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WTO TRADE TALKS: A BIRD IN THE HAND IS WORTH TWO IN THE BUSH

Six months have passed since the suspension of the WTO negotiations and the ability of countries to reach an agreement on the Doha Development Agenda is still doubtful. However, the consolidation of the progresses achieved during the last five years is within reach. We can deplore that the introduction of sensitive products, partially exempted from liberalisation, will reduce by half the gains of such an agreement. However, this flexibility seems a sine qua non condition for making a deal to reap half of the gains from real free trade. We feed the discussion using simulations made with the MIRAGE model and stress that, for the particular case of Sub-Saharan Africa Least Developed Countries, the losses coming from the multilateral liberalisation could be largely offset by an unrestricted access of their products into major emerging economies.

An Agreement within reach

On July 24, 2006, WTO Director-General Pascal Lamy recommended a "time-out" and the indefinite suspension of the WTO Doha Development Agenda (DDA) negotiations. At this time, the G-6 group (Australia, Brazil, India, EU, Japan and USA) was still not able to bridge their gaps on agricultural domestic support and market access, the main stumbling blocks of the Doha Round for several months. Since then, a new timeframe to resume the talks has not been set. However, during the Davos Forum on the 24-28 of January 2007, the key players illustrate their will to rekindle the negotiations. The time is critical: only the perspective of submitting an acceptable deal to major trading partners will allow the Bush Administration to ask for an extension of the trade promotion authority (the so-called "Fast track"). Without it, any chance of reaching an agreement will vanish for years. Time to push partners to fulfill ambitious DDA's goals is out, now it is time to consolidate the significant progresses that have been already made.

During the five years of negotiations some significant advances have been done, in particular compared to previous rounds:

✦ In agriculture, a substantial reduction of the ceiling for trade distorting subsidies in agriculture (60% to 70% reduction, maybe more, to be compared to 20% for Uruguay Round – UR); total elimination of export subsidies and equivalent measures (21% for UR); substantial reduction of farm bound tariffs, more than 50% on average, to be implemented on all tariff lines. Let's remind than the UR's deal led to almost no effective liberalisation.[1]

✦ In industry: the elimination of tariff peaks in developed countries, in particular on textile and clothing, and reduction of their tariffs to extremely low levels (2-3%); some cuts in applied tariffs in emerging economies.

✦ In services: meaningful commitments by developed countries and emerging economies on key services sectors (*e.g.* telecom, financial, construction, computer and related services, distribution services). This should include the

1. The Uruguay Round ended with a 36% average decrease, but as most of the tariffs were not bound, this did not entail any effective reduction in applied tariffs.

binding of the existing level of market openness and liberal cross-border trade commitments.

In parallel, WTO Members were about to agree on improved trade rules on subsidies and on anti-dumping with an enhancement of transparency and fair treatment. Concerning disciplines on regional trade agreements (RTAs), they agreed on more transparency, allowing more speedy and comprehensive reviews. In particular, a clarification of some rules on RTAs was in sight. Moreover, a new multilateral agreement on trade facilitation was also in the basket with new binding rules applicable to all WTO Members regarding transparency, simplification and modernisation of import-export customs procedures, as well as measures to facilitate transit which is crucial for landlocked developing countries.

In spite of the overall consensus on the issues to discuss, an agreement on all the modalities has still to be found. Indeed, members displayed different ranges of sensitivity to components of the deal, which led to the failure in negotiations. In agriculture, tariff dismantling is particularly sensitive for the European Union and the G10 members (*e.g.* Japan, Norway, Switzerland, Korea...), while the US are mostly bothered by their own commitments on internal support. For industrial products, the compromise represents a sizeable cut in bound tariffs for many emerging economies, while the effort – meaning the real cuts – are concentrated on a limited number of sectors in the North, basically the labour intensive ones, for which North America is more concerned than Europe and Japan.

