

**Trade Policy Review Body**

**OVERVIEW OF DEVELOPMENTS IN THE  
INTERNATIONAL TRADING ENVIRONMENT**

Annual Report by the Director-General<sup>1</sup>

**1. Introduction**

1. Global output is forecast to pick up to some 4% in 2004, improving steadily from the sharp slowdown in 2001, and returning close to trend.<sup>2</sup> As a consequence of a pick up in demand, particularly in the United States, Japan and some Asian countries, growth is likely to be stronger, up from around 3.2% in 2003. World trade too has recovered, roughly in line with global output, with the volume of trade in goods and services expected to increase by about 3% in 2003, with an acceleration to between 7-8% in 2004. Although encouraging, the situation is not without a certain downside risk, especially the persistence of large financial imbalances. These complicate trade policy formulation and add emphasis to the need to make progress in the Doha Development Agenda. Against this background, this paper presents developments in major trade policy instruments.

**2. Tariffs ... considerable unfinished business**

2. Since the establishment of the General Agreement on Tariffs and Trade (GATT) in 1947, successive rounds of multilateral trade negotiations have greatly reduced impediments to trade, especially tariffs. One of the main principles underlying the GATT is that trade barriers, insofar as they are used at all, should involve tariffs rather than non-tariff barriers (NTBs); negotiations could then concentrate on binding tariff rates and securing multilateral reductions therein. As a result of such negotiations, tariff levels on industrial goods have declined dramatically. Once commitments made under the Uruguay Round (UR) are fully implemented, the overall import-weighted tariff average on industrial products will have reached less than 4% in industrial countries, compared with about 40% at the time of GATT's establishment.<sup>3</sup>

3. Notwithstanding the considerable achievements of the Uruguay Round and previous rounds of negotiations, tariffs remain an important impediment to international trade and consequently a source of inefficiency.<sup>4</sup> Even in industrialized countries, where average MFN tariff rates are seemingly low<sup>5</sup>, the existence of tariff "peaks" in certain sectors, notably agricultural products, textiles, clothing, and footwear, constitutes *prima facie* evidence that the dead-weight and net welfare losses caused by tariff protection could, if eliminated, raise incomes by 5% in developing countries,

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<sup>1</sup> As explained to the Trade Policy Review Body (TPRB), this Report is an abridged version of that prepared for distribution in November 2003. The Report is now presented for the record, but remains subject to comment from Members, either at a future meeting of the TPRB or in writing. A report for 2004, self-standing but complementary to the World Trade Report and the WTO Annual Report, is being prepared for discussion by the TPRB in late 2004.

<sup>2</sup> International Monetary Fund (2003), *World Economic Outlook September*, p. 3.

<sup>3</sup> See Blackhurst, R., A. Enders and J. Francois (1996), "The Uruguay Round and Market Access: Opportunities and Challenges for Market Access", in W. Martin and A. Winters (eds), *The Uruguay Round and Developing Countries*, Cambridge University Press.

<sup>4</sup> Tariffs are not only a barrier to imports but also constitute, insofar as they are levied on inputs, export taxes to the extent that the final products are tradeable.

<sup>5</sup> The measured overall level of tariff protection can vary considerably depending on the tariff rates and especially the weighting method used (Annex 1)

thereby lifting 300 million people out of poverty by 2015, the target date for achieving the UN Millennium Development Goals.<sup>6</sup>

4. Particular attention is focused on the so-called "Quad" group of major traders (the United States, the European Union, Japan, and Canada) as these four Members' tariffs can have serious repercussions for their trading partners, especially developing and least developed countries (LDCs). This may also be true in the case of China, which became a Member of the WTO in December 2001 and, during the past two years, has overtaken Canada as the world's fourth largest trader. The use of tariffs by the Quad and China to impede access to their markets can therefore lead to welfare losses not just domestically, but on a global scale, because they tend to hamper countries' efforts to efficiently allocate their resources. It should also be noted that the use of generally higher tariffs by developing countries also contributes to an inefficient domestic allocation of their resources.

5. Some simple summary indicators that capture the level and structure of tariffs in the Quad are reported in Table 1 for 1995, prior to the implementation of the UR tariff cuts (or 1996, if data for 1995 were not available), and for 2002.<sup>7</sup> They are also reported under full implementation of the UR (and ITA); the latter indicators provide a benchmark for the current negotiations on tariffs at the WTO. Similar indicators are reported for selected developing countries including those reviewed in 2002/03 (China, Indonesia, Chile, and South Africa) in Table 2 and for selected LDCs (Burundi, Haiti, Niger, and Zambia) in Table 3.<sup>8</sup>

#### **Bound MFN tariffs**

6. Bindings are a key element of trade liberalization as they reduce the uncertainty concerning Members' trade regimes. In addition to achieving higher levels of bindings on industrial products, all Members bound 100% of their tariff lines on agricultural items as a result of the WTO Agreement on Agriculture; the outcome was the "tariffication" of non-tariff barriers (NTBs) for agricultural products.<sup>9</sup>

7. The Quad have bound close to 100% of their tariff lines. Full implementation of their bindings results in relatively low simple average bound rates for industrial products, although wide differences exist across products. While the simple average of final bound MFN rates is in the range of 4.6% in the United States to 8.4% in Japan, the average bound rate for agricultural products is two to three times higher; this reflects the frequent "peaks" in bound tariffs for more "sensitive" agricultural product categories. Among industrial products, bound rates are highest for textiles and clothing, with the final bound rate average ranging from 6.7% in Japan to 12.2% in Canada.

8. China too has bound 100% of its tariff lines; with full implementation, its average bound rate will be 9.9%, compared with 12.4% at present, although the average bound rate for agricultural products will be 14.5% and that for textiles and clothing will be 11.5%.

9. Whereas Indonesia, Chile, Niger and South Africa have bound most, if not all, of their tariff lines, Burundi and Haiti have each bound roughly one fifth (Tables 2 and 3). As regards other major developing and least developed countries, Brazil has bound most of its tariff lines, while India has bound less than three quarters and Bangladesh some 13%.<sup>10</sup>

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<sup>6</sup> World Bank, 2002 *Global Economic Prospects*.

<sup>7</sup> The methodology used to construct the tariff indicators found in this and other tables is outlined in Daly, Michael, and Hiroaki Kuwahara, 1998, "The Impact of the Uruguay Round on Tariff and Non-Tariff Trade Barriers in the Quad", *The World Economy* 21(1), pp. 207-234.

<sup>8</sup> Except in the case of China, Trade Policy Reviews were conducted for these Members during the past year.

<sup>9</sup> Notable initial exceptions to tariffication included rice in Japan and Korea.

<sup>10</sup> See WTO (2002), *Trade Policy Review – India*; and WTO (2000), *Trade Policy Review – Bangladesh*.

**Table 1**  
**Structure of MFN tariffs in the "Quad"**  
(Per cent)

	United States <sup>a</sup>			European Union			Japan			Canada		
	1996	2002	F.B. <sup>b,c</sup>	1995 <sup>d</sup>	2002	F.B. <sup>b,c</sup>	1996 <sup>f</sup>	2002 <sup>f</sup>	F.B. <sup>b,g</sup>	1995 <sup>d</sup>	2002	F.B. <sup>b,h</sup>
1 Bound tariff lines (% of all tariff lines)	100 <sup>i</sup>	100 <sup>i</sup>	100 <sup>i</sup>	..	100	100	98.9	98.9	98.9	..	99.8	99.7
2 Duty free tariff lines (% of all tariff lines)	18.2	31.2	37.6	9.4	21.5	28.0	34.9	36.7	40.6	18.2	49.0	29.6
3 Non-ad valorem tariffs (% of all tariff lines)	14.1	12.2	10.8	10.2	9.7	10.1	7.1	7.2	6.2	7.4	3.9	5.1
4 Tariff quotas (% of all tariff lines)	1.9	1.9	1.9	3.3	3.1	3.3	1.6	1.7	1.7	2.2	2.2	2.2
5 Non-ad valorem tariffs with no AVEs (% of all tariff lines)	3.1	0.0	0.2	2.0	2.6	3.5	..	1.2	0.8	5.8	0.5	1.4
6 Simple average bound rate	..	..	4.6	..	6.5	6.3	10.3	8.5	8.38	..	..	8.4
Agricultural products (HS01-24)	..	..	8.1	..	16.2	16.3	..	26.6	26.5	..	..	23.1
Industrial products (HS25-97)	..	..	4	..	3.8	3.6	..	4.1	3.9	..	..	5.8
WTO agricultural products	..	..	8.3	..	16.1	16.3	..	28.9	28.9	..	..	24.4
WTO non-agricultural products	..	..	4.0	..	4.2	4.0	..	3.9	3.8	..	..	5.7
Textile and clothing	..	..	9.0	..	8.4	8.0	9.8	7.1	6.7	..	..	12.2
7 Nuisance bound rates (% of all tariff lines) <sup>j</sup>	..	..	6.7	..	12.9	6.4	..	6.7	1.1	..	..	1.1
8 Simple average applied rate	6.4	5.1	..	10.2	6.4	..	9.0	6.9	..	13.2	6.8	..
Agricultural products (HS01-24)	10.0	9.5	..	23.7	15.9	..	..	18.6	..	28.6	21.2	..
Industrial products (HS25-97)	5.7	4.2	..	6.6	3.8	..	..	3.9	..	10.5	4.2	..
WTO agricultural products	10.3	9.8	..	24.5	16.1	..	..	20.0	..	30.3	21.7	..
WTO non-agricultural products	5.7	4.2	..	6.9	4.1	..	..	3.9	..	10.4	4.2	..
Textile and clothing	11.5	9.7	..	10.4	8.4	..	8.7	7.0	..	18.4	9.9	..
9 Domestic tariff "peaks" (% of all tariff lines) <sup>k</sup>	4.0	5.3	..	4.0	5.2	..	..	6.0	..	1.4	1.6	..
10 International tariff "peaks" (% of all tariff lines) <sup>l</sup>	8.9	6.3	..	11.0	7.7	..	..	7.6	..	17.0	9.8	..
11 Overall standard deviation of tariff rates	13.4	12.3	..	16.5	11.3	..	40.8	32.6	..	30.0	24.4	..
12 Coefficient of variation of tariff rates	2.1	2.4	..	1.6	1.8	..	..	4.7	..	2.3	3.6	..
13 Nuisance applied rates (% of all tariff lines) <sup>j</sup>	8.9	12.6	..	1.0	12.9	..	..	6.1	..	1.2	2.2	..

.. Not available.

F.B. Final bound

- a. The United States levies its *ad valorem* duties on the basis of the "f.o.b." ("free on board") price, thereby excluding the costs of insurance and freight. By contrast, most other WTO Members, including the EU, Japan and Canada, levy *ad valorem* import duties on the "c.i.f." price, which includes these costs. As the c.i.f. price exceeds the f.o.b. price by the amount of insurance and freight costs, a tariff levied on the f.o.b. price affords less protection than one levied at the same rate on the c.i.f. price.
- b. Including ITA.
- c. Based on 1998 tariff schedule.
- d. Pre-Uruguay Round tariff.

- e. Based on 1999 tariff schedule.
- f. Fiscal year.
- g. Based on 2002 tariff schedule.
- h. Based on 2000 tariff schedule.
- i. Two lines, applying to crude petroleum, are not bound.
- j. Nuisance rates are those greater than zero, but less than or equal to 2%.
- k. Domestic tariff peaks are defined as those exceeding three times the overall simple average applied rate (indicator 8).
- l. International tariff peaks are defined as those exceeding 15%.

Note: AVEs have been used as available. In case of unavailability, the *ad valorem* part is used for compound and alternate rates. For the European Union 2003 tariff data is available but does not include AVEs.

Source: WTO Secretariat calculations, based on data provided by the Members.

**Table 2**  
**Structure of MFN tariffs in selected developing countries**  
(Per cent)

	China			Indonesia			Chile			South Africa		
	1996	2002	F.B. <sup>a</sup>	1998	2002	F.B. <sup>b,c</sup>	2000	2002	F.B. <sup>d</sup>	1997	2002	F.B. <sup>e</sup>
1 Bound tariff lines (% of all tariff lines) <sup>f</sup>	n.a.	100.0	100.0	93.2	93.2	93.2	100.0	100.0	100.0	96.3	96.2	96.3
2 Duty free tariff lines (% of all tariff lines)	1.9	4.8	7.6	20.2	21.9	1.7	0.4	1.2	0.0	42.4	43.4	9.9
3 Non-ad valorem tariffs (% of all tariff lines)	0.0	0.7	0.0	0.0	0.2	0.0	0.0	0.5	0.0	25.6	25	0
4 Tariff quotas (% of all tariff lines)	..	0.8	0.8	0.0	0.0	0.0	0.0	0.0	0.0	4.2	3.8	3.8
5 Non-ad valorem tariffs with no AVEs (% of all tariff lines)	0.0	0.7	0.0	0.0	0.2	0.0	0.0	0.0	0.0	25.6	25	0
6 Simple average bound rate	..	12.4	9.9	..	..	37.6	25.1	..	25.1	..	..	20.9
Agricultural products (HS01-24)	..	17.9	14.5	..	..	47.3	25.6	..	25.6	..	..	46.8
Industrial products (HS25-97)	..	11.4	9.1	..	..	35.9	25.0	..	25.0	..	..	18.1
WTO agricultural products	..	18.2	15.2	..	..	47.7	25.7	..	25.7	..	..	43.5
WTO non-agricultural products	..	11.5	9.0	..	..	35.9	25.0	..	25.0	..	..	18.1
Textile and clothing	..	17.6	11.5	..	..	29.3	25.0	..	25.0	..	..	26.8
7 Nuisance bound rates (% of all tariff lines) <sup>g</sup>	..	1.9	2.4	..	..	0.0	0.0	..	0.0	..	..	0.0
8 Simple average applied rate	23.6	12.3	..	9.5	7.2	..	9.0	5.9	..	15.0	11.4	..
Agricultural products (HS01-24)	35.4	18.0	..	8.6	8.3	..	9.0	6.1	..	11.3	11.5	..
Industrial products (HS25-97)	21.7	11.3	..	9.7	7.0	..	9.0	5.9	..	15.4	11.4	..
WTO agricultural products	33.8	18.2	..	8.8	8.3	..	9.0	6.1	..	9.4	9.6	..
WTO non-agricultural products	22.1	11.3	..	9.6	7.0	..	9.0	5.9	..	15.7	11.6	..
Textile and clothing	32.8	17.5	..	14.6	10.5	..	9.0	6.0	..	35.1	24.4	..
9 Domestic tariff "peaks" (% of all tariff lines) <sup>h</sup>	1.1	1.8	..	1.8	1.5	..	0.0	0.1	..	4.0	3.9	..
10 International tariff "peaks" (% of all tariff lines) <sup>i</sup>	55.2	29.5	..	14.5	3.4	..	0.0	0.1	..	39.3	34.8	..
11 Overall standard deviation of tariff rates	17.4	9.1	..	15.7	11.1	..	0.5	1.2	..	17.8	12.6	..
12 Coefficient of variation of tariff rates	0.7	0.7	..	1.7	1.5	..	0.1	0.1	..	1.2	1.1	..
13 Nuisance applied rates (% of all tariff lines) <sup>g</sup>	1.0	1.6	..	0.0	0.0	..	0.0	0.0	..	0.2	0.0	..

n.a. Not applicable.

.. Not available.

F.B. Final bound

a. Based on 2002 tariff schedule.

b. Including ITA.

c. Based on 1998 tariff schedule.

d. Based on 2000 tariff schedule.

e. Based on 2001 tariff schedule.

f. Including fully bound and partially bound rates.

g. Nuisance rates are those greater than zero, but less than or equal to 2%

h. Domestic tariff peaks are defined as those exceeding three times the overall simple average applied rate (indicator 8).

i. International tariff peaks are defined as those exceeding 15%.

Note: Calculations exclude specific rates and include the *ad valorem* part for compound and alternate rates.

Source: WTO Secretariat calculations, based on data provided by the Members.

**Table 3**  
**Structure of MFN tariffs in selected least-developed countries**  
(Per cent)

	Burundi		Haiti		Niger		Zambia	
	2003	F.B. <sup>a</sup>	2002	F.B.	2002 <sup>b</sup>	F.B. <sup>c</sup>	2002	F.B. <sup>d</sup>
1 Bound tariff lines (% of all tariff lines) <sup>c</sup>	21.6	21.6	..	..	96.9	96.9	16.2	16.2
2 Duty free tariff lines (% of all tariff lines)	0.1	0.7	66.6	..	0.0	0.5	20.9	0.0
3 Non- <i>ad valorem</i> tariffs (% of all tariff lines)	0.0	0.0	0.0 <sup>*</sup>	..	0.0	0.0	1.3	0.0
4 Tariff quotas (% of all tariff lines)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
5 Non- <i>ad valorem</i> tariffs with no AVEs (% of all tariff lines)	0.0	0.0	0.0 <sup>*</sup>	..	0.0	0.0	1.3	0.0
6 Simple average bound rate	68.4	68.3	..	..	..	44.6	..	107.3
Agricultural products (HS01-24)	94.0	94.0	..	..	..	80.1	..	122.8
Industrial products (HS25-97)	37.7	37.5	..	..	..	38.0	..	67.8
WTO agricultural products	95.1	95.1	..	..	..	82.2	..	123.0
WTO non-agricultural products	28.1	27.9	..	..	..	37.9	..	43.3
Textile and clothing	26.0	26.0	..	..	..	36.0	..	40.0
7 Nuisance bound rates (% of all tariff lines) <sup>f</sup>	0.0	0.0	..	..	..	0.0	..	0.0
8 Simple average applied rate	23.4	..	2.9	..	14.6	..	13.4	..
Agricultural products (HS01-24)	35.4	..	5.2	..	17.5	..	19.6	..
Industrial products (HS25-97)	21.6	..	2.5	..	14.1	..	12.5	..
WTO agricultural products	32.6	..	5.5	..	16.7	..	18.5	..
WTO non-agricultural products	22.1	..	2.5	..	14.3	..	12.7	..
Textile and clothing	35.2	..	5.0	..	19.8	..	18.3	..
9 Domestic tariff "peaks" (% of all tariff lines) <sup>g</sup>	0.0	..	17.8	..	0.0	..	0.0	..
10 International tariff "peaks" (% of all tariff lines) <sup>h</sup>	42.9	..	0.0 <sup>e</sup>	..	41.3	..	31.0	..
11 Overall standard deviation of tariff rates	14.4	..	4.8	..	6.9	..	9.5	..
12 Coefficient of variation of tariff rates	0.6	..	1.6	..	0.5	..	0.7	..
13 Nuisance applied rates (% of all tariff lines) <sup>f</sup>	0.0	..	0.0 <sup>e</sup>	..	0.0	..	0.0	..

.. Not available.

\* Negligible.

F.B. Final bound.

a Based on 2003 tariff schedule.

b Based on tariff actually applied: MFN custom duties plus a statistical charge and community solidarity levies.

c Based on 2002 tariff schedule.

d Based on 2001 tariff schedule.

e Including fully bound and partially bound rates.

Note: Calculations exclude specific rates and include the *ad valorem* part for compound and alternate rates.

Source: WTO Secretariat calculations, based on data provided by the Members.

### Applied MFN tariffs

10. Applied MFN tariffs are generally at, or close to, bound rates in the Quad. Thus, like bound tariffs, the level of applied tariff protection, although declining, also varies widely. The average applied MFN rate (2002) for all products ranges from 5.2% in the United States to 6.9% in Japan.<sup>11</sup> Nonetheless, these low average applied tariff levels disguise much higher rates applied to agricultural products and textiles, clothing, and footwear.

<sup>11</sup> Average applied MFN rates are below 5% in Australia, Iceland, and New Zealand and zero in Hong Kong, China and Macau, China; Singapore applies tariffs to six tariff lines.

11. Applied MFN tariffs tend to be much higher in developing countries; for example, the average applied MFN tariff rate for China is 12.3%, although this is roughly half the level in 1996 (Table 2). However, China's current average is rather low compared with some other major developing countries. Furthermore, by the time its bound rates are fully implemented, China is committed to an average bound rate of 9.9%, which means that applied rates will need to be brought down so as not to exceed this level. In selected African countries (Tables 2 and 3), applied MFN tariffs average range from 11.4% in South Africa to 23.4% in Burundi. By contrast in Haiti and Indonesia the averages are 2.9% and 7.2%, respectively. The averages in India (2001/02), Bangladesh (1999/2000), and Brazil (2002), are around 32%, 22%, and 14%, respectively.

12. One important reason for such high rates in these and other developing-country Members is that tariffs often serve a dual purpose; they protect domestic industries from foreign competition and are a major source of revenue. It follows that tariff reform can have important revenue implications in such Members, and reductions in average tariffs can depend heavily on tax reform. However, the possible fall in the revenues resulting from across-the-board cuts in tariff rates can be mitigated by the elimination of exemptions and other concessions in Members' tariffs; moreover, to the extent that broad tariff cuts are reflected in lower domestic prices for imported products, the amount of revenue collected (from the tariff and internal indirect taxes) could rise insofar as demand for such products is sufficiently responsive. Financial support (from institutions such as the IMF or World Bank) could help developing countries to manage any loss of tax revenues arising from tariff cuts.

13. Whereas in developed countries applied MFN tariffs are generally at, or close to, bound rates, they are often significantly below bound rates in developing countries, thus providing considerable scope for applied tariffs to be raised and thereby imparting a degree of unpredictability to the tariff. This gap is the result of two factors: the negotiation of ceiling bindings in the GATT 1994, and unilateral reductions in applied tariffs since the WTO came into existence. Such unilateral trade liberalization has been undertaken by a number of Members.

14. So called "nuisance" tariffs (applied rates exceeding zero and no more than 2%) involve as many as 12.3% of all tariff lines in the United States, 12.9% in the EU, and 6.1% in Japan.<sup>12</sup> In China, however, they cover only 1.9% of all tariff lines. In general such tariffs seem to be negligible in developing countries and LDCs.

### **Tariff dispersion and "peaks"**

15. The efficiency losses associated with tariffs depend not just on average applied MFN rates, but also on their dispersion across products. For any given average tariff, the wider the dispersion in applied MFN rates, the greater the likelihood that consumers' and producers' decisions are distorted by the tariff structure.

16. Among the Quad, applied MFN tariff rates three or more times the average continue to protect certain sectors from imports. These "peaks" cover from 1.6% of tariff lines in Canada to between 5.2% and 6% in the EU, Japan and the United States. By and large, tariff peaks are concentrated in agriculture and food products, partly due to tariffication, as well as textiles, clothing, and footwear (Chart 1), which tend to be labour intensive. Many of these products are of major export interest to developing countries; indeed, exports by LDCs are disproportionately affected by tariff peaks in the Quad.<sup>13</sup> Not surprisingly, therefore, the problem of tariff peaks features prominently in the Doha Development Agenda (DDA).

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<sup>12</sup> Canada has a mechanism whereby "nuisance" rates are automatically eliminated.

<sup>13</sup> The value of Quad imports subject to international tariff peaks (that is, rates exceeding 15%) was nearly US\$93 billion in 1999, roughly 60% of which originated in developing countries. This represents about

17. In major developing and least developed countries, such tariff peaks tend to be less pervasive, largely due to the higher overall levels of tariff protection in these countries. In China, for example, peaks cover only 1.8% of tariff lines (Table 2). In Indonesia and South Africa, the proportions are 1.5% and 3.9%, respectively, while they are negligible in Burundi, Chile, Niger, and Zambia. Although such peaks in these countries do arise in agriculture and food products, textiles, clothing and footwear, they are less pronounced than in the Quad (Charts 2 and 3).

