

# COMMONWEALTH TRADE POLICY DISCUSSION PAPERS

**What Do Small and Poor Developing Countries  
Need from the Multilateral Trading System?**

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### Abstract

This paper reflects on small and poor developing countries’ needs from a multilateral trading system. Having recognised the importance of the WTO in ensuring predictability for producers and consumers and the limited negotiating capacity of small and poor countries, the paper examines three potential areas of constraint on trading by them: market access in goods, costs of trading and opening up of services trade. Several proposals that are currently under negotiations are then examined to suggest areas where these countries should focus their efforts in the WTO.

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## Abbreviations and acronyms

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AfT	Aid for Trade
BoP	balance of payments
DFQF	duty-free, quota-free
EU	European Union
GATS	General Agreement on Trade in Services
GDP	gross domestic product
GNI	gross national income
LDC	least developed countries
MFN	most-favoured nation
OECD	Organisation for Economic Co-operation and Development
ROO	rules of origin
WTO	World Trade Organization

# 1. Introduction

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The participation of small and poor developing countries in multilateral trade negotiations has given rise to a plethora of analyses and polemics about what can/should/might be agreed and, implicitly, whose fault it will be when agreement is not reached. It is neither an attractive nor a particularly constructive position to be in, and certainly not one that fills the independent observer with much hope. This paper takes a slightly different slant by going back to basics to ask a more fundamental question: what do small and poor developing countries need from a trading system, and then working out from there what to make out of the multilateral trade negotiations. Its purpose is not to create a shopping list or a negotiating position for World Trade Organization (WTO) negotiations, but rather to help prioritise issues for the group of least developed countries (LDCs) and to put into perspective what we actually end up with (which, of course, I am not attempting

to predict). It is thus basically a normative exercise.

I argue that trade is an essential part of the cocktail to deliver economic growth and development to poor countries, albeit only one part. The trading system needs to deliver predictability for producers and consumers in developing countries (in any country, actually). That is aided by simplicity, which is also a key requirement for releasing skilled bureaucrats and negotiators from the grind of WTO negotiations to perform the myriad important domestic tasks like regulating transport, educating girls or providing hospitals. With these two criteria I examine three potential areas of constraint on trading by poor countries: market access in goods, the costs of trading and providing services. Within each I examine several proposals that are currently prospective negotiations in the WTO and seek to prioritise them.

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## 2. Small and poor developing countries

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For shorthand I shall refer to the small and poor developing countries as SPCs; this group, which I do not define precisely, is not a club or a negotiating group but an analytical construct that indicates countries whose economic mass is so small that they represent a threat to hardly any other country's interests, offer

rather small economic opportunities to other countries and are broadly seen to warrant some sort of special treatment. The group is similar but not identical to the LDCs, a group which figures in several of the topics below, because the WTO Enabling Clause permits discrimination in favour of LDCs.

**Table 1. Statistics on least developed countries (LDCs) and small countries as percentage of world figures (World Bank definitions), 2010**

	LDCs	Small countries
Population, total	12.18	0.41
GDP (current US\$)	0.93	0.23
GNI per capita, Atlas method (current US\$)	7.38	53.77
Exports of goods and services (BoP, current US\$)	1.03	0.40
Imports of goods and services (BoP, current US\$)	1.17	0.37
Exports of goods and services (% of GDP)	95.88	160.50
Imports of goods and services (% of GDP)	124.09	182.83

**Notes:** GDP: gross domestic product, GNI: gross national income, BoP: balance of payments.

**Source:** World Development Indicators, World Bank

Table 1 reports a few statistics for the LDCs and for small economies (as defined by the World Bank), groups that overlap somewhat: small and vulnerable economies are a recognised group within the WTO, but attract no preferential treatment in their own right. While not wishing to get into a debate about exactly which countries should warrant which preferences, the data in Table 1 suggest that granting anything to small countries would be unlikely to be disruptive. While LDCs

contain perhaps 12 per cent of the world's population, they are very poor, with gross domestic product (GDP) per head of only 7.5 per cent of the world average. Small economies contain less than half a per cent of population, but have average incomes about half the world average. Thus, overall, LDCs and small economies account for less than 1 per cent and less than a quarter of 1 per cent of world GDP, respectively, and about 1 per cent and two-fifths of a per cent, respectively, of world exports.

