

Doha Round and Developing Countries: Will the Doha deal do more harm than good?

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Now that the tear gas has cleared in Hong Kong and negotiations have moved to London and Geneva, the broad outlines of a new WTO agreement are emerging from the haze. Advocates of meaningful economic development cannot be happy with what they see. As the Doha negotiations limp toward an illdefined finish line, it is not surprising that many developing country negotiators are asking themselves if the emerging deal is better than no deal at all.

The round began with vows to enable poorer nations to develop their economies. The deal taking shape now offers limited economic gains for the developing world as a whole, and many countries end up worse off, according to recent economic projections. Hidden behind those modest benefits are costs that should give negotiators pause. Tariff losses and other "adjustment costs" may be prohibitively high, some countries will experience a loss in national production after opening their manufacturing and services sectors to rich-country competition, and all face the loss of autonomy to pursue the kinds of national development policies that have proven effective in the past.

Small Gains, and Only for a Few

The World Bank and other economic modelers have generated a raft of new projections of the economic gains from further global trade liberalization. Though they differ in important ways, the recent estimates share two features: The economic benefits are much smaller than previously estimated, and developing

countries see losses or small gains of well under one percent of GDP.

The shrinking gains since the earlier estimates are by now well known. For the Cancun ministerial, the World Bank and others produced estimates of more than \$500 billion in developing country benefits from liberalization. More than 100 million people were to be lifted out of poverty. These estimates, which used a 1997 base year, were rightly updated for the Hong Kong meetings. The new figures include China's liberalization as an accomplished fact rather than a prospective gain from the negotiations, incorporate existing trade preferences, and use applied rather than bound tariff rates, along with several other improvements.

Projections of global gains from full trade liberalization dropped from \$832 billion to \$287 billion; the developing country share fell from \$539 billion to just \$90 billion. Fortunately, the modelers did not stop there. An added feature of these new economic analyses is the attempt to project not just the abstract gains from a level of worldwide liberalization no one expects to happen but also the likely gains from the current round of negotiations.

The results of two recent projections are presented in Table 1. The World Bank's projections, which were out before the Hong Kong meetings and received widespread publicity, showed a "likely Doha scenario" of just \$16 billion, out of a global total of \$96 billion.

In Hong Kong nations agreed to allow exemptions from negotiated liberalization levels for so-called Special and Sensitive Products (SSPs) in agriculture. As the table shows, after adjusting the Bank's likely scenario for the special products exemptions, based on its own modeling scenario, developing country gains fall to just \$6.7 billion, out of a total of \$38.4 billion. [1] This amounts to less than a penny a day for those in the developing world.

Using the same underlying economic model and data, the Carnegie Endowment for International Peace (CEIP) produced a different set of projections based on a policy scenario more representative of what was negotiated in Hong Kong and an interesting adjustment to the assumptions used by the World Bank and most other modelers. [2] Most models assume full employment; a country that expands its exports will only do so by shifting workers from a contracting

sector to an expanding one. CEIP adjusted its modeling to recognize the prevalence of urban unemployment and rural underemployment in developing countries. Thus export gains can lead to net expansion of employment with a greater effect on national income. However losses of export market share can mean greater unemployment, as well, with no guarantee that workers will be absorbed in other sectors. The presence of unemployed labor also means that competitive exporters can expand production and exports without facing increased wages and thus will maintain their price competitiveness until the unemployed and underemployed labor is absorbed.

The gains to currently competitive countries will be larger, but the prospect for less competitive countries to gain market share in the future will be more remote.

The CEIP projections remain of the same order of magnitude as the Bank's, with global gains from a more limited "Hong Kong scenario" of just \$43 billion. Because of CEIP's more realistic policy scenario and assumptions, a larger share - \$21.5 billion - goes to developing countries. Also of interest are their findings that the gains come not from agriculture but entirely from manufacturing and go overwhelmingly to China, which gets \$10.6 billion - nearly half of that income.

The CEIP study concludes that the emerging Doha deal will leave some of the world's poorest countries worse off unless issues of surplus labor in developing countries are dealt with in a sustained manner.

While these results highlight important differences between the two studies, and the authors draw very different conclusions, they coincide on the order of magnitude of the developing country gains from the Doha negotiations. The developing country share is projected to be small, between \$6.7 billion and \$22 billion, well under one-half percent of GDP. These findings coincide with other recent studies.

