Trading Opportunities for the Least Developed Countries

6
Chapter

When it comes to integrating into international trade, the Least Developed Countries are in a very vulnerable position. They typically have small economies, difficult topographies, and are located far from international markets, in which they are minor and weak players. They do benefit from some concessions from the developed countries, but will need fairer treatment at the WTO, as well as international assistance, if they are to use international trade to promote human development.

In principle, all countries should be able to use their comparative advantages to benefit from international markets and free trade. In practice, the scales are heavily weighted in favour of the larger and more advanced countries. The developing countries, and particularly the Least Developed Countries (LDCs), find themselves in a much weaker position.

The Asia-Pacific region is home to 37 per cent of the world's LDC population, with 14 of the 50 LDCs. They are: Afghanistan, Bangladesh, Bhutan, Cambodia, Kiribati, Lao PDR, Maldives, Myanmar, Nepal, Samoa, Solomon Islands, Timor-Leste, Tuvalu and Vanuatu. All qualify as LDCs because they satisfy three criteria: low incomes, human resource weakness and economic vulnerability.[1] Even so, they are clearly a very diverse group. Indeed, the region is home to the world's most populous LDC, Bangladesh, and the least, Tuvalu. Geographically too they can be very different: four are landlocked countries, for example, while seven are island states[2] (Table 6.1).

The LDCs are vulnerable on many fronts:

- *Economic*. Exposure to exogenous shocks that adversely affect incomes, employment, domestic production, distribution, markets, consumption, and the stock of wealth. LDCs also have a limited capacity to deal with such shocks.
- *Environmental*. Exposure to calamities induced by natural or human-made factors. Small island states of the Pacific, for example, are often hit by droughts, floods, hurricanes, and volcanoes and earthquakes, while mountainous countries in Asia are prone to flashfloods, volcanic eruptions and earthquakes.
- *Social*. Exposure to factors that undermine social cohesion, introduce systemic social pathologies, and erode social capital. Because the LDCs have little capacity to respond, these events tend to recur.
- *Institutional*. Limited capacity of domestic institutions, including the State, to respond to the complexity and intensity of pressures flowing from globalization.

As a group, the region's LDCs have made significant progress. During the period 1990–2000, they increased their average per-capita GDP by one and a half times and their exports three times. Social indicators also improved. Over the same period the adult literacy rate increased from 60 to 71 per cent, life expectancy rose from 58 to 62 years, and the infant mortality rate per 1,000 live births rate dropped from 77 to 55.

Nevertheless, they were starting from quite low levels and still have high rates of poverty and hunger. In 2003 the average per-capita GDP

TABLE 6.1

Key Indicators of Asia-Pacific Least Developed Countries

Country	*Geographic status*	*Population in 2003 (millions)*	*GDP per capita in 2003 (constant 2000 $)*	*Aid per-capita in 2003 (current $)*	*Indebtedness* status in 2003*	*Exports as % of GDP in 2003*	*Human development index (HDI) status in 2003 (HDI value; HDI rank out of total 177)*
Afghanistan	Landlocked	22.2	..	..	Not classified	..	..
Bangladesh	Coastal	138.1	395	10.1	Less indebted	14.2	Medium (0.520; 139)
Bhutan	Landlocked	0.9	680	88.1	Severely indebted	22.0	Medium indebted (0.536; 134)
Cambodia	Coastal	13.4	313	37.9	Moderately indebted	62.0	Medium (0.571; 130)
Kiribati	Small island	0.1	569	190.6	Not classified	..	..
Lao PDR	Landlocked	5.7	352	52.8	Severely indebted	25.5	Medium (0.545; 133)
Maldives	Small island	0.3	2,548	61.3	Less indebted	85.2	Medium (0.745; 96)
Myanmar	Coastal	49.4	..	2.5	Severely indebted	..	Medium (0.578; 129)
Nepal	Landlocked	24.7	241	18.9	Less indebted	16.7	Medium (0.526; 136)
Samoa	Small island	0.2	1,522	185.6	Severely indebted	..	Medium (0.776; 74)
Solomon Islands	Small island	0.5	597	131.9	Moderately indebted	31.0	Medium (0.594; 128)
Timor-Leste	Small island	0.9	421	171.9	Not classified	..	Medium (0.513; 140)
Tuvalu	Small island	0.0	..	..	Not classified	..	..
Vanuatu	Small island	0.2	1,098	154.3	Less indebted	..	Medium (0.659; 118)
Asia-Pacific LDCs		256.3	375	13.6	..	18.8	..
Asia-Pacific Other Developing Countries	3,016.6	854	2.7	..	34.8	..	

Note: * Indebtedness is as defined by the World Bank. 'Severely indebted' means either the present value of debt service to GNI is at a critical level, 80 per cent or more, or the present value of debt service to exports is at a critical level, 220 per cent or more. 'Moderately indebted' means either of the two key ratios exceeds 60 per cent of, but does not reach, critical levels. All other economies are listed as less indebted. See www.worldbank.org/data/countryclass/countryclass.html
'..' = not available.
There are significant data issues for many of the LDCs. Different sources provide differing estimates for the same indicator and there also tend to be data gaps.
Sources: UNDP and UNESCAP 2005; World Bank 2005; UNDP 2005a; ESCAP 2005.

in the region's LDCs was $375 – less than half that of the Asia-Pacific developing countries. Economically they are extremely vulnerable – often remote from markets, operating at low levels of technology and dependent on a small range of exports for which both demand and prices can be quite volatile. They have few natural resources and are prone to natural disasters.