18. In general, a movement towards a lower and more uniform tariff in developed and developing Members alike would tend to improve resource allocation and thereby raise economic welfare.<sup>14</sup> High and disparate tariffs foster inefficiency by penalizing efficient activities, including exports; by promoting a high-cost economy, they impair the competitiveness of exporters. Border taxes levied on imports are, in effect, shifted onto exports. Reducing tariff dispersion will tend to reduce these adverse effects.

19. It is estimated that if Quad Members were to accord LDCs duty-free access for products currently subject to tariff peaks, LDCs' exports to these major markets would rise by between 30% and 60%, or by as much as US\$2.5 billion; the latter is equivalent to an 11% increase in LDCs' total exports.<sup>15</sup> Part of this increase in LDCs' exports would be at the expense of other developing countries.

### Specific tariff rates

20. Tariff peaks are often concealed by specific rates, which are an important feature of the Quad Members' tariff schedules, particularly for agricultural products and especially in the United States and the EU, where they account for 12.1% and 9.7% of tariff lines, respectively. This is partly the consequence of the "tariffication" of agricultural NTBs, which were largely converted into specific or mixed duties<sup>16</sup>, rather than into pure *ad valorem* tariffs, and often combined with tariff quotas.

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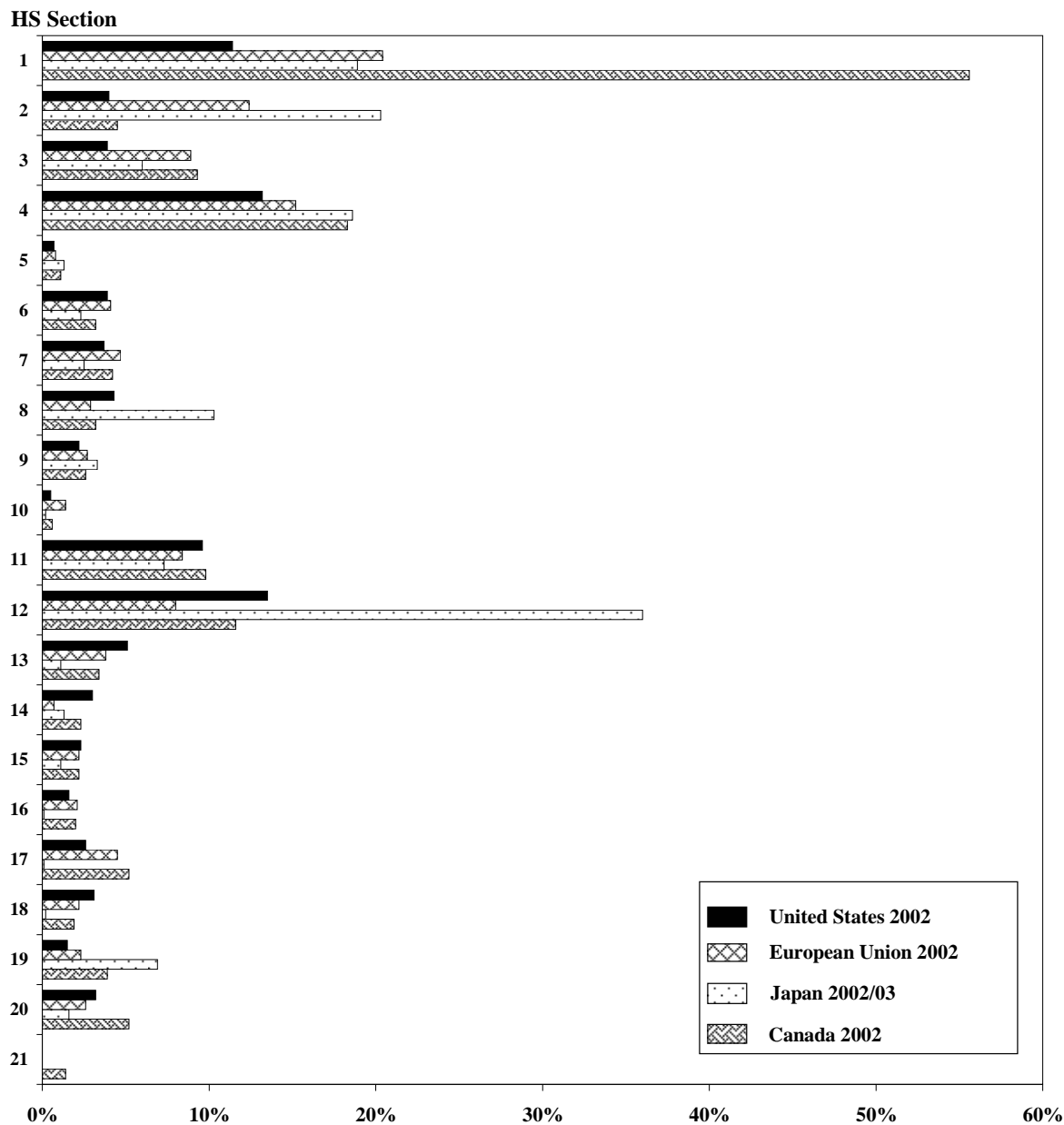
5% of developing countries' total exports to the Quad. Products subject to peaks accounted for 15% to 30% of these countries' total exports to Canada, the EU, and the United States. Up to US\$22 billion of tariff revenue may be collected by Quad Members on those imports subject to such tariff peaks; half of this amount is contributed by developing country exporters and LDC exporters may pay up to US\$200 million in tariff revenue notwithstanding tariff preferences (Hoekman, Bernard, Francis Ng and Marcelo Olarreaga, 2002, "Reducing Agriculture Tariffs Versus Domestic Support: What's More Important to Developing Countries?", CEPR Discussion Paper No. 3576).

<sup>14</sup> Strictly speaking, a uniform, non-zero nominal tariff minimizes the net welfare cost of such protection only if import demand elasticities are uniform across commodities and cross-price effects are negligible. Tariff uniformity may be desirable, however, on administrative simplicity and political grounds. For a discussion of these and related matters, see Panagariya, A. and D. Rodrik, 1993, "Political Economy Arguments for a Uniform Tariff", *International Economic Review* 34(3), 685-703.; WTO (1999), *Trade Policy Review – Solomon Islands*; and WTO (2000), *Trade Policy Review – Papua New Guinea*. A notable example of a country with a nearly uniform tariff since the late 1970s is Chile (see WT/TPR/S/124, *Trade Policy Review – Chile*); in addition, as mentioned, Hong Kong, China and Macau China have zero tariffs, while Singapore's tariff is virtually zero.

<sup>15</sup> See Hoekman, Ng and Olarreaga (2002), p.25.

<sup>16</sup> Mixed (or alternative) tariff rates ensure a minimum (or maximum) level of protection through a choice between an *ad valorem* rate and a specific rate (e.g., 15% or US\$5 per kg., whichever is more).

**Chart 1**  
**Simple average MFN tariff rates for the "Quad", by HS Section**



- |                           |                             |                          |                         |
|---------------------------|-----------------------------|--------------------------|-------------------------|
| 01 Live animals and prods | 07 Plastic and rubber       | 13 Articles of stones    | 19 Arms and ammunition  |
| 02 Vegetable products     | 08 Hides and skins          | 14 Precious stones, etc. | 20 Miscellaneous manufs |
| 03 Fats and oils          | 09 Wood and articles        | 15 Base metals and prods | 21 Works of art, etc.   |
| 04 Prepared food, etc.    | 10 Pulp, paper, etc.        | 16 Machinery, etc.       |                         |
| 05 Mineral products       | 11 Textiles and articles    | 17 Transport equipment   |                         |
| 06 Chemicals and prods    | 12 Footwear, headgear, etc. | 18 Precision instruments |                         |

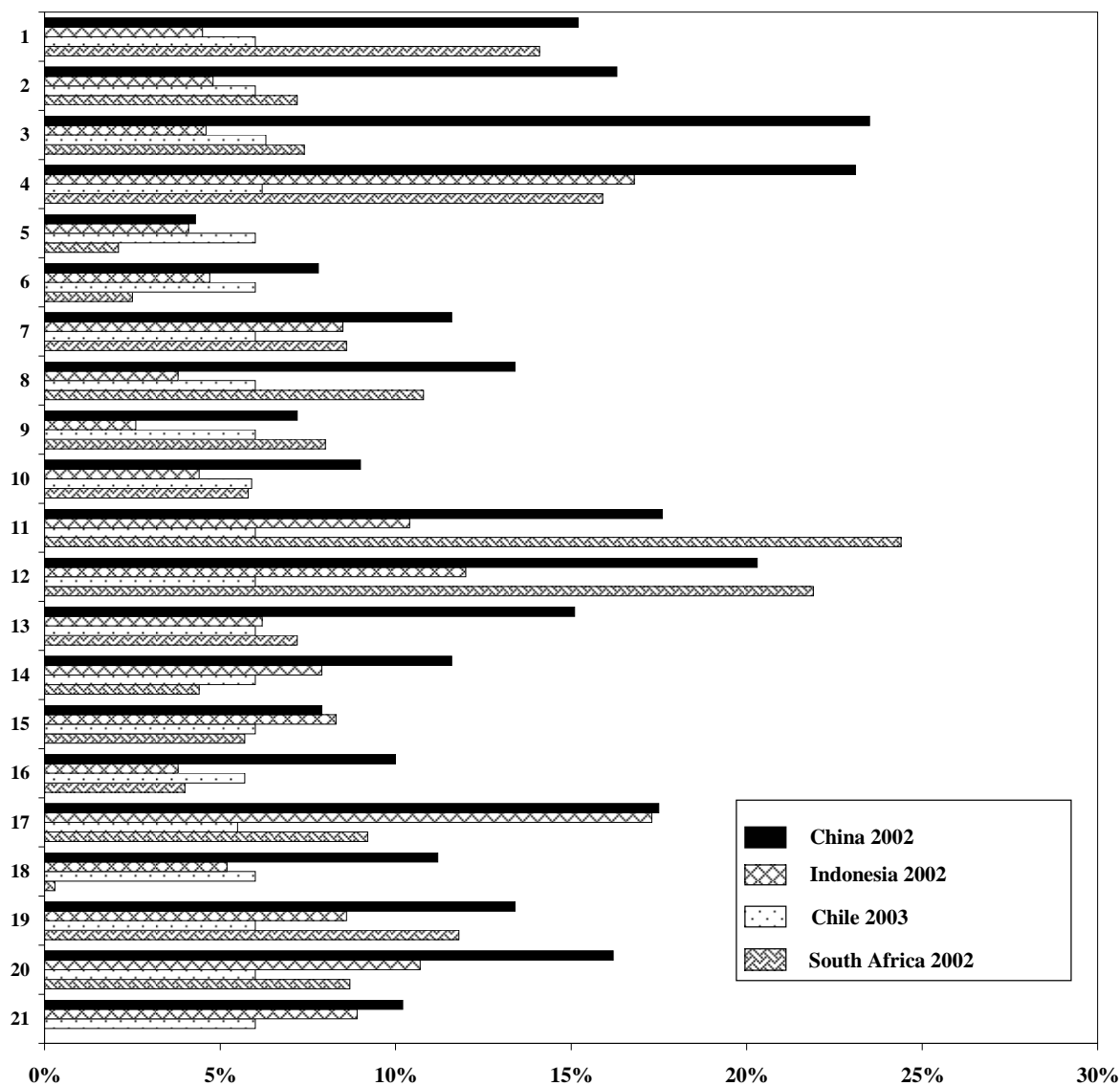
**Note:** Calculations include AVEs where available; where they are not available, the *ad valorem* part is used for alternate and compound rates.

**Source:** WTO Secretariat calculations, based on information provided by Members.



**Chart 2**  
**Simple average MFN tariff rates for selected developing countries, by HS section**

HS Section

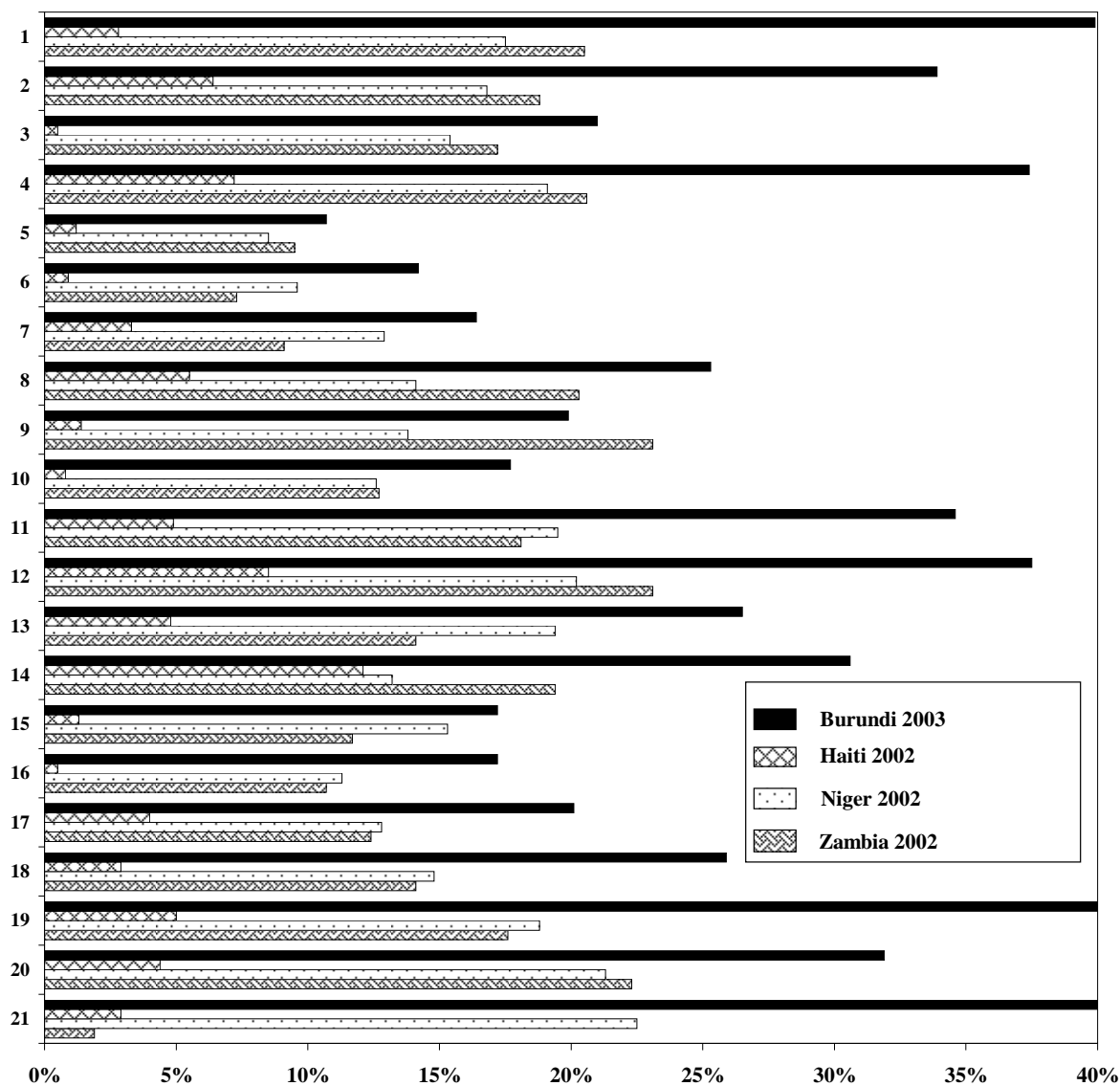


- |                           |                             |                          |                         |
|---------------------------|-----------------------------|--------------------------|-------------------------|
| 01 Live animals and prods | 07 Plastic and rubber       | 13 Articles of stones    | 19 Arms and ammunition  |
| 02 Vegetable products     | 08 Hides and skins          | 14 Precious stones, etc. | 20 Miscellaneous manufs |
| 03 Fats and oils          | 09 Wood and articles        | 15 Base metals and prods | 21 Works of art, etc.   |
| 04 Prepared food, etc.    | 10 Pulp, paper, etc.        | 16 Machinery, etc.       |                         |
| 05 Mineral products       | 11 Textiles and articles    | 17 Transport equipment   |                         |
| 06 Chemicals and prods    | 12 Footwear, headgear, etc. | 18 Precision instruments |                         |

Note: Calculations exclude specific duties and include the *ad valorem* part for alternate and compound rates.

Source: WTO Secretariat calculations, based on information provided by the Members.

**Chart 3**  
**Simple average MFN tariff rates for selected least developed countries, by HS section**  
HS Section



- |                           |                             |                          |                         |
|---------------------------|-----------------------------|--------------------------|-------------------------|
| 01 Live animals and prods | 07 Plastic and rubber       | 13 Articles of stones    | 19 Arms and ammunition  |
| 02 Vegetable products     | 08 Hides and skins          | 14 Precious stones, etc. | 20 Miscellaneous manufs |
| 03 Fats and oils          | 09 Wood and articles        | 15 Base metals and prods | 21 Works of art, etc.   |
| 04 Prepared food, etc.    | 10 Pulp, paper, etc.        | 16 Machinery, etc.       |                         |
| 05 Mineral products       | 11 Textiles and articles    | 17 Transport equipment   |                         |
| 06 Chemicals and prods    | 12 Footwear, headgear, etc. | 18 Precision instruments |                         |

Note: Calculations exclude specific duties and include the *ad valorem* part for alternate and compound rates.

Source: WTO Secretariat calculations, based on information provided by the Members.

21. By contrast, China's tariff appears to be relatively transparent in this regard, with only 0.7% of all tariff lines subject to specific rates. Likewise, specific duties are negligible in Burundi, Chile, Haiti, Indonesia, Niger, and Zambia. Such duties currently apply to roughly one quarter of tariff lines in South Africa, although they are expected to disappear once the UR is fully implemented.

### **Tariff quotas**

22. As a consequence of the UR, and especially the tariffication of agricultural NTBs, tariff rate quotas as a proportion of all tariffs increased considerably in Canada, Japan and the United States, they were already significant in the EU prior to the UR. As a consequence, tariff quotas account for 1.7% of tariff lines in Japan to 3.2% in the EU. Out-of-quota rates (and even in-quota rates) in the Quad, often entail potentially prohibitive tariff peaks. By contrast, China's tariff schedule contains relatively few tariff quotas. While tariff rate quotas were necessary to administer minimum access requirements under the UR, they have left considerable scope for discretion in the allocation of quota volumes, thereby retaining a number of the drawbacks associated with previous quantitative restrictions, which reduce the benefits of tariffication.

### **Tariff escalation**

23. A non-uniform tariff is often used to provide an escalating degree of tariff protection so as to encourage downstream processing. This may be accomplished by levying relatively low duties on raw materials with progressively higher tariffs applied to more processed goods involving greater value added. The outcome is that the level of effective protection increases as goods undergo further processing.<sup>17</sup> What may be mild escalation in nominal tariff terms can provide very high effective (net) assistance to downstream activities.

24. Tariff escalation is a feature of industrial-product tariffs in the Quad. Such escalation is present in the same sectors that are affected by peaks, most notably textiles and clothing, leather and footwear products (Table 4). Tariff escalation is also a feature of China's tariff, for several categories of products, especially textiles and clothing, leather and footwear, wood and furniture, paper, printing and publishing, non-metallic minerals (tariff escalation in selected developing countries and LDCs is shown in Annex 2.) Tariff escalation is a potential impediment to the efficient allocation of resources in the importing country, and it can constitute an obstacle to local processing of domestically produced primary products and of semi-finished goods in the exporting country; consequently, it impedes the industrialization of developing countries and LDCs seeking to export products with higher value added, if not mitigated by the GSP or other preferences.

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<sup>17</sup> The effective rate of protection (ERP) measures the protection provided by the entire structure of tariffs, taking into account those levied on inputs as well as those on outputs. It is defined as  $ERP = (V_D - V_W)/V_W$ , where  $V_D$  is the value added in the given sector at domestic prices, which includes tariffs, and  $V_W$  is value added at world prices. If the nominal tariff on the final product is  $t$ , the share of each imported input  $i$  in the total value of the final product is  $a_i$ , and the nominal tariff on each imported input is  $t_i$ , then the effective rate of protection can be written as:  $ERP = (t - \sum a_i t_i)/(1 - \sum a_i)$ . Thus, if  $t = 10\%$ ,  $t_i = 5\%$  for all inputs and  $\sum a_i = 0.8$ ,  $ERP = 30\%$ . See Corden, W.M., 1971, *The Theory of Protection* (London: Oxford University Press) for a full discussion of the concept of effective protection.

**Table 4**  
**Tariff escalation in the Quad by 2-digit ISIC industry**

		United States 2002	EU15 2002	Japan 2002/03	Canada 2002
Food beverages and tobacco	First stage of processing	3.1	13.2	23.6	10.2
	Semi-processed	7.4	19.1	20.3	6.8
	Fully processed	12.4	18.7	22.6	34.1
Textiles and leather	First stage of processing	2.9	1.0	10.2	1.1
	Semi-processed	9.1	6.7	6.8	6.9
	Fully processed	10.0	9.8	12.0	13.5
Wood and furniture	First stage of processing	0.1	0.0	0.0	0.0
	Semi-processed	2.1	3.0	4.3	2.1
	Fully processed	2.2	2.1	2.0	5.1
Paper, printing and publishing	First stage of processing	0.0	0.0	0.0	0.0
	Semi-processed	0.5	2.1	0.5	0.4
	Fully processed	0.6	1.5	0.3	1.0
Chemicals	First stage of processing	1.9	1.7	2.4	1.5
	Semi-processed	4.3	4.5	2.8	3.0
	Fully processed	3.9	3.8	2.0	4.8
Non-metallic mineral products	First stage of processing	0.0	0.0	0.4	0.0
	Semi-processed	2.1	2.9	1.5	0.7
	Fully processed	5.6	4.0	1.1	3.8
Basic metal	First stage of processing	0.4	0.0	0.4	0.0
	Semi-processed	1.7	1.9	1.1	0.9
	Fully processed	2.5	2.4	0.5	3.7
Fabricated metal products and machinery	Semi-processed	2.7	1.9	1.8	1.5
	Fully processed	2.2	2.5	0.3	2.6
Other	First stage of processing	1.6	1.2	0.2	1.2
	Semi-processed	0.4	1.8	0.1	0.0
	Fully processed	3.6	3.0	2.8	4.8
Total	First stage of processing	3.8	8.1	14.5	5.0
	Semi-processed	4.7	4.9	4.9	3.9
	Fully processed	5.5	7.0	7.8	8.9

Note: For countries with non-*ad valorem* rates AVEs have been used as available. In case of unavailability, the *ad valorem* part is used for compound and alternate rates. Averages differ from those in the DG's Overview 2002, due to changes in concordance between HS and ISIC.

Source: WTO Secretariat calculations, based on data provided by the Members.

### Preferences for developing and least developed countries

25. Applied tariff rates may be lower than MFN rates owing, *inter alia*, to non-reciprocal preferences granted to developing countries under the Generalized System of Preferences (GSP) and other preferences for LDCs. Such preferences are prominent forms of special and differential (S&D) treatment aimed at increasing export opportunities for developing and least developed countries.

