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Global trade

Weighed in the balance

WASHINGTON, DC

The Doha round of world trade negotiations was supposed to lift many millions out of poverty. It looks unlikely to do so

LAUNCHED in a spirit of global solidarity two months after the terrorist attacks of September 11th 2001, the Doha round of global trade talks has always been billed as being about more than just trade. Its official title is the "Doha Development Agenda". Its purpose, as Tony Blair recently put it, is "to create the conditions in which millions of people will have a chance to escape poverty."

Such lofty aspirations are sure to be given voice often in Hong Kong next week, when the world's trade ministers meet with the aim of reviving the flagging negotiations. Whether the Doha round will live up to those aspirations is less certain. This is not only because the talks are stalled. Perhaps more important, the benefits of the round to the world's poorest people have anyway been overstated. And most important of all, neither developed nor developing countries have been ambitious enough to seek the degree of trade liberalisation needed to help the poorest.

Start, though, with the state of the talks. Originally, they were supposed to have finished a year ago. Then it was agreed that the outlines of a deal would be set in Hong Kong. That deadline will also now be missed. The most important decisions—how much to cut farm subsidies and tariffs or to lower barriers to industrial goods—will be put off again, probably until March.

The gaps, especially on tariffs, between the main sides are too wide to be bridged. America wants deep cuts across the board. The European Union wants to see big developing countries, in particular, reduce industrial protection, but is loth to slash its farm tariffs—the developing countries' price for any cuts of their own.

The Hong Kong meeting may yield something to allow the politicians to claim that Doha's pro-poor mission will be fulfilled: maybe a promise of the faster removal of cotton subsidies; perhaps a pledge by the rich to waive tariffs and quotas on all, or almost all, exports from the 50 countries officially designated as "least developed". But not even this is assured. America, a heavy subsidiser of cotton, opposes a special deal for the crop. Its textile industry is also opposed to free access for imports from the poorest countries.

Eventually, if not in Hong Kong, a deal of some sort will probably be done. Economists have been ruminating on what this agreement might contain and how much it might help the world's poor. Their conclusions are disappointing. Two new books* from the World Bank suggest that the Doha round, if it stays on its present course, will do much less for the poor than promised.

And found wanting

The Bank's most comprehensive trade model, for instance, estimates that if trade in industrial and farm products were fully freed, the one-off gains from reallocating resources more efficiently could boost income in developing countries by $86 billion by 2015 and pull an extra 30m people out of extreme poverty. Two-thirds of these would be in Africa.

A more plausible assumption, however, would split the difference between the American and European positions on farm trade and allow developing countries to cut their tariffs by much less than rich ones. This would raise developing countries' income by $16 billion by 2015. Only 2.5m more people would be freed from extreme poverty than if there were no deal at all. Sub-Saharan Africa would gain almost nothing and only 500,000 of its people would escape extreme poverty.

The Bank used to sound much more optimistic (see chart 1). In early 2002, just ▸▸

* "Agricultural Trade Reform & the Doha Development Agenda", edited by Kym Anderson and Will Martin, and "Putting Development Back into the Doha Agenda: Poverty Impacts of a WTO agreement", edited by Thomas Hertel and Alan Winters.

after the Doha round was launched, it estimated that the efficiency gains from full trade liberalisation would boost developing countries' increase by almost $200 billion and reduce the number of extremely poor by over 100m. Subsequently, it suggested that a less ambitious round could still lift at least 60m people out of the direst poverty. Now, says one Bank economist privately, Doha could mean only "small beer" for the poor.

Why does the round now seem to offer so little? Part of the reason lies in the computable general equilibrium (CGE) models used by the Bank's (and other) economists. Some models are "static", measuring only the one-off reallocation of resources that comes from freeing trade, which means they understate the long-term gains. Others are "dynamic", trying to capture how trade gains boost investment and productivity growth. The Bank's flagship model lies in the middle. It captures only the one-off gains, but looks at their effect on the world economy over a decade. It misses out trade's effects on productivity and the benefits of freer trade in services. Therefore it understates the likely long-term gains.

Some aspects of early estimates exaggerated Doha's potential. Until this year, all CGE models were based on tariff data from 1997 and hence attributed all liberalisation since then (such as that coming from China's accession to the World Trade Organisation) to the Doha round. Nor did they take into account the preferential low tariffs that rich countries already offer to some of the poorest countries.