LDCs and Liberalization

Trade represents a significant proportion of economic activity

One area where LDCs are especially exposed is international trade. For many LDCs trade – exports plus imports – represents a significant proportion of economic activity. In fact, their trade-to-GDP ratios are often higher than those of many developing countries, or even developed ones: 127 per cent for Cambodia in 2002, for example, and 152 per cent for Maldives. They also tend to have very open trade regimes, with low tariff or non-tariff barriers. According to the IMF's index of trade restrictiveness, of the 46 LDCs around the world for which data were available in 2004, only four had average tariff rates above 25 per cent. Moreover, for 29 countries their non-tariff barriers were either low or minor.[3]

However, these open trade regimes are not primarily the result of multilateral commitments negotiated during the Uruguay Round or with the WTO. More often, LDCs have taken unilateral steps to open up their economies as part of broader programmes of domestic reform. Of the 21-percentage-point cut in average weighted tariffs of all developing countries between 1983 and 2003, two-thirds was the result of autonomous liberalization.[4]

Why do LDCs not Benefit Sufficiently from Trade?

Conventional wisdom suggests that increasing exports of any kind should be beneficial – providing much-needed foreign exchange to invest in economic development and alleviate poverty. Unfortunately, although LDCs have often had dynamic export sectors since the late 1980s, they have not achieved commensurate economic growth, or a significant reduction in poverty.

Why have the LDCs not been able to use trade to boost economic growth? Many of the constraints are the same as those that hold back economic development generally: low levels of skill and technology that lead to low productivity; poor infrastructure; few linkages between productive sectors; and the lack of a financial sector that can provide capital at reasonable interest rates.

Many also face serious geographic obstacles. Afghanistan, Bhutan, Nepal and Myanmar, for example, have some very inaccessible mountainous terrain. Since road construction is expensive, these countries can link many of their regions only by air transport or tortuous, winding roads, adding greatly to the cost of doing business. Economic development can also be slowed if populations are very scattered across the landscape – whether over mountain ranges, or widely separated islands, as in the Maldives, for example, or the Solomon Islands. This not only makes it more difficult to provide social services but also slows economic integration.

Geography hampers not just national economic development but also international trade. Many landlocked countries face high transport costs that eat into the revenue from exports, and also add to the costs of imports. These countries are also vulnerable to policy changes in the neighbouring countries through which their goods have to transit.

But geography can impede trade even for countries with their own coastlines. The poorest countries tend to have only a few major ports, so exporters located far from those ports are at severe cost disadvantages. Indeed, if their export volumes do not justify regular ship calls, exporters might have to use ports in neighbouring countries.[5]

LDCs with small economies can find themselves with multiple disadvantages

LDCs with small economies can thus find themselves with multiple cost disadvantages. One estimate suggests that telephone services, electricity services and personal travel in micro-states cost around twice as much as in the average country and are particularly damaging to trade – sea freight costs can be three times as high.[6]

LDCs also suffer in international trade because they are minor players. For individual commodities, they typically make only a small contribution to the global market so they cannot influence international prices. This means they become 'price takers' and have to accept what they are offered. If other producers increase their output, this can push down international prices, wiping out the LDCs' already-low profit margins. In the short term, this can deliver a sharp economic shock or in the longer term, push them into a 'poverty trap'.[7]

They are also vulnerable if they have a limited range of exports. LDCs have to specialize in products in which they have a comparative advantage, and as a result, many still rely on agricultural goods: for Kiribati, for example, agricultural products account for nearly 89 per cent of exports, and for Vanuatu 54 per cent.[8] Even countries that export manufactured goods tend to concentrate on one sector such as textiles and clothing – which in 2003 accounted for 40 per cent of exports from Nepal, 76 per cent of those from Bangladesh, and 95 per cent of those from Cambodia. Of the 4,162 products exported by the LDCs to 30 major trading partners in 2000, 127 accounted for 90 per cent of their total export trade.[9] For all LDCs, the export concentration ratio – the share of the principal export product in the total export value – has remained high and largely unchanged since 1980.[10]

Trade integration has had a limited impact on poverty because it encourages an 'enclave-type' growth pattern

Trade integration has also had a limited impact on poverty because it encourages an 'enclave-type' growth pattern. Certain sectors do reasonably well, but leave the rest behind. Even the agricultural export sector tends to have few links with the subsistence agrarian activities on which most people depend for their livelihoods.

In these circumstances, it may not be obvious why LDCs would want to gain access to the World Trade Organization and the further liberalization that this implies. For most, however, the alternative is worse – marginalization or bilateral control by one or two major powers. The multilateral WTO is still a better option if it offers some consistent basic ground rules.[11] Accession to the WTO can offer:

- Binding commitments to stable policies
- Predictability of market access
- Shelter against unilateral pressures from powerful countries
- Access to a powerful dispute settlement mechanism
- Expectations of a role in shaping the future of world trade

Experience with Trade Integration

In the past, most LDCs have liberalized trade unilaterally. In future, however, they are more likely to do so on a reciprocal basis, multilateral, regional or bilateral. Their main multilateral option is the WTO which currently has 149 members. Of the 50 LDCs, 32 are now WTO members, and 8 others are in the process of accession. A few Asian LDCs, such as Bangladesh, were founder members of the WTO when it was signed into existence in 1994, but others joined later. Of the Asia-Pacific LDCs, Bangladesh, Cambodia, the Maldives, Myanmar, Nepal and the Solomon Islands are now members, while Bhutan, Lao PDR, Samoa and Vanuatu are in the process of joining.