26. Under GSP, developed countries discriminate in favour of qualifying developing ones by granting them non-reciprocal tariff reductions below MFN rates for certain products. For example, Quad Members' average GSP rates range from 4.2% to 5.7%; their average applied MFN rates range from 5.2% to 6.9% (Table 5). Recent Trade Policy Reviews of other major providers of GSP preferences show a similar pattern; the differentials between MFN and GSP rates are, however, considerably smaller for "sensitive" sectors such as agriculture, and textiles and clothing, both of which are frequently excluded from GSP and other unilateral preferences.

**Table 5**  
**MFN and developing country preferential tariffs**  
(Per cent)

	MFN	GSP <sup>a</sup>	LDC <sup>b</sup>
United States 2002	5.2	3.7	2.7
WTO agricultural products	10.4	8.4	6.2
Textiles and clothing	9.7	9.4	9.4
EU 2002 <sup>c</sup>	6.4	4.5	1.7
WTO agricultural products	16.1	14.5	9.0
Textiles and clothing	8.4	7.2	0.0
Japan 2002/03	6.9	5.7	3.6
WTO agricultural products	20.0	19.3	18.3
Textiles and clothing	7.0	5.4	0.1
Canada 2002 <sup>d</sup>	6.8	5.4	4.1
WTO agricultural products	21.7	20.8	18.2
Textiles and clothing	9.9	8.9	7.1
Australia 2001/02 <sup>e</sup>	4.3	3.9	1.8
WTO agricultural products	1.3	1.0	0.0
Textiles and clothing	12.3	12.3	8.6
New Zealand 2002	4.1	3.5	0.0
WTO agricultural products	2.1	1.6	0.0
Textiles and clothing	9.5	9.0	0.0
Czech Republic 2001	6.1	5.1	..
WTO agricultural products	13.4	13.2	..
Textiles and clothing	6.6	6.2	..
Slovak Republic 2001	6.1	5.2	4.6
WTO agricultural products	13.2	13.0	13.0
Textiles and clothing	6.7	6.2	5.9

.. Not available.

a Generalized System of Preferences.

b Least developed countries preferences.

c Data for the EU's GSP and LDC rates are based on the 2001 tariff nomenclature.

d Canada has provided duty- and quota-free access to imports of textiles and clothing products from LDCs as of 1 January 2003.

e As of 1 July 2003, Australia has removed all tariffs on LDCs.

Note: Calculations include AVEs where available; where they are not available, the *ad valorem* part is used for alternate and compound rates.

Source: WTO Secretariat calculations, based on data provided by Members.

27. This exception to MFN treatment under the GATT was authorized through a ten-year waiver in 1971 and given permanent legal status in 1979 under the Enabling Clause. Such preferences are

perceived to enhance the ability of developing countries' exporters to compete in developed countries' markets. More than 30 years after the GATT first authorized the GSP as a "temporary" measure, it appears to remain highly popular among developing countries as an important instrument for ensuring their "special and differential treatment" within the multilateral trading system through improved access to developed countries' markets without reciprocal liberalization. Recently, Quad and other industrialized countries have passed legislation providing improved, if not duty-free, access for LDCs for almost all products. More specifically, the United States enacted the African Growth Opportunities Act (AGOA) in May 2000 and the EU enacted the Everything But Arms (EBA) scheme in March 2001.<sup>18</sup> New Zealand (as of 1 July 2001), Norway (as of 2002) and most recently Australia (as of 1 July 2003), have also granted LDCs duty-free access to their markets for all products.<sup>19</sup>

28. However, as Table 5 and numerous studies have shown, protectionist interests in the major developed Members of the WTO greatly curtail the benefits of the GSP so that this scheme is not as advantageous to developing countries as it appears; the broad conclusion of these studies is that GSP has at best yielded only a "modest" increase in imports from beneficiary countries, with some of those gains due merely to trade diversion rather than trade creation.<sup>20</sup> Even in the cases of more recent supplementary initiatives, such as the AGOA and the EBA, analyses suggest that market access will be only slightly improved for the countries concerned.<sup>21</sup> There are several possible reasons for this outcome. First, such preferences are seldom generalized; they frequently exclude precisely those products (e.g. textiles, clothing and footwear) in which developing countries have the greatest comparative advantage, and moreover, where their exports tend to face tariff peaks in major markets. This is evident from preferential tariff rates for LDCs provided by the Quad and other countries in textiles and clothing and agriculture (Table 5). Further, as such preferences are beyond the purview of the binding rules of the GATT/WTO system, they can be unilaterally revoked or modified at any time by the according Member, thereby leading to uncertainty. In particular, a developing country may be "graduated" out of a preference for a product just as it begins to achieve significant success in an export market, thereby discouraging efforts to expand exports.<sup>22</sup> Moreover, conditions may be attached to these preferences in order to obtain concessions from developing countries, sometimes in non-trade areas.<sup>23</sup> Even when eligibility is not a problem, full use of the GSP system and other recent initiatives is hampered by the complexity of the system and technical capacity of developing

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<sup>18</sup> Under AGOA, 38 African countries currently qualify for preferential treatment; in order to qualify for AGOA, the country must already be eligible for GSP treatment. AGOA extends GSP for eligible sub-Saharan African countries until 1 September 2008. The EBA grants duty-free and quota-free access for all products from LDCs except arms and munitions and three agricultural products (bananas, rice, and sugar); tariffs and quotas on the three agricultural products will be liberalized gradually (tariffs will be removed in 2006 for bananas and 2009 for rice and sugar).

<sup>19</sup> Announcement by Hon. Mark Vaile, Minister for Trade on 27 May 2003 [Online]. Available at: [http://www.trademinister.gov.au/speeches/2003/030527\\_development.html](http://www.trademinister.gov.au/speeches/2003/030527_development.html), [8 July 2003]. This follows publication by the Australian Productivity Commission in 2002 of a report concluding that the removal of all barriers to trade with LDCs would have a small impact on Australia (Productivity Commission, 2002, *Removing Tariffs on Goods Originating from Least Developed Countries*, Research Report, October).

<sup>20</sup> See, for example, studies cited in Ozden and Reinhardt (2003), "The Perversity of Preferences: GSP and Developing Country Trade Policies 1976-2000", World Bank Working Paper no. 2955, January.

<sup>21</sup> See, for example, Mattoo, Aaditya, Devesh Roy and Arvind Subramaniam (2002), "African Growth and Opportunity Act and Its Rules of Origin: Generosity Undermined?", World Bank Research Working Paper 2908, October; and Brenton, Paul (2003), "Integrating the Least Developed Countries into the World Trading System: The Current Impact of EU Preferences under Everything But Arms", World Bank Policy Research Working Paper no. 3018, April.

<sup>22</sup> For example, since the GSP scheme of the United States was introduced in 1976, 36 of the 154 eligible countries have graduated.

<sup>23</sup> In some instances, the EU explicitly links its granting of preferences in addition to those provided by the GSP to beneficiary countries' adherence to labour and environmental standards (see for example, WTO, 2000, *Trade Policy Review – European Union*). Likewise, U.S. trade laws allow the President to use GSP to promote labour standards and intellectual property rights; this has been extended to the AGOA Act.

countries' exporters. In particular, certain rules of origin must be satisfied by exporting countries; these rules usually involve a minimum amount of value added, which can be a deterrent to small countries with limited technological capacity. Also, rules of origin often require beneficiaries to use inputs produced in the country granting the preference, with potential adverse effects on their exporters' competitiveness.<sup>24</sup> Last, but not least, developing countries' exports are often impeded by supply-side constraints, including lack of trade finance (possibly owing to market failure) and poor infrastructure.

29. A more fundamental problem with GSP and similar preferences might be that such non-reciprocal preferences may have the effect of delaying trade liberalization by recipients; that is, developing countries removed from GSP tend to adopt more liberal trade policies than those remaining eligible.<sup>25</sup> The reason is that with trade barriers reflecting the Government's balancing of political support from import-competing and export sectors, the non-reciprocity feature of the GSP shifts the balance in favour of the import-competing sectors in developing countries; it does this by reducing one of the main incentives that developing countries' export industries have to oppose protectionist trade policies at home instead of trying to secure the export sectors' support for more liberal trade policies. Further, given that the value of GSP preferences tends to be eroded by negotiated multilateral reductions in MFN rates, they can provide the wrong signal to exporters in developing countries regarding their long-term comparative advantage and might even deter developing countries from agreeing to reductions in MFN rates. The non-reciprocal preferences such as the ACP and AGOA also create a systemic risk by excluding some countries that are already recipients of preferences under a different GSP arrangement; the resulting complex set of preferential trading arrangements arbitrarily exclude certain countries and reduces predictability and stability in the multilateral trading system.<sup>26</sup> This raises the question of what measures, if any, might be taken to help developing countries adjust to the erosion of the tariff preferences they currently enjoy.<sup>27</sup>

30. It is arguable that developing countries might be better served by becoming more fully engaged as WTO Members, with full obligations and rights under the WTO Agreements, than by special GSP-style tariff preferences. Developing countries have no legal avenues to protect their rights under such schemes, and there is evidence that they also tend to prolong protectionist policies among recipient countries. Certain more temporary and targeted forms of special and differential (S&D) treatment might be appropriate, where these are designed to address constraints on developing countries' institutional capacity to implement existing as well as new WTO Agreements and their

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<sup>24</sup> Such sourcing may not be the cheapest available, thus raising the production costs of exporters and affording protection to preference-granting producers of the inputs involved.

<sup>25</sup> See Ozden and Reinhardt (2003).

<sup>26</sup> Page, S. and A. Hewitt ((2002), "The New European Trade Preferences: Does 'Everything but Arms' (EBA) Help the Poor?", *Development Policy Review*, 20 (1), pp. 1-13) point out that in addition to countries such as Guyana and Kenya, other major "losers" from such trading arrangements are the large, poor, developing countries such as India, Pakistan, and Indonesia. However, Pakistan was granted special EU and other preferences and debt relief (for its support in the war in Afghanistan) and has now been added to the list of countries in Latin America who receive additional "super GSP" preferences as part of the war on drugs; Indonesia, as a member of OPEC also receives special preferences. As for the above-mentioned additional preferences under the EU's GSP scheme as part of the war on drugs, the Panel in *EC-Tariff Preference* recently found that the EC measure is inconsistent with Article I.1 of GATT 1994 because it failed to demonstrate that the measure is justified under the Enabling Clause or Article XX(b) of GATT 1994. The EU has appealed this ruling.

<sup>27</sup> According to the IMF, in most LDCs the welfare losses associated with preference erosion are likely to be relatively modest – less than 2% of LDCs' aggregate exports; hence, the countries most affected by the adverse effects of such erosion could be comfortably compensated through increased assistance. Such assistance would be especially important for LDCs that are currently most heavily dependent on such preferences (see "Communication from the IMF: Financing of Losses from Preference Erosion", WTO document WT/TF/COH/14, 14 February 2003).

different developmental priorities, or where additional time and possible assistance might be required to allow the appropriate sequencing of various macroeconomic and structural reforms (including trade liberalization), and for their economies to adjust to these and other reforms.

### **Bilateral and regional preferences**

31. The proliferation of bilateral and regional agreements since the WTO was established in 1995 has eroded the scope of application of MFN tariffs; such discriminatory agreements, which are mainly among developed countries and thereby effectively exclude many developing countries and especially LDCs, constitute a systemic threat to the MFN principle, one of the cornerstones of the WTO. The outcome is that MFN tariffs tend to be the exception rather than the rule, especially for the United States, the EU, and Canada.

## **3. Agriculture ... the most distorted sector**

### **Overview**

32. Agriculture is important in developing countries' economies, accounting for some one quarter of their GDP and about half of their employment;<sup>28</sup> by contrast, agriculture in OECD countries accounts for around 2% of GDP and 7.3% (in 2001) of employment. With nearly three quarters of the world's poor concentrated in rural areas, mainly in developing countries, and depending heavily on agriculture for their livelihoods, trade liberalization in agriculture is crucial to the alleviation of poverty. The conversion of non-tariff barriers into tariffs (through a process of tariffication), the curtailment of subsidies and the establishment of strengthened rules covering market access, domestic support and export competition, were among the major achievements of the Uruguay Round as regards agriculture; tariffication of agricultural NTBs, in particular, paved the way for future reductions in agricultural tariffs.<sup>29</sup> Nonetheless, both tariffs and domestic support for agriculture are still relatively high, especially in many OECD countries. In the "Quad" group of major traders, for example, applied MFN tariffs on agricultural products are far higher than those on non-agricultural products. According to the OECD, total support to agriculture by OECD countries is close to US\$1 billion per day, more than six times all development assistance. Much of this support is linked to production; this encourages higher output resulting in large surpluses, especially in several countries where such support is most generous. Support linked to production in combination with export subsidies drives down world prices of agricultural products and leads to the displacement of developing countries' products, not just from subsidizing countries' markets, but also from their own and third markets, to the detriment of poor farmers in developing and least developed countries. Consequently, agriculture remains the most protected, subsidized, and thus distorted sector of many Members' economies, with far-reaching social and economic repercussions, not just domestically, but globally. According to estimates by the World Bank, phasing out these measures world-wide would raise annual income by over US\$350 billion.<sup>30</sup>

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<sup>28</sup> This suggests that, on average, labour productivity in agriculture in developing countries is roughly one third of the overall level in their economies.

<sup>29</sup> The Uruguay Round Agreement of 1994 resulted in significantly strengthened disciplines of trade-related agricultural policies. The Uruguay Round Agreement on Agriculture (URAA), replaced non-tariff import barriers by bound tariffs, obliged Members to open closed markets, curbed export subsidies, categorized domestic programmes on the basis of their potential to distort trade, and disciplined the most trade-distorting forms of support. Agriculture was also affected by other agreements, notably SPS and TBT, which aimed was to forestall the use of such measures for purposes of protection.

<sup>30</sup> Liberalization of the sugar market, for example, would result in an increase of some 20% in international trade and income gains of some US\$4.7 billion, most of which would go to the poor (World Bank, 2004, *Global Economic Prospects*, 2004).



33. Agricultural support programmes are justified by some Members using them as necessary to address non-trade concerns, including income support for agricultural households, preservation of the environment, and food security. While this view is widely shared among WTO Members, some attach more importance to them than others. The debate, therefore, has been largely about the magnitude of total support to agriculture together with the appropriateness and effectiveness of various measures aimed at achieving these objectives. Trade-distorting measures are unlikely to be effective instruments in addressing non-trade concerns.

34. Clearly, domestic agricultural policies and international trade are closely intertwined; protective border measures are often necessary for the maintenance of domestic support programmes. In particular, a domestic support programme that holds the domestic price above the world level requires accompanying import restrictions, such as tariffs. Furthermore, to the extent that domestic support programmes are high enough to generate a production surplus, export subsidies are frequently used to help dispose of the surplus.

#### **Indicators of government assistance**

35. Total support to agriculture by OECD countries, as measured by the total support estimate (TSE), remains high; indeed, it is estimated to have increased slightly, from US\$311 billion in 2001 to US\$318 billion in 2002, roughly equivalent to sub-Saharan Africa's annual GDP.<sup>31</sup> The EU, Japan, and the United States collectively account for over four fifths of such support, although as a percentage of the value of gross farm receipts, support is highest in Switzerland, Norway, Korea, Iceland, and Japan. Total support was the equivalent of 1.2% of GDP in the OECD area, compared with an annual average of 2.3% in the peak 1986-88 period, when the Uruguay Round negotiations were under way. Agriculture's contribution to GDP in the OECD area is currently about 2%. In Japan, Korea, Norway, and Switzerland, total support to agriculture is close to, or even exceeds, the sector's contribution to GDP.

36. Nearly three quarters of total support is provided to farmers. Such support, as measured by the producer support estimate (PSE), rose slightly from US\$231 billion in 2001 to US\$235 billion in 2002; this represents 31% of total farm receipts, the same as in 2001, but down from 38% in 1986-88. The corresponding PSEs for Japan, the EU, Canada, and the United States were 59%, 36%, 20% and 18%, respectively. Thus, for every 100 yen a Japanese farmer earned in 2002, 59 yen came from support measures. Support levels in 2002 were the lowest in New Zealand (1%) and Australia (5%)<sup>32</sup>; they were highest in Iceland, Korea, Norway, and Switzerland, where they ranged between 63% and 75%. Rice, sugar, and milk are the most supported commodities, with transfers to producers close to, or exceeding, half of gross receipts for these products.

37. As reflected in the producer nominal protection coefficient (NPC), prices received by OECD farmers in 2002 were on average 31% above world prices (compared with 57% in the mid-1980s), thereby shielding farmers in many countries from world market signals. Whereas in Australia and New Zealand, prices received by farmers were, on average, the same as those at the border, they were 10% higher in the United States, 35% higher in the EU, and more than double in Iceland, Japan, Korea, Norway, and Switzerland.

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<sup>31</sup> OECD (2003), *Agricultural Policies in OECD Countries: Monitoring and Evaluation*, 28 April 2003 (AGR/CA/APM(2003)1/FINAL). These estimates include "Green Box" measures.

<sup>32</sup> While government support in Australia and New Zealand is low, these countries have relatively strict sanitary and phytosanitary regulations, which they consider necessary to ensure that the reputation of these island economies as reliable exporters of high quality agricultural products is not jeopardized by pests and diseases, but which nonetheless tend to impede imports of such products. (See WTO, 2003, *Trade Policy Review – Australia*; and WTO, 2003, *Trade Policy Review – New Zealand*).

38. At the same time, the prices paid by OECD consumers (consumer NPC) in 2002 were on average 37% higher than world prices. Whereas in Australia prices paid by consumers were, on average, the same as those at the border, they were 10% higher in the United States, 42% higher in the EU, and more than double in Japan, Korea, Norway, and Switzerland. Overall, consumers in OECD countries were implicitly taxed at a rate of 24% (percentage consumer support estimate (CSE)). The implicit tax rates are negligible in Australia, New Zealand, and the United States; they exceed 50% in Japan, Korea, Norway, and Switzerland.

39. Output-based support (market price support (MPS) and output payments (OP)) and input subsidies remain the dominant forms of producer support in most OECD countries, together accounting for more than three quarters of support to producers, compared with 90% in 1986-88. These measures are the most distorting forms of production and trade assistance; they contribute to over-production in the OECD area to the detriment of the supporting countries themselves, of OECD Members, where support is relatively low, and of developing countries.<sup>33</sup>

40. Government intervention in agriculture is also extensive in many developing countries. Tariff bindings on agricultural products can be just as high or even higher in developing as in OECD countries, although applied rates are often below bound rates. Subsidies in developing countries tend to be lower than those in developed countries owing to budgetary constraints.<sup>34</sup> In a number of developing countries, agriculture is actually "taxed" due to factors such as overvalued exchange rates, low government procurement prices or export taxes levied on agricultural commodities.

### **Objectives of support and related measures**

41. Farm support programmes have multiple domestic objectives, including: income support for agricultural households; preservation of the environment, notably traditional rural life and amenities; food security; and food safety.<sup>35</sup> Some of these objectives result from situations where markets alone may fail to achieve a socially desirable outcome owing to the existence of "externalities" or "public goods".<sup>36</sup> Accordingly, two broad types of agricultural policies can be distinguished; those intended to redistribute income, and those aimed more at addressing market failure. In this regard, there would appear to be a serious mismatch between these objectives and the policy measures designed to achieve them, thus casting doubt on the appropriateness and effectiveness of such measures. In designing policy, income support objectives need to be distinguished clearly from those concerning the correction of market failure. Moreover, one instrument needs to be targeted at one objective.

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<sup>33</sup> Under the WTO Agriculture Agreement, domestic support measures that are considered to distort production and trade (with some exceptions) fall into the so-called "amber box", which is defined in Article 6 of the Agreement as all domestic support other than that in the "blue" and "green" boxes. The "blue" box covers support under production-limiting programmes. "Green" box subsidies are those that do not distort production or involve minimal distortion. Whereas in the United States and Japan "amber" box subsidies accounted for less than one quarter of total domestic support in 1998 (the latest year for which such data are available), such subsidies accounted for more than half of total support in Canada and the EU.

<sup>34</sup> Some developing countries, including India, are heavy users of certain forms of subsidies, notably for inputs such as fertilizer, power and water (WTO, 2002, *Trade Policy Review – India*, p.106).

<sup>35</sup> OECD (2002), "Agricultural Policies in OECD Countries: A Positive Reform Agenda", 6 November 2002 (COM/AGR/TD/WP(2002)19/FINAL).

<sup>36</sup> An externality arises where a decision by one agent, whether a producer or consumer, has side-effects that impinge on others. For example, farms may produce excessive pesticide residues (negative externalities) as well as crops; they may also produce environmental as well as aesthetic benefits (positive externalities). In these cases, the market-determined output may be higher than optimal because of unpaid external costs or sub-optimal owing to uncompensated external benefits. A public good, such as clean air or an attractive countryside, is a good for which the use by one agent does not diminish the amount available to another. A public good may be a joint output, and therefore an externality, of private production. As in the case of positive externalities, the market tends to result in too few public goods.

### *Income support*

42. Policy measures linked to production and consumption are relatively inefficient instruments for delivering income support to rural households. According to OECD estimates of income transfer efficiency, no policy measure linked to agricultural activity succeeds in delivering more than half of the monetary transfers from consumers and taxpayers as additional income to farm households.<sup>37</sup> The proportion is one quarter or less in the cases of market price support and deficiency payments, and less than one fifth for input subsidies. Notwithstanding its low income transfer efficiency, roughly two thirds of agricultural support in OECD countries involves measures that keep product prices above levels that would otherwise prevail. An intrinsic feature of measures based on agricultural activity is that they cannot be targeted at relatively poor households. In the case of open-ended price support, the size of the transfer is directly proportional to the level of production. Consequently, the bulk of the support that reaches farmers goes to the larger ones, many of whom already have higher incomes. It is not surprising, therefore, that under the CAP, 70% of support (that is, market price support plus payments to producers) is allocated to the largest 25% of the EU's farms<sup>38</sup>; in the United States, Canada, and Japan the corresponding amounts of support allocated to the largest 25% of farms are 89%, 75% and 68%, respectively. In contrast to the above measures, direct income payments are much more efficient in delivering income support, especially if they are de-coupled from agricultural activity; such payments can also be targeted more easily at those households felt to be most in need of assistance. If the current production-based support measures were replaced by direct income payments, efficiency costs could be halved without reducing the incomes of farm households.<sup>39</sup> The savings would be even greater if support were targeted at lower income farm households through the income tax system or social security programmes. The more a policy measure pays to domestic farmers without affecting their production decisions, the greater the share of income retained by farm households and the lower the impact on production and trade.

43. In addition, by distorting production and trade, such support, including export subsidies, has a negative impact on farm incomes in third countries, including developing countries, because such support drives down international prices and increases their volatility. Consequently, returns from agriculture in developing countries are lower than otherwise, thus exacerbating poverty.