Beyond the global impact of this quasi-agreement, it is worth assessing the real scope of the main actors' efforts. A second issue rises on the "development" dimension of the round. Even if it has already been questioned in different studies, a few points deserve to be clarified. For instance the impact of pro-LDCs initiatives and their consequences for Africa.

Potential gains

To shed light on both questions, we assess the impact of the "20/20/20 Lamy's compromise".[2] Since market access is still at the heart of the negotiation process, we focus only on reduction of trade barriers for goods, keeping in mind that other issues, such as services, will bring additional gains. Trade facilitation as well as a potential "Aid For Trade" package would smooth adjustments for developing economies, making it possible for the poorest to reap the benefits of trade liberalisation.[3]

This compromise can be described as:

- a Swiss formula with a coefficient 10 for developed countries and 20 for developing ones in Non Agricultural Market Access (NAMA).
- the G20 proposal in agriculture (a tiered formula for tariffs, a new ceiling for domestic support in the North[4] and the phasing out of export subsidies at the 2013 horizon).
- a Special and Differential Treatment making LDCs exempted from any tariff cuts and asking them to just continue the binding process.

Moreover, to enhance LDCs' integration in the global trade system, the unilateral initiatives already applied by the Triad[5] will be adopted by other OECD countries, as well as by some emerging countries, granting free access for 97% of the products exported by LDCs.

All these trade liberalisation components are introduced in a world scale model (MIRAGE), with a dynamic path up to 2020. The world economy growth is consistent with the GDP and population prospects provided by the World Bank and the United Nations respectively. Before looking at figures, let us recall that results produced by such exercises have always small magnitude. They should be considered as lower bound of the gains since the model focus only on effects that could be measured in a robust way, and it does not take into account some dynamic effects that can have an important impact, as stressed by some empirical works.

The role of sensitive products

This compromise, as previously defined (scenario 1), will lead to an increase of the world GDP by 0.19% in 2020, and to 2.9% additional global trade, relatively to the benchmark situation, without liberalisation (table 1). This is half of what free trade between WTO members (S0) would bring to the world economy in terms of GDP gains. Still, the political economy of the negotiations calls for the introduction of

2. See *La Lettre du CEPII* n° 257, "Doha: No Miracle Formula", for a discussion of this proposal.
3. Simulations realised by Decreux and Fontagné (2006), show that services liberalisation and trade facilitation initiatives may offset any losses associated with goods liberalisation. At the world level, the gains will be respectively increased, by 63 and 330 billions (See *CEPII Working Paper* n° 06-10, "A Quantitative Assessment of the Outcome of the Doha Development Agenda"). The measurements of trade facilitation gains are difficult and policy makers should take results related to them with caution. For instance, whenever market access negotiations will lead to direct reduction in tariffs, trade facilitation relies on more blurred commitments and indirect mechanisms.
4. The last proposal on the table will bring significant reduction in the actual level of subsidies for a very limited number of countries such as EFTA. The CAP reform has already brought EU's support level close to the future bound level. The US are in a similar situation: the 20 USD billions, that might be accepted as a new cap, are above their current subsidies level.
5. The EBA (Everything but Arms) initiative of the EU, launched in 2001, has been mimicked by Japan during the last years. Meanwhile the US has implemented the AGOA for Africa, which includes the majority of LDCs. These initiatives might be more ambitious than the 97% contemplated here: EBA will cover all products except arms at the horizon considered here.

exceptions: the so-called sensitive and special products,[6] selected here on the basis of political criteria. To avoid the drastic discipline driven by the formula, countries claim for a partial or total exclusion of some products. Even if the arguments are diverse (food safety, extreme vulnerability of some sectors or workers, powerful lobbies), the result is the same: exceptions lead to a strong reduction in the effective liberalisation. Flexibility halves the gains at the world level (S2 compared to S1); but this scenario (S2), which becomes our central scenario, still reaps one fourth of the gains of free trade (S0). The outcome is more deceiving in terms of trade flows: 1.8% additional trade, to be compared with 11.7% under free trade. This confirms that sensitive products are a key issue in the negotiation.