Many LDCs find this accession process very difficult. They lack the trained people needed to understand the implications of trade agreements – either the commitments or the policy flexibilities. Even the few Asia Pacific LDCs that have missions in Geneva can devote only a few staff members to participate in WTO negotiations. As a result, even well-meaning officials may be unable to exploit opportunities during negotiations and can sign agreements that compromise national interests and human development priorities.

The same limitations are evident in civil society organizations. They too lack the

resources and capacity for specialized research, and few can conduct informed advocacy at the policy level. Consequently, they may have to base their campaign strategies on their perceptions of how trade agreements work, which may not necessarily accord with reality.

The situation is even more difficult for the LDCs now trying to join. Because the rules for accession to the WTO are vague, incumbent members have been able to exploit them to impose onerous conditions on the acceding countries. They try to extract maximum concessions for three reasons: first, because this will help them set a precedent for later applicants; second, because it provides them benefits for which they do not need to reciprocate; third, because they can use these terms as instruments in subsequent multilateral trade negotiations.

The extra conditions they apply are of two types – 'WTO-minus' and 'WTO-plus'. The WTO-minus conditions are those that prevent the new arrivals from taking advantage of certain rights contained in the WTO agreements and already enjoyed by existing members. WTO-plus conditions are additional obligations that are either not a requirement of the WTO or have not been undertaken by its existing members.

These conditions can have serious implications, because the WTO rules, unlike those for GATT, influence national policies, including many that are critical for human development. Poor countries acceding to the WTO now find it more difficult to obtain special and differential treatment to allow them to delay some commitments.

However, certain agreements within the WTO do provide more policy space. For example, the General Agreement on Trade in Services respects members' rights to pursue their human development objectives – allowing them to retain certain conditions related to market access and national treatment. Even at the time of accession, some countries have used this opportunity to negotiate reasonable terms (Box 6.1).

Although these demands on newly acceding countries cover a wide range of issues, they can be considered in two groups – those related to policy space and those related to systemic issues.

Policy Space

These refer to restrictions on freedom of action. Generally, the founding and existing members have retained considerable freedom of manoeuvre while giving new arrivals much less scope. They use a number of instruments that compress the policy space of newly acceding members, including:

- *Tariffs*. One of the most important issues is the flexibility to alter tariff rates. If, within

WTO rules influence national policies, including many that are critical for human development

BOX 6.1

Nepal's Cautious Approach to Liberalizing Services

At the time of accession to the WTO, Nepal liberalized 11 service sectors and 70 sub-sectors. This seems like a lot, but in fact, Nepal managed to negotiate liberalization for only a select group of services: First, those in which the Nepalese private sector may never get involved, given the huge investment cost and high gestation periods – such as pipeline transportation; second, those in which the Nepalese private sector is already competitive and able to outperform foreign service suppliers – such as banking services; third, sectors that have a high potential to employ local people – such as computers and related services.

A few other measures of restriction negotiated by Nepal include:

(a) capping foreign investment in most sectors at 51 per cent; while in some others at 66-67 per cent and only in two sectors at 80 per cent;
(b) the requirement that a majority of the board members of basic telecom providers should be Nepalese nationals, and in the case of financial institutions, the composition of the board should be proportionate to the shareholding pattern;
(c) foreign banks, with minimum 'B' rating by a credit rating agency, can only establish branches in Nepal for wholesale banking, not retail banking;
(d) incentives and subsidies should be available only to enterprises wholly owned by Nepalese nationals;
(e) not allowing foreigners to purchase or own land in Nepal; and
(f) movement of natural persons to be limited to intra-corporate transferees at the executive, managerial or specialist levels, with a proviso that the number of such transferees shall not exceed 15 per cent of the number of local employees in the firm.

Source: Adhikari 2004.

the WTO, a member has 'bound' a tariff, it is then committed not to increase this above a specified rate. Most developing-country members of the WTO bind some, but certainly not all, of their tariff lines and can raise them, even astronomically, if circumstances so dictate. Indeed, some African countries have bound a very small proportion: Tanzania and Cameroon, for example, 0.1 per cent; Mozambique, 0.5 per cent; Togo, 0.9 per cent; and Ghana, 1.2 per cent.[12] All the acceding countries, on the other hand, have been asked to bind tariffs on almost all lines.

- *Other duties or charges*. Similarly, many WTO members still maintain 'other duties and charges' (ODCs) and have never been challenged to remove them.[13] The acceding countries, on the other hand, have been asked to either bind ODCs at zero, or phase them out over a short period – though in fact, the only acceding countries that have been allowed to maintain ODCs with an agreed timeline to phase them out are Bulgaria[14] and Nepal;[15] all others have been compelled to bind them at zero from their date of accession.
- *Special and differential treatment*. The WTO acknowledges that developing countries can have difficulties in taking on multilateral commitments and obligations. It thus grants them longer grace periods before complying with agreements (Box 6.2). Existing WTO members get 'special and differential treatment' rights automatically, but acceding countries have to negotiate these on a case-by-case basis – and most have been denied them.
- *Export duties*. The WTO does not oblige members to bind, reduce or eliminate export duties, and virtually all members have avoided binding them. However, some acceding countries have been compelled to eliminate export duties or bind them at a certain level.
- *Services liberalization*. In various service sectors acceding countries have been asked to make commitments far more extensive than those of incumbent members.

BOX 6.2

Special and Differential Treatment Provisions in the WTO

Developing countries have been granted some flexibility in applying the conditions of membership of the WTO through 'special and differential treatment' (SDT). This treatment applies to both binding and non-binding provisions.

Binding Provisions

Some of these can be implemented unilaterally, without having to wait for action by others. Under this heading, there are two kinds of SDT.