### *Correction of market failure*

44. Governments also justify assistance for agriculture on the grounds that market-oriented agriculture would fail to take due account of externalities, such as the protection of the environment, a non-trade concern explicitly mentioned in the Preamble of the WTO Agreement on Agriculture. In their view, a certain level of domestic support and border protection is necessary to maintain agricultural production, especially in areas with low agricultural potential, and thus ensure provision of environmental externalities. This reflects a perception that there is a very close relationship between agricultural production and the provision of positive externalities, including those associated with public goods. In fact, there is very little evidence on the extent of the externalities generated by agriculture, which makes it very difficult to measure the full benefits of government support measures and thus to ensure that these benefits are not outweighed by their costs. Hence, it is also difficult to compare the effectiveness of different support measures in achieving their objectives. In any event, there are very few cases or circumstances where jointness in production exists and even in such instances, trade-distorting measures are unlikely to be effective instruments for addressing the problem.

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<sup>37</sup> OECD (2002), *The Incidence and Efficiency of Farm Support*.

<sup>38</sup> Farms are classified according to the size of their gross sales (for more details, see OECD, 2002, "Farm household income issues in OECD countries: a synthesis report", AGR/CA/APM(2002)FINAL, Paris).

<sup>39</sup> OECD (2002), "Agricultural Policies in OECD Countries: A Positive Reform Agenda", 6 November 2002 (COM/AGR/TD/WP(2002)19/FINAL, p. 34).

45. The externalities generated by agriculture are not exclusively positive, however; there may also be some significant negative externalities, directly linked to production. Thus, protection and domestic support policies may encourage environmentally harmful agricultural practices, including high use of fertilizers and pesticides. The outcome is resource degradation and environmental stress, such as adverse effects on the ground water, the soil, and biodiversity. Furthermore, by depressing incomes and exacerbating poverty in developing countries, such policies make it more difficult for farmers in these countries to move towards more environmentally sustainable practices.

46. Governments may also be concerned by the possible failure of market forces to ensure food security; this may be threatened by sharp increases in food prices, which make food unaffordable owing to supply shocks caused by adverse climatic conditions, diseases, wars or embargoes. As highlighted above, however, in most OECD countries domestic prices are already considerable higher than world prices. Heavy reliance on domestic production exposes countries to the risk of domestic crop failure due, for example, to floods and droughts, as well as to interruptions in the supply of key inputs (such as fuel) that are essential for food production. The effects of supply shocks can be mitigated more effectively by a combination of domestic production, maintenance of domestic production capacity, stockholding, and access to a wide range of foreign suppliers.

47. Multilateral trade liberalization of agriculture, including the removal of subsidies, may result in higher world prices, and thus cause food import bills to rise in some developing countries, with a potentially negative short term effect on food security, and the poor being the hardest hit. However, these negative short-term terms of trade effects have to be weighed against the benefits associated with the longer-term allocation effects; that is, higher food prices would encourage greater production in developing countries and result in higher incomes, including for poor farmers, and thus increased purchasing power. Even in developing countries, food security is achieved most effectively at the household level by alleviating poverty and then by allowing households to buy food from domestic or foreign sources at prices that are not artificially inflated by import barriers. In India, where food security has long been a major policy objective, support has contributed to burgeoning costs associated with the accumulation of grain stocks that greatly exceed food security needs.<sup>40</sup>

### **Agriculture and the Doha Development Agenda**

48. More careful design and better targeting of agricultural policies would enable governments not only to pursue their multiple objectives in a more cost-effective manner, but with minimal disruption to international markets for agricultural products. The Doha Development Agenda (DDA) presents Members with the opportunity to achieve such reforms multilaterally, thereby benefiting industrialized and developing countries alike. According to the IMF, removal of agricultural support (tariffs and subsidies) as part of a comprehensive effort to lower trade barriers would raise global economic welfare by US\$128 billion annually, the bulk of which appears to be due to the removal of tariffs.<sup>41</sup> While nearly US\$98 billion of this welfare gain would accrue to industrial countries, through more efficient production and lower food prices for many consumers, the benefits to developing countries would also be substantial, at some US\$30 billion.<sup>42</sup> These gains are particularly large for food-exporting regions, including sub-Saharan Africa, where many of the world's poorest live.

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<sup>40</sup> WTO (2002), *Trade Policy Review – India*, p. x.

<sup>41</sup> The estimated US\$128 billion relates only to static gains; dynamic gains (from higher investment and faster productivity growth) may well be several times larger (IMF, *World Economic Outlook*, 2002, September, p. 85).

<sup>42</sup> According to a recent study by Hoekman, Bernard, Francis Ng and Marcelo Olarreaga, 2002, "Reducing Agriculture Tariffs Versus Domestic Support: What's More Important to Developing Countries?", CEPR Discussion Paper No. 3576), a 50% cut in tariffs would have a much greater positive effect on the exports and welfare of developing countries than a 50% cut in domestic support.

49. Despite the large overall gains from liberalization of agriculture, some developing countries may gain very little, or even be harmed, by liberalization – unilateral or multilateral – of commodity markets particularly in the short-term. For example, there is some evidence that the long-run benefits of liberalization in the cocoa market, where changes have been most pronounced, accrue largely to consumers in developed countries at the expense of the exporting countries (owing to loss of implicit or explicit export taxes) and farmers in non-liberalizing countries; farmers in liberalized African markets are broadly neither better nor worse off.<sup>43</sup> However, the DDA addresses all agricultural products, including processed products, and reducing tariff escalation will create opportunities to move up the value-added chain and away from commodities that are undergoing long-term price declines anyway and are often subject to significant price fluctuations. Some of the greatest losses would affect developing countries that depend on preferences to gain access to their main export markets. The value of these preferences is already being eroded through regional trade agreements and preferences granted to other developing and least-developed countries, but tariff reductions under the multilateral process would also contribute to preference erosion. As production and export subsidies are reduced, net food-importing countries may also face increased food import bills as prices rise, at least in the short term. For these, and others that may lose out in liberalization, it may be necessary to develop complementary policies and, in some cases, assistance from international agencies designed to redress the unfavourable effects.<sup>44</sup>

50. While agriculture is of great immediate importance to developing countries, commodity prices have been in long-term decline, with occasional price peaks, for at least forty years. This trend has been exacerbated by the high levels of protection throughout the world, including production and export subsidies in many OECD countries.<sup>45</sup> Reducing competition from production and export subsidies and improving access to export markets will benefit efficient producers in developing countries. However, as prices and terms of trade continue to decline, agricultural exporters will find that they have to export increasing volumes of commodities in exchange for the same value of manufactured goods and services. Therefore developing countries need to look beyond exporting primary agriculture and towards processed products and even beyond agriculture, in the current negotiations. Furthermore, for developing countries to fully benefit from lower protection of agriculture (and other sectors), they also need to overcome a wide range of supply constraints on their exports. These constraints include a lack of finance and poor infrastructure but also national policies that discourage agricultural development.

#### **4. Market access in textiles and clothing**

##### **Introduction**

51. Overall, the implementation of the Agreement on Textiles and Clothing (ATC) is on track. The Agreement will terminate on 31 December 2004. As scheduled, the quantitative restrictions

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<sup>43</sup> Whereas producer prices have tended to rise as a share of f.o.b. prices, as intermediation costs and tax have declined, the downward shift in the aggregate supply curve in conjunction with inelastic demand results in lower world prices. Farmers thus get a larger share of a lower price (see Gilberts, Christopher, and Panos Varangis, 2003, *Globalization and International Commodity Trade with Specific Reference to the West African Cocoa Producers* in R.E. Baldwin and L.A. Winters, Eds, *Challenges to Globalization*, NBER).

<sup>44</sup> The vulnerabilities of poor countries and net food importing nations has been recognized in the WTO through the Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on LDCs and net food importing countries.

<sup>45</sup> The above example concerning cocoa highlights the limits to the benefits accruing to producer countries from the liberalization of trade in commodities whose demand is not very elastic. As noted, a deterioration in the terms of trade can reduce the beneficial impact of growth on economic welfare in an open economy. If the deterioration in the terms of trade more than outweighs the primary gain from growth, the outcome is "immiserizing" growth (see Bhagwati, J., 1958, "Immiserizing Growth: A Geometrical Note", *Review of Economic Studies*, 25, pp. 201-205).

covered by the Agreement will be eliminated and trade in the sector will be integrated into normal GATT/WTO rules at the end of 2004. The expiry of the ATC will be a landmark for the multilateral trading system, marking the completion of the implementation of one of the major results of the Uruguay Round. Multilateral rules will be re-asserted over trade in the sector. Implementation will contribute to growth in the global economy through efficiency gains. Nonetheless, at the same time as the termination of the Agreement draws closer, questions are being posed and issues being raised about: the adjustment costs; competitive challenges; and, the evolution of the structure and trade flow patterns in the post-ATC trading environment.

### **Quotas to be phased out**

52. The Agreement on Textiles and Clothing (ATC) envisages a removal of all quantitative restrictions on imports of textiles and clothing by 31 December 2004. Quotas are being integrated into GATT/WTO Rules in three stages (1995-1997; 1998-2001; and 2002-2004). At the beginning of each stage, Members were required to integrate a minimum 16%, 17%, and 18%, respectively, of their total volume of imports of textiles and clothing in 1990 that were covered by the ATC. Each stage had to include products from each of the four main categories (tops and yarns; fabrics; made-up textile products; and clothing), although the combination of these products to be liberalized could be chosen by each Member concerned. Finally, the remaining quotas had to be increased by at least 16%, 25%, and 27%, respectively, in each of the three stages, to provide improved market access to exporting countries.

53. In the WTO, developing countries argue that the integration thus far, while in line with the phases envisaged by the ATC, has been based on "backloading" with a majority of imports (both products and quotas) to be liberalized only in the final stage. Reviews of the first and second stages of integration, undertaken by the WTO's Textiles Monitoring Body, found that all countries that undertook the integration programme as well as those applying quotas under the ATC (Canada, the European Union, Norway, and the United States), had met the minimum integration requirements. Norway, moreover, phased out all its restrictions between 1996 and 2001. For the other three Members, however, the overall elimination of restrictions maintained under the ATC had been relatively modest. The reviews also found that the products selected for integration had been concentrated in the lower value added range of products suggesting, first, escalation in non-tariff protection (greater protection extended to higher value products), and second, that the concentration on lower value added products would impede developing countries' efforts to move up the value added chain. To address some of the concerns of the developing countries, Ministers at Doha requested the Council for Trade in Goods to examine and make recommendations to the General Council for appropriate action proposals concerning the calculation of quota levels for the remaining period up to 31 December 2004.<sup>46</sup> However, consensus could not be reached on this issue and the discussions concluded without agreement.<sup>47</sup>

### **Tariffs are an additional barrier to trade**

54. While the ATC's quotas are the most restrictive aspect of international trade in textiles and clothing, the sector is also subject to relatively high tariff protection in most developed and developing countries. In the Quad, for instance, while the overall simple average MFN tariff ranges from 5.2% to 6.9%, the simple average for textiles and clothing is higher, ranging from 7% to almost 10%. Textiles, clothing and leather (along with food, beverages and tobacco) is also subject to higher escalation than other sectors (Table 4). In addition, the textiles and clothing sector is often subject to

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<sup>46</sup> Paragraphs 4.4 and 4.5 of the Doha Ministerial Decision on Implementation-Related Issues and Concerns (WTO document, WT/MIN(01)/17, 20 November 2001).

<sup>47</sup> WTO documents WT/GC/M/75, 27 September 2002; and WT/GC/70, 14 February 2003.

non-*ad valorem* tariffs, such as specific, compound or alternative duties<sup>48</sup>; these rates often tend to conceal tariff peaks and also render the tariff more complex and make an analysis of the level of tariff protection in the sector difficult. The sector is most frequently excluded from preferential tariff rates granted to developing and LDCs under programmes such as the Generalized System of Preferences and other preferences for LDCs; with the exception of the EU and New Zealand, whose rates on textiles and clothing are zero for LDCs, and Japan (0.1%), other countries provide relatively few preferences for this sector; Australia announced recently that as of 1 July 2003, it was removing all tariffs on imports from LDCs, while Canada removed all tariffs and quotas on imports of textiles and clothing from LDCs on 1 January 2003 (Table 5).<sup>49</sup> Insofar as the import prices of textiles and clothing decline, they can also result in an increase in "real" tariff protection.<sup>50</sup>

55. The situation regarding MFN rates is similar in developing countries. Of countries reviewed recently under the TPRM, developing countries that have a significant textiles and clothing sector continue to protect against competition through relatively high tariffs. South Africa's simple average MFN rate for textiles and clothing, for example, was 24.4% in 2002, compared with an overall simple average rate of 11.4%. Morocco also has relatively high protection at 39.2%, and the tariff for textiles and clothing in China is 17.5%, compared with an overall rate of 12.3% in 2002. Tariffs on textiles and clothing are high in other major developing country exporters also: 31.5% in Bangladesh (1999/2000); 31.3% in India (2001/02); 26.4% in Pakistan (2001); 24% in Mexico (2001); and 21.7% in Thailand (2003). Developing countries maintain a high percentage of non-*ad-valorem* tariffs for the sector, including South Africa (77.2%), Thailand (40.9%), and India (32.7%).

56. Thus, while quotas and tariffs are major barrier to exports to industrialized countries, tariffs in several developing countries are extremely high. This is especially true for major exporters of textiles and clothing. For many such countries, moreover, with the major exception of China, tariffs for these products were bound at considerably higher rates than the current applied rates. Therefore, they will not necessarily fall from their present rates and will continue to be barriers to trade in the post-ATC period. These tariff peaks will have negative implications for market access for other developing countries and LDCs and could prevent expansion of south-south trade.

### **Preparing for the end of the ATC: Are Members Ready?**

57. Much of the discussion in the WTO has been on monitoring the stages of integration and less on whether countries (both importers and exporters) are sufficiently prepared for a post-ATC, quota-free regime. Considerable research has been done recently to try and quantify the welfare gains and losses in importing and exporting countries. In general, there appears to be consensus that welfare gains from the integration of textiles and clothing into GATT 1994 are likely to be considerable. Moreover, the major importers that maintain quotas have accepted that the quotas will be removed at the end of 2004 and that appropriate adjustments will have to be made.<sup>51</sup> However, given that most quota holders have only liberalized the minimum 51% share of their trade volume, implying therefore, the removal of the remaining 49% by the end of 2004, this will require a major readjustment over a relatively short period. It is not clear what the welfare implications of a possible surge in imports

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<sup>48</sup> Amongst the Quad countries, for example, the range is wide: the percentage of *ad valorem* rates in textiles and clothing is 99.8% for the European Union, 98.8% for Canada, 92.1% for the United States, and 88% for Japan.

<sup>49</sup> WTO (2003), *Trade Policy Review – Canada*, WTO Geneva.

<sup>50</sup> In the United States, for example, the *ad valorem* equivalents of specific rates applied to certain clothing items increased between 1997 and 2002.

<sup>51</sup> This was reaffirmed at a recent meeting on textiles and clothing organized by the European Commission in May 2003. Online information available at: [http://trade-info.cec.eu.int/textiles/prog\\_en.pdf](http://trade-info.cec.eu.int/textiles/prog_en.pdf), [10 July 2002].

resulting from this relatively short period of liberalization will be and whether such surges may lead to the use of other forms of protection.<sup>52</sup>

58. There have been several quantitative studies on the welfare impact of textiles-trade liberalization on an overall basis and also for groups of, and individual, countries. In general they find that the overall welfare impact will be positive although the size of the overall gains depends on the basic assumptions of the models and their specifications.<sup>53</sup> The overall welfare effects on developing countries will also depend on the loss of quota rents associated with the ATC. In most countries whose exports are currently constrained under the ATC, higher prices paid by consumers in the importing countries are transferred to the exporting country in the form of quota rents. These will be eliminated once the quotas are removed. There will also be adjustments within the textiles and clothing sector and between it and other sectors in the economy as economic resources adjust to changing demand conditions. There may even be shifts within the textiles and clothing sector itself as exporters base their output on comparative advantage rather than pre-set quotas.<sup>54</sup> Thus, while it is true that overall welfare is likely to be increased as a result of a removal of quotas under the ATC, there will be benefits and losses as firms in various countries adjust to changing market conditions and a different set of economic signals. In addition, there will be an impact on upstream producers of cotton, an industry which is currently suffering from overproduction and a long-term downward trend in commodity prices.

59. China's accession to the WTO brought it within the rules of the ATC. Therefore, quotas on China's exports of textiles and clothing are scheduled to be removed by 2005<sup>55</sup>, except for the safeguard measures that its trading partners could use.<sup>56</sup> The removal of these quotas is expected to bring about significant welfare changes for major importers of textiles and clothing, for the Chinese textiles and clothing sector, for China's major competitors and lower consumer prices globally. Various analyses have been carried out using different models and methodologies, most of which point to major market share gains for China with the removal of quotas.<sup>57</sup>

60. While the overall impact on welfare (especially consumer welfare) of a removal of quotas in the major importing and quota-holding countries is positive<sup>58</sup>, a removal of quotas will necessitate considerable industrial restructuring in these countries. As is the case for developing countries, the

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<sup>52</sup> As discussed further below, pressure is already growing on governments to deal with such surges through safeguard measures.

<sup>53</sup> For a review see OECD (2003), "Liberalizing Trade in Textiles and Clothing: A Survey of Quantitative Studies", Working Party of the Trade Committee, Trade Directorate, (TD/TC/WP(2003)2/Rev 1), 1 April.

<sup>54</sup> One of the reasons given by exporting countries for their inability to fill quotas in some subsectors is that they do not have comparative advantage in those particular products; they argue that once the constraints are removed, production will shift into subsectors in which they do have comparative advantage (but are currently constrained).

<sup>55</sup> See WTO Press/243, 17 September 2001, "WTO successfully concludes negotiations on China's entry".

<sup>56</sup> These are listed in China's Protocol of Accession to the WTO; textiles safeguards can be used for an eight-year period and the Transitional Product Specific Safeguard measures can be used for a 12-year period following China's accession in 2001.

<sup>57</sup> See for example, Ianchovichina, E. and W. Martin (2001), "Trade Liberalization in China's Accession to the World Trade Organization", World Bank Working Paper no. 2623, June; Ianchovichina, E. and W. Martin (2003), "Economic Impact of China's Accession to the World Trade Organization", World Bank Working Paper no. 3053, May; and T. L. Walmsley and T. W. Hertel (2001), "China's Accession to the WTO: Timing is Everything", *World Economy*, August 24(8), pp. 1019-1049.

<sup>58</sup> For example, the annual welfare gains for consumers in the EU were estimated at some ECU 25 billion based on tariffs and quotas in 1997, Francois, J.F., H. H. Glismann, D. Spinanger (2000), "The Cost of EU Protection in Textiles and Clothing" Kiel Institute of World Economics, Working Paper no. 997, August.



size of the impact varies depending on the assumptions used, although various studies expect a contraction in textiles and clothing subsectors in these countries.<sup>59</sup> Some of the studies point out, however, that while the textiles and clothing sector will contract, there will be positive readjustment effects in other sectors.<sup>60</sup>

61. The considerable adjustment costs of dismantling quotas and the fact that 49% of quotas must be removed over a relatively short period, raises the question of whether the adjustment can be made in an orderly manner.<sup>61</sup> The importing countries have reaffirmed their commitment to removing all quotas by the end of 2004, as planned under the ATC. However, developing countries worry that the backloading of the ATC, whereby most quotas are to be liberalized only at the end 2004, may lead to a surge in imports of textiles and clothing into industrialized countries and therefore to the imposition of trade defence measures such as anti-dumping and safeguard measures.<sup>62</sup> Several Members have already expressed concern about the use of anti-dumping measures against their exports of textiles and clothing products. China, as one of the largest exporters of textiles and clothing and a recent Member of the WTO may be particularly vulnerable as, under its protocol of accession to the WTO, other WTO Members may take special safeguard measures to protect themselves from surges in imports of textiles and clothing from China. An added concern is the complexity of rules of origin concerning preferential access to markets. Ministers, at the Fourth Ministerial Conference, held in Doha in 2002, agreed that Members would exercise restraint for a period of two years following the end of the ATC, on their use of anti-dumping measures and would also notify any changes to their rules of origin concerning textiles and clothing to the Committee on Rules of Origin, for examination.<sup>63</sup>

62. An added concern among a number of developing countries is that despite having comparative advantage in the sector, they will continue to be at a disadvantage because of a growth in regional and bilateral preferential trading arrangements. They argue that these arrangements have already eroded market access for third countries because the ATC and MFN tariffs are higher than preferential tariffs, sometimes by a considerable margin.<sup>64</sup> The end of the ATC will remove the quota but market access will still be impeded by the difference between MFN and preferential tariffs for countries outside such agreements; this includes large exporters such as China, India, and Pakistan, although Pakistan was recently granted duty-free (but not quota-free) access to some markets. Recent research on preferential agreements between the EU and countries bordering the Mediterranean Sea,

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<sup>59</sup> See for example, Francois, J. F., H.H. Glissmann and D. Spinanger (2000), "The Cost of EU Protection in Textiles and Clothing," Kiel Institute of World Economics, Working Paper, no. 997, August; Cline, W. (1987), *The Future of World Trade in Textiles and Apparel*, Institute for International Economics, Washington DC; and Hanson, K.A. and K.A. Reinert, (1997), "The Distributional Effects of U.S. Textile and Apparel Protection" *International Economic Journal*, Vol. 11, No. 3, Autumn.

<sup>60</sup> Francois, J. F., H.H. Glissman and D. Spinanger (2000), find that while textiles and clothing will be affected negatively, positive readjustment affects will be felt in other industries, notably heavy manufacturing.

<sup>61</sup> Spinanger, D. (1999), "Faking Liberalization and Finagling Protectionism: The ATC at its Best", Background Paper for ERF/IAI/World Bank Workshop, "Preparing for the WTO 2000 Negotiations: Mediterranean Interests and Perspectives", Cairo, 14-15 July, points out that in addition, the 49% probably includes the most sensitive products, which are thus still subject to market access restrictions; these are also products that have the highest tariff rates and were reduced less in the course of the Uruguay Round negotiations.

<sup>62</sup> This was claimed recently by the Small Industries Development Bank of India (SIDBI) and supported by the Secretary General of the Indian Cotton Mills Federation ("Rich Nations Likely to Resort to Non-tariff Barriers after Quotas", *Financial Express*, 4 March 2003). See also Spinanger, D. (1999), "Faking Liberalization and Finagling Protectionism: the ATC at its Best".

<sup>63</sup> WTO document WT/MIN(01)/17, 20 November 2001.

<sup>64</sup> That preferential agreements, notably NAFTA, impeded market access for exports from other countries, was one of the reasons put forward by India for some of its quotas remaining unfilled (WTO, 2002, *Trade Policy Review – India 2002*).

for example, suggests that there are considerable advantages to being in such preferential agreements.<sup>65</sup>

63. There is also concern that LDCs will be least able to adjust to a post-ATC world and it has been suggested that preferential access for these countries should be maintained by the major importers.<sup>66</sup>

## 5. Contingency measures

64. Trade remedies, such as anti-dumping and countervailing measures and safeguards, are permitted under the WTO Agreements subject to certain prescribed rules. For instance, if a government has sufficient evidence that imported goods are dumped and causing injury to the domestic industry producing a like product, it may initiate an investigation; the investigation may or may not lead to definitive measures being taken against the dumped goods. WTO Members have resorted mostly to anti-dumping measures, with much less use being made of countervailing measures, which are intended to “countervail” subsidies when it is determined, after investigation, that subsidized imports cause injury to the domestic industry producing a like product.