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### 3. Trade as part of the development cocktail for SPCs

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International trade plays a fundamental role in stimulating income (or more loosely in facilitating growth): see, for example the Commission on Growth

and Development (2008) or Winters and Masters (2013). It permits countries to specialise in goods for which world prices exceed those that would be available at

home, reap economies of scale, improve performance in the face of external competition and benefit from better inputs and technologies available from abroad. In each case the benefits are more important to small countries than to large ones and we do indeed see small countries trading more than larger ones (Table 1). All these things require long-term commitments in terms of investment, skills, etc. The purpose of trade agreements – of which the WTO Treaty is the paramount example – is to create sufficient predictability to allow the benefits of trade to be manifest.

We have overwhelming evidence of the link between trade and income and very strong evidence from a variety of sources that a good part of it reflects causation from trade to income. There has emerged in recent years, however, a suggestion that the gains from trade or trade liberalisation have been lower for poorer countries

(e.g. Chang et al. 2009). Researchers have variously located the problems in areas such as inflexible labour markets, poor education levels, poor incentives to invest in new enterprise and poor institutions, but to date no definitive culprit has emerged, other than being poor. However, this result may, in fact, just be a statistical artifact associated with the fact that most of the trade liberalisations that we have observed among poor countries were in Africa in the 1990s, during which Africa had many growth problems unrelated to trade. However, what these results do remind us, is that there is far more to growth and development than just trade and trade policy, and this alone ought to be enough to teach us that a great virtue of trade policy and the trading system should be simplicity. To waste valuable resources – public and private – negotiating trade interventions of uncertain value is not much short of crazy.

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## 4. What are the key constraints on trade?

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Given the analysis above, what factors are stopping SPCs from gaining the maximum benefits from their international trade, and to what extent are these amenable to negotiation? From these answers, what priority should SPCs place on trade negotiations, given the manifest need for progress on the domestic agenda at the same time?

### 4.1 Market access in goods

Negotiations in the WTO tend to focus most on this aspect of market access and

this is true of the Doha Development Agenda. There are a number of specific issues over market access, but for most SPCs I doubt that they are actually the most binding of the constraints on their international trade. One exception, of course, is cotton, where continuing distortions from subsidies and import restrictions clearly impact heavily on the C-4 (Benin, Burkina Faso, Chad and Mali). Here the problem is not so much the significance of the issue but the ability to bring it to a successful conclusion, given the US resistance.

The more general issue of market access resides in duty-free, quota-free access (DFQF). Most developed WTO members already provide either full or apparently nearly full DFQF market access to LDC products. According to Elliott (2010), Australia, the European Union (EU), New Zealand, Norway and Switzerland have implemented DFQF access for LDCs for 100 per cent of products, i.e. no exceptions. Canada's programme spans 99 per cent of products, excluding only some sensitive agricultural products (dairy, poultry and eggs); Japan offers about 98 per cent product coverage, with exclusions for fish, footwear, rice and sugar. The US does not have a programme specifically targeting LDCs, but provides duty-free access to African countries under the African Growth and Opportunity Act. Thus, if all Organisation for Economic Co-operation and Development (OECD) countries offered complete DFQF access, LDC exports could increase only by up to US\$2 billion (Bouët et al. 2010), a gain of about 6 per cent. This is certainly desirable, but it is not critical.

More important is the fact that a number of emerging-market countries have now started DFQF programmes. These are large and currently much more dynamic markets and opening these up would be worth much more – perhaps by up to US\$5 billion even at present – reflecting the higher tariffs that these countries have. But of course it will also be more difficult politically. The big attraction to developed countries of offering DFQF is that almost no domestic production activity is put at risk by exports from LDCs – the (small) burden is borne by other low-income countries whose exports are displaced. In contrast, for emerging markets, there are still activities that compete with LDCs and

whose protection would be reduced by DFQF. Nonetheless, this is a goal more deserving of negotiating capital than OECD DFQF and if there is no progress in the Doha Round, maybe the G20 or another forum would do.

Once one has accepted DFQF as the route to market access in goods one is immediately confronted by rules of origin (ROOs). These can eliminate the benefits of tariff preferences if they mean that LDCs cannot take advantage of the preferences because as SPCs they cannot generate the required amounts of value added or transformation to meet the ROOs. In addition, the complexity of ROOs imposes a disproportionate burden on small exporters. The one-time costs of devising and proving compliant production structures apply equally to small values of trade and the repeated fixed per-consignment costs penalise countries that tend to have small consignments (see Hayakawa et al. 2013).