The Bank's economists have also scaled back their estimates of how much trade reduces poverty. Early models assumed that extreme poverty in any country would fall by 2% for every 1% increase in its income. The new numbers suggest a bigger impact in East Asia but a far smaller effect (0.9%) in sub-Saharan Africa.

You might conclude from all this that free trade has little to offer the world's poor, especially in Africa. That would be wrong. Even the Bank's new estimates say that fully free trade in goods could boost

Africa's income by more than, say, this year's much-hailed deal on debt relief.

The Doha round has always been very unlikely to end in fully free trade. Yet even by more modest standards, it has ended up with the wrong emphasis. Worse, it has been plagued by a lack of ambition on the part of the poor as much as the rich.

Agriculture is the prime example of how the round has got its priorities wrong. In goods, freer farm trade could in theory yield the most for the world's poor. However, negotiators have made more progress in pledges to cut rich countries' subsidies than they have in slashing tariffs—and more than 90% of the gains from freer farm trade come from tariff-cutting. Contrary to received wisdom, slashing the rich world's trade-distorting subsidies has a relatively small effect on poor countries.

Granted, big developing-country exporters, notably Brazil and Argentina, would gain from reduced subsidies. So would Africa's cotton producers (which is why a quick deal on cotton subsidies is a good idea). But many poor countries are net importers of food. If subsidies are removed, world food prices will rise, helping their farmers but harming their consumers. Overall, developing countries do gain, but by much less than from lower tariffs.

And if the rich cut tariffs, it would hurt some of the poor, because America and the EU already offer selected poor countries preferential access to their markets. These countries lose if tariffs fall, because the margin of preference is eroded. European officials have used this as an argument against deep tariff cuts. "Be aware", Peter Mandelson, Europe's top trade negotiator, warned the poorest countries last week, "that some of the alternative tariff-cutting proposals on the table will...wipe out whole sectors of your economy."

However, the truth is that thanks to restrictive rules, tariff preferences, particularly the EU's, are less generous than they look. Nor are they all targeted at the poor: many of the world's poorest people live neither in the 50 least developed countries nor in Europe's ex-colonies. And although a few countries (such as Malawi, Mauritius and several Caribbean islands) would lose a lot, most would lose a little. Overall, the gains from lower tariffs outweigh the costs. Cutting tariffs and compensating the losers with increased aid makes sense.

A lack of ambition

Rich countries have deservedly taken much of the blame for the sorry state of the Doha round. But an important reason why the round will produce fewer benefits than it could has more to do with poor countries' trade policies. Half of what developing countries could gain from fully free trade would come from their own tariff cuts, because a third of their exports are to other poor countries and because their tariffs are much higher than those of the rich. But because trade diplomacy starts from the assumption that free trade is a concession to foreigners, not a boon in itself, poor countries are usually expected to liberalise less. Doha's "pro-poor" promise has merely reinforced this practice.

The negotiations are suffused with special terms for developing countries. The poorest, including most of Africa, will not have to lower their legal tariff limits at all. Even the likes of India or Brazil will have more exceptions and will cut their tariff limits by less than the rich.

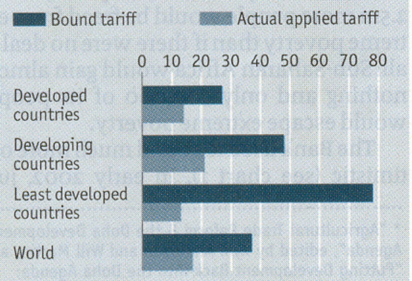
Most developing countries set actual tariffs far below the legal ceilings, but this makes matters worse, not better. They need to cut their negotiated level by more if they are to reduce their levies at all. The EU's average actual farm tariff, for example, is 12%, while the average bound tariff is 21%. In developing countries the average actual farm tariff is 21%, against a bound rate of 48%. In the poorest countries the discrepancy is greater still (see chart 2). Poorer countries would gain most by making proportionately bigger cuts, the opposite of the Doha logic.

It is true that the poorest countries often face the biggest obstacles to reaping the gains from trade and that economists' models often assume these obstacles away. Many rely on tariffs as a source of government revenue. Weak infrastructure and underdeveloped credit markets can make economic restructuring difficult. These problems underline why trade liberalisation is no substitute for either more domestic reform or foreign aid. They also suggest that some of the poorest countries need more time to open their markets than others. Unfortunately, the Doha negotiators are taking that logic much too far. And the losers will be the world's poor. ■

Food for thought 2

Average agricultural import tariffs*

2001, % ad valorem equivalent



Source: World Bank *Weighted by imports