

**Informal Review Session on Chapter III of the Monterrey
Consensus**

**"International trade as an engine for development"
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Key messages by:

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1. Trade liberalisation is good for development

- Despite frequent political rhetoric and popular press, in fact any serious economist would agree that trade is good for growth.
- History gives us the most persuasive arguments for trade liberalisation. Although not true for all to the same degree, developing countries that have opened their markets have often seen high growth rates and many have found that, in a sound domestic policy context, trade openness can be an important basis for economic growth. On the other hand, no developing country has achieved sustained growth by putting up high trade barriers and limiting exports.
- However trade openness is a necessary but not a sufficient requirement for development. Trade liberalisation and greater integration into global markets alone can not ensure that a country develops, but without it, development is unlikely to occur. In fact the wider policy environment in DCs is a key factor, as are its resource endowments and the structure of its society in terms of equality and access to imports and factors like education. Economists argue essentially about the broader policy mix and the best sequencing of different elements (trade/investment liberalisation, institutional capacity building, social safety nets, domestic reforms and deregulation, etc).
- Overall, developing countries have benefited from the globalisation process and we see that many have impressive growth rates based to some extent on rapidly growing trade. In addition DCs are moving from the basic products and raw materials that had been the backbone of their trade into higher value added sectors which help to foster growth. The WB's analysis of globalisation growth and poverty¹ found that DCs which are home to 3bn people have broken

¹ *Globalisation, growth and poverty WB 2001.*

into manufactured goods markets, which in turn has helped them to reduce poverty. DCs now account for a quarter of global trade in industrial products –twice the level in 1980. High tech exports from DCs have increased by 20% annually since 1980, twice the level for industrialised countries².

2. South-South trade (including services/investment)

- There is a rapid expansion in trade among developing countries – South-South trade – especially in Asia which provides new opportunities for development. In fact, the emergence of the dynamic South and the significant growth of South-South trade and investment flows present an important window of opportunity for all countries, regardless of their level of development.
- While it does not always attract enough attention, trade in services accounts for almost one quarter of trade in goods. And it is not the privilege of a small group of rich countries or the subject of North-South trade exclusively: South-South trade accounts for around 10% of global trade in services (OECD).
- Estimates of benefits of trade liberalisation vary for individual countries depending on the initial levels of protection and the assumed reduction in market access and/or national treatment barriers. In simulations of global service-trade liberalization, developed countries gain more in absolute terms—which is not surprising given the relative size of their economies—but developing countries also see significant increases in their GDP. One model predicts gains of between 1.6 per cent of GDP (for India) to 4.2 per cent of GDP (for Thailand) if tariff-equivalents of protection were cut by one-third in all countries³. The gains from liberalizing trade in services may be substantially greater than those from liberalizing trade in goods, because current levels of protection are higher and because liberalization would also create spill over benefits from the required movement of capital and labour. For instance, one model finds that the welfare gains from a 50 per cent cut in services-sector protection would be five times larger than the gains from non-services sector trade liberalization⁴
- The same can be said of investment. Foreign Direct Investment (FDI) brings both capital and expertise to developing economies; it creates direct and indirect jobs.
- However South-South trade remains hampered by significant trade barriers that still exist among developing countries. Overall, the

² *Human development Report 2005, UNDP*

³ (Chadha et al., 2003)

⁴ (Robinson et al., 1999). (Source: Mattoo, Aaditya, Robert M. Stern, and Gianni Zanini. *A Handbook of International Trade in Services*. Oxford: Oxford University Press, 2007)

barriers facing South-South trade are estimated to be almost three times higher (11.1%) than those facing North-North trade.⁵ More than 60% of import tariffs collected on DCs' trade is collected by other DCs. In this regard, for instance, it will be particularly important that not only developed countries but also developing countries in a position to do so grant DFQF market access to LDCs, as agreed at the Sixth WTO Ministerial Conference in Hong Kong.

- The potential benefit from freer South-South trade may indeed be at least as large as the gains that developing countries can obtain from better access to rich countries' markets. The evidence currently available suggests that on average, a 10% tariff cut in South-South trade is estimated to be associated with a 1.6% increase in exports. This could translate into an additional USD 5.7 billion in export earnings a year.
- Interestingly, the data indicate that an equivalent reduction in North-North or North-South tariff barriers would have a lesser impact on trade flows. This suggests a considerable scope for trade policy to boost trade between low- and lower-middle-income countries, and thus help boost economic development and reduce poverty.
- Simulations of tariff reductions performed by the OECD suggest that this seems to be particularly the case for agricultural products, but projected gains from liberalising South-South trade in manufactured goods are also substantial.
- However, benefits for DCs are risked of not being fully realised in some regions/developing countries where south-south market opening/liberalisation is still not happening in a way or another. Therefore, multilateral negotiations are still a good deal for those regions/developing countries because they present the opportunity to boost trade in a way that bilateral deals do not.

3. Aid for Trade

- Nevertheless, all these concepts such as trade liberalisation, south-south trade, market access, investment, services, etc alone are not a guarantee that all DCs will be able to become competitive.
- Aid for Trade (AFT) is a vital component of the policy mix: AFT can help to increase DCs trading capacity, address the constraints on their trade potential such as physical infrastructures for trade (communication, transport, power facilities and markets) and address adjustment needs so enabling them to cope with obligations

⁵ *Source:* OECD (2006), Dihel, N., Kowalski, P., Shepherd, B. (2006), "South-South Goods and Services Trade", in Douglas Lippoldt (ed.), *Trading Up: Economic Perspectives on Development Issues in the Multilateral Trading System*, OECD, Paris.

arising from the multilateral trading system, to compete more successfully in local, regional and global markets. For weaker and less competitive developing countries, Aid for Trade is particularly important if they are to harness trade to drive economic growth, sustainable development and poverty reduction.

- However, Aid for Trade will only happen on the ground if all parties involved play their part. Without full DCs input and participation in needs assessment, prioritisation and planning of activities, the full potential of AfT will not materialise. This is a real challenge for all the international community.
- The EU, the largest provider of trade-related assistance and Aid for Trade worldwide (including productive capacity building, trade-related infrastructures and trade related adjustment), has taken a very active role in work aimed at developing a global vision on Aid for Trade. Following the endorsement of the concept of Aid for Trade in WTO in mid-2006, the EU has made significant efforts to operationalise it. The EU Joint Aid for Trade Strategy adopted on 15 October 2007 provides details on the implementation of the EU's specific pledge on Trade-related assistance made in Hong Kong in December 2005 and on how to improve both the quality and quantity of Aid for Trade provided by the EC and EU Member States more generally.
- The EU is now moving ahead to implement the Strategy adopted last October in its own right, independently of the outcome of the DDA or any other trade negotiations.
- Other donors also need to make reinforced efforts to provide Aid for Trade to support Developing Countries, especially LDCs and other weaker economies.

Conclusion

- International trade, including well-designed trade liberalisation, plays an important role assisting developing countries in reducing poverty. Many DCs have caught up with the average income levels of developed countries or are on the path to do so.
- Trade has played an important role in this process and will continue to do so. The challenge for the international community is to work to ensure that other DCs and LDCs are also enabled to use the potential of international trade to support their own development.