65. Initiations of anti-dumping investigations, although falling to 310 in 2002 from 366 in 2001, remain high (Chart 4). (In the first half of 2003, 78 investigations were initiated.) About half of the investigations initiated in 2002 were in chemicals and articles thereof, and base metals. Base metals has also been the category most affected by anti-dumping investigations (some 31%) since 1995 (Chart 5). The largest number of initiations in 2002 were reported by India, followed by the United States, China, Thailand, and the European Union. Overall, since 1995, India has also been the largest initiator of anti-dumping investigations, with a cumulative total of around 15% of all initiations, followed by the United States, the European Union and Argentina.

66. The number of measures taken in 2002, as reported by WTO Members was higher (212) than in 2001 (Chart 4). (In the six months through June 2003, 113 measures were taken.) India took the largest number of measures (63) in 2002, followed by the EU (25), Argentina (24), and the United States (24). The countries most affected were China (37), followed by Chinese Taipei (14), the Republic of Korea (13), and the United States (10). As at 30 June 2003, a total of 1,323 anti-dumping measures were in force, compared with 1,189 as at June 2002. The United States maintained 278, followed by India (210), the European Union (204), and South Africa (96).

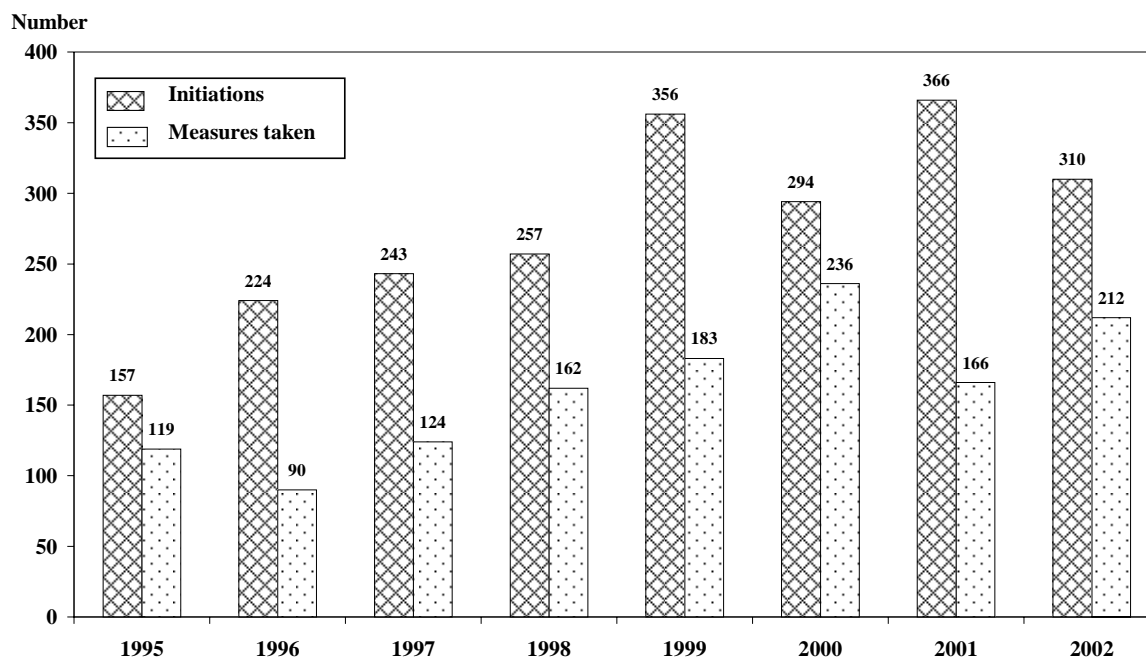
67. Countervailing measures have been used significantly less by Members, 161 initiations during the period 1995-June 2003, compared with 2,284 for anti-dumping. In 2002, ten countervailing investigations were initiated, a considerable decline, from 27, in 2001; seven were initiated in the first half of 2003. Since 1995, the main user has been the United States (65 between 1995 and end-June 2003, of which three in the first half of 2003). The countries mainly affected by countervailing investigations are India (36), and Korea (13); the EU (9) and its members (altogether 39) have also been affected.

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<sup>65</sup> Fouquin, M., P. Morand, R. Avisse, G. Minville and P. Dumont (2002), "Mondialisation et régionalisation: le cas des industries du textile et de l'habillement", Centre d'Etudes Prospectives et d'Informations Internationales, No. 2002-08, Septembre.

<sup>66</sup> A recent meeting on textiles and clothing organized by the European Commission examined the impact of a removal of quotas maintained under the ATC. Among the major conclusions was a suggestion that preferential access should be maintained or even accelerated for LDCs.

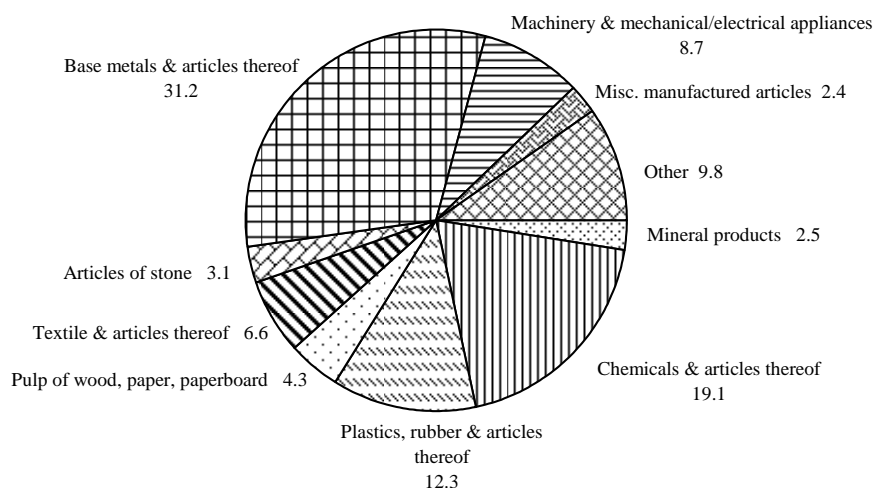
**Chart 4**  
**Anti-dumping: initiations of investigations and measures taken, 1995-2002**



Source : WTO Secretariat.

**Chart 5**  
**Anti-dumping initiations by sector, 1995-June 2003**

Per cent



**Note:** Other includes live animals & products (1.6%); vegetable products (1.4%); fats & oils (0.2%); prepared foodstuffs, beverages, tobacco (1.8%); raw hides & skins (0.1%); wood & articles (1.4%); footwear & headgear, etc. (0.9%); precious stones etc. (0.1%); transport equipment (0.8%); precision instruments (1.2%); and works of art (0.5%).

Source : WTO Secretariat.

68. As with other trade defence measures, safeguards are being used more frequently by Members. In 2001/02 (30 October 2001 to 28 October 2002), Members notified the initiation of 33 safeguard investigations and 16 in the same period 2002/03, a sharp increase over 2001 (13). The number of definitive measures imposed has also risen steadily, from eight in 2001 to 14 in 2002 and 20 between October 2002 to October 2003. While the use of trade defence measures in general appears to be on the rise, some Members, such as Australia and New Zealand, in the context of their bilateral free trade agreement (ANZCERTA), and members of the European Union have chosen to deal with the issue of "unfair" competition through the application of competition policy, rather than through the use of trade defence measures; they continue, however, to use trade defence measures against imports from third countries.<sup>67</sup>

## **6. Technical regulations, and sanitary and phytosanitary measures**

69. As tariff and non-tariff barriers are being removed progressively, there are some fears that certain technical, safety, and health standards may be used instead to deter imports. Standards are used in order to, *inter alia*, guarantee certain quality, facilitate production and trade (by providing information regarding characteristics, quality and compatibility with other systems), and provide public goods (such as clean air through emission standards). Under the WTO Agreements on Technical Barriers to Trade (TBT) and Sanitary and Phytosanitary (SPS) Measures, Members may impose on imports national standards (equivalent to those on domestic goods) related to technical, health, safety, environmental, and SPS requirements. Imports of such goods are permitted subject to presentation of the appropriate health or conformity assessment certificates or upon completion of inspection procedures at the border.

70. While permitted under the WTO Agreements, the use of standards and SPS measures appears to have become more contentious in recent years. An increasing number of measures have been notified to the WTO, both by developing and developed countries, and an increasing number of such measures have become subject to dispute settlement in the WTO: the number of technical regulations notified increased to 581 in 2002, from 538 in 2001, although the degree of conformity with international norms varies from country to country (see below). The largest number of notifications were made by the EU and its member states (96) followed by Brazil (45), the Czech Republic (43), and Argentina (39). Since 1995, WTO Members have made 4,666 notifications; over half of these have been made by developed countries.<sup>68</sup> Members notified 660 SPS measures to the WTO Secretariat in 2002. The largest number were notified by the United States (126), followed by New Zealand (35), the EU (34), and Canada (33); for the period January to end July 2003, the figures were 493 in total, with 126 for the United States, 56 for New Zealand, 28 for the EU, and 23 for Canada. The number of SPS and TBT measures that have become the source of disputes in the WTO has risen between July 2002 and December 2003 from 21 to 30 and 25 to 31, respectively.

71. Standards and SPS measures, like other regulatory measures, exist mainly to achieve important public policy goals, such as protecting public health and the environment, and ensuring that products of high quality reach consumers. However, there are concerns that they could also be used as a potential barrier to imports, not just in terms of an additional requirement that must be met by foreign producers but also in inefficient and duplicative testing and conformity assessment requirements.<sup>69</sup> While most countries acknowledge that standards and SPS measures are necessary, and impose certain additional costs on the exporter, developing country Members in particular complain that multiple testing requirements associated with similar standards in different markets as

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<sup>67</sup> See for example, WTO (2002), *Trade Policy Review – Australia*; and WTO (2003), *Trade Policy Review – New Zealand*.

<sup>68</sup> Based on WTO document G/TBT/12, 21 February 2003.

<sup>69</sup> The concept of national treatment in the WTO Agreements plays an important role in ensuring that these measures do not discriminate in favour of domestic producers and against importers.

well as the rising complexity of conformity assessment requirements make these costs prohibitive.<sup>70</sup> Conformity assessment, in particular, according to some, presents the largest potential technical barrier to trade.<sup>71</sup> In addition, many LDCs simply do not have the technical or financial means to upgrade their production facilities in order to meet these standards. An added problem is the increasing use of mutual recognition agreements (MRAs) between countries, which aim to reduce the costs associated with standards, but discriminate against countries outside the MRA grouping.

72. The proliferation of standards and SPS measures in both industrialized and developing countries has led to efforts to try to quantify these measures and to understand their effects on trade. The first problem for researchers is to find a common standard or benchmark by which to measure a particular standard. While the WTO Agreements encourage the use of international agreements, such as CODEX Alimentarius for SPS measures and ISO and IEC codes for standards, several countries use their own national standards, which may differ from international standards. Trade Policy Reviews show, for example, that while there is an overall trend towards adopting international standards, several Members have standards that have no international equivalents. For example, among the Quad countries, 90% of Japan's standards were based on international standards on 31 March 2001, while 40% and 80% of standards issued by the EU's standards setting organizations CEN and CENELEC, respectively, were harmonized with international standards; data for Canada and the United States were not available, although both countries state that they are attempting to harmonize their standards with international norms as much as possible. Among other industrialized countries, standards that have equivalent international standards are around 80% in Australia, and around one-third in New Zealand; around 87% in Switzerland are equivalent to international or EU standards. Most of the transition economies reviewed are moving towards basing their standards on EU standards, while for some developing countries, the extent of harmonization varies (42% for Indian standards issued during 1998-2001; 60% at least partial concordance for Mexico; over half for Pakistan; 31% overall and 80% for standards issued in 1998 and 1999 for Malaysia; and generally equivalent for South Africa). Maskus, Wilson and Otsuki (2000) describe four approaches in the literature to measuring standards and other regulations affecting trade: surveys of firms' cost responses to regulations; econometric analyses of standards and trade at a macroeconomic level; partial equilibrium models; and general equilibrium models. Methodologies to measure sanitary, phytosanitary, and technical barriers to trade have also been discussed in the OECD.<sup>72</sup> Some studies have also looked at the additional costs imposed by a standard that is higher than the international norm.<sup>73</sup> A more comprehensive study has also been launched recently by the World Bank.

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<sup>70</sup> Even amongst countries at similar levels of industrialization different standards can be problematic. Research on the EU Single Market programme illustrates the costs associated with meeting standards in EU member States, and research by the OECD found that the costs of meeting differing standards and technical regulations in its member states along with testing and certification could range from 2-10% of overall product costs. Wilson, J.S. (2002), "Standards, Regulation and Trade: WTO Rules and Developing Country Concerns", in Hoekman, B., A. Mattoo and P. English Eds, *Development, Trade and the WTO: A Handbook*, World Bank, pp. 428-438).

<sup>71</sup> For example, Governments in importing countries may refuse to recognize tests performed by exporting firms or their public authorities, may not accept conformity declarations made by the exporter, and may insist on performing their own inspections of exporters' premises associated with time delays, bureaucratic non-transparency, etc. Maskus, K.E., J.S. Wilson and T. Otsuki (2000), "Quantifying the Impact of Technical Barriers to Trade: A Framework for Analysis", World Bank Working Paper no. 2512, December.

<sup>72</sup> Beghin, J.C. and J-C Bureau (2001), *Measurement of Sanitary, Phytosanitary and Technical Barriers to Trade*: A Consultant's Report prepared for the Food, Agriculture and Fisheries Directorate, OECD, 17-18 September.

<sup>73</sup> See for example, Otsuki, T., Wilson, J.S. and M. Sewedeh (2001), "A Race to the Top? A Case-study of Food Safety Standards and African Exports", World Bank Working Paper, no. 2563, World Bank, February. This paper finds that high standards in the EU on aflatoxins, which would reduce health risks in the EU by approximately 1.4 deaths per billion per year, would cost African countries US\$670 million in lost export

73. An important question that arises is how developing countries in particular can meet these requirements and maintain market access for their exports. The Doha Ministerial Decision on Implementation-Related Issues and Concerns, *inter alia*, urged Members to provide technical and financial assistance to ease implementation issues faced by least developed country Members. In this regard, the Standards and Trade Development Facility has been established by the Food and Agriculture Organization (FAO), the World Animal Health Organization (OE), the World Bank, the World Health Organization (WHO) and the WTO. The Facility provides for: small grants for pilot projects to build capacity in standards in developing countries; assistance to government and private sector in meeting international standards; and stronger inter-agency coordination and donor collaboration in the delivery of technical assistance in standards.<sup>74</sup> In addition, as noted, the adoption of international standards by countries would ensure a common standard, and reduce unnecessary and duplicative testing and certification requirements, which add to the cost of meeting divergent standards across importing countries. Difficulties remain in assessing the impact on trade of national standards that are not equivalent to international standards.

## 7. Market Access for Services

74. Services account for some 65% of world GDP, with just under 70% in industrialized countries and around 50% in developing countries.<sup>75</sup> Growth in world trade in commercial services averaged almost 5.5% during the period 1992-2002. Rapid growth of FDI in services has also been a major source of expansion; the World Bank estimates that services account for more than half of the stock of FDI in most industrialized countries.<sup>76</sup> International trade in services is classified under four "modes of supply" in the WTO's General Agreement on Trade in Services (GATS). Data on trade for all four modes of supply are subject to statistical limitations and, for some modes, only rough estimates are available. Estimates by the WTO's Economic Research and Statistics Division indicate that the largest mode of supply is commercial presence (around 56% of the total value of services trade), followed by cross-border supply (some 28%), and consumption abroad (14%). In comparison, the share of services traded through mode 4 (movement of natural persons) is relatively small, some 1.4%.<sup>77</sup>

75. The economic and trade performance of an economy is often dependent on the efficiency of the services sector. Economic growth in many countries, especially developing countries, may well be hampered by supply and regulatory bottlenecks in services, including telecommunications, transport, and utilities. (Services also tend to be one of the largest sources of employment in the

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revenue (a decrease of 64%) compared with the situation where international standards were used. Another study, on divergent aflatoxin standards in 15 importing countries (of which four were developing) found that use of a worldwide standard (based on current international guidelines) would increase cereal and nut trade between the countries studied by US\$61 billion from 1998 levels and that total world exports would rise by US\$38.8 billion if an international standard based on Codex were adopted. Wilson, J.S. and T. Otsuki (2001), "Global Trade and Food Safety: Winners and Losers in a Fragmented System", World Bank Working Paper NO. 2689, October.

<sup>74</sup> Standards and Trade Development Facility, "Background" [Online]. Available at: <http://www.standardsfacility.org/background.htm> [12 August 2003].

<sup>75</sup> Data from WTO Economic Research and Statistics Division. The largest shares of world trade in services are accounted for by the European Union (45%), North America (22%) and Asia (21%), together accounting for some 88% of world trade in services (McGuire, 2002, "Trade in Services: Market Access Opportunities and the Benefits of Liberalization for Developing Economies", *Policy Issues in International Trade and Commodities, Study Series no. 19*, United Nations Conference on Trade and Development (UNCTAD), Geneva).

<sup>76</sup> World Bank (2003), *Global Economic Prospects 2003*, World Bank, Washington DC.

<sup>77</sup> Based on IMF balance of payment statistics on compensation of employees (Karsenty, G., 2002, *Trends in Services Trade Under GATS: Recent Developments*, presentation at the Symposium on Assessment of Trade in Services, WTO, 14-15 March).

economy.) Thus, the actual measures of the contribution of services to GDP may underestimate their importance.

76. Unlike merchandise trade, where the quantification of barriers to trade, including tariffs and non-tariff barriers such as quotas, and licensing, is well advanced, this is a much more difficult task in services. Given the potential gains from liberalization of trade in services, as well as the spillover effects from such liberalization on other economic activities, it is, however, necessary to try and quantify these barriers.<sup>78</sup> Some recent efforts have been made to quantify barriers to trade in services.<sup>79</sup> Early work done by Hoekman (1996) used information provided by the GATS Schedule to develop a numerical index on barriers to trade in services. This has since been developed further, especially by the Australian Productivity Commission, and alternative methodologies, such as the use of price impact measures and quantity impact measures, have also been developed.<sup>80</sup> A more recent discussion of barriers to trade in services can be found in WTO (2003).<sup>81</sup>

77. Recognizing the contribution of services to trade and economic growth, WTO Members agreed to make commitments in services at the multilateral level. The General Agreement on Trade in Services (GATS) is a multilateral framework within which WTO Members can negotiate with each other and obtain commitments on liberalization in a wide range of services.<sup>82</sup> Although Members can liberalize their services and set up the appropriate regulatory mechanisms unilaterally, as many have indeed done, Members have chosen to schedule commitments in the GATS. There are several ways in which the GATS complements the growth of trade in services. As is the case with tariff bindings, GATS commitments offer security of market access and a set of rules governing trade in services that all Members agree to. GATS commitments may also be used to advance the domestic liberalization agenda. Barriers to market access abroad can also be lowered through multilateral negotiations, which are more beneficial to smaller countries than bilateral negotiations. Finally, the rapid expansion of trade in services has hastened the need for a multilateral framework of rules such as the GATS within which Members can pursue further liberalization and improved market access.

78. All WTO Members submitted a Schedule of Specific Commitments under the GATS. The Schedule indicates the sectors in which Members agree to market access and national treatment commitments; the Schedule also indicates any limitations imposed by the Member under the four modes of supply (cross-border supply or Mode 1; consumption abroad or Mode 2; commercial presence or Mode 3; and the presence of natural persons or Mode 4). All services, except air traffic

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<sup>78</sup> Most studies that have attempted to model the gains from liberalizing trade in services have found major positive gains, especially for the less liberalized economies (see for example, OECD, 2001, *Quantification of the Costs to National Welfare from Barriers to Services Trade: A Literature Survey*, OECD Trade Directorate, Working Party of the Trade Committee, 14 November).

<sup>79</sup> Stern, R.M. (2002), "Quantifying Barriers to Trade in Services", in Hoekman, B., A. Mattoo, P. English (eds), *Development, Trade and the WTO: A Handbook*, World Bank, pp. 247-258 for example classifies these into quantitative restrictions, price based instruments, standards, licensing and procurement and discriminatory access to distribution networks.

<sup>80</sup> Instead of the GATS Schedule, for example, the negative list of barriers to investment in services has been used to develop quantitative restrictions on trade in services maintained by APEC countries (Hardin and Holmes, "Assessing barriers to service sector investment" in Warren, T. and C. Findlay (eds) (2000) *Impediments to Trade in Services: Measurement and policy implications*, Routledge Studies in the Growth Economies of Asia, London, pp. 52-70. They found that restrictions were greatest in communication and financial services. Price impact measures and quantity impact measures have been used by Bosworth, M., C. Findlay, R. Trewin and T. Warren "Price impact measures of impediments to services trade", in Warren and Findlay (2000), pp. 42-51 and also applied to telecommunication services, banking and maritime services in the same volume. The quantity impact approach is applied to telecommunication services barriers in Warren, T., "The impact on output of impediments to trade and investment in telecommunication services", in Warren and Findlay (2000), pp. 85-100.

<sup>81</sup> WTO (2003), *World Trade Report*, Geneva.

<sup>82</sup> The GATS covers most services sectors (with the exception of a few services discussed later).

and directly related services and all services provided in the exercise of governmental authority<sup>83</sup>, are covered by the GATS, reflecting some 160 sectors. However, Members have thus far made commitments in a range of 1 to 140 sectors. Developing countries have, in general, scheduled fewer sectors although the range of commitments is high for least developed and developing and transition Members. The largest number of commitments were made in tourism related services, financial services, business services, communication and transport services. Fewer Members made commitments in what are traditionally regarded as "social services" such as health and education.

79. The concept of successive rounds of negotiations, aimed at "achieving a progressively higher level" of liberalization is enshrined in the GATS itself. According to Article XIX:1, the first such round was to start not later than five years from the date of entry into force of the Agreement, i.e. 1 January 2000. An important step was taken when, in March 2001, the Council for Trade in Services adopted Guidelines and Procedures for the Services Negotiations.<sup>84</sup> New elements in the Guidelines include: (i) the need to give "due consideration to the needs of small and medium-sized service suppliers, particularly to those of developing countries"; (ii) conclusion of the negotiations on emergency safeguards by 15 March 2002 (extended to 15 March 2004) and the negotiations in other rule-making areas under GATS – domestic regulation, government procurement, and subsidies - prior to concluding the negotiations on specific commitments; (iii) preference for the request-offer approach as the main method of negotiation; and (iv) the continuation of the assessment of trade in services, provided for under Article XIX:3, as an ongoing activity of the Services Council.

80. Another important step in the negotiations, up to the Doha Ministerial, concerned the submission of negotiating proposals by individual or groups of Members. Most of these proposals (more than 100 were received before the Doha Ministerial Conference) were devoted to explaining trade problems, policy concerns and negotiating objectives in sectors and areas of interest. The Doha Declaration of November 2001 reaffirmed these guidelines as a basis for continuing the negotiations and integrated services into the general context of the negotiations. Initial requests and initial offers were to be submitted by 30 June 2002 and 31 March 2003, respectively. As at 6 October 2003, 38 offers, from 52 Members, have been received by the Secretariat.<sup>85</sup> Of these 52 Members, almost half are developing and transition economies.<sup>86</sup>

81. The highest number of offers has been in business services, followed by transport services, financial services, tourism, and telecommunication services (Chart 6). Twenty of the offers propose to improve horizontal commitments and 11 offer either to withdraw MFN exemptions or to reduce the scope of such exemptions. Relatively few offers pertain to education or health services, and these offers tend to be from developing and transition economies. This may be attributable to concerns that commitments may unduly limit governments' scope to pursue basic social policy objectives. Offers and existing commitments in these sectors have aimed, for example, to foster greater competition amongst private service suppliers and to attract foreign investment (and foreign consumers) in areas of particular interest, e.g., language schools.

