33128

Trade Note

June 27, 2005

Agricultural Market Access: The Key to Doha Success

The World Bank Group
www.worldbank.org

International Trade Department

By Kym Anderson and Will Martin

Trade Note 23

Almost two-thirds of the economic gains that would come from dismantling all merchandise trade barriers and farm subsidies globally would come from agriculture. According to our latest research[1], this is so for the world as a whole, and also for developing countries as a group. Developing countries are therefore right to focus on agriculture in the negotiations.

To date that focus has been almost exclusively on developed country policies. That is understandable, given that many in developing countries feel they did not get a good deal out of the Uruguay Round and so are determined to get significantly more commitments under Doha from developed countries before they contemplate opening their own markets further. However, our modeling suggests that over half the gains to developing countries from global agricultural reforms would come from liberalization by developing countries themselves (Table1). The reason is two-fold: because agricultural tariffs are even higher in developing than developed countries (18 compared with 16 percent on average in 2001), and because a large minority of developing country trade is now with other developing countries.

Table 1: Effects on developing country economic welfare of full trade liberalization from different groups of countries and products, 2015 (percent)

	From full liberalization of:			
	Agriculture and food	**Textiles and clothing**	**Other manufactures**	**All Goods**
Percentage due to:				
Developed country policies	30	17	3	50
Developing countries' policies	33	10	7	50
All Countries' Policies	63	27	10	100

Within agriculture, developing countries – including the G-20 – are emphasizing especially the need for cuts to agricultural subsidies. This is partly because they do not want to lower their own food import restrictions, as well as because it may adversely affect their international terms of trade. However, this may be detrimental economically: our modeling results indicate that 93 percent of the welfare gains from removing distortions to agricultural incentives globally would come from reducing import tariffs, while only 2 percent is due to export subsidies and 5 percent to domestic support measures (Table 2). Certainly it is important to discipline those domestic subsidies and phase out export subsidies, so as to prevent re-instrumentation of assistance from tariffs to domestic subsidies and to bring agriculture into line with non-farm trade in terms of not using export subsidies. But to ignore market access in the Doha round would be to forego most of the potential gains from goods trade reform.

The Three Pillars

The current Doha round has the advantage over the Uruguay Round of beginning from the framework of rules and disciplines agreed in that previous Round's Agricultural Round. In particular, it has the three clearly identified "pillars" of market access, export subsidies, and domestic support on which to focus. True, it took more than three years to agree on a framework for the current negotiations, reached at the end of July 2004, but now that July Framework Agreement is likely to guide the negotiations for some time. It therefore provides a strong basis for undertaking *ex ante* analysis of various options potentially available to WTO members during the Doha negotiations.

Table 2: Distribution of global welfare impacts of fully removing agricultural tariffs and subsidies, 2001, (percent)

	Beneficiary region:		
Agricultural liberalization component: High-income[a] countries' liberalization of:	**High-income[a] countries**	**Developing countries**	**World**
Import market access	66	27	93
Export subsidies	5	-3	2
Domestic support	4	1	5
All measures	75	25	100

[a] High-income countries include the newly industrialized East Asian customs territories of Hong Kong, Korea, Singapore and Taiwan as well as Europe's transition economies that joined the EU in April 2004.

In turning to what might be achievable under a Doha partial reform package, the devil is going to be in the details. For example, commitments on domestic support for farmers are so much higher than actual support levels at present that the 20 percent cut in the total bound AMS, promised in the July Framework Agreement as an early installment will require no actual support reductions for any WTO member. Indeed a cut as huge as 75 percent for those with most domestic support is needed to get some action, and even then it would only require cuts in 2001 levels of domestic support for four WTO actors: the US (by 28 percent), the EU (by 18 percent), Norway (by 16 percent) and Australia by 10 percent – and the EU and Australia have already introduced reforms of that order since 2001, so may need to do no further cutting under even that formula.

Large cuts in bound rates are needed also to erase binding overhang in agricultural tariffs. Table 3 shows there is substantial binding overhang in agricultural tariffs: the average bound rate in developed countries is almost twice as high as the average applied rate, and in developing countries the ratio is even greater. Thus large reductions in bound rates are needed before it is possible to bring about *any* improvements in market access. To bring the global average actual agricultural tariff down by one-third, bound rates would have to be reduced for developed countries by at least 45 percent, and up to 75 percent for the highest tariffs, under a tiered formula.

