would be adversely affected by such a provision.

A number of concerns have been raised about this 'right to trade'. One is the lack of specificity. What exactly is embraced within this 'right'? We are of two minds. On the one hand, specificity may help reduce trade uncertainty. Precisely defined rights give

guidance to countries concerning what is and is not allowed. On the other hand, in today's world of regulatory arbitrage, a high degree of specificity is likely to give rise to 'circumvention': attempts to devise policies that are consistent with the letter of the law (regulation), the specifics of the provision, but against its spirit. This is evidenced by the considerable ingenuity that has been exhibited in trying to circumvent existing liberalisation and anti-subsidy measures. This helps explain why in other contexts, countries have moved toward 'principles-based' regulation.[37] Both within the WTO and elsewhere, legal and regulatory systems with broadly defined rights and obligations have worked reasonably well. South Africa's constitution, for instance, includes a broad array of rights (such as the right to housing), which have proved effective in fulfilling the intention in ways consistent with the country's resources and without imposing undue uncertainty.[38]

We believe that the 'right to development' and the 'right to trade' should be enshrined at a high level of generality, partly because trade negotiators from developed countries will try to impose restrictions on its applicability that will create large 'carve outs' that will eviscerate the effect of the provision.[39]

For the least-developed countries, we believe that the 'right to trade' and 'right to development' should be enforceable within the WTO dispute resolution mechanism, partly because as we suggested the principle has already largely been accepted.

Emerging markets (middle-income countries) present a more difficult problem, as they have grown to the point where the trade restrictions that they do or could adopt can impose real costs on developed countries. Still, these countries have per capita incomes that are far below those of the more developed countries; they typically have large fractions of the population in poverty, and development and poverty eradication remain an imperative.

If the multilateral trading system is to flourish, those in these emerging market countries must see it to be not only fair, but consistent with their developmental aspirations. For these countries, a 'softer' version of the 'right to development' and 'right to trade' may be appropriate, whereby such a country (or a group of countries or groups within a country) may bring an action, asking for a declaratory judgment that the practices of a given country (or group of countries) has an adverse effect on trade or development, perhaps with a suggestion concerning alternatives that might have less adverse effects. Hopefully, such judgments would put pressure on the offending parties to change their policies or practices. At

the very least, an accumulation of such findings should spark discussion within the WTO for the need for reform of existing disciplines and rules – and aid for trade – so that the multilateral regime can be pro-development and pro-trade.

Some concern has been expressed too about the broadening of the private rights to bring action. Many look at the provisions of the bilateral investment treaties that give the right to private parties to bring actions against states as misguided; and while our proposal might be seen as counterbalancing this asymmetry, they argue that a preferred remedy is to withdraw the right of private parties to bring actions. We believe that the arguments presented here are, in fact, more compelling than in the bilateral investment agreements: as we noted, states can be put under pressure by the developed countries violating these rights not to bring action, so action will be taken in some cases only if the right is extended more broadly.

If there are worries about these rights to private action, then we suggest that such complaints be filed through the office of the Defender of the Right to Trade described earlier. Such an office would vet the claims, ensuring that only those that have a reasonable chance of success would go forward. If (and only if) private rights of action by corporations are restricted, then it might make sense to restrict the private rights to action proposed here; in which case the office of the Defender of the Right to Trade would bring suit directly.

4.2 Global Trade Facility

In addition to the right to trade, we propose the creation of a Global Trade Facility – a dedicated fund established at the global level, to which all donors would contribute resources that would be allocated to developing countries based on their needs.

This new fund would retain the concept of the Integrated Framework – where international organisations effectively co-operate on aid for trade – but concentrate its management within one institution. Dedicated funds for aid for trade should be allocated to a special facility to be administered by UNCTAD, much as the Global Environment Facility is administered by the World Bank and supported by a small secretariat operating within but independent from UNCTAD.[40]

This body would oversee the aid for trade programme, support the allocation of funds according to an agreed set of principles, create and monitor a common set of performance criteria and report on effectiveness. (The aid projects themselves would be

carried out by a variety of national and international institutions and organisations.)