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<sup>83</sup> These latter services are defined in Article 1:3 of the GATS as those supplied neither on a commercial basis nor in competition with other suppliers.

<sup>84</sup> WTO document S/L/93, 29 March 2001. The Guidelines offer parameters to the negotiations, building on key principles already contained in the text of the Agreement such as increasing participation by developing countries in services trade and an obligation to respect national policy objectives and to accord appropriate flexibility in the scheduling process.

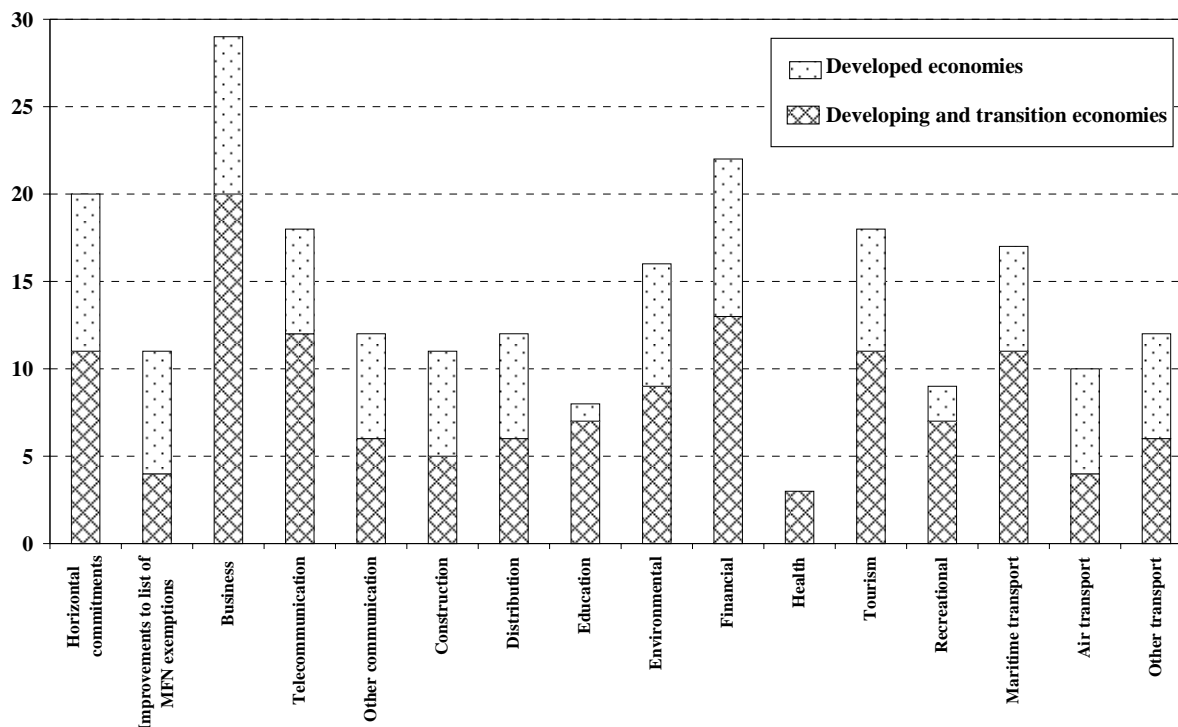
<sup>85</sup> These Members are: Argentina; Australia; Bahrain; Bolivia; Canada; Chile; China; Chinese Taipei; Colombia; Czech Republic; European Communities; Fiji; Guatemala; Hong Kong, China; Iceland; Israel; Japan; Republic of Korea; Liechtenstein; Macao, China; Mexico; New Zealand; Norway; Panama; Paraguay; Peru; Poland; Senegal; Singapore; Slovak Republic; Slovenia; St Kitts and Nevis; Sri Lanka; Switzerland; Thailand; Turkey; United States; and Uruguay.

<sup>86</sup> The majority of the 38 offers originate from developing or transition economies, since the European Communities submitted one offer for 15 Members.



**Chart 6**  
**Offers by sector and issue (as at 6 October 2003)**

Number of members

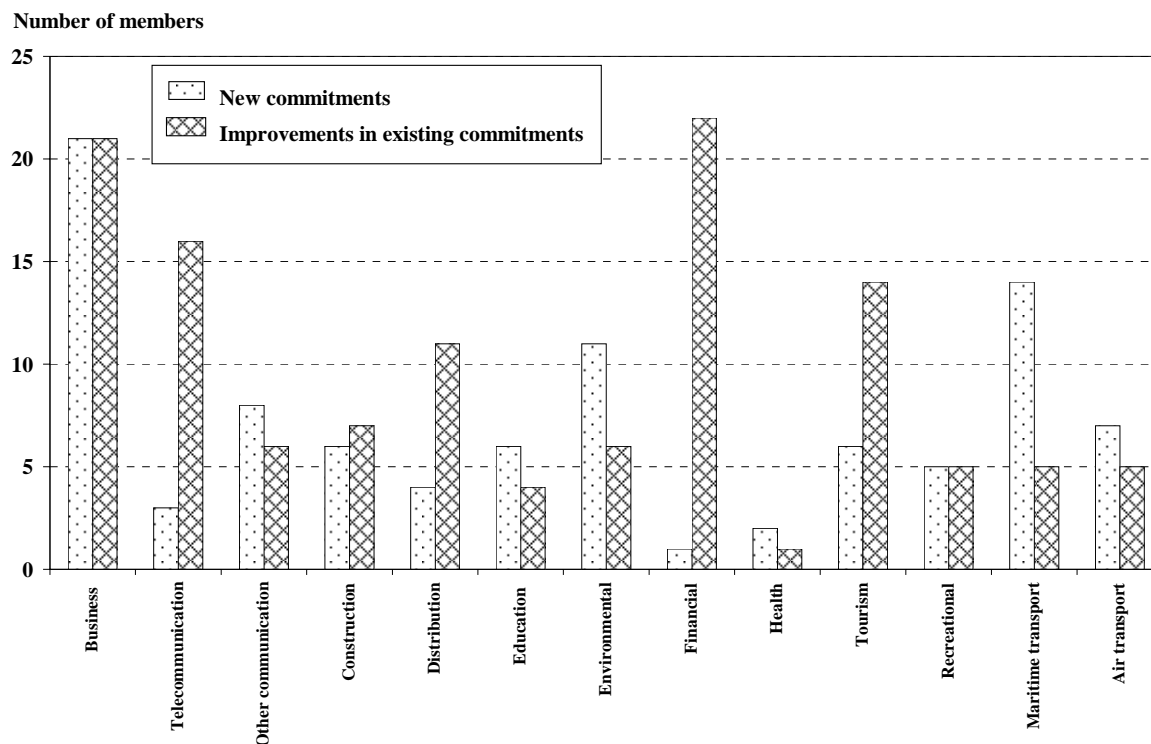


Source: WTO Secretariat.

82. Most modifications to schedules *in initial offers* take the form of improvements of existing commitments in sectors such as telecommunications and financial services, where a number of Members already have commitments. New specific commitments tend to be concentrated in business services, transport (including auxiliary maritime service), and environmental services (Chart 7). Overall, the initial offers received from 52 Members include 322 new specific commitments and improvements to 435 existing specific commitments. Regarding improvements to existing specific commitments, 117 were with respect to market access for mode 4, and 43 specific commitments that were left "unbound" for market access under mode 1 and/or mode 2 are proposed to be bound (either fully or with some limitations). In addition, 28 economic needs test are proposed to be withdrawn from schedules.

83. Other areas of negotiations relate to negotiating mandates under Articles VI (Domestic Regulation), X (Emergency Safeguard Measures), XIII (Government Procurement), and XV (Subsidies). The Special Session of the Council for Trade in Services adopted the Modalities for the Treatment of Autonomous Liberalization Measures undertaken by WTO Members since the previous multilateral negotiations, in March 2003, and the Modalities for the Special Treatment for Least-Developed Country (LDC) Members in the Negotiations on Trade in Services, in September 2003. The modalities for autonomous liberalization establish criteria and procedures for Members' granting of negotiating credit for liberalization measures undertaken autonomously since the previous round, and the modalities for special treatment of LDC Members stipulate ways for providing special priority to concerns and interests of LDC Members.

**Chart 7**  
**Offers by Members on new specific commitments and/or improvements to existing specific commitments, by sector (as at 6 October 2003)**



Source: WTO Secretariat.

84. A key factor of the GATS is that it does not compel Members to make sector-specific commitments, but gives them the opportunity, should they so wish. The few restrictions include: once a commitment has been made, it must be extended to all other WTO Members on a most-favoured-nation (MFN) basis<sup>87</sup>; and a scheduled commitment can only be modified or withdrawn once compensation with affected Members has been agreed.<sup>88</sup>

85. While the objective of the GATS is progressive liberalization of trade in services, two services are excluded: services provided in the exercise of governmental authority; and the air transport sector, air traffic rights and all services directly related to the exercise of air traffic rights.<sup>89</sup> For some public services, the classification of government services is relatively clear, for example, defence. In several Member countries, education and health services and utilities are also provided only by the government. However, in recent years, there has been increasing pressure on

<sup>87</sup> The MFN clause, which forms the basis of the WTO Agreements is a powerful instrument to protect the fairness of the system, ensuring that all countries are treated equally. In the GATS negotiations, exceptions to MFN were permitted for a ten-year period (in principle) provided they were scheduled when the GATS came into effect.

<sup>88</sup> Article XXI of the GATS allows Members to modify or withdraw any commitment in their Schedule at any time after three years from the date of entry into force of the commitment. If the parties are unable to agree an appropriate level of compensation, arbitration can be requested; if the Member does not agree with the compensation amount set by the arbitrator, the Member requesting arbitration may withdraw or modify substantially equivalent benefits in conformity with the arbitrator's findings.

<sup>89</sup> Services provided in the exercise of governmental authority are defined as any services that are supplied neither on a commercial basis nor in competition with one or more service suppliers.

governments to relax monopoly controls on certain services for various reasons, including fiscal and supply bottlenecks. The case of telecommunications, for example, shows that in most developed and several developing countries the incumbent public-sector supplier has gradually been exposed to competition from private-sector suppliers. This may, at least in part, have helped contain prices and alleviate supply bottlenecks. In the case of other public services, for many Members that have aging populations and increased pressure on public health systems, the provision of health services is often mixed, with both public and private sector components. The definition of governmental services, therefore, has become less clear with regard to such service sectors.

86. The GATS and subsequent liberalization negotiations have raised a number of fears regarding the erosion of consumer access to basic services. In recent times this criticism has been extended to sectors generally considered "public or social" such as health, education, and water. In the current negotiations, as of end April 2003, two Members had made offers in health services and four in education services. Critics of the current negotiations allege that such commitments will lead to an erosion of the quality of some of these services and will undermine consumer access through increased privatization and foreign investment. In this context, it should be noted that making commitments in the GATS does not imply that Members can no longer regulate the service and ensure that certain standards are met through the appropriate policy framework.<sup>90</sup> For example, recent Trade Policy Reviews have found that in most Members that have undertaken liberalization of telecommunications services, there is a universal service requirement, often funded by contributions from all or the main telecommunication operators. Members are free to restrict their offers to certain subsectors while not making offers in other subsectors.<sup>91</sup>

87. There are similar fears about the inclusion of other sectors considered to be part of essential social services, such as water and electricity. Here the concern expressed most frequently is that commitments would result in privatization, which in turn would move them out of the reach of the poorer sections of society. Again, the GATS does not advocate privatization but instead would require any Member making a commitment in these services to guarantee national and MFN treatment to other WTO Members.

88. A key area of the GATS in which developing countries would like to see greater liberalization is in the movement of natural persons (mode 4). It is the area in which Members made the fewest commitments; moreover, the sectors in which commitments were made are frequently subject to market-access and national treatment restrictions.<sup>92</sup> This mode of supply accounts for about 1.5% of trade in services, implying that there is considerable scope for its liberalization and growth.<sup>93</sup> The liberalization of mode 4 is also likely to play a crucial role for developing countries, some of which

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<sup>90</sup> In the case of telecommunications, for example, most evidence gathered from recent TPRs shows that rather than worsening services, reform in the sector has led to improved access to telecommunication services and reduced user charges. Moreover, the Telecommunications Reference Paper gives Members the flexibility to decide on appropriate policy mechanisms to ensure, *inter alia*, universal services etc.

<sup>91</sup> For example, in education services, offers may be restricted to certain education activities, such as adult education services, while excluding commitments in other education services. The offer of course would depend on the needs of the particular Member and/or pressure from other Members to make such commitments.

<sup>92</sup> National treatment exemptions, for example, may relate to the import of labour from certain countries or regions only. Market-access commitments often specify the type of person that can enter the market, such as managers, specialists, and others for the purposes of establishing commercial presence.

<sup>93</sup> Data estimated by the WTO Economic Research and Statistics Division and measured by compensation of foreign employees as shown in the balance of payments. In comparison, commercial presence accounts for 56%, cross-border supply for 28% and consumption abroad for 14% (these figures are all calculated from balance-of-payments statistics from the IMF and Foreign Affiliates Trade Statistics from the OECD).

are highly dependent on workers' remittances for foreign exchange.<sup>94</sup> These remittances are roughly equivalent to the total annual aid given by industrialized to developing countries.<sup>95</sup> However, several potential constraints may need to be addressed: these relate mainly to domestic regulations and include immigration-related issues, recognition of qualifications and training, differences in the treatment of domestic and foreign workers, and regulations in other modes. Suggestions on dealing with some of these constraints include: clear criteria and guidelines regarding the use of economic needs test; distinction between administrative procedures for temporary workers and for those seeking more permanent immigration; norms to deal with social security and access to health insurance; and a strengthening of norms and disciplines on recognition of qualifications and for facilitating mutual recognition agreements among Members.<sup>96</sup>

89. As the impact of domestic regulations on trade in services may be significant, the Council for Trade in Services was mandated under Article VI:4 of the GATS to develop necessary disciplines to prevent domestic regulations (qualification requirements and procedures, technical standards, and licensing requirements) from constituting unnecessary barriers to trade. The Guidelines and Procedures for the services negotiations, approved by the Council for Trade in Services in March 2001 and confirmed in the Doha Ministerial Declaration, envisage that these negotiations be completed prior to the conclusion of the current negotiations on specific commitments. The negotiations are being conducted in the Working Party on Domestic Regulation (WPDR). Issues currently under consideration in the WPDR include a necessity test, transparency, equivalence, and the use of international standards as benchmarks.<sup>97</sup>

## **8. Intellectual property rights**

90. Along with the GATT and the GATS, the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) is an important cornerstone of the WTO Agreement. The TRIPS Agreement ensures *inter alia* minimum standards for intellectual property rights protection for all WTO Members, with transition periods for developing and LDCs.

91. Intellectual property rights recognize both the (private) rights of, and investment by, the inventor in developing the invention, and those of the public to use the knowledge generated by the invention (a public good) for further scientific advancement which would provide benefits to the society in general.<sup>98</sup> The right conferred on the inventor is a monopoly on the use of the particular invention, for a limited period of time, for patents currently a minimum of 20 years under the TRIPS Agreement. During this time the inventor may licence the invention upon negotiating appropriate remuneration; there are also a number of exceptions where the invention may be licenced, such as for

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<sup>94</sup> In 2001, it was estimated that remittances to developing countries from overseas resident and non-resident workers amounted to around 1.3% of their GDP; the remittances are particularly important for low-income developing countries (World Bank, 2003, *Global Development Finance*, p. 158). Such remittances may well be more targeted than official aid. The definition used of workers remittances is broader than the one used by the WTO, and includes workers remittances recorded under the heading "current transfers" in the current account; compensation of employees recorded under the income sub-category of the current account; and migrants' transfers recorded under "capital transfers" in the capital account.

<sup>95</sup> According to the World Bank, workers' remittances were US\$72.3 billion in 2001, and for most of the 1990s these exceeded official development assistance (World Bank, 2003, *Global Development Finance 2003*, pp. 157-8).

<sup>96</sup> See for example, India's proposals in the current negotiations (WTO document S/CSS/W/12).

<sup>97</sup> An overview of these issues is given in WTO document see S/C/W/96, 1 March 1999.

<sup>98</sup> Most intellectual property rights regimes thus require some information regarding the patent to be published, thereby becoming available for others to use.

national emergencies. In addition, the potential dangers of granting such a monopoly with regard to competition are also recognized under the TRIPS Agreement.<sup>99</sup>

### **The Debate on the TRIPS Agreement and Public Health**

92. Trade, growth and the good health of a country's population are mutually reinforcing. Trade, by helping to increase economic growth, contributes to the alleviation of poverty, which is perhaps a major cause of the growth of HIV/AIDS and other forms of sickness and disease in developing countries. At the same time, measures to improve the health of a country's labour force increase labour productivity, and thus its competitiveness, thereby contributing to economic growth. In August 2003, WTO Members reached a decision granting a waiver under Article 31(f) of the TRIPS Agreement enabling the export of pharmaceutical products made under compulsory licences. The decision effectively permits LDCs and other developing countries who do not have the means to produce pharmaceuticals required for pandemics such as HIV/AIDS, to import them from the cheapest source, thereby fulfilling one of the major goals of the DDA.

#### *Discussions in the TRIPS Council*

93. The debate on the TRIPS Agreement and Public Health arose essentially out of the current HIV/AIDS crisis and access to medicines, most of which are still under patent and whose cost is therefore prohibitive for most least developed and developing countries. UNAIDS estimates that some 95% of HIV/AIDS sufferers are currently in developing and least developed countries with some 70% of them in sub-Saharan Africa alone.<sup>100</sup> In many countries, the economic and social cost of the disease has been enormous through its adverse effect on the productive population; according to the latest data from UNAIDS, the average life expectancy in sub-Saharan Africa is currently 47 years, when it was estimated to have been 62 years without AIDS.<sup>101</sup> While the AIDS epidemic was the main factor behind the current debate on the TRIPS Agreement, other diseases widespread in developing countries make access to medicines a broader problem. With many developing countries required under the TRIPS Agreement to provide patent protection for most products by 2005 and at the latest by 2010, the need to address its long term implications on public health policy has also become urgent.

94. The Fourth Ministerial Conference of the WTO, held in Doha, Qatar, adopted a Declaration on the TRIPS Agreement and Public Health. The purpose of the Declaration was to respond to concerns about the possible implications of the TRIPS Agreement for access to medicines. Although the TRIPS Agreement allows countries to take various kinds of measures that can qualify or limit intellectual property rights, including for public health purposes, some doubts had arisen about the nature and limitations of such flexibility.

95. The Declaration responds to these concerns in a number of ways. It emphasizes that the TRIPS Agreement does not and should not prevent countries from taking measures to protect public health, and reaffirms the right of countries to use, to the full, the provisions of the TRIPS Agreement that provide flexibility for this purpose. It signals an acceptance by all WTO Members that they would not seek to prevent other Members from interpreting the Agreement in a pro-public health way. It contains a number of important clarifications of some of the flexibilities contained in the TRIPS

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<sup>99</sup> Under Article 40, governments may put into place measures to control anti-competitive practices, if it is believed that the monopoly rights conferred through IPRs are detrimental to competition.

<sup>100</sup> UNAIDS (2002), *Report on the Global HIV/AIDS Epidemic: "The Barcelona Report"*, July, [Online]. Available at: <http://www.unaids.org/barcelona/presskit/embargo.htm>, [16 June 2003].

<sup>101</sup> UNAIDS (2002), *HIV/AIDS: Human resources and sustainable development*, prepared for the World Summit on Sustainable Development, Johannesburg, South Africa, August. [Online]. Available at: <http://www.unaids.org/whatsnew/conferences/wssd>, [16 June 2003].

Agreement, especially with respect to the freedom to determine the grounds upon which compulsory licences are granted, and the right to permit parallel imports. This clarification on compulsory licences is, for example, a useful corrective to the view sometimes expressed that some form of emergency is a pre-condition for compulsory licensing under the TRIPS Agreement. The Declaration further makes it clear that each Member has the right to determine what constitutes a national emergency or other circumstances of extreme urgency (when a compulsory licence can be granted without a prior effort to obtain a voluntary licence), and that public health crises, including those relating to HIV/AIDS, tuberculosis, malaria, and other epidemics, can represent such circumstances.

96. The Declaration contains an agreement of Ministers to accord least developed country Members an extension of their transition period, until the beginning of 2016, in regard to the protection and enforcement of patents and rights in undisclosed information with respect to pharmaceutical products. The TRIPS Council took the necessary action under Article 66.1 of the TRIPS Agreement to give effect to this in June 2002 and, at the same time, recommended a parallel waiver for these countries from obligations under the "exclusive marketing rights" provisions of Article 70.9. The waiver was adopted by the General Council in July 2002.

97. While emphasizing the scope in the TRIPS Agreement to take measures to promote access to medicines, the Declaration recognizes the importance of intellectual property protection for the development of new medicines and reaffirms the commitments of WTO Members in the TRIPS Agreement.

#### **Problem of countries with insufficient manufacturing capacities in the pharmaceutical sector**

98. An issue that arose in the work on the Declaration was the ability of countries with limited manufacturing capacities to make effective use of compulsory licensing. It is not in dispute that Members can issue compulsory licences for importation as well as for domestic production. However, there was concern about whether supplies would be available from generic producers in other countries to meet the demand for imports under a compulsory licence, given the requirement in Article 31(f) of the TRIPS Agreement that, normally, compulsory licences shall be "predominantly for the supply of the domestic market of the Member" granting the compulsory licence. This constraint might be increasingly felt after 2005 when countries with important generic industries, such as India, come under an obligation to provide patent protection for pharmaceutical products. The Declaration recognized the problem in its paragraph 6 and instructed the Council for TRIPS to find an expeditious solution to it and to report on this before the end of 2002.

99. On 16 December 2002, following intensive work in the Council for TRIPS during the second half of 2002, the Chairman of the Council presented a draft Decision on the subject representing his best assessment of how to achieve a balanced result, taking all positions and concerns into account. Not all Members were ready to adopt the Decision at that time, either because they considered that it was too open-ended and open to abuse, or that it was too burdensome in some respects. After further work, the Chairman's proposal was adopted by the General Council on 30 August 2003, at which meeting a Chairman's statement containing several key shared understandings of Members was also put on record.