(a) Permitting developing countries to assume lesser obligations. In the Agreement on Agriculture, for example, the *de minimus* levels of domestic support to agriculture are 5 per cent, but for developing countries they are 10 per cent. Similarly, the developed countries have to commit to 36 per cent tariff reductions but developing countries to 24 per cent; for the reduction in subsidies, the corresponding proportions are 20 per cent and 13 per cent.

(b) Providing transitional time periods, which are higher for the developing countries. In TRIPS, for example, developed countries have only a one-year transition period to implement the commitment, while developing countries were given five years and LDC were given even more generous treatment.

Other binding provisions require action from others, particularly developed countries. For example, Article 66.2 of TRIPS required developed-country members to provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer to LDCs.

Non-binding Provisions

These are also known as best-endeavour clauses. For these the SDT concessions are of three types:

(a) Requiring WTO members to safeguard the interest of developing countries – as with the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS), which requires members to take into account the special needs of the developing countries and LDC members.

(b) Requiring developed countries to provide technical assistance to the developing countries and the LDCs. For example, the Agreement on Technical Barriers to Trade (TBT) requires members to provide technical assistance to developing countries and the LDCs, on mutually agreed terms and conditions, for the establishment of national standardizing bodies.

(c) Requiring developed countries to enhance trade opportunities of the developing countries and LDCs. For example, the need to provide market access: Article XXXVII.1 of the GATT requires the developed members to accord high priority to the reduction and elimination of barriers on products currently or potentially of particular export interest to developing member countries.

- *Intellectual property protection*. For the protection of new plant varieties, the developing countries often prefer to use their own systems that better suit their social, economic and environmental needs. The developed countries, however, argue that the only effective *sui generis* system is that of the International Union for the Protection of New Varieties of Plants (UPOV) and are trying to impose this model on each acceding country.[16] China and Cambodia, for example, have been cajoled into signing on to UPOV as a part of their accession deal – though Nepal was able to fend off these pressures due to the collective efforts of the government and civil society organizations. Although the data protection measures are not mandated by TRIPS, new countries are also being required to enforce these, Cambodia being an example (Box 6.3).
- *Plurilateral agreements*. These are commitments that were agreed to by only a limited number of members, at the founding of the WTO. Some members are now insisting, however, that the acceding countries agree to accept these agreements, or at least enter into negotiations to do so. Vanuatu, for example, had to accept this demand.[17]
- *Participation in sectoral initiatives*. These are tariff reduction initiatives, such as the Information Technology Agreement. For existing WTO members, participation in these is optional, and they have the flexibility to choose which products they would like to cover. But all the acceding countries have been asked to participate in one or more of these initiatives.

Systemic Issues

The demands from the WTO also concern some fundamental issues that affect the organization of economies. These include:

BOX 6.3

TRIPS and the Looming Public Health Crisis in Cambodia

An estimated 2.8 per cent of the adult population in Cambodia are infected with HIV/AIDS, one of the highest rates in Asia. Tens of thousands have already died, and within the next five to ten years 200,000 people, including children, could develop HIV/AIDS (Ouyahia-McAdams 2002).

Combating HIV/AIDS requires, among other things, providing antiretroviral (ARV) drug therapy. Cambodia was already finding this hard: until recently, humanitarian agencies and NGOs were providing drugs to only 700 patients (Macan-Marker 2003). But accession to the WTO makes things even more difficult. During the negotiations Cambodia was forced, as a 'WTO-plus' requirement, to agree to protect undisclosed test or other data for pharmaceutical products for five years. This will be devastating for Cambodia's efforts to tackle HIV/AIDS, for during the period of the patent, Cambodia will not even be able to use test data to assess bio-equivalent generics to be prepared for when the patent expires. Instead, the generic producing or importing company would have to repeat the trials – a costly and slow process – or wait for five years (Charveriat and Kirkbride 2003). ARV medicines will thus become even more scarce and expensive – and exacerbate an already serious public health crisis.

Source: Adhikari 2004a.

- *Non-market economy status*. The WTO agreements do not demand that countries have a market economy. But existing members have effectively pushed new members, including China, Kyrgyzstan and Mongolia, in this direction, and are likely to apply the same pressure on Viet Nam.
- *Privatization of state owned enterprises*. The WTO mandate does not require countries to embark on the privatization path. Nevertheless, acceding countries such as Cambodia and Mongolia have been asked to report periodically to the WTO about the status of their privatization programmes.
- *Investment regime*. The agreement on Trade Related Investment Measures (TRIMs) prohibits governments from imposing 'export balancing requirements' on firms – preventing them from importing further inputs unless they have met certain export targets. However, in accession negotiations some WTO members have requested new applicants to ban export performance requirements even when they are not linked to import volume or value.[18]

Implementation Problems

A number of LDCs have had problems implementing their WTO agreements. This is partly because, for the accession countries in particular, these agreements are often onerous and unreasonable. But LDCs can also have a limited capacity to fulfil even the normal conditions. Some agreements are easy and cheap to implement: tariffs, for example, can be reduced by the stroke of a minister's or a legislator's pen. But others require a huge investment – in the purchase and installation of equipment and procedures and the training of staff – as with customs valuation, and intellectual property rights and standards.[19] In addition, LDCs may not have the administrative capacity or the funds to create the requisite institutions.