This organisation would not directly manage the assistance programmes, but would allocate resources based on proposals from a wide range of development organisations, which could include multilateral institutions (including the World Bank and regional development banks), NGOs and countries themselves. (It would necessarily also have to have some responsibilities for oversight and evaluation.) This would encourage transparency, needs-based allocation and competition among aid recipients and deliverers to develop the most effective and efficient aid for trade projects and programmes.

The Global Trade Facility (GTF) would support the right to trade by providing resources to support developing countries' actions and fund genuine aid for trade – including assisting countries to maximise the benefits of new market access won through the dispute settlement system. The facility could also compensate developing countries for any losses – such as reduced aid or other retaliation[41] – associated with any right to trade dispute. It would also provide some adjustment assistance and even ongoing support to developing countries that may be negatively impacted as a result of changes to advanced countries' trade policies – for example, where a developing country was receiving preferences whose value is eroded by liberalisation.

As we have proposed (Stiglitz and Charlton 2006) the GTF should be supported by a funding commitment along the following lines:

i. The advanced industrial countries would contribute 0.05 per cent of their GDP to the GTF. This means that the aid to trade facility would comprise approximately 7 per cent of the total commitment (of 0.7 per cent of GDP) to developing countries, an amount that seems balanced within the framework of overall development needs.

ii. There would be an *additional* commitment of a small percentage of the value of the advanced countries' exports to least-developed countries. One can think of this as a partial substitution of the revenues that would have been received as tariffs; but it takes advantage of the greater administrative capacity of the developed countries, and avoids all of the distortionary and political economy 'costs' associated with tariffs. The advanced industrial countries need not actually levy the amount as a tax on exports, but simply pay the

amount (small relative to GDP of the advanced industrial countries) out of general revenues.[42]

iii. There would be an *additional* commitment of 5 per cent of all agricultural subsidies and 15 per cent of all arms sales to developing countries, partially reflecting the costs that these impose on developing countries.

These mechanisms would give aid for trade an annual flow of more than US$40 billion. This is around the quantum of ODA currently labelled aid for trade (OECD and WTO 2011). However, under the GTF framework this flow would be more secure, predictable and genuinely additional.

Chapter 5

Conclusion

Aid for trade was a pragmatic response to challenges facing the global trade and aid system. By 2005 the trade community faced pressure to increase the development focus of its agenda and provide tangible benefits to developing countries. At the same time, the aid community was looking for avenues to efficiently and effectively disburse growing aid budgets and demonstrate greater long-term impacts from funded projects. Aid for trade suited the political economy in which both groups found themselves.

Nonetheless, behind the aid for trade movement has been recognition that trade liberalisation by itself is not a sufficient condition for an increase in trade, economic development or societal welfare; and in the short run at least, trade liberalisation can have serious adverse effects on developing countries, and particular groups within those countries. There has been a significant and welcome step forward by the international community towards a greater understanding of the complex relationship between trade liberalisation and economic development in poorer countries.

However, while there is considerable promise in aid for trade, so far it has not delivered on that promise. It has not proved to be additional, predictable and effective. Indeed without additionality, aid for trade is just another form of conditionality, and may actually impair the overall effectiveness of assistance programmes. Worse still, aid for trade has become a substitute for meaningful reform of the global trading system.

The multilateral trading system is at risk. As progress on the Doha Round has slowed, with many giving up hope that it will be completed any time soon, bilateral trade agreements (including international 'partnership' agreements) have proliferated. Bilateral bargaining is even more asymmetric than multilateral bargaining, and the agreements that are emerging often reflect these asymmetries. 'Divide and conquer' has sometimes proved to be an effective strategy for the more developed countries. These bilateral agreements are replacing the multilateral system with a distortionary 'spaghetti bowl' set of trade provisions, undermining the functioning of the global market economy.[43]

The proposals we have made for a 'right to trade', a 'right to development' and a 'Global Trade Facility' would help ensure that international trade works for poor countries and the poor within those countries, and will help preserve the multilateral trading system.