100. The Decision grants three distinct waivers from the obligations set out in subparagraphs (f) and (h) of Article 31 of the TRIPS Agreement with respect to pharmaceutical products, subject to certain conditions. It covers any patented product, or product manufactured through a patented process, of the pharmaceutical sector needed to address the public health problems as recognized in paragraph 1 of the Doha Declaration on the TRIPS Agreement and Public Health, including active ingredients necessary for its manufacture and diagnostic kits needed for its use. The three waivers are:

- (i) A waiver of the obligation of an exporting Member under Article 31(f) of the TRIPS Agreement to the extent necessary for the purposes of production and export of the needed pharmaceutical products to countries that do not have sufficient capacity to manufacture them. This waiver is subject to certain conditions to ensure transparency in the operation of the system and that only countries with insufficient domestic capacity import under it, and to provide for safeguards against the diversion of products to markets for which they are not intended.
- (ii) A waiver of the obligation under Article 31(h) of the TRIPS Agreement on the importing country to provide adequate remuneration to the right holder in situations where remuneration in accordance with Article 31(h) is being paid in the exporting Member for the same products. The purpose of this waiver is to avoid double remuneration of the patent owner for the same product consignment.
- (iii) A waiver of the obligation under Article 31(f) of the TRIPS Agreement on any developing or least developed country that is party to a regional trade arrangement of which at least half of the current membership is made up of countries presently on the United Nations list of least developed countries. The purpose of this waiver is to enable such countries to better harness economies of scale for the purposes of enhancing purchasing power for, and facilitating the local production of, pharmaceutical products.

101. The Chairman's statement at the time of the adoption of the Decision was designed to meet the concerns of those who feared that the Decision was too open-ended and might be abused in a way that would undermine the benefits of the patent system. For example, it recognizes that the system should be used in good faith to protect public health and not be an instrument to pursue industrial or commercial policy objectives; it addresses some concerns relating to the risk of diversion; and it sets out ways in which any differences arising from the implementation of the system can be settled expeditiously and adequately. The Decision also records that 23 countries have agreed to opt-out of using the system as importers<sup>102</sup>, to be joined by the ten countries acceding to the European Union after their accession. In addition, 11 other Members have agreed to use the system as importers only in situations of national emergency or other circumstances of extreme urgency.<sup>103</sup>

102. The waivers provided for in the Decision will remain in force until an amendment to the TRIPS Agreement replacing its provisions takes effect. The TRIPS Council will initiate work by the end of 2003 to prepare this amendment, with a view to its adoption within six months. It is understood that the amendment will be based, where appropriate, on the Decision.

103. The system established by the Decision is a small component of a much larger effort required to address the grave public health problems afflicting many developing and least-developed countries and to facilitate their access to medicines. The international community is increasingly seized with these problems, but further concerted action is required in the relevant fora, including to increase funding, develop social and health infrastructure, and to increase R&D for neglected diseases that afflict mainly the developing world.

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<sup>102</sup> Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, United Kingdom, and the United States of America.

<sup>103</sup> Hong Kong, China; Israel; Korea; Kuwait; Macao, China; Mexico; Qatar; Singapore; Chinese Taipei; Turkey; and the United Arab Emirates.

## 9. Special and differential treatment for developing countries in the WTO

104. Few would dispute that the liberalization of trade in goods and services must be an essential element in any strategy to stimulate growth and economic development. The Millennium Declaration, for instance, reflects this link in several of its specific goals and targets. The main contribution the WTO is expected to make in this regard is the fulfilment of its mandate in all areas of work contained in the Doha Development Agenda. Successful conclusion of the Doha negotiations will amplify economic opportunities for all countries and increase security and predictability as to the terms of market access and the rules of trade.

105. There is, however, also a recognition that individual countries may face constraints that impair their ability to benefit as rapidly from the opportunities offered by trade liberalization as others. Some may also experience difficulty in implementing certain WTO rules, raising the question of the balance between the resource costs of implementation and the benefits of certain agreements to the economy. With that in mind, Ministers at Doha also emphasized the notion of special and differential treatment (S&D) and mandated Members to strengthen S&D provisions and to make them more precise, effective and operational. An important part of what S&D provisions aim at is to address a lack of institutional capacity and resources for the management of trade policy and policy priorities. They also seek to render the trade policy regime as supportive as possible of the development aspirations of developing countries.

### S&D past and present

106. The concept of S&D is not new. The first S&D provisions can be found in the 1954-55 GATT Review Session, following which Article XVIII(b) and (c) on balance-of-payments provisions were incorporated into the GATT. As early as 1958, the Haberler Report recognized the special trade needs of developing countries.<sup>104</sup> The discussion it engendered resulted in an eight-point Plan of Action as part of the Kennedy Round, which was, however, never implemented to any significant degree. Nevertheless, the success of developing countries in placing their issues centre-stage in the GATT contributed to the decision to establish Part IV in 1965, designed to promote development and developing-country interests in the trading system.

107. During the Tokyo Round, the negative consequences of hitherto widely favoured import substitution policies began to be felt in many parts of the developing world. These experiences gave rise to a greater outward orientation leading to both heightened demands for market access and an increased focus on developing countries' own trade policies in order to remove an anti-export bias. A new framework was established to define and codify key legal rights and obligations of developing countries under the GATT. The 1979 Decision on Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries, also known as the Enabling Clause was the first formal recognition of the LDCs as a group in the GATT, and provided permanent legal cover for the Generalized System of Preferences, for S&D provisions under GATT agreements, for certain aspects of regional or global preferential agreements among developing countries, and for special treatment for least-developed countries. The Enabling Clause also restated the principle of non-reciprocity, as first spelled out in Part IV, and further stated that developing countries expected their capacity to make contributions, or negotiate commitments, to improve with the progressive development of their economies and improvement in their trade situation.

108. At the conclusion of the Tokyo Round, developing countries were afforded considerable flexibility. Yet, they had gained little from the system; they had neither been helped in formulating better trade policies nor received much from their trading partners in view of their own limited commitments and obligations. This situation changed drastically at the end of the Uruguay Round,

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<sup>104</sup> GATT (1958), *Trends in International Trade: A Report by a Panel of Experts*, GATT Secretariat.



when developing countries assumed a much higher level of commitments. Already at the second WTO Ministerial Conference, held in Geneva in May 1998, developing countries raised concerns as to their capability to implement all of their obligations. The “implementation” debate, in the course of which more than 100 proposals for changes or clarifications of existing agreements have been put forward, has since become a major element in WTO discussions.

### **Developments in the DDA**

109. As part of the Decision on Implementation – and emphasized also by the Ministerial Declaration – a work programme on S&D was agreed upon at Doha. This was established later by the Trade Negotiations Committee (TNC) in February 2002.<sup>105</sup> To a certain extent, it has resulted in a parallel track to implementation discussions with another 88 Agreement-specific proposals being put on the table. Their underlying motivation is similar to what has been driving implementation debates, and a quarter of the S&D proposals are virtually identical to implementation issues raised. Developing countries have aimed in particular at making best endeavour provisions mandatory and approval procedures for exemptions automatic, in order to make them more operationally effective and/or predictable in relation to the degree of policy flexibility afforded to them. A number of proposals also seek extended time-periods given the difficulty some developing countries encounter in implementing their obligations, bearing in mind the costs, administrative aspects and human capital requirements of implementation.

110. After long debate, the Special Session of the Committee on Trade and Development, by the beginning of 2003, requested the General Council for a clarification of its mandate. It had failed to meet a second deadline to make clear recommendations after having missed already the original deadline of July 2002 set by ministers. The work done so far cannot leave any doubt about the importance for a significant segment of the Membership of defining an appropriate approach to S&D and an adequate set of provisions thereon. The fact that there are more than 150 S&D provisions in the WTO Agreements greatly complicates matters, not least because taken individually, these provisions vary greatly in their degree of importance from a development perspective. The tendency until recently to place practically all of these provisions on the table has rendered more difficult the analytical task of identifying what matters most. Developing countries have shown some reluctance to allow the discussion to move in the direction of considering further the objectives, principles and modalities that should underlie the WTO’s approach towards S&D. This reluctance is partly driven by the concern that such a discussion will deflect attention from the specifics of what developing countries believe S&D provisions should comprise. At the same time, developed countries have been unwilling to consider some of the more far-reaching proposals on how to improve S&D provisions outside a negotiating context. Also, while going along with the almost exclusive focus on the 88 Agreement-specific S&D proposals, many developed countries found themselves unable to make S&D provisions legally enforceable in the absence of discussions on the broader systemic questions that also form part of the S&D mandate.

111. In February 2003 Members agreed that the Chairman of the General Council would hold consultations on how to take the S&D discussions forward. On the basis of his initial consultations with Members, the Chairman of the General Council put forward an approach based on the principle that all Agreement-specific proposals on S&D treatment were on the table and would be considered and that further progress could only be made by rationalizing the work through an informal categorization of the 88 Agreement-specific proposals that had been made. Based on this approach, all the Agreement-specific proposals were divided into three broad categories: (i) those on which there appeared to be a greater likelihood of coming to an agreement and which appeared to have a greater developmental value; (ii) those made in areas where mandated negotiations were ongoing, or those whose operative part was already being considered in the respective WTO bodies; and

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<sup>105</sup> WTO document TN/C/1, 4 February 2002.

(iii) those on which there appeared to be a wide divergence of views, and on which it seemed that progress may not be possible without a certain degree of redrafting. Consultations were held on this basis and during the run-up to Cancún, Members agreed in principle to make recommendations on 25 Agreement-specific proposals; this progress was reflected in the draft ministerial text sent to Cancún. A further three recommendations were included in the package at Cancún. However, these 28 Agreement-specific proposals are yet to be adopted by the Members.

## 10. **Regional trade agreements**<sup>106</sup>

### **Introduction**

112. The post-Doha period has been one of the most prolific in terms of notifications of regional trade agreements (RTAs) since the creation of the WTO, and the trend is set to continue, perhaps even to accelerate in response to Cancún.<sup>107</sup> Thus, Members, while working together in the DDA to improve the regulatory framework for global trade, are also building a patchwork of less-than-global trade agreements.

113. The promotion of free trade by targeting multiple fronts, globally, regionally and bilaterally<sup>108</sup>, may provide a certain logic in this situation: while preserving the philosophy and principles underlying the WTO, it recognizes that the WTO is not the only platform from which to promote these objectives. This approach is firmly grounded on the belief that RTAs complement the multilateral trading system (MTS) by encouraging trade liberalization. Many economists, however, highlight the discriminatory nature of RTAs, their potential to distort trade flows, and the diversion of limited resources from multilateral to regional and bilateral trade negotiations. The benefits of freer trade are not being questioned; rather the conditions under which it is pursued are at issue. The present proliferation of RTAs contains the seeds of a discordant regulatory environment for the development of world trade, disconnected from the spirit of WTO principles. That WTO Members currently lack effective monitoring and coordination mechanisms on RTAs adds to that concern.

114. Ministers at Doha put forward the objectives of promoting trade liberalization, fostering economic development, and complementing the multilateral trading system, as principles that should inform the current negotiations on RTA rules. Proposals have been made to enhance the transparency of RTAs, which, if agreed, would increase knowledge on the interrelation between RTAs and the MTS. A good step, but only a first step. The broad Doha negotiating mandate on WTO provisions for RTAs also calls for Members to explore a number of systemic issues, and thus better balance the global and RTA options.

### **A global view of RTAs**

115. The rapid surge in RTAs, which began in the early 1990s, has been such that virtually all WTO Members are engaged in furthering their RTA trade strategy. As of January 2004, 281 RTAs have been notified to the GATT/WTO, of which 157 have been notified since January 1995. Over

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<sup>106</sup> Regional trade agreements, even when they link only two neighbouring or geographically distant countries, are intergovernmental treaties through which signatories agree to more advantageous conditions, in the conduct of their mutual trade relations, than those applied to other, non-signatory, WTO partners.

<sup>107</sup> Since 1 January 2002, 41 RTAs have been notified to the WTO and, although a number of these were under negotiation before the Fourth Ministerial in Doha, negotiations on many more RTAs have begun or have been considered since.

<sup>108</sup> Sometimes defined as "competitive liberalization".

190 notified agreements are currently in force<sup>109</sup>, and 70 or more are estimated to be operational but have not yet been notified.<sup>110</sup>

116. The apparent rush to negotiate RTAs may reflect a certain anxiety by countries of being left behind. This has been particularly noticeable in East and Southeast Asia, a traditional bastion for multilateral-only trade liberalization. The United States is also actively pursuing the regional path, and China has recently negotiated RTAs with Hong Kong, China and Macau, China. By contrast, the EU has decided not to negotiate any new RTAs before the conclusion of the Doha Round. However, the impending negotiation of Economic and Partnership Agreements (EPAs) with the African, Caribbean and Pacific countries (ACP) show that RTAs are still present on the EU policy agenda.

117. The traditional imperative of RTAs for the economic integration of geographically contiguous markets has considerably weakened. Today, most agreements link pairs of partners, and an increasing number link countries thousands of miles apart.<sup>111</sup> At the same time, however, initiatives to establish large regional economic groupings, such as the Free-Trade Area of the Americas, the eastern enlargement of the EU, and ASEAN + 3 (China, Japan, and Korea), are also being pursued.

118. With regard to scope, earlier trends are being confirmed. Modern RTAs most often go far beyond traditional tariff-cutting exercises and even beyond existing multilateral rules by including regional rules on investment, competition, environment, and labour. Some WTO Members, as hubs of RTA networks, are increasingly taking advantage of RTA relations to break new ground in trade policy regulation.<sup>112</sup>

### Why RTAs?

119. Policy makers often emphasize the most conspicuous economic gains of RTAs, such as economies of scale, increased competition, and attraction of foreign direct investment<sup>113</sup>, to advocate that bilateral or regional trade liberalization complements multilateral liberalization. By contrast, for RTA sceptics, preferential agreements encourage beggar-thy-neighbour trade practices and detract Members' focus and resources from multilateral liberalization and rule making.

120. Analytical research on the impact of RTAs has been unable to produce solid responses to those arguments. Building upon Jacob Viner's theoretical approach and the concepts of trade creation and trade diversion, most empirical research has focused on the economic costs and benefits of dismantling barriers within a specific RTA for the parties and those left outside. Assessments vary for different RTAs, sometimes even for the same RTA.<sup>114</sup>

121. Even more difficult to assess are the economic effects of the increasing complexity of regulations introduced through these agreements. For instance, RTA rules of origin are usually quite stringent, the more so for products for which the margin of preference (difference between the MFN

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<sup>109</sup> Included in these statistics are notifications made under GATT Article XXIV, GATS Article V, and the Enabling Clause, including accessions to existing RTAs.

<sup>110</sup> By the end of 2007, if RTAs reportedly planned or already under negotiation are concluded, the total number of RTAs in force might well surpass 300.

<sup>111</sup> These cross-regional RTAs forge strategic trade relationships at non-MFN terms between countries, wherever they are situated. US-Jordan, EC-Mexico, and even New Zealand-Singapore FTAs, to take a few examples, hardly fit the geographical meaning of "regional" trade agreements.

<sup>112</sup> The growing relevance of standards for market access makes RTAs very attractive in this respect.

<sup>113</sup> These gains, however, can also be attained through unilateral liberalization or multilateral negotiation. Though politically more difficult to ensure, these gains are also potentially higher since MFN liberalization does not carry the discriminatory element of RTAs.

<sup>114</sup> For a thorough analysis of economic concepts and available evidence, see WTO (2003) *World Trade Report*, Chapter I.B.3.

and the preferential tariff) is larger. Origin rules could then have an effect similar to that of a trade barrier protecting domestic production of final goods. Rules of origin may even be seen by traders as a factor of production *per se*, to be considered in the same manner as the availability and cost of inputs, labour costs, infrastructure, etc. In that sense, rules of origin can influence investment decisions, both with respect to input sourcing and location of production, and thus reinforce an RTA's investment diversion.

122. In the absence of a decisive economic test in support of RTAs, and given that a plethora of RTA relations may entail a burden for business practice, why are countries currently putting so much energy into negotiating numbers of them?

123. Adherents to the political economy perspective would argue that, factors other than the expansion of trade and investment are at play.<sup>115</sup> One such factor would be the use of RTAs to cement diplomatic ties and forge new geopolitical alliances. The economic side of this strategy is to deal with certain trade issues at the bilateral or regional level while leaving the most sensitive ones (such as agriculture) at the multilateral level. A "hub-and-spoke" RTAs web may be particularly effective in this respect as the leverage the hub has on the spokes at the bilateral level could be used to advance or resist specific issues at the multilateral level. Hence, webs of RTAs can be effective in promoting "competitive liberalization", but the setting of common standards and regulations among a group of countries may also produce vested interests and powerful constituencies that will resist advances at the multilateral level.

124. Also, market-access concerns may have become a compelling factor in RTA negotiations. By not adhering to the RTA "band-wagon", a country could find its products discriminated against by competitors in markets where it has no preferential access. Economies with a relatively small domestic market are particularly vulnerable to these pressures and often have no alternative than to conclude RTAs despite the strain this may place on their limited administrative resources.<sup>116</sup>

### **Multilateralizing regionalism?**

125. Do RTAs complement the MTS, helping to build and strengthen it, or do they undermine it? To ensure that regional initiatives are fully instrumental, alongside multilateral efforts, in furthering the development of world trade and balanced international trade relations, there is a need for rules and mechanisms capable of driving RTAs on a firm intersecting road with the multilateral trading system.

126. The principles identified in 1947 and enshrined in GATT Article XXIV (for customs unions and free-trade areas, in trade in goods), and in GATS Article V (for agreements on trade in services) remain sound. WTO provisions basically direct Members that conclude RTAs to promote deep intra-regional trade liberalization and facilitation (including for sensitive sectors), while maintaining the significance of multilateral liberalization and rule making.

127. These principles, however, are not always reflected in today's regional landscape. One example is with respect to scope, coverage, and depth of liberalization, where the spectrum of RTAs varies widely. A study by the Secretariat<sup>117</sup> showed that, while RTAs have been effective in eliminating or substantially reducing tariffs on industrial products, they have not done the same for agricultural goods. Most often, agricultural trade, even on a preferential basis, remains subject to

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<sup>115</sup> Traditional political arguments, such as regional security, increased bargaining power, and locking-in of domestic reforms, are important motivating factors for certain small or politically unstable countries. However, they seem less relevant when considering the economic and political fabric of many of the countries actively pursuing the RTA option today.

<sup>116</sup> Even the United States and the EU admit that the administration of several RTAs strains their resources to the limit.

<sup>117</sup> WTO document WT/REG/W/46: "Coverage, Liberalization and Transitional Provisions in RTAs".

barriers.<sup>118</sup> Another example is the increasingly broader regulatory framework of RTAs, which, while potentially useful in raising new trade issues on the international agenda, is, in effect, weakening the WTO regulatory function. The latitude enjoyed by parties to RTAs to set up their own regulatory frameworks could lead to a global patchwork of differing trade regulations. These may not only be difficult to harmonize at a later stage, but may also become effective trade barriers, ultimately adding to the costs of doing trade.

128. That the WTO basic principles governing RTA formation have often been only partially applied suggests that RTAs are unlikely to melt automatically into multilateralism in the name of systemic rationality. It also indicates that the WTO Membership is not adequately equipped to face the challenges that the proliferation of RTAs pose for the functioning of the rules-based MTS. Clearly there is a need to beef up the principles on RTAs with mechanisms that are effective and operational.

129. The decision by WTO Members, meeting at the Fourth Ministerial Conference in Doha, to launch negotiations aimed at clarifying and improving the disciplines and procedures under the existing WTO provisions on RTAs, reflects these concerns. It is premature to speculate on whether these negotiations will result in a redrafting of the WTO-RTA relationship or to a piecemeal re-interpretation and clarification of existing rules. However, the focus on transparency during the initial phase of the negotiations would seem to reflect a growing awareness of the need for closer surveillance and public scrutiny of RTAs, and to encourage greater adherence with the relevant WTO provisions.

## **11. Disputes: the caseload becomes heavier**

130. The dispute settlement mechanism (DSM), established at the time of the WTO, was intended to ensure that Members abide by the WTO's rules and disciplines. It has been described as effective although measures have been suggested to improve its effectiveness, especially for "small" countries.<sup>119</sup> Many proposals to improve and clarify the Dispute Settlement Understanding have been tabled in special sessions of the Dispute Settlement Body as a part of the DDA negotiations.

131. Since 1 January 1995, a total of 306 cases have been filed with the Dispute Settlement Body (up to 31 January 2004). Of these, 125 have resulted in panels covering 155 disputes.<sup>120</sup> The majority of dispute settlement cases have involved industrialized countries: 60% (200) as complainant and 61% (187) as respondent. The developing country share has been some 40% (133 cases) as complainant, and 39% (119 cases) as respondent, during this period. Up until the end of 2003, the LDCs have not been participants in the system, either as complainants or as respondent. However, in January 2004, Bangladesh requested consultations with India.<sup>121</sup> Among the industrialized countries, the largest users are the Quad: the United States (76 as complainant and 81 as respondent), the European Union and its member States (63 as complainant and 61 as respondent), Canada (24 as complainant and 12 as respondent) and Japan (11 as complainant and 13 as respondent). A significant number of cases have been directly between the two largest traders, the United States and the EU (42,

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<sup>118</sup> Broad duty-free product coverage in RTAs tends to be the exception rather than the rule, since the domestic forces that resist trade liberalization at the multilateral level are just as likely to resist it at the regional level.

<sup>119</sup> For example, Hoekman, B. and P. Mavroidis (1999), "WTO Dispute Settlement, Transparency and Surveillance", World Bank, November.

<sup>120</sup> In some cases, where disputes are similar or concern the same issue, the dispute brought by several Members has been consolidated under one panel. For example, the recent US—Steel Safeguards case was established as one panel but includes eight complaints (WT/DS248, WT/DS249, WT/DS251, WT/DS252, WT/DS253, WT/DS254, WT/DS258, and WT/DS259).

<sup>121</sup> There have been some cases where LDCs participated as third parties to the dispute. Among the LDCs are: Bangladesh, Benin, Chad, Madagascar, Malawi, Senegal, and Tanzania.

or 14%). Among the developing countries, the largest users are Brazil with 34 cases (22 as complainant and 12 as respondent), India with 31 cases (15 as complainant and 16 as respondent), and Argentina with 24 (9 as complainant and 15 as respondent). The main areas of complaint are: GATT 1994 (222 requests of which 89 on national treatment, 80 on MFN treatment and 71 on quantitative restrictions)<sup>122</sup>, subsidies (53), agriculture (51) and anti-dumping (51).

132. Up to the end of January 2004, a panel report had been circulated in 81 cases (and possibly later appealed); 26 of these cases were initiated by developing countries; 52 by industrialized countries; and three by a combination of both. Looking at the two largest traders, the EU initiated 16 cases as sole complainant and pursued eight jointly with others; the United States initiated 12 as sole complainant and pursued seven jointly with others. In terms of respondents, there have been 25 developing countries in cases where a report had been circulated. The EU was respondent in 12 cases and the United States in 29 cases.