A paper by the International Food Policy Research Institute (IFPRI) found developing country gains ranging from \$8-21 billion, depending on the "levels of ambition" in agricultural reform. [3] Others have found even smaller gains, with some projecting negative welfare effects for developing countries as a whole from agricultural trade reforms alone. [4] Even projections that include services liberalization yield only an additional \$6.9 billion for the developing world in a likely scenario of fifty percent reduction in services

trade barriers. [5]

The Case for Special Products

The World Bank suggested in issuing its study that the results highlighted the importance of pursuing deep cuts in order to realize the gains for developing countries, and the importance of developing countries making deep cuts themselves. The Bank also argued that virtually all the gains from agricultural liberalization would be lost if negotiators allowed any significant level of exemption for “Special and Sensitive Products” (SSPs), which the WTO’s July 2004 Framework Agreement explicitly sanctioned to promote “food security, livelihood security, and rural development.”

The World Bank ran a simulation allowing a modest SSP exemption for 2 percent of product lines for rich countries, 4 percent for developing countries. Indeed, they found that the \$9 billion in gains for developing countries from agricultural liberalization vanished with even that modest SSP allowance.

As with much of the Bank’s presentation of its research, the underlying numbers do not always justify its policy conclusions. The economic rationale for recognizing special products for developing countries is well-founded, even if the case for developed country “sensitive products” is not. Many developing countries still have sizable populations of small-scale farmers growing basic staples for home consumption and sale on local markets. Trade liberalization can swamp those producers with a flood of imports from richer countries. Often, those crops are subsidized in both explicit (farm payments) and implicit (oil or irrigation subsidies) ways. In addition, large transnational exporters wield undue market power, limiting full competition in the marketplace. In such a context, continued protection is warranted as a form of market correction rather than market distortion; tariffs are often the best available policy instrument to achieve this.

The World Bank’s data on the costs of exempting SSPs suggest that those costs are very low - about \$9 billion for the developing world as a whole, well under a penny a day per capita. Little of that cost comes from granting special product exemptions to developing countries, so there is little justification for denying developing countries ample policy space

under SSP guidelines.

Hidden Costs

Much of the discussion of the Doha Round's development impact has centered on the potential benefits of the round, but less attention has been paid to the costs. When the costs of adjustment, deindustrialization, and the loss of policy space for development are juxtaposed with the relatively small projected gains from the deal on the table, it becomes clear why many developing country governments are questioning the utility of the Doha round.

In terms of adjustment costs, tariff losses for developing countries could outweigh the benefits by a factor of four. These losses are not reported in discussions of the gains from trade because they are assumed away in the modeling exercises. A key assumption in most models is that governments' fiscal balances are fixed-in other words any losses in tariff revenue are offset by lump sum taxes. While there is evidence that shifting from trade to consumption taxes can be better for welfare, in the real world such taxation schemes cost political capital and in some cases may not even be possible. Indeed, it has been shown that tariffs may be preferable in developing countries with large informal sectors that cannot be taxed efficiently.

Using the same model as the World Bank, UNCTAD has projected tariff revenue losses under the proposed reduction levels in the ongoing NAMA negotiations. [6] These tariff revenue losses for the world and selected regions and countries are shown in Table 2 compared to the World Bank benefit projections with and without SSPs.

Many developing countries rely on tariffs for more than one quarter of their tax revenue. For smaller nations with little diversification in their economies, tariff revenues provide the core of government budgets. According to the South Centre, in the Dominican Republic, Guinea, Madagascar, Sierra Leone, Swaziland, and Uganda tariff revenues represent more than 40 percent of all government revenue. Table 2 shows that the tariff revenue losses will be significant and even outweigh the benefits. Total tariff losses for developing countries under the NAMA could be \$63.4 billion, or almost ten times the projected gains. Africa, the Middle East, and

Bangladesh-areas with large informal economies and where tariffs are key for government revenues-are predicted to be net losers in terms of benefits; they will suffer even larger losses in tariff revenues.

In a recent issue of Foreign Affairs, Jagdish Bhagwati commented that more attention needed to be paid to this issue: "If poor countries that are dependent on tariff revenues for social spending risk losing those revenues by cutting tariffs, international agencies such as the World Bank should stand ready to make up the difference until their tax systems can be fixed to raise revenues in other, more appropriate, ways."

At present even the most ambitious "aid for trade" packages come nowhere near filling the gap in lost tariff revenue predicted by UNCTAD.

De-industrialization

Recent UNCTAD research highlights how far the Doha Round has strayed from its development mission. Development is a process of transforming an economy from concentrated assets based on primary products to a diverse set of assets based on knowledge. This process involves investing in human, physical and natural capital in manufacturing and services while moving away from extractive industries and lowproductivity agriculture. The move from lessdeveloped to developed country has been associated with industrial diversification.

