

CONSTRAINING AND ENHANCING POLICY SPACE: THE WTO AND ADJUSTING TO GLOBALISATION

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I. INTRODUCTION

Among the criticisms of the World