133. Several reasons are given for the lack of participation of LDCs in the dispute settlement mechanism. These include: lack of sufficient knowledge and resources to collect information on other Members' trade measures; resource constraints in mounting a challenge in the DSB; and also fear of counter measures that may affect normally good relations with the trading partner concerned. While some of these measures are difficult to address, efforts can be made on other fronts. On the issue of resource constraints, for example, the Advisory Centre on WTO Law (ACWL) was formed in October 2001 to help developing and especially LDC Members to utilize more effectively the WTO's dispute settlement mechanism. The ACWL provides: legal advice on WTO law; support to parties in WTO dispute settlement; and training in WTO law. The fees charged for its services are modest and vary with the size and standard of living of the user. During its first year (July 2001 to July 2002), the Centre provided legal advice to six countries, and assistance in six WTO DSB proceedings.<sup>123</sup>

134. More than 40 proposals to improve and clarify the Dispute Settlement Understanding have been tabled in special sessions of the Dispute Settlement Body in the context of the negotiations started under the DDA. These proposals address almost every stage of the process, including the enhancement of third-party rights; improvement of panel selection processes; treatment of confidential information; clarification of "sequencing" between compliance procedures and retaliation authorization procedures; strengthened remedies; enhanced transparency; enhanced Member-control over the process, and enhancement of developing country interests at various phases of the proceedings. A number of these proposals are reflected in the Chairman's text issued in May 2003.<sup>124</sup> Both the Chairman's text and other proposals put forward by Members will form the basis for future work.<sup>125</sup>

135. A large number of cases that go through formal WTO dispute settlement procedures are resolved through bilateral consultations between the Members involved. In instances where the case goes beyond formal consultations and a panel, it appears that most of these go beyond the panel to the appeal stage. In some cases, where Members have been unable to agree on implementation of the recommendations and rulings by the DSB, the disputes have been decided through recourse to the dispute settlement procedures under Article 21.5 of the Dispute Settlement Understanding (DSU). In general, Members have implemented the recommendations and rulings by panels and by the Appellate

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<sup>122</sup> There is some double counting as some of the 89 cases brought under Article III of the GATT 1994 are also brought under Article I.

<sup>123</sup> Further details are available from ACWL (2002), "Advisory Centre on WTO Law: Report on Operations, July 2001-July 2002" [Online]. Available at: <http://www.acwl.ch/> [10 June 2003].

<sup>124</sup> See TN/DS/9 for the latest version of the Chairman's text.

<sup>125</sup> At its meeting of 24-25 July 2003, the General Council agreed to extend the timeframe for completion of these negotiations by one year, until May 2004 (See WT/GC/M/81, paras. 71 to 75).

Body in the "reasonable period of time" determined under Article 21.3 of the DSU. However, in a few cases, under the Compliance Review Procedure of the DSU, compliance by Members has been contested, resulting in authorization by the DSB to suspend concessions and obligations (that is, retaliate) against the non-complying Member. There have been a few such cases since the formation of the WTO:

- EU ban on meat and meat products (complaints by the United States and Canada)
- EU banana regime (complaints by the United States and Ecuador)
- Brazil export financing for aircraft (complaint by Canada)
- United States Foreign Sales Corporations (FSCs) (complaint by the EU)
- Canada export credits and loan guarantees for aircraft (complaint by Brazil)

136. With the exception of retaliation authorized for the United States and Ecuador against the EU, which the retaliating countries decided to lift because of a change in the EU's import regime for bananas, these cases are still in force. The EU recently issued a list of products worth US\$4 billion in relation to the DSB's authorization to suspend concessions and obligations in the FSC dispute. It has indicated, however, that it will wait until January 2004 to suspend concessions and obligations on these products.

## **12. WTO Activities**

137. Some previous issues of this Report by the Director-General have included a section on WTO Activities. These are now presented in detail in the WTO Annual Report (forthcoming for 2004).

### **Annex 1: Measurement of tariff protection**

Overall tariff protection can vary considerably depending on the *tariff rates* and *weighting method* used.

#### *Tariff rates*

In computing tariff averages, a clear distinction should be made between the nominal, collected, and effective rates. The simplest and most straight forward nominal tariff rate to use is the applied MFN rate. The latter should be distinguished from the bound MFN rate, which is usually the highest rate of duty permissible under a Member's schedule of commitments at the WTO; bound tariffs can be exceeded, but only in special circumstances. Thus, average bound MFN rates tend to exceed applied MFN rates, especially in developing countries. Not all tariffs are bound, however, so that in some instances bound rates do not exist.

The collected tariff rate is the amount of customs duties as a proportion of the value of imported products; it thus reflects the average transfer to the Government from domestic consumers of the products subject to duty. In contrast to the applied MFN rate, the collected rate includes preferential rates and exemptions and therefore tends to be lower than the applied MFN rate; the greater the use of preferences and exemptions, the greater the difference between the two rates. The collected tariff rate does not necessarily bear any relation to the "marginal" tariff rate, however, which is the most appropriate indicator of the potential dead-weight (efficiency) losses caused by duties. In particular, it ignores prohibitive tariffs that do not yield any revenues at all. As a consequence, the collected tariff rate is not usually regarded as a reliable indicator of the level of tariff protection or of the potentially distorting effects of the tariff structure on domestic resource allocation.

In contrast to the nominal tariff rate, which concerns protection in relation to merchandise prices, the effective tariff rate relates to the production activity's value-added, thereby taking into account the impact of tariffs on inputs used by domestic producers (allowing for industry-specific tariff concessions). Insofar as domestic industry uses inputs that are subject to duty, the nominal tariff rate applied to imports of a particular product is not an indicator of the effective rate of protection (ERP). The extent to which value-added is protected is a more accurate indicator of the potential distortion in domestic resource allocation. A low level of nominal applied MFN protection may conceal high effective protection.

#### Weighting methods

Average nominal tariffs can vary considerably depending on the weights used. The main drawback of the simple (unweighted) arithmetic average of the tariff rates is that it takes no account of the relative importance of various products. Among the main alternatives to simple averages are weighted averages using the shares of imports or of domestic production.<sup>a</sup> The use of actual import volumes assigns a small weight to the highly protected products, however, thus tending to underestimate the degree of protection, with no weight at all being given to prohibitive tariffs. Furthermore, the use of variable import weights can result in spurious movements in weighted averages over time as the weights themselves would tend to be inversely related to a Member's tariff rates. By contrast, although the use of actual domestic production weights over-represents highly protected products, it avoids the spurious movements often associated with variable import weights. As none of the viable weighting methods is free from drawbacks, with each method giving rise to some aggregation bias, only simple averages for both bound and applied MFN tariffs are reported in Tables 1, 2 and 3.

Both simple and import-share-weighted averages have been used in relation to GATT/WTO negotiations. Import-weighted averages have been used by the GATT/WTO as an indicator of progress in achieving MFN tariff reductions. By contrast, commitments to reduce agricultural tariffs following the "tariffication" exercise agreed in the Uruguay Round were measured in terms of simple averages (presumably on simplicity grounds and because some tariffs may have been prohibitive). As required by the GATT/WTO, adjustments in the EU tariff in order to compensate non-Member countries for the accession of Austria, Finland, and Sweden were based on collected tariff averages for various groups of products.

- a The ideal weights to use in calculating import-weighted or production weighted averages are obviously the values of imports or production in the absence of barriers. Unfortunately, these values are unobservable. For effective rates of protection, weights should be based on domestic value-added rather than domestic production weights.



**Annex 2**  
**Tariff escalation by 2-digit ISIC category**

Country/ Year	Stage of process <sup>a</sup>	Food, beverages & tobacco	Textiles & leather	Wood & furniture	Paper, printing & publishing	Chemicals	Non- metallic mineral products	Base metal	Fabricated metal products & machinery	Other	Total
<b>North America</b>											
United States 2002	1	3.1	2.9	0.1	0.0	1.9	0.0	0.4	n.a.	1.6	3.8
	2	7.4	9.1	2.1	0.5	4.3	2.1	1.7	2.7	0.4	4.7
	3	12.4	10.0	2.2	0.6	3.9	5.6	2.5	2.2	3.6	5.5
Canada 2002	1	10.2	1.1	0.0	0.0	1.5	0.0	0.0	n.a.	1.2	5.0
	2	6.8	6.9	2.1	0.4	3.0	0.7	0.9	1.5	0.0	3.9
	3	34.1	13.5	5.1	1.0	4.8	3.8	3.7	2.6	4.8	8.9
Mexico 2001	1	21.9	12.6	13.0	4.8	12.5	7.0	10.1	n.a.	13.6	15.1
	2	27.1	17.8	18.6	13.3	11.3	17.7	12.9	13.8	13.0	13.2
	3	34.3	31.5	21.9	14.9	13.5	18.3	15.6	15.4	21.7	18.5
<b>Latin America</b>											
Argentina 2000	1	10.2	11.4	5.0	6.6	9.4	9.0	5.2	n.a.	11.7	9.7
	2	14.1	18.8	9.9	14.6	10.1	10.3	13.2	17.0	14.2	12.0
	3	16.5	22.4	18.0	15.2	12.1	14.2	20.6	14.1	20.5	15.0
Brazil 2000	1	10.2	10.7	5.0	6.6	9.7	10.7	5.2	n.a.	11.7	9.7
	2	14.0	18.7	9.9	14.4	10.1	10.3	12.9	17.0	14.2	11.9
	3	16.3	22.2	17.7	14.9	11.9	14.3	20.4	15.6	20.4	15.8
Chile 2003	1	6.0	6.0	6.0	6.0	6.0	6.0	6.0	n.a.	6.0	6.0
	2	6.9	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0	6.0
	3	6.0	6.0	6.0	5.7	6.0	6.0	6.0	5.7	6.0	5.9
Costa Rica 2000	1	12.3	3.0	8.0	1.7	2.5	8.6	1.9	n.a.	8.4	7.4
	2	12.7	8.5	8.2	3.8	2.2	3.1	3.0	1.0	3.0	4.3
	3	19.7	13.0	12.3	8.9	6.3	8.2	4.2	4.2	9.8	8.2
Dominican Rep. 2002	1	13.5	1.9	3.0	3.0	2.9	17.6	3.0	n.a.	9.5	7.9
	2	14.0	1.9	4.7	3.3	4.0	5.1	6.1	8.0	2.8	4.4
	3	17.0	17.4	14.8	12.5	9.0	11.1	15.0	7.2	16.4	10.8
Guatemala 2001	1	9.8	2.0	0.0	0.0	2.6	11.0	0.0	n.a.	8.8	5.8
	2	10.4	14.3	7.0	3.5	1.4	2.3	2.0	0.0	1.3	5.1
	3	12.8	19.0	12.1	7.7	6.5	7.2	4.1	4.0	9.6	8.1
Guyana 2002	1	24.4	5.4	7.5	5.0	7.0	20.0	5.6	n.a.	28.9	16.2
	2	16.7	5.1	9.7	4.9	5.8	5.9	5.6	5.0	5.0	6.1
	3	25.5	17.4	14.1	11.4	11.3	10.8	14.0	10.2	15.5	13.8
Honduras 2002	1	10.3	2.0	0.0	0.0	1.8	9.0	0.0	n.a.	8.2	5.9
	2	10.7	10.9	7.3	4.9	1.4	2.3	1.9	0.0	1.3	4.5
	3	12.4	13.4	11.9	7.4	5.9	7.1	3.8	3.6	9.5	7.1
Haiti 2002	1	2.4	4.5	0.0	0.0	0.0	12.0	0.0	n.a.	9.3	2.4
	2	4.7	5.3	0.0	0.6	0.7	1.4	1.3	0.0	0.0	2.0
	3	6.5	5.2	6.1	1.5	3.5	5.2	0.0	1.7	4.5	3.3
Venezuela 2002	1	14.6	11.0	5.0	6.3	8.2	9.0	2.8	n.a.	11.3	10.7
	2	17.7	17.5	12.1	12.4	7.5	9.3	11.1	7.0	15.0	10.9
	3	18.6	19.3	16.6	15.1	10.9	14.7	15.0	11.0	15.6	13.4
<b>Western Europe</b>											
EU15 2002	1	13.2	1.0	0.0	0.0	1.7	0.0	0.0	n.a.	1.2	8.1
	2	19.1	6.7	3.0	2.1	4.5	2.9	1.9	1.9	1.8	4.9
	3	18.7	9.8	2.1	1.5	3.8	4.0	2.4	2.5	3.0	7.0

Country/ Year	Stage of process <sup>a</sup>	Food, beverages & tobacco	Textiles & leather	Wood & furniture	Paper, printing & publishing	Chemicals	Non- metallic mineral products	Base metal	Fabricated metal products & machinery	Other	Total
Switzerland 2000	1	8.0	2.9	2.9	1.4	0.9	1.5	0.4	n.a.	2.0	4.4
	2	27.7	5.7	2.4	6.2	0.9	2.9	1.8	0.8	3.7	4.0
	3	36.8	6.3	2.3	4.1	2.3	2.7	2.4	1.1	2.0	8.5
<b>Eastern Europe</b>											
Bulgaria 2003	1	11.9	3.4	0.0	0.0	4.5	0.7	0.0	n.a.	2.3	8.1
	2	22.7	12.8	5.0	9.0	7.4	9.7	4.8	5.0	0.6	8.8
	3	27.3	19.8	13.7	9.4	9.1	13.4	11.0	6.7	7.7	13.5
Czech Republic 2001	1	1.7	0.2	0.8	0.0	1.9	0.3	0.3	n.a.	0.4	1.3
	2	17.6	4.6	2.7	7.6	3.8	8.2	3.8	2.8	8.7	4.9
	3	16.2	8.5	5.6	6.4	4.1	6.5	5.8	4.0	4.6	7.4
Slovak Republic 2001	1	1.7	0.3	0.6	0.0	1.9	0.3	0.3	n.a.	0.4	1.3
	2	14.4	4.6	2.7	7.1	3.7	8.3	3.8	2.8	8.7	4.7
	3	16.1	8.5	5.6	5.8	4.0	6.5	5.8	4.0	4.6	7.4
Slovenia 2001	1	4.9	2.1	1.0	0.4	3.9	1.0	0.1	n.a.	5.9	3.9
	2	16.2	9.6	4.6	8.7	7.8	5.4	6.9	6.2	10.0	8.3
	3	19.8	16.4	14.2	13.6	9.0	9.9	12.2	9.9	13.6	13.1
<b>Middle East</b>											
Bahrain 2000	1	4.7	9.5	6.3	5.0	6.4	8.3	5.0	n.a.	8.9	6.1
	2	2.8	10.0	5.2	5.2	5.4	5.1	5.0	5.0	5.0	6.2
	3	11.3	8.7	8.8	7.3	7.0	7.1	5.8	9.3	8.1	9.0
<b>East Asia</b>											
Brunei Darussalam 2000	1	0.0	0.3	12.0	0.0	0.0	0.8	0.0	n.a.	1.5	0.4
	2	0.0	0.1	19.4	0.0	0.1	0.0	0.0	0.0	0.0	0.4
	3	0.0	1.5	3.7	0.0	2.9	0.9	0.0	8.8	2.9	5.2
China 2002	1	15.3	13.0	0.0	0.0	7.1	2.3	2.8	n.a.	14.5	11.3
	2	28.1	15.1	5.7	8.4	7.2	10.7	5.3	6.8	8.9	9.7
	3	21.5	20.4	11.8	11.5	10.7	15.1	13.1	11.2	17.1	14
Hong Kong, China 2002	1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	n.a.	0.0	0.0
	2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Indonesia 2002	1	3.8	5.5	1.3	2.6	4.0	3.0	2.9	n.a.	7.5	4.1
	2	4.7	8.3	1.7	4.8	5.2	3.9	7.3	5.0	5.0	6.1
	3	12.9	12.2	9.5	4.4	7.1	6.4	9.5	6.6	10.4	8.6
Japan 2002/03	1	23.6	10.2	0.0	0.0	2.4	0.4	0.4	n.a.	0.2	14.5
	2	20.3	6.8	4.3	0.5	2.8	1.5	1.1	1.8	0.1	4.9
	3	22.6	12.0	2.0	0.3	2.0	1.1	0.5	0.3	2.8	7.8
Korea, Rep. Of 2000	1	54.7	5.5	3.5	1.8	6.7	5.0	1.7	n.a.	6.1	28.3
	2	99.3	8.8	5.9	7.8	8.0	7.5	6.0	8.0	8.0	10.9
	3	36.2	11.4	6.4	5.4	7.6	7.9	8.0	6.4	7.8	10.7
Malaysia 2001	1	1.2	0.3	15.0	0.0	7.6	3.3	0.3	n.a.	0.0	2.9
	2	5.3	13.3	2.2	6.5	7.2	22.0	9.3	1.0	7.5	7.7
	3	4.4	17.0	13.4	15.0	7.5	19.9	9.6	16.8	11.4	13.6
Singapore 2000	1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	n.a.	0.0	0.0
	2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Country/ Year	Stage of process <sup>a</sup>	Food, beverages & tobacco	Textiles & leather	Wood & furniture	Paper, printing & publishing	Chemicals	Non- metallic mineral products	Base metal	Fabricated metal products & machinery	Other	Total
Thailand 2003	1	17.4	3.8	1.0	1.0	9.1	2.8	1.0	n.a.	10.2	10.0
	2	24.6	15.6	10.3	11.8	5.1	14.7	7.3	12.8	17.5	9.5
	3	29.3	28.5	20.6	20.6	14.9	18.6	20.0	12.7	16.6	18.1
<b>South Asia</b>											
Bangladesh 2000	1	20.3	16.2	3.8	0.0	12.2	15.0	5.7	n.a.	25.1	15.0
	2	24.8	26.4	16.0	25.5	16.4	29.7	19.2	27.5	25.0	20.7
	3	29.5	36.5	30.1	28.1	24.2	25.2	27.8	18.6	32.2	24.1
India 2001/02	1	36.3	25.9	12.5	7.1	25.8	33.0	23.8	n.a.	35.0	28.6
	2	36.6	28.4	31.1	34.7	33.6	34.1	33.0	19.0	35.0	32.3
	3	48.2	34.2	34.8	29.4	33.5	34.1	35.0	29.1	33.4	33.0
Maldives 2002	1	16.3	19.3	15.0	25.0	21.3	25.0	21.3	n.a.	25.0	19.6
	2	14.5	17.5	15.0	11.4	14.8	19.5	21.2	25.0	10.0	16.8
	3	18.9	24.7	20.6	19.8	23.8	24.2	24	23.9	21.4	23.2
Pakistan 2001	1	12.6	10.4	8.8	6.1	13.6	10.0	14.7	n.a.	14.3	12.1
	2	19.2	23.6	19.1	24.1	14.0	23.8	15.4	20.0	25.0	17.5
	3	29.8	29.2	28.4	23.5	21.1	25.6	24.6	21.2	21.8	23.6
<b>Oceania</b>											
Australia 2001/02	1	0.3	0.1	2.5	0.0	1.7	0.0	0.3	n.a.	0.0	0.7
	2	0.4	9.9	3.9	3.9	1.7	1.9	3.0	2.0	4.2	4.1
	3	2.2	14.5	4.0	3.4	3.5	4.0	6.5	3.4	2.8	5.1
New Zealand 2002	1	0.4	2.4	0.0	0.0	0.9	0.0	0.0	n.a.	1.2	0.8
	2	2.6	2.8	3.1	5.2	1.2	0.5	2.3	0.0	4.9	2.2
	3	3.0	14.8	4.9	4.1	3.5	3.7	4.3	3.8	3.8	5.6
<b>Africa</b>											
Burundi 2003	1	35.5	14.6	14.0	10.0	10.3	34.0	10.0	n.a.	40.0	22.6
	2	35.3	33.3	12.0	10.7	10.7	10.3	16.6	10.0	10.0	18.4
	3	36.0	37.7	35.7	25.8	25.7	27.9	19.2	19.3	0.0	26.1
Gabon 2000	1	23.2	11.6	25.0	10.0	9.8	22.5	10.0	n.a.	24.7	16.6
	2	22.8	18.0	29.7	10.9	10.4	21.6	14.4	10.0	7.5	14.6
	3	25.6	28.0	27.3	18.2	16.8	22.8	12.7	15.9	27.9	20.2
Ghana <sup>b</sup> 2000	1	16.7	15.0	17.5	12.2	10.2	16.0	15.6	n.a.	21.3	14.9
	2	18.8	16.6	19.6	19.3	10.9	11.3	11.0	10.0	20.0	13.1
	3	23.8	30.0	24.5	16.9	22.7	14.6	18.2	7.6	18.2	15.5
Madagascar <sup>b</sup> 2000	1	24.7	7.0	5.0	5.0	7.0	25.0	5.0	n.a.	22.2	15.2
	2	18.3	22.2	14.7	9.5	5.8	8.4	8.4	15.0	7.0	11.9
	3	23.8	28.6	20.3	22.5	17.7	18.5	25.5	13.8	24.7	19.0
Mauritania 2001	1	15.9	2.8	0.0	0.0	2.4	18.6	5.5	n.a.	11.6	8.6
	2	10.9	12.6	9.3	6.9	4.7	9.7	8.3	8.0	5.0	8.0
	3	14.4	18.2	17.5	11.7	11.5	14.8	12.9	9.0	18.2	12.3
Mauritius 2001	1	11.1	6.8	0.0	0.0	1.7	0.0	0.0	n.a.	16.0	6.7
	2	18.9	0.0	1.8	0.0	4.2	5.9	12.3	0.0	7.5	5.5
	3	29.2	64.8	53.8	43.4	32.5	29.5	37.7	17.7	33.9	30.4
Morocco 2002	1	43.2	10.2	30.0	21.5	16.9	29.8	20.7	n.a.	32.2	29.2
	2	47.9	37.3	35.0	45.2	28.5	31.8	24.5	23.2	45.0	32.5
	3	61.8	46.4	47.3	41.9	30.8	38.2	41.0	20.9	34.1	34.3
Mozambiqu e 2000	1	22.7	3.8	2.5	7.5	3.3	7.5	2.5	n.a.	15.7	12.0
	2	17.7	21.6	7.5	10.3	3.8	7.3	5.6	7.5	23.1	9.5
	3	23.8	27.5	21.1	18.3	15.1	11.5	22.5	10.7	26.0	16.6

Country/ Year	Stage of process <sup>a</sup>	Food, beverages & tobacco	Textiles & leather	Wood & furniture	Paper, printing & publishing	Chemicals	Non- metallic mineral products	Base metal	Fabricated metal products & machinery	Other	Total
Niger <sup>b</sup> 2002	1	15.8	9.1	7.5	7.5	8.9	10.5	7.5	n.a.	10.6	11.7
	2	17.1	18.4	11.9	10.3	8.7	19.4	12.0	22.5	11.2	12.5
	3	19.3	21.7	20.0	16.6	14.8	19.0	19.8	13.3	20.5	16.3
Senegal <sup>b</sup> 2002	1	16.1	9.1	7.5	7.5	8.9	10.5	7.5	n.a.	10.4	11.8
	2	16.9	19.0	12.5	10.1	8.7	19.4	12.1	22.5	11.3	12.6
	3	19.4	21.8	20.0	16.6	14.7	19.0	19.4	13.3	19.8	16.2
South Africa 2002	1	10.7	5.0	0.0	0.0	3.7	0.0	0.0	n.a.	2.5	5.5
	2	10.3	22.1	6.2	5.9	3.5	4.9	3.2	1.7	4.3	12.9
	3	15.4	32.4	15.5	7.7	7.9	7.1	2.9	5.2	7.3	11.5
Zambia 2002	1	20.0	14.6	22.5	5.0	6.3	15.8	2.8	n.a.	18.8	14.2
	2	19.1	14.0	22.8	9.9	6.0	13.1	7.1	21.0	12.5	8.8
	3	20.7	24.1	23.1	18.1	15.5	14.3	20.3	12.8	19.8	16.5

n.a. Not applicable.

a 1 = First stage of processing; 2 = Semi-processed; 3 = Fully processed.

b Including import taxes and (in the case of Senegal and Niger) other duties and charges.

Note: For countries with non-*ad valorem* rates AVEs have been used as available. In case of unavailability, the *ad valorem* part is used for compound and alternate rates. Averages differ from those in last year's publication due to changes in concordance between HS and ISIC.

Source: WTO Secretariat calculations, based on data provided by the Members.