Notes

1 The importance of their doing so was even then becoming increasingly obvious, as their share of global GDP was increasing. Today, it is unimaginable for there to be a global trade regime without, for instance, China.
2 Sub-Saharan Africa was estimated to have lost US$1.2 billion as a result of the Uruguay Round (UNDP 1997).
3 In some cases, setting standards has positive effects on trade, as it provides assurances of the safety of imported products. On the other hand, there are numerous instances in which phytosanitary conditions have been used to effectively bar products that were safe. In any case, the imposition of these standards may impose large costs on developing countries, in order for them to meet the standards. One of the objectives of aid for trade should be to provide the requisite assistance.
4 As we show below, many African countries (and others among the least developed) were actually worse off as a result of the Uruguay Round.
5 As Stiglitz and Charlton (2004) explain, there was an understanding that in return for giving the developed countries what they wanted – a financial services agreement and an intellectual property rights agreement – the developing countries would get what they wanted – a marked reduction in agricultural subsidies and an end to the multi-fibre agreement. The developed countries got what they wanted; the developing countries did not. As we note, many were actually worse off as a result of the agreement.
6 The protestors also included those concerned about adverse effects of trade agreements on the environment and labour rights.
7 The spirit of global co-operation that pervaded after 9/11/2001 also probably played a role in the ability to reach an agreement.
8 He did not, however, consider the effects on development, or even growth. In later work, he noted that even if both countries were in a sense better off, there were distributive consequences. There were losers as well as winners. Even if the winners could in principle compensate the losers, they seldom did.
9 In particular, he made all the assumptions of what has since come to be called the neoclassical model – perfect competition, perfect markets, perfect information, no transactions costs, no frictions – which implied, in particular, that there was no unemployment. He also ignored risk. The neoclassical model underlies much of the neoliberal policy. It is increasingly realised that what separates developed from developing countries is a disparity in knowledge, and that an essential element in development is closing the knowledge/technology gap. Thus, the neoclassical model (and neoliberal policies based on that model) assume away a central issue in development (see Greenwald and Stiglitz [forthcoming]).
10 Latin America's lost decade, the 1980s, was often blamed on its pursuit of failed import substitution policies. More recent rethinking of the lost decade (and the subsequent lost half-decade under the influence of the Washington consensus policies), has shifted the emphasis away from failed import substitution policies towards excessive debt obligations undertaken in the 1970s, and the flaws in the handling of the resulting debt crisis, both by Western creditor governments and institutions and by the developing countries (Bértola and Ocampo 2012). The World Bank, especially in the

work of its chief economist, has in recent years been actively arguing for industrial policies, some of which involve trade interventions (Lin 2012).

11 The debates continue both in the interpretation of the cross-country data, as well as the experiences of individual countries. For instance, Rodrik and Subramanian (2004) argue that India's growth dates not to the period of trade liberalisation in the early 1990s, but much earlier, to the 1980s, when it engaged in internal liberalisation, taking on a more pro-business stance.

12 That trade liberalisation *by itself* would not ensure growth should have been obvious from the large disparities that exist within developed countries: there are no trade barriers between north and south Italy (no barriers even to the movement of capital), and yet there have been persistent large differences in income. So too for the United States, until the federal government undertook actions (including assistance) that led to the narrowing (but far from eliminating) the gap in income between the north and the south.

13 Stolper and Samuelson 1941. This theorem was based on the same assumptions that underlay Samuelson's earlier analysis of the welfare gains from free trade. At the extreme, Samuelson showed that if there was free trade, factor prices would be fully equalised between countries with the same technologies. That that has not happened should be obvious. Nonetheless, Samuelson and Stolper did identify an important force that was at play: trade in goods was a (partial) substitute for the movement of factors.

14 The political economy of this asymmetric liberalisation was understandable, especially given the impetus for liberalisation came from developed countries where capital was in abundance. However, this means that it may not be likely that future trade agreements will be associated with significant increases in symmetry. To the extent that labour market liberalisation is included, it focuses on skilled workers.