Table 1 – Changes in world trade and GDP according to various scenarios
Volume changes from the baseline scenario in 2020

	World Trade %	World GDP %	World GDP bn USD
• S0 Free trade between WTO members	11.7	0.40	201
• S1 Plausible outcome (no special/sensitive products)	2.9	0.19	96
S1A of which agriculture	*0.7*	*0.11*	*55*
• S2 Central scenario = S1 + special/sensitive products	1.8	0.11	55
S2A of which agriculture	*0.3*	*0.05*	*25*
• S3 100% North = S2 + free access of LDCs to OECD	1.8	0.11	55
• S4 100% fully consolidated = S2 + free access of LDCs to OECD and major emerging markets	1.9	0.12	60

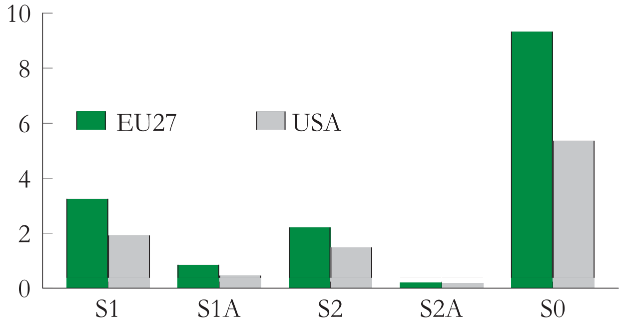
Source: Authors' calculations based on Mirage and MAcMap.

EU one step before the US

Our simulations also allow for measuring the degree of different partners' commitments in the global trade openness. Figure 1 compares the changes in the EU and US imports. With no sensitive and special products, extra-EU imports would be roughly 3% above their reference level, as against 2% for the US. Of course those are just aggregated figures, a detailed analysis would point to larger increases in some sectors. As expected, the introduction of special and sensitive products downsizes the impact on trade: our central scenario, S2, points to a 2.2% increase in EU imports, compared with a 1.5% increase in US imports, or a 1.8% increase in world imports. On such basis it would be difficult to consider that the global move reflects a lower commitment of Europe.

The contentious issue, however, is about agriculture. Our scenario 2A limits the liberalisation to agriculture. In this case, the picture is similar on both sides of the Atlantic. Once again, the role of sensitive products is striking: leaving some products aside allows the EU to record a rise in their imports similar to the US; otherwise (S1A), the increase will be relatively more important.

Figure 1 – Percentage changes in EU and US imports in 2020, according to various scenarios

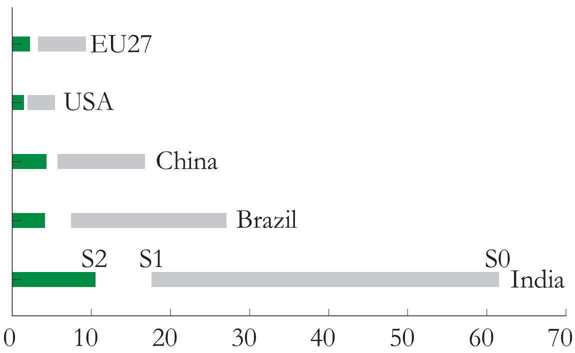


Source: Authors' calculations based on Mirage and MAcMap.

A similar question arises on emerging economies: do they contribute to the global deal by effectively opening their markets? Leaving aside agricultural scenarios, which are less interesting here, figure 2 displays the effects on major emerging countries' imports, namely Brazil, India and China. Not surprisingly, given its high initial level of protection, India is the country where the impact of liberalisation could be the largest, as shown by the outcome of S0: with free trade between WTO members, Indian imports would increase by 61%, to be compared with 27% for Brazil and 16% for China. The compromise with no flexibility (S1) represents a significant share of this total openness: more than the third for China, 29% and 27% respectively for India and Brazil.