Human Development Implications of Trade Integration

Assessing the impact of trade integration on human development for LDCs is a challenging task. It is difficult enough to determine whether integration even increases trade, let alone what are its precise effects on different segments of society.[20] At the most general level, however, it is clear that trade integration does create winners and losers. The winners are usually those who can best organize themselves in the private sector, or occasionally in trade unions – who can press for their interests during trade discussions, and if they think they will be disadvantaged, bargain for compensation payments. The losers are less organized, and usually more numerous – small farming households, for example, or workers in import-competing industries who will lose the protection of high tariffs – not to mention taxpayers who have to fill the gaps left in government budgets by cuts in customs revenues.

Governments need to support those who suffer from trade liberalization

Institutions and Governance

Governments need to support those who suffer from trade liberalization. One priority should be to build social safety nets – offering unemployment allowances and facilities for retraining, while helping businesses make any necessary social adjustments. Some governments have done this quite successfully and provided extensive protection. Indeed, there is often a striking correlation between a country's exposure to foreign trade and the size of its welfare state: the most open countries such as Sweden, Denmark and the Netherlands have also seen the greatest boosts in spending on income transfers.[21] Unsurprisingly, these countries also have some of the best human development achievements.

But these enlightened policies need not be limited to richer countries. Ecuador, for example, a middle-income developing country, has made similar efforts. In 2001 after acceding to the WTO and signing several regional trade agreements, it enacted a new Social Security Law that provides for an unemployment allowance to those losing jobs in the private and public sectors. Mongolia too, after accession to the WTO, and with the help of a loan from the Asian Development Bank, strengthened its social security programme so that, among other things, it could help the unemployed and underemployed to find jobs.

Public Health

Trade liberalization can affect public health in a number of ways. One is by accepting intellectual property regimes that influence the availability and pricing of drugs. Previously, developing countries that did not operate patents systems could produce generic drugs similar to, but far cheaper than, the original branded versions. India, for example, built up a sophisticated and efficient pharmaceutical industry to produce generic drugs for both local consumption and export. Neighbouring Pakistan, on the other hand, which also had a sizable pharmaceutical industry, but which did respect patents, had prices from 3 to 14 times higher.[22]

All this changed from 1994 with the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). All WTO members now have to comply with strict intellectual property provisions covering such issues as copyright and patents. This has serious implications. First, there are the economic costs: TRIPS is expensive to implement – revising laws, training officers, and testing and enforcing patents, and the economic benefits are unclear.[23] But there can also be catastrophic social costs. By restricting the opportunities to produce affordable, generic versions of drugs, TRIPS is set to create a public health crisis in Asia and the Pacific. One of the most severe impacts will be on HIV/AIDS. More than 7 million people in the region suffer from HIV/AIDS, and almost half a million die from the disease each year.[24] Cambodia, for example, which has recently acceded to the WTO, will now find it even more difficult to provide anti-retroviral therapy (Box 6.3).

The full effects have yet to be felt because many of the TRIPS provisions included a ten-year exemption period that only expired on 31 December 2004. The LDCs also have the advantage of a longer stay of execution. In November 2001, the Doha Declaration on TRIPS and Public Health granted LDCs an extension of the transition period for pharmaceutical products until 2016. And in June 2002, the TRIPS Council exempted all LDC members from applying certain parts of the TRIPS agreement in relation to pharmaceuticals until 2016.

The General Council has also made it somewhat easier for LDCs to import generics. Previously, companies producing under compulsory licences had to manufacture predominantly for their domestic markets. In August 2003, however, these companies were given a waiver from this requirement for exports to countries that had an insufficient manufacturing capacity – though there are some procedural constraints on this provision.

Finally, in November 2005, the Least Developed Country members as a group were granted an extension of the transitional period for TRIPS as a whole for 7.5 years – that is, until July 2013, or until such a date on which they cease to be a LDC. But the decision freezes the status quo since it stipulates any changes in laws, regulations and practice made during the additional transitional period should not result in a lesser degree of consistency with the provisions of the TRIPS agreement.

Environmental Protection

Developed countries have argued that lax environmental standards offer some developing countries an unfair competitive advantage – in particular, that many of their enterprises can produce goods much more cheaply, largely because they do not have to worry about, or pay for, the pollution they cause. This, they say, will inevitably lead to a 'race to the bottom' in what have been called 'pollution havens'.

Empirical evidence does not support this hypothesis. One survey of five polluting industries in 119 countries found that, except for iron and steel products, there was no clear evidence that national governments were deliberately setting low environmental standards, and it concluded that the case for including such standards in the WTO framework was weak. The same applies to environmental standards in regional trade agreements like NAFTA and the US-Singapore bilateral agreement.[25]

The developing countries, for their part, agree that it is important to improve environmental protection, but this should not be a part of trade negotiations since it offers the developed countries even more opportunities to raise arbitrary and discretionary trade barriers. And in any case, the GATT already allowed for restrictions if trade was harmful to the interest of plant, animal or human health or to the goal of conservation of natural resources.

Instead, developing countries prefer to focus on the more positive potential of trade to transfer technologies that offer better environmental

Developing countries, as a group, have insisted on SDT, saying that applying the same rules to unequal trading countries could be disastrous

protection. The Doha Declaration, for example, mandates a liberalization of trade in environmental goods and environmentally sound technologies.

Initiatives to Address LDC Vulnerability

The developed countries recognize that when integrating into international trade the LDCs are likely to be vulnerable and have, therefore, made some efforts to protect their interests. But most such endeavours, although genuine, have failed to achieve their objectives.