The EU has taken steps towards loosening its ROOs over the last few years and SPCs would have a strong interest in further steps by the EU and in other DFQF markets following suit. One should not underestimate the political difficulties that such improvements would pose, for all traders know that ROOs are just as protective as tariffs. However, the returns to progress on ROOs would be great. For exporters, and even for importers, simplification would offer resource savings, while liberalisation would allow SPC exports to grow. The LDC Group submission for Bali (TN/C/W/63) makes some sensible suggestions based around simple value rules with exceptions for a few specific sectors. These again are worth arguing for, although I must note that the gain from liberal ROOs is capped by the



size of the most-favoured nation (MFN) tariff avoided through the preferences in question. This again suggests that the emerging markets should receive as much attention as the OECD ones, especially since the former may not already have such well-established ROOs.

The LDC Group proposal also deals with regional cumulation. However, it wisely notes that while such provisions are 'laudable and highly desirable', cumulation is not a substitute for liberal ROOs. It is both bureaucratically complex and restrictive on the sources of inputs that may be used. If ROOs are genuinely liberal, the SPC producers can source their inputs worldwide and increase their competitiveness as a result. Finally, I note that preferential ROOs are not a traditional topic of negotiation within the WTO, and this will reinforce the difficulties of getting action in the WTO.

## 4.2 Trading costs

Market access is permissive – it removes barriers that might be faced if at the border – but for many SPCs the more critical issue is getting to the border in the first place. The challenges are both physical – trade logistics – and bureaucratic – the need to both design and market goods that satisfy the importers' regulations and standards. Both the Aid for Trade (AfT) Initiative and trade facilitation potentially deal with these issues, and the challenge is to ensure that they actually meet SPCs' requirements.

First, however, it is important to realise that discussion of standards raises an issue to which SPCs have considerable exposure but little leverage. There is a growing interest in plurilateral agreements within the WTO and a clear trend towards

mega-regional arrangements outside it. In both cases the large players are aiming to design rules and regulations that will operate between themselves. For a plurilateral agreement the story is that any developing country can join the agreements subject to accepting its conditions and one hears similar suggestions (not very plausibly) about the mega-regional arrangements too. In both cases there is no provision for negotiation prior to post-establishment accession (not that SPCs could ever expect to be able to extract many concessions – consider the accession process to the WTO), and so the position is that rules that may eventually affect SPCs quite significantly are being written now with no SPC representation at all. I find this alarming – as I did 10 years ago (see Schiff and Winters 2003). SPCs have a lot to gain from the introduction of common regulations across markets, because it will reduce the fixed costs of supplying different markets, but they have a lot to lose if those regulations effectively exclude them from markets now or are so tough as to preclude transition towards achieving them in future.

The solutions to these dilemmas are not easy, but they seem to me to include elements such as the following:

- where WTO plurilateral agreements liberalise market access, they should wherever possible be applied on a MFN basis;
- wherever possible, exceptions should be made to standards for small scale and artisanal products from poor countries. For health and safety regulations this may not be possible or wise – we do not want products from developing countries

- labelled as unsafe – but in other cases it may be;
- developing country interests should be represented at the negotiating table, even if such countries have no prospect or interest in immediate membership: this may be done by, for example, the WTO Secretariat, the World Bank, the Commonwealth Secretariat or a non-official body;
  - a means must be found to manage this representation in a way that assuages developing country fears but does not absorb a lot of domestic capacity: we cannot afford a further diversion of SPC talent from the issues of domestic growth and development towards international negotiations which may bear no fruit;
  - the costs of representation need to be met by binding and additional technical assistance budgets; and
  - similarly binding and additional technical assistance budgets need to be provided over long periods to aid developing countries and specifically SPCs to meet standards over the long run.

Concern over trade costs leads immediately to the trade facilitation agenda. This is important, especially for small isolated economies where trade costs are inevitably high (Winters and Martins 2004). The negotiations on trade facilitation are aimed at simplifying export/import processes, including customs rules and procedures. Two issues are occupying developing country negotiators: first, technical assistance and capacity-building – for the first time the implementation of commitments might be made conditional upon the existence of appropriate capacity. Developing

country members are asking for independent needs assessment to identify what needs to be done under the agreement, which in turn, should guide sufficient technical assistance and financial support. I entirely sympathise. Second, negotiators want flexibility to self-designate the type of commitments that they would enter and the timetables for achieving them. This may be appropriate, but there is a danger that it just becomes another example where developing countries fail to take steps that are in their own interests because they seek a quid pro quo in negotiation. For sure, there are questions about how to balance trade facilitation with other domestic priorities, but overall this seems to be a case where SPCs could benefit from an agreement that developed countries seem to want. Better an agreement with good technical assistance and financing than no agreement at all.