Table 3: Agricultural weighted average import tariffs, by region, 2001, (percent, ad valorem equivalent, weights based on imports)

	Bound tariff	Applied tariff[a]
Developed countries	27	14
Developing countries	48	21
of which: LDCs	78	13
World	37	17

[a] Includes preferences and in-quota TRQ rates where relevant, as well as the ad valorem equivalent of specific tariffs. Developed countries include Europe's transition economies that joined the EU in April 2004. The 'developing countries' definition used here is that adopted by the WTO and so includes East Asia's four newly industrialized tiger economies.

Even large cuts in bound tariffs do little if "sensitive products" are exempted. If members succumb to the political temptation to put limits on tariff cuts for the most sensitive farm products, much of the prospective gain from Doha could evaporate. Even if only 2 percent of HS6 agricultural tariff lines in developed countries are classified as sensitive (and 4 percent in developing countries, to incorporate also their "Special Products" demand), and are thereby subject to just a 15 percent tariff cut (as a substitute for the TRQ expansion mentioned in the Framework Agreement), the welfare gains from global agricultural reform would shrink by three-quarters. However, if at the same time any product with a bound tariff in excess of 200 percent had to reduce it to that cap rate, the welfare gain would shrink by 'only' one-third.

Given the high binding overhang of developing countries, even with their high tariffs – and even if tiered formulae are used to cut highest bindings most – relatively few of them would have to cut their actual tariffs and subsidies at all. That is even truer if "Special Products" are subjected to smaller cuts. Politically this makes it easier for developing and least developed countries to offer big cuts on bound rates.

Expanding non-agricultural market access would add substantially to the gains from agricultural reform. By adding a 50 percent cut to non-agricultural tariffs by developed countries (and 33 percent by developing countries and zero by LDCs) to the tiered formula cut to agricultural tariffs would double the gain from Doha for developing countries. That would bring the global gain to $96 billion from Doha merchandise liberalization, roughly one-third of the potential welfare gain from full liberalization of $287 billion.

These absolute numbers undoubtedly underestimate the actual magnitudes of prospective benefits. First, merchandise trade liberalization opens domestic markets to new competition and improved technology, and this, together with scale effects from specialization, tends to increase productivity. These dynamic productivity effects can multiply the gains several-fold. Second, our calculations assume preferences in regional and other preferential trading arrangements are fully utilized, and that developing countries have access at the listed rates. However, more detailed analysis shows that rarely is this the case. Brenton (2003), for example, found that much eligible trade does not take advantage of preferential access, probably because of onerous rules of origin obligations or quantitative limits built into the schemes. Our modeling cannot take this underutilization into account and hence overstates the degree of liberalization in the base year and thus understates the effects of further MFN liberalization. Third, the analysis here considers only merchandise trade effects and does not incorporate effects of services trade distortions. The services negotiations have proceeded fitfully and the amount of new liberalization may eventually prove to be minimal. Nonetheless, services liberalization has a powerful growth effect (Mattoo, et al, 2001), and these are not included in our calculations. Cutting in the opposite direction is that fact that benefits are not as automatic as the models assume because real world constraints on supply response may impede exporters in developing countries from taking advantage of new opportunities. Nonetheless, the weight of these facts suggests that the absolute benefit is likely to be larger than the $96 billion in our calculations.

Most of the developing countries' gains from that comprehensive Doha scenario go to numerous large developing countries, notably Brazil, Argentina and Other Latin America plus India, Thailand and South Africa plus others in southern Africa. The rest of Sub-Saharan Africa gains when non-agricultural market access is expanded and especially when developing countries participate as full partners in the negotiations. An important part of this result is increases in market access – on a non-discriminatory basis – by other developing countries.

Some least developed countries in Sub-Saharan Africa and elsewhere may be slight losers in our static Doha simulations when developed countries cut their tariffs and those LDCs choose not to reform at all themselves. That results from their terms of trade deteriorating either because of tariff preference erosion on their exports or because they are net food importers and so would face higher prices for their imports of temperate foods. Our simulations overstate the benefits of tariff preferences for LDCs, however, since they ignore the trade-dampening effect of complex rules of origin and the grabbing of much of the rents by developed-country importers. But even if they were to be losers after correcting for those realities, it remains true that preference-receiving countries could always be compensated for preference erosion via increased aid at relatively very small cost to current preference providers – and in the process other developing countries currently hurt by LCD preferences would enjoy greater access to the markets of reforming developed countries.

What is to be Done?

Several clear implications for the Doha round follow from this analysis. First, *in addition to outlawing agricultural export subsidies, domestic support bindings must be cut very substantially, to reduce binding overhang*. In so doing, the highest-subsidizing countries, namely the EU and US, need to reduce their support, not just for the sake of their own economies but also to encourage developing countries to reciprocate by opening their markets as a quid pro quo. An initial installment of a 20 percent cut is nothing more than a start towards getting rid of that overhang.