Here again, exceptions related to sensitive products reduce strongly the impact of liberalisation on imports, in particular for Brazil and India. Overall, the increase related to S2 would represent 15% of the free trade impact for Brazil, 17% for India and 26% for China, to be compared to 24% for the EU and 28% for the US. These figures are averages, and the political impact of such liberalisation very

Figure 2 – Percentage changes in Brazil, China, India, EU and US imports in 2020, according to various scenarios



Source: Authors' calculations based on Mirage and MAcMap.

6. In agriculture, developing countries could exclude from liberalisation 10% of their products. Sensitive products allow developed and developing countries to apply just half of the cut driven by the formula for 4% of products. In industry, developing countries are entitled to do the same for 10% of their products (up to 10% of their imports).

much depends on the dispersion of the protection. This being said, one would hardly conclude that offers made by advanced economies are negligible compared to the ones by the emerging world.

Subsaharan Africa and emerging markets

Numerous studies have shown that poor countries are expected to gain very little, and worse, that Sub-Saharan Africa may suffer net economic losses as a result of deteriorated terms of trade, reduced margin of preferences and, maybe more importantly, the lack of efforts demanded to these countries to reduce their own tariffs. The issue of LDC's access to third markets has to be examined carefully. This can be done considering free access (zero tariff-zero quota) for 100% of LDCs' exports, instead of 97% in the central scenario. First, we make all the OECD countries granting these preferences and, second, major emerging countries join the move. In both cases, the impact on the world economy is rather modest, due to the small size of LDCs economies. But for Sub-Saharan African countries, the opening of emerging countries makes a difference. We find that the opening of the emerging markets to 100% of their exports would alleviate half of the welfare losses potentially faced, bringing them to 135 current USD millions, a level that can be easily compensated. This is an outcome that would not be obtained whenever limiting the consolidation of free access schemes to developed economies.[7] Therefore, besides gains associated to trade facilitation or to some "aid for trade" package, we can conclude that one of the key elements to mitigate LDCs' losses would be the widely openness to their exports by emerging markets, compensating the preference erosion on Northern (and especially european) markets by creating preferential margins in new and fast-growing markets.

Finally, the agreement under scrutiny here will consolidate several unilateral decisions of liberalisation as well as some progresses in the multilateral framework: the reduction of EU subsidies associated to the CAP reform and the end of their rise in the US, the phasing out of export subsidies, the first significant cuts in agricultural protection, and, in emerging markets, the openness for manufacturing goods associated to a strong reduction of binding overhang, which is a key element for future negotiations. If flexibility is the price to get a deal that will be politically acceptable, so be it... after all, a bird in the hand is worth two in the bush. Indeed, a round that would deliver between one-third to half of the benefits of a total liberalisation of good markets is already a significant achievement, barely matched up by previous rounds results. The agreement in services will also bring significant gains, especially for the US-EU relation, a case where a bilateral agreement seems far for being plausible. The initial ambition of the DDA has met the harsh reality of domestic political trade-off. At this stage of the negotiations, and in a context where protectionists' discourses are on the rise, it is no time for asking "more". It is time to consolidate the advances and to focus efforts on specific items of the negotiations to get a "better" outcome. Moreover, a failure will forbid to get an agreement for the next three or four years. Meanwhile, many preferential trade agreements will be signed, increasing the complexity of trade policies and undermining the incentives of major economies to go back to the multilateral approach. Beyond the specific commitments of this first WTO round, what is at stake is the protection of two valuable global public goods: the institution as itself and non conflictual trade relations.

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7. For other LDCs, such as Bangladesh that does not benefit initially from generous access in the US, the story is quite different. The 97% clause OECD wide will increase its welfare gains from 0.10 % to 0.14% of its real income. Moving to 100%, the gains jump to 0.83%. Due to its extreme specialisation in textile, this country is very sensitive on any product exclusion from its partners. Finally, extending the free access to major emerging countries will bring the welfare gains to 1.25%.

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