15 The problems just described arising from trade liberalisation were often exacerbated by other liberalisation measures that often accompanied them. Capital and financial market liberalisation and banking deregulation often led to an increase in instability, with adverse effects on inequality and growth (see Stiglitz 2008, 2010, 2011, 2012).

16 While the Doha 2001 agreement clearly put development at the centre of trade negotiations, the link between development and trade liberalisation was even more ambiguous than that between growth and trade liberalisation. And trade ministers, especially from the developed countries, were ill-prepared to analyse the implications of alternative proposals for development. Under GATT, developing countries were somewhat protected by the commitment towards Special and Differential Treatment. The obligations undertaken by the developing countries as part of the Uruguay Round significantly reduced the policy space for developing countries. It made, for instance, the imposition of infant industry/economy protection more difficult, even though many developed countries had used such instruments in earlier stages of their own development, and even though advances in economic theory had shown the desirability of such policies, e.g. in the context of 'learning by doing' (see, for instance, Greenwald and Stiglitz 2006 and Stiglitz forthcoming). Development, it was increasingly recognised, required a transformation of the economy (see, e.g. Stiglitz 1998), a structural transformation that market forces were unlikely to accomplish on their own, and which could be facilitated by well-designed trade interventions. Developing countries began to demand greater flexibility for policy space, including greater freedom to pursue

industrial policies and to address supply-side constraints via government interventions, preferential market access and support for institution and capacity building.

17 The Gleneagles 'Africa' Communiqué.

18 G8 Finance Ministers, 'Final Communiqué'.

19 Doha Work Programme, Ministerial Declaration, WTO, adopted on 18 December 2005.

20 See International Lawyers and Economists Against Poverty 2006.

21 See the final text of agreements and commitments adopted at the International Conference on Financing for Development, Monterrey, Mexico, 18–22 March 2002.

22 ODA from development assistance countries was US$79.9bn in 2004, and it rose to US$133.5bn in 2012, around 0.31 per cent of GNI (and an average country effort of 0.46 per cent). If it had increased to 0.7 per cent for all Development Assistance Committee countries, net ODA would have been US$430.7bn. The shortfall between promised and delivered is some US$297bn.

23 Easterly 2006. He has since been joined by a host of critics (cited below) making similar observations.

24 In the last decade, significant resources have been devoted to understanding and improving the effectiveness of aid. In an early study, for instance, Burnside and Dollar (2000) showed that aid has no impact in countries with 'poor' institutions and policies, but can support GDP growth in developing countries with 'sound' institutions and economic policies. More recently, Rajan and Subramanian (2008) found that aid flows have very little impact on economic growth.

25 This was partly because, at the time, the prevalent belief in the development community was that increasing trade would lead to more growth, and more growth would lead to less poverty (both directly and indirectly because the increased growth resulted in more resources for poverty alleviation.) We have explained why those presumptions may not necessarily be correct. Aid for trade may still, however, promote growth and development (and poverty reduction) if it, for instance, offsets the loss of tax revenues from trade liberalisation or increases the pace of job creation through supply-side measures.

26 Though developed country exporters were more interested in expanding imports into developing countries; firms in developed countries that competed with developing country exports were not so interested in increasing the capacity of developing countries to compete.

27 At the same time, it should be recognised that much of the broader 'trade' agenda has for the past two decades consisted of cramming issues like investment and intellectual property into trade negotiations. TRIPS actually embraced virtually all of intellectual property rights.

28 Yet ironically many trade agreements have included provisions (such as those relating to financial market liberalisation), which have systemically resulted in a diminution in credit flows to small and medium enterprises (SMEs). See Detragiache et al. 2008.

29 And, indeed, doing so in ways that are consistent with poverty alleviation, through positive impacts on employment. Note that trade liberalisation by developing countries was often associated with increased imports and job destruction, while the aid for trade is associated with increased exports and job creation.