Second, *even more importantly, agricultural tariff bindings must be cut hugely so that some genuine market opening can occur*. Getting rid of the tariff binding overhang that resulted from the 'dirty tariffication' of the Uruguay Round should be the first priority, but more than that is needed if market access is to expand. Exempting even just a few "Sensitive" and "Special" products is undesirable as it would reduce hugely the gains from reform and would tend to divert resources into, instead of away from, enterprises in which countries have their least comparative advantage. If it turns out to be politically impossible not to designate some "Sensitive" and "Special" products, it would be crucial to impose a cap such that any product with a bound tariff in excess of, say, 100 percent had to reduce it to that cap rate.

Third, *expanding non-agricultural market access at the same time as reforming agriculture is essential.* A balanced exchange of concession is impossible without adding other sectors. With other merchandise included, the trade expansion would be four times greater for both rich and poor countries – and poverty in low-income countries would be reduced considerably more.

And fourth, *developing countries have to contribute to the round*, particularly through South-South "concessions". Since developing countries are trading so much more with each other now, they are the major beneficiaries of reforms within their own regions. Upper middle-income countries might consider giving least developed countries duty-free access to their markets (mirroring the recent initiatives of developed countries), but better than such discriminatory action would be MFN tariff reductions by them. Even least developed countries should consider reducing their tariff binding overhang at least, since doing that in the context of Doha gives them more scope to demand "concessions" (or compensation for preference erosion or other contributors to terms of trade deterioration) from richer countries – and yet would not require them to cut their own applied tariffs very much.

Conclusion

The good news is that there is a great deal to be gained from liberalizing merchandise – and especially agricultural – trade under Doha, with a disproportionately high share of that potential gain available for developing countries (relative to their share of the global economy). To realize that potential gain, it is in agriculture that by far the greatest reform is required. However, the political sensitivity of farm support programs, coupled with the complexities of the measures introduced in the Uruguay

Round Agreement on Agriculture and of the modalities set out in the Doha Framework Agreement of July 2004, ensure the devil will be in the details of the final Doha agreement. To realize more of their potential gains from trade, developing and least developed countries would need to fully participate in trade (and complementary domestic) reforms, and to invest more in trade facilitation. High-income countries could encourage them to do so by being willing to open up their own markets more to developing country exports, and by providing more targeted aid.

To that end, a new proposal has been put forward to reward developing country commitments to greater trade reform with an expansion of trade-facilitating aid, to be provided by a major expansion of the current Integrated Framework which is operated by a consortium of international agencies for least developed countries (Hoekman and Prowse, 2005). This may well provide an attractive path for developing countries seeking to trade their way out of poverty, not least because it would help offset the tendency for an expanded aid flow to cause a real exchange rate appreciation. As well, it is potentially a far more efficient way for developed countries to assist people in low-income countries than the current systems of tariff preferences.

1 Detailed analysis is forthcoming in the author's article in the September 2005 issue of The World Economy, and in a World Bank book edited by the authors called Agricultural Trade and the Doha Development Agenda to be co-published by Palgrave Macmillan and The World Bank by November 2005. Chapters can be downloaded at http://www.worldbank.org/trade/wto

References

Brenton, P., 2003 "Rules of Origin in Free Trade Agreements" Trade Note No. 4. Washington, D.C.: The World Bank, http://www.worldbank.org/trade/

Hoekman, B., and Prowse, S., 2005, "Development and the WTO: Beyond Business as Usual", *Bridges*, No.2-3 February-March 2005, International Centre for Trade and Sustainable Development, Geneva, Switzerland.

Mattoo, et al., 2001, "Measuring Services Trade Liberalization and its Impact on Economic Growth: An Illustration." Policy Research Working Paper No. 2655. Washington, D.C.: The World Bank.

Further Reading

Anderson, K. and W. Martin (2005), 'Agricultural Trade Reform and the Doha Development Agenda', Policy Research Working Paper No. 3607, The World Bank, Washington, DC, May. (Forthcoming in *The World Economy* 28(9), September.)

Anderson, K., W. Martin and D. van der Mensbrugghe (2005b), 'Would Multilateral Trade Reform Benefit Sub-Saharan Africa?' Policy Research Working Paper, The World Bank, Washington, DC, July.

This note was prepared by Kym Anderson, Lead Economist (Trade Policy) and Will Martin, Research Manager in the Development Research Group of the World Bank in Washington DC. The authors are grateful for the collaboration of numerous colleagues, especially Dominique van der Mensbrugghe and Tom Hertel, and for research funding from the UK's Department for International Development. This Trade Note can be downloaded at http://www.worldbank.org/trade/