Special and Differential Treatment

One approach has been to allow developing countries some leeway under the umbrella of 'special and differential treatment' (SDT). Developing countries, as a group, have insisted on SDT, saying that applying the same rules to unequal trading countries could be disastrous. Instead, they would prefer modulated commitments – based on their trade, development and financial needs: well-designed, effective, enforceable and timebound SDT that can help developing countries and LDCs integrate into the multilateral trading system.[26] Just as important, SDT offers ways of modifying the trade regime to take better account of human development objectives.[27]

Within Asia, many of the middle- to higher-income countries have limited imports from LDCs in the region because their import needs are different from what these LDCs can supply (Box 6.4).

In response, the various WTO agreements contain 124 separate articles or paragraphs containing around 160 provisions for SDT.[28] They can be broadly divided into 'binding' and 'non-binding', that is, enforceable and non-enforceable (Box 6.2). These are presently being reviewed by the WTO's Committee on Trade and Development – with a view to strengthening them and making them more precise, effective and operational, though so far there have been few signs of progress.[29]

Some analysts oppose SDT on principle, arguing that developing countries should not demand such treatment because it further marginalizes them.[30] But others take the view that SDT is necessary if the poorest countries are to integrate successfully, but emphasize that it is by no means sufficient.[31]

BOX 6.4

Trade Between Asia-Pacific LDCs and China

China's trade with Asia-Pacific countries has grown rapidly and now accounts for 53 per cent of its global trade. But much of this trade, almost 78 per cent, is with high-income countries of the region, such as Japan, the Republic of Korea, Singapore, Hong Kong (China) and Taiwan (China). Within middle-income countries, the major trading partners are Malaysia, Thailand and Indonesia.

Imports by China from Asia-Pacific LDCs are extremely limited – about $300 million. All LDCs have trade deficits with respect to China. A striking example is Bangladesh, which exports goods valued at only $57 million and imports goods worth $1,906 million from China.

Given China's import requirements, primarily of high-tech equipment, machinery and parts, fuel and raw materials, it is not surprising that most of the trade is with high-income countries. LDCs have limited scope for benefiting from the booming Chinese market – which is growing at over 15 per cent per annum. On the other hand, LDCs imports from China are large and account for over 20 per cent of all their imports, which implies big and growing trade imbalances with respect to China and the possibility that Chinese imports are displacing some domestic industries.

Clearly, there is a strong case for China, along with other middle- and high-income countries of Asia-Pacific, to provide special and differential treatment to LDCs through a Generalized System of Preferences (GSP) involving concessional tariffs.

Trade balance of Asia-Pacific countries with China, 2004 ($ millions)

	Exports to China	*Imports from China*	*Trade Balance*
LDCs			
of which:	314	3,560	–3,246
Bangladesh	57	1,906	–1,849
Cambodia	30	452	–422
Lao PDR	12	101	–89
Myanmar	207	938	–731
Nepal	8	163	–155
Low-income countries	11,460	12,945	–1,485
Middle-income countries	46,017	25,140	20,877
High-income countries	247,109	228,419	18,690
Total Asia-Pacific	304,900	270,064	34,836

Source: ITC Trade map. Accessed May 2006.

Preferential Market Access

This refers to various concessions that allow duty-free access for certain goods for developing countries. Preferential access could also be considered a subset of SDT, though this particular form of special treatment has deeper historical roots. In 1965 the members of the GATT added articles to give preference to goods from developing countries. Then in the 1970s several advanced economies introduced the Generalized System of Preferences (GSP), voluntarily offering unilateral preferential tariff rates to imports from developing countries. From 1979, this was instituted as a permanent feature of the multilateral trading system. Subsequently, in the 1980s many other developed countries introduced bilateral schemes.

In 1979 the EU provided a second preferential market access scheme under the Lomé Convention – now the Contonou Agreement – offering their former colonies, including the Pacific countries, far deeper preferences than those in the GSP schemes. Then in 2001 the EU presented a new agreement with special terms for LDCs – the 'Everything But Arms' (EBA) initiative – which provides duty- and quota-free access to the EU market for all products other than arms and munitions, although three products were to be phased in later: bananas in 2006, and rice and sugar in 2009. Similarly, 27 other countries have either offered some form of preferential market access to the LDCs or are in the process of doing so.[32] These include:

Canada. In January 2003, Canada introduced a new GSP scheme. This is very liberal, though it excludes dairy products, eggs and poultry. It also has an innovative approach for rules of origin, using a cumulative system that allows access to products that include inputs from any of the beneficiary countries.

Japan. Japan has extended its GSP scheme until 2014, and in 2003 further improved it by allowing LDCs duty-free entry not only for industrial goods but also for a few agricultural products, such as prawn and frozen fish fillets.

United States. In addition to the concessions it offers through its regular GSP scheme, the US provides deeper preferences to selected African countries through the African Growth and Opportunity Act (AGOA) and to Caribbean countries through the Caribbean Basin Initiative. However, the US GSP scheme offers less favourable treatment to countries in Asia and the Pacific.

Nevertheless, the take-up of these preferences has been disappointing. The developed countries still take a very small proportion of their imports from LDCs: 0.6 per cent for the EU; 0.2 per cent for Canada; 0.4 per cent for Japan; and 0.8 per cent for the US.[33] These figures have remained unchanged since 1992; indeed, for Japan the figure has declined.