30 Thus the critique is far more fundamental than that there have not been appropriately designed 'random trials'.

31 That is, in this case the 'counterfactual' is that there would have been the same amount of aid in the absence of the aid for trade movement, but the aid for trade movement has imposed an additional constraint, diverting money that was more targeted at poverty reduction to other uses.
32 The existence of these impediments, which lowers exports from LDCs to developed countries, heightens the imbalances in tariffs: if they had been able to export more, the tariff revenues collected from developing countries would have been even larger.
33 WTO dispute cases numbers 58 and 61, for more information see: www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm
34 The right to development has emerged in a number of different contexts. It was first recognised in 1981 in Article 22 of the African Charter on Human and Peoples' Rights which states, 'All peoples shall have the right to their economic, social and cultural development with due regard to their freedom and identity and in the equal enjoyment of the common heritage of mankind'. The United Nations subsequently recognised the right to development in 1986 in the 'Declaration on the Right to Development', which was adopted by the United Nations General Assembly Resolution 41/128. Article 3.3 states: 'States have the duty to co-operate with each other in ensuring development and eliminating obstacles to development. States should realize their rights and fulfil their duties in such a manner as to promote a new international economic order based on sovereign equality, interdependence, mutual interest and co-operation among all States, as well as to encourage the observance and realization of human rights'. See, for example, Fukuda-Parr 2012.
35 One of the details which should, however, probably be pre-specified is the 'breadth' of the set of actions that might fall within the scope of the provision, i.e. the trade rules *as a whole* might be pro-development, even if a specific set of rules (e.g. relating to access to knowledge) impaired development. There should, however, be a presumption against actions that impair exports from least developed countries to either emerging markets or developed countries, or from emerging markets to developed countries.
36 Additionally, they should be able to freely agree among themselves on the allocation of sanction rights (some countries within the group may be better able to impose effective sanctions). Note that such collective action is akin to class action suits, which have proved to be one way that countries like the United States have responded to the asymmetries between large corporations and the many individuals with limited economic resources that may be affected adversely by the actions of those large corporations.
37 Some of America's recent economic problems have been attributed to its rules-based accounting systems, where corporations complied with the rules, to provide a grossly distorted picture of the firm's financial position (see, e.g. Stiglitz 2003). However, there are numerous other examples (cf. transfer pricing; the shadow banking system).
38 In the *Grootboom* case, the South African Constitutional Court, 'made it plain that the right of access to housing could not be separated from the right to human dignity' (Sachs 2005: 147). Such issues are largely a matter of degree: within the current WTO framework, there are agricultural subsidies that are described as 'trade distorting' and forbidden, while others are permitted. The US claims that its subsidies are not trade-distorting; most economists say that they are. Whether they are, or the extent to which they are, depends heavily on the 'model' of the economy. The WTO, in effect, left such matters to be resolved by the dispute resolution process.

39 A notorious example is the US offer to open its markets to 97 per cent of the products of the least developed countries. However, the 3 per cent 'carve out' embraced essentially all of the exports from some of the least developed countries. Still, there may need to be some specificity, such as discussed in footnote 35 above.

40 The reason for choosing UNCTAD is explained more fully in Stiglitz and Charlton 2006. One wants an institution in which the developing countries have more voice than say the World Bank, and one wants an institution that is less committed to the neoclassical model (in which there is no unemployment) and more committed to development.

41 The adjudication of the magnitude of the aid required to compensate might of course be a complex matter, but no more complex than the assessment of the value of compensation associated with any other trade violation. The GTF could also compensate developing countries in the case of other trade violations (including for already existing rights) where it is determined existing enforcement mechanisms are inadequate, e.g. because the implementation of such sanctions would impose significant costs on the developing country.

42 The tax could be thought of in part as a 'benefit tax' – exporters to developing countries are among those benefitting most from changes in the global trading regime that results in enhanced trade. The gains in 'equity' from such targeted taxation have to be balanced against the resulting distortions, which given the proposed rates are likely to be very small.

43 Even strong advocates of trade liberalisation have been highly critical of these bilateral and regional trade agreements. See Bhagwati (1995) who coined the term 'spaghetti bowl'.

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