Aid for Trade should also figure in this discussion – not only in terms of financing physical infrastructure, but also to support standards activities, policy and even, possibly, development. AfT has become quite an industry over the last 8 years and has aroused some concerns that it is out of control, with donors logging projects as AfT when they actually have nothing to do with trade. Halleart (2013) argues that the initiative must be more tightly focused on the specific needs of the trading sector. There is validity in this view, if only for us to understand better exactly what is going on in the aid world, but conversely, the strengthening of market access clearly will need both private and public investment to be fully effective and AfT could play a useful role in this. The recent Fourth Aid for Trade Review in July 2013 argued for much

more focus on integrating developing countries into value chains.

Aid for Trade is not strictly a Doha issue, but it is intimately connected to it and could still, as originally intended, provide much-needed lubrication to get the negotiating machinery working again. With aid facing stronger and more widespread fiscal challenges, there will be no alternative than to try to ensure that AfT is spent wisely and generates observable results, so scrutiny, monitoring and evaluation will increase, and SPCs would do well to welcome and advance such goals. Not all projects lend themselves to the narrow evaluation creed of randomised controlled trials, but no developed country is going to keep lending or giving without serious attempts to assess what the benefits are.

### 4.3 Services

The ministerial conference of 2011 formalised a so-called services waiver, which permits members to waive MFN obligations under the General Agreement on Trade in Services (GATS) in order to grant preferential market access to LDC services and service firms – a sort of enabling clause for services. With services such a dominant part of the world economy (for example, even LDC economies have service shares of GDP above 40 per cent, and services may account for up to 30 per cent of the value of a typical manufacture: see the OECD's recent world input–output tables), and an increasing part of world trade, helping LDCs to enter the market seems an obvious step. However, it is worth recalling that preferences for goods have been disappointing, so one needs to keep this initiative in perspective.

In fact, so far nothing has happened and some argue that redressing this is a high priority for WTO negotiations. Studies are being undertaken to establish the sectors in which LDCs might possibly be competitive. This set is likely to be quite small and so the chances of there being a significant overlap between the preferences offered to LDCs and LDC capacity to produce is likely to be correspondingly small. For example, one area in which LDCs have a comparative advantage is tourism, but this allows little scope for preferences, because developed countries do not restrict their residents' travel. Another important area of potential is supplying services through the temporary mobility of labour (Mode 4). The benefits could be huge, but few developed countries show much stomach for such mobility and even fewer a willingness to commit and bind such concessions for large groups of countries (let alone the whole GATS membership). Thus, Mode 4 has long been a disappointment (see, for example, Winters (2005) for some of the reasons why) and the waiver, per se, unlikely to correct this.

However, if the services waiver were to permit agreements between an individual developed or emerging market and an individual SPC, it could play a significant role. I am opposed to bilateralism in trade relations and would like to see Mode 4 prosper, but given that, in truth, Mode 4 is pretty similar to temporary migration, it seems to me that in this case an exception might be tolerated. Several of the more enlightened bilateral schemes have demonstrated the potential of temporary mobility to raise incomes in SPCs. For example, deriving in part from two pieces of research commissioned by the Commonwealth Secretariat (Winters et al. 2003 and Winters

and Martins 2004), New Zealand's Recognised Seasonal Employers Scheme allows workers from poor Pacific Islands to work for the agricultural season in New Zealand. A formal evaluation shows that affected households from Vanuatu and

Tonga experienced average increases in income of over 30 per cent (Gibson and McKenzie 2010), and in Vanuatu (population 245,000), 2,500 workers benefit each year (*Vanuatu Daily Post*: [www.dailypost.vu/content/vt38-billion-rse-5-years](http://www.dailypost.vu/content/vt38-billion-rse-5-years)).

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## 5. Conclusion

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The exercise in prioritisation leads me to suggest that SPCs should focus their efforts in the WTO on:

- DFQF and ROOs with emerging markets – but simple ones;
  - a decent settlement for financing trade facilitation – again sufficiently simple to allow easy implementation and monitoring;
  - a seat at the table of plurilaterals and (almost unimaginable) the mega-regionals, supported by sufficient technical assistance so as not to divert too many resources from other governmental tasks; and
- a modification to the waiver to allow bilateral labour mobility deals plus an explicit willingness by OECD countries to negotiate such deals.

SPCs should also be robust in the face of disappointment and remember that the trading system already delivers significant benefits to them even if the rate of advance is slow. Predictability is worth a great deal and this depends on system credibility. It would be a massive own-goal if the SPCs contributed to the collapse of the system because they could not get even more from it.

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