The take-up of preferences has been disappointing

There have been a number of explanations for this. One is that exporting countries do not want to invest in building new markets in these countries, since the preferences are unilateral and optional and could be eliminated at any time. They also point out that the schemes exclude certain 'sensitive' sectors and often apply excessively stringent rules of origin, making it difficult for industrial products that incorporate materials from several other countries. Moreover, many enterprises do not really understand these rules or are generally unaware of the preferences available.[34]

Another problem is that the developed countries are increasingly protecting their markets using non-tariff barriers. The EU and the US, for example, have been using the Agreement on the Application of Sanitary and Phytosanitary Measures to keep out some exports of agriculture, livestock, horticulture and floriculture. These measures are often inappropriate for the circumstances of producers

and represent disproportionately onerous burdens for small exporters.[35]

'Preference sceptics' say that these schemes are inherently discriminatory: although they benefit some developing countries, they do so at the expense of others.[36] But 'GSP reformers' take a more positive line arguing that these schemes have played a positive role.[37] Others go further, claiming that GSPs have approximately doubled trade between developing and developed countries[38] and that they contributed to the 'Asian success story', allowing a number of countries to penetrate markets and sustain themselves there to build the necessary competitiveness.[39]

BOX 6.5

Aid-for-trade: The Way Forward

If the least developed and low-income countries are to take full advantage of a more liberalized global economy, they will need more support from the richer countries through 'aid for trade'. This should enable LDCs to use trade as an instrument of development policy – helping them, for example, to apply appropriate standards, diversify their agricultural, industrial and services exports and deal with supply-side constraints – human, institutional and infrastructural.

Aid for trade, in the form of grants or concessional loans, should also help countries cope with fiscal losses and deteriorating terms of trade; other short-, medium- and long-term preference erosion; and the costs of implementing trade agreements.

Some developing countries have reservations about this initiative. They fear that aid for trade may serve as the basis of a new form of conditionality based on a country's trade negotiating position in the Doha Round. They also wonder whether this is new and additional aid money. If not, they would like to know if trade is considered more important than health or education. They also wonder whether it will be multilateral or bilateral, and whether it will come in the form of budget support or project support.

Nevertheless, there does seem to be political backing for the concept. The British Government, for example, championed it in its Commission for Africa Report, and both the Millennium Project Report and the UN Secretary-General's Report for the 2005 World Summit identified scaled up aid for trade as a priority. The World Bank and the International Monetary Fund have also endorsed a proposal for "an enhanced Integrated Framework . . . including expanding its resources and scope and making it more effective."

The 2005 Ministerial Meeting of the WTO produced a strong consensus for an enhanced Integrated Framework. A new Aid for Trade Task Force will provide recommendations to the WTO General Council by July 2006. The EU also announced that it would raise aid-for-trade spending, excluding infrastructure, to approximately €2 billion a year by 2010. Japan has committed $10 billion, and the US announced that it would double its aid for trade to $2.7 billion annually by 2010.

However, even an ambitious aid for trade package cannot and should not be viewed as a substitute for the development dimensions of the Doha Round. Rather, it should be thought of as complementary.

A new school of thought is emerging on this issue. It suggests that developed countries should not offer preferences but instead liberalize across the board on a 'most favoured nation' basis – while also offering LDCs support for their adjustment programmes, and for strengthening their supply capacity and competitiveness through 'aid for trade'. Of course, various WTO agreements already include provisions for technical assistance that have frequently failed to materialize. Even so, it should be possible to strengthen aid for trade measures.

Trade-related Technical Assistance

The developed countries recognize that many LDCs will need support if they are to integrate productively into the multilateral trade system. They have, therefore, considered two types of trade-related assistance (Box 6.5).

The first and more difficult type is designed to help the recipients compete more effectively in the international arena. This involves helping remove capacity constraints – building better infrastructure, for example, or improving levels of skill in the workforce.

The second type of assistance focuses more narrowly on improving the capacity of public officials to deal with trade issues and to operate more effectively at the WTO and other trade negotiations. It also conducts studies on related issues. Thus far, most multilateral and bilateral donors and institutions, including the WTO, have focused more on this second type of assistance.

To try to ensure a more comprehensive and effective approach, in 1997 six multilateral institutions – the IMF, UNDP, the World Bank, the International Trade Centre, UNCTAD and the WTO – launched the Integrated Framework for Trade-Related Technical Assistance to Least Developed Countries, also known as the 'Integrated Framework' (IF). The IF has two objectives: first, to integrate trade into the LDCs'

national development plans such as the Poverty Reduction Strategy Papers; second, to respond to needs identified by the LDCs with a coordinated delivery of trade-related technical assistance. In order to finance the IF activities, donors have established a Trust Fund that has two main 'windows': one to finance the Diagnostic Trade Integration Study (DTIS) and the other, created in 2003, to finance capacity building projects identified by the DTIS.[40]

The IF has received support from both development and trade communities. In July 2003, for example, the heads of the six IF agencies and their representatives issued a joint communiqué underscoring their commitment to the IF model. Then, in December 2003 in Doha, the WTO Ministers endorsed the IF as a viable model for the LDCs' trade development. Despite this support, the IF seems to be having a limited impact, and critical trade infrastructure remains unfunded. Some of the problems are common to many multilateral ventures. One is a lack of funds: the budget per country under Window II is only $1 million. The DTIS has had little influence on the allocation of donor funds.[41]

Recent Developments

The current round of trade negotiations, the Doha Development Agenda, recognized the special needs of the Least Developed Countries within the multilateral trading system. The Doha Ministerial Declaration spoke not just of the importance of speedy accession of the LDCs into the WTO, but also of the need for technical assistance and capacity building.

Since then, however, there has been little effort to convert this political commitment into practical action. In 2004, following the failure of the Cancun Ministerial Conference of the WTO, a group of influential developing and developed countries, with limited participation of LDCs, hammered out the 'July Framework'. But even this failed to address most of the concerns relating to LDC integration into the multilateral trading system. The language is weak on a number of issues. For example, rather than obliging the developed countries to give SDT to the poorer developing countries, it only says that 'disciplines on export support will be developed with consideration of the impacts on least-developed and net food-importing developing countries'. The language is similarly non-committal when it comes to ways of achieving fuller integration of small, vulnerable economies into the multilateral trading system.