According to UNCTAD, India is predicted to experience significant output and employment losses in high value-added sectors such as chemicals, leather, and food processing industries while gaining in textiles and apparel, further down the technological ladder. [7]

Brazil is predicted to lose in the metals, machinery, motor vehicles, and chemicals industries in exchange for modest gains in its soy and meat sectors. In both cases, these large and dynamic developing countries are projected to see their levels of industrial development decline with a Doha agreement.

Countries that have yet to develop their industrial sectors will find themselves even more locked in to primary production. According to the CEIP projections, only China sees significant gains in its manufacturing sector from a Doha agreement. Not surprisingly, developing countries see their

terms of trade - the price ratio between a country's exports and its imports - decline, by .74 percent according to CEIP. Declining terms of trade indicate a failure to move up the value chain to higher value-added forms of production. According to CEIP, India's terms of trade will decrease by 1.62 percent. Even Brazil is predicted to see its terms of trade decrease by .18 percent. With long-term trends showing declining prices for non-oil commodities, terms of trade are likely to worsen over time.

With these structural shifts, of course, comes unemployment. While some nations may see net gains in employment, many will see job losses in industrial areas as part of the deindustrialization process. These workers are unlikely to move to rural or coastal areas to work in expanding industrial agriculture or apparel industries, adding to urban unemployment in countries such as Brazil.

Conclusion

Of course, the biggest cost to developing countries is hard to calculate - the loss of policy space. In exchange for limited gains in agriculture and low-technology manufacturing, developing countries will have to surrender the right to use many of the policy instruments that have proven successful in moving countries toward higher levels of development and improved incomes for their people. Where the Asian Tigers, for example, used a shifting mix of selective tariffs, export and credit subsidies, and the strategic use of foreign investment, many of those policy instruments will no longer be available following a Doha deal.

Under the proposed NAMA agreement, for example, nations will have to bind virtually all of their tariffs using the so-called Swiss Formula, which prevents countries from keeping low average tariffs while using high tariffs in strategic industries. Like the developed world before them, nations such as Taiwan and South Korea have relied on such tariff strategies to industrialize their economies, and China and India now make liberal use of such measures. These countries also developed formidable financial, telecommunications, and construction sectors, taking advantage of the policy space in the previous agreement to hold off on liberalizing key service sectors. Current proposals would adopt a "one size fits all"

approach that would make developing countries liberalize a certain percentage of all services at once with no room for strategic exemptions. WTO members agreed that the current round of trade talks should focus on development. The deal that seems to be emerging, however, is unlikely to deliver. The benefits are small for developing countries and the costs are high. It will be up to developing country governments to decide whether the Doha deal does more harm than good to their prospects for economic advancement.

TABLES

Table 1. Assessing the Gains from Doha

Welfare Gains from Partial Trade Liberalization, Two Models (billions of 2001 US dollars)

	World Bank CEIP Hong Kong			Doha Scenario* Scenario**		
	Manuf.	Agric.	Total	Manuf.	Agric.	Total
High-income countries	13.6	18.1	31.7	16.4	5.5	21.9
Developing countries total	7.1	-0.4	6.7	21.7	-0.06	21.5
Brazil	0.3	1.1	1.4	0.8	0.3	1.1
India	2.0	0.2	2.2	2.3	-0.04	2.3
China	2.2	-1.5	0.7	10.6	-0.3	10.3
Argentina	0.3	1.0	1.3	0.2	0.4	0.6
Bangladesh	0.1	0.0	0.1	-0.03	-0.02	-0.05
Vietnam	0.4	0.0	0.4	1.8	-0.2	1.6
South Africa	0.3	0.3	0.6	0.3	0.06	0.3
Rest of Sub-Sah. Africa	0.6	-0.3	0.3	-0.08	-0.11	-0.19
World total	20.7	17.7	38.4	38.1	5.4	43.4

* Anderson and Martin, *Agricultural Trade Reform and the Doha Development Agenda*, World Bank, 2005; Table 12.14, Scenario 7 with SSPs.

** Polaski, Sandra, "Winners and Losers: Impact of the Doha Round on Developing Countries," CEIP 2006; Figures 3.1, 3.3, 3.5, 3.8.

**Table 2. Doha's Hidden Price Tag
Doha Benefits vs. NAMA Tariffs Losses
(billions of 2001 US dollars)**

	WB "Likely" Scenario*	WB Doha Scenario*	NAMA Tariffs Losses**
Developed	79.9	31.7	38.8
Developing	16.1	6.7	63.4
Selected developing regions	.	.	.
Middle East and North Africa	-0.6	-0.1	7.0
Sub-Saharan Africa	0.4	0.6	1.7
Latin America and the Caribbean	7.9	2.4	10.7
Selected Countries	.	.	.
Brazil	3.6	1.4	3.1
India	2.2	2.2	7.9
Mexico	-0.9	-0.7	0.4
Bangladesh	-0.1	0.1	0.04

* Anderson and Martin (2005), Agricultural Trade Reform and the Doha Development Agenda. World Bank Table 12.14; scenario 7, and adjusted for SSPs.

** De Cordoba and Vanzetti (2005). Coping with Trade Reforms. UNCTAD. Table 11.

Endnotes

* For further background on this issue, see: Wise and Gallagher, "Doha Round's Development Impacts: Shrinking Gains and Real Costs," RIS Policy Brief #19; Kevin Gallagher's Putting Development First: The Importance of Policy Space in the WTO; Frank Ackerman, "The Shrinking Gains from Trade: A Critical Assessment of the Doha Round Projections," GDAE Working Paper No. 05-01, October 2005: Available at http://www.ase.tufts.edu/gdae/policy_research/WTO05.htm

1 Anderson, Martin, and van der Mensbrugghe, "Market and Welfare Implications of Doha Reform Scenarios," in Agricultural Trade Reform and the Doha Development Agenda, Anderson and Martin, World Bank 2005. Doha scenario includes in agriculture, elimination of export

subsidies; reductions in domestic subsidies of 28 percent for the U.S., 18 percent for the EU, and 16 percent for Norway; cuts in bound tariffs for developed countries in three bands (45 percent, 70 percent, and 75 percent), with four bands for developing countries (35 percent, 40 percent, 50 percent and 60 percent cuts), and none for LDCs; SSP exemptions of 4 percent for developing and 2 percent for developed countries (from Scenario 2); in manufacturing, developed countries reduce bound tariffs 50 percent, developing countries 33 percent, LDCs none. Gains include estimated income growth through 2015 from the 2001 base year, which increases the estimates by about 45 percent. Numbers in Table 1 are from Scenario 7 with the gains from agriculture adjusted downward for SSPs, as modeled in Scenario 2.

2 Polaski, "Winners and Losers: Impact of the Doha Round on Developing Countries," CEIP 2006. Hong Kong Scenario is more modest than the World Bank's Doha scenario. It includes, in agriculture, elimination of export subsidies; 33 percent reductions in domestic support for developed and developing countries; cuts in applied tariffs of 36 percent for developed countries, 24 percent for developing countries; no Special and Sensitive Products exemption; in manufacturing, 36 percent tariff cuts for developed, 24 percent for developing countries. LDCs are exempt from all reduction commitments. Gains are for 2001, so without incorporating income growth through 2015.

3 Bouet, Mervel, and Orden, "More or Less Ambition? Modeling the Development Impact of U.S.-EU Agricultural Proposals in the Doha Round," IFPRI, 2005.

4 See, for example, Bouet, Bureau, Decreax, and Jean, "Multilateral Agricultural Trade Liberalization: The Contrasting Fortunes of Developing Countries in the Doha Round," CEPII Working Paper No. 2004-18, November 2004. Three recent papers offer good overviews of the different models and their results: FAO, "Trade Policy Simulation Models: Estimating global impacts of agricultural trade policy reform in the Doha Round," FAO Trade Policy Technical Notes No. 13, 2005; Bouet, "What Can the Poor Expect from Trade Liberalization? Opening the Black Box of Trade Modeling," IFPRI, MTID Discussion Paper No. 93, March 2006; Congressional Budget Office, "The Effects of Liberalizing World Agricultural Trade: A Survey," December 2005.

5 Francois, J., H. van Meijl and F. van Tongeren (2003). Trade Liberalization and Developing Countries Under the Doha Round. Tinbergen Institute Discussion Paper

2003-060/2. Rotterdam and Amsterdam, Tinbergen Institute. These figures are based on the older 1997 base year data and would themselves have to be revised downward to reflect the changes in the world economy since then.

6 UNCTAD uses the so-called Swiss Formula with approximate coefficient of 10.

7 UNCTAD (2006). Trade Adjustment Study: India. Geneva.

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P.S.

* RIS Policy Briefs # 22, April 2006.

* Research and Information System for Developing Countries (RIS) Policy Briefs are prepared to communicate results of RIS research on specific policy issues to the policy makers. This policy brief has been prepared by Timothy A. Wise, Deputy Director of the Global Development and Environment Institute at Tufts University; and Dr. Kevin P. Gallagher, a Senior Researcher at the Institute, and a Professor of International Relations at Boston University.