The Hong Kong Ministerial Meeting in December 2005 made more progress. Members agreed that developed-country members *shall*, and developing-country members declaring themselves in a position to do so *should*, provide duty-free and quota-free market access on a lasting basis, for all products originating from all LDCs by 2008, or no later than the start of the implementation period of the Doha Round in a manner that ensures stability, security and predictability. However, members who find this difficult would be allowed to permit duty-free and quota-free market access for only 97 per cent of products originating from LDCs. And developing-country members would be allowed to phase in their commitments and enjoy appropriate flexibility in coverage.

There has been little effort to convert this political commitment into practical action

Following the Hong Kong Ministerial, the LDCs were also allowed to maintain, on a temporary basis, existing measures that deviate from their obligations under the TRIMs agreement.[42] They would also be able to take new measures, if they obtained approval from the WTO's Council, for Trade in Goods. These can last for five years and are renewable, but have to be phased out by 2020.

Finally, it was reaffirmed that LDC members will only be required to undertake commitments and concessions to an extent consistent with their individual development, financial or trade needs, or their administrative and institutional capacities.

The Way Forward

The Least Developed Countries of the region can engage more fruitfully with the international trading system, but this will need more determined action at both national and international levels.

The National Agenda

Governments need to integrate trade issues into their overall development architectures

- *Giving a higher priority to trade issues*. Governments need to integrate trade issues into their overall development architectures – including the Poverty Reduction Strategy Papers – to ensure national ownership and facilitate better coordination among different agencies. And when negotiating international trade commitments, they should ensure that these take full account of human development priorities. They also need to work closely with the private sector and civil society organizations and seek their input at every stage.
- *Increasing productivity and competitiveness*. This will mean investing in infrastructure – including roads, telecommunications, warehouses, and port facilities. Though LDCs should be able to count on external assistance, they would also need to mobilize some domestic resources. In addition, they will have to enhance the capacity of domestic enterprises, particularly by harnessing the potential of the knowledge-based economy. At the same time, they will need to strengthen institutions and the regulatory system to foster competition and prevent fraud, deception and capital flight.
- *Providing compensation and human development safeguards*. Governments should seek ways to compensate those that lose out in the short run from trade integration – for example, through retraining facilities, unemployment benefits and adjustment credits. They will also need to safeguard areas of vital human development interest, such as food security and public health.
- *Diversifying exports and markets*. In order to prevent deterioration in the terms of trade triggered by international volatility of commodities exports, the LDCs should not only diversify into more valued-added, dynamic manufacturing sectors, but also into service sectors – making special efforts to identify niche products and services as well as new destinations for exports (Box 6.6).

BOX 6.6

NICHE PRODUCTS: AN OPPORTUNITY FOR LEAST DEVELOPED COUNTRIES

Some landlocked or small countries can adopt the niche market approach to export production. Of special interest are opportunities in markets for nature-based 'green' products such as organic fruits or vegetables; and woollen floor coverings or shawls that use only natural fibres and vegetable dyes. These mainly cater to the tastes of an ever-growing segment of 'green consumers' in the developed countries.

Niche products could also cash in on the unique cultural heritage of these countries. Several Pacific nations – Samoa, Tonga and Vanuatu – could develop as an exportable item kava, a traditional drink and medicinal plant.

Similarly, there are services that depend on natural features such as unspoiled scenic beauty – for example, environmental tourism in Nepal and Bhutan, and 'bungalow tourism' in Vanuatu. Also in the tourism sector, there are other possibilities for specialization, such as yacht chartering or sports fishing in archipelagic waters, as in the Maldives.

Source: Adapted from UNCTAD 1999b.

The International and Regional Agendas

- *Building credible alliances*. The LDCs cannot effectively influence negotiations by acting individually or even in small groups. Instead, they need to build broader alliances around specific principles or on issues such as vulnerability and negotiate as a bloc.
- *Achieving fairer terms of accession*. The LDCs need to advocate for clear-cut guidelines for WTO accession. These should include the timeframe for each stage of negotiations, maximum levels of market access commitments and a requirement to genuinely take into account their trade, development and financial needs and their institutional capacity. Further, they should

tie implementation of their commitments to the availability of technical assistance. 'WTO-plus' conditions should be stopped.

- *Targeting technical assistance*. Many of the trade participants, including industry, farmers and service providers, would benefit from carefully targeted technical assistance programmes. Such external assistance would free government resources for the social sector investment that is crucial for achieving human development objectives.
- *Strengthening SDT provisions*. SDT should be made operational, effective and enforceable. This means not just including such provisions in the WTO architecture, but also building mechanisms to monitor their implementation. For this purpose, the various committees in the WTO should be required to submit regular reports.
- *Offering aid for trade*. The potential losses of trade integration for LDCs suggest a new role for aid – compensating for losses and offering help for restructuring. Aid should also be provided to develop the capacity of country negotiators and build stronger institutions. In addition, it should address supply-side constraints that inhibit export responsiveness.
- *Focusing on human development*. Trade is not an end in itself; it is a means to an end. All trade initiatives and negotiations should, therefore, be based on a human development perspective. The focus should be not merely on market access, but on achieving improved human development outcomes – through trade rules that allow for diversity in national institutions and standards.

All trade initiatives and negotiations should be based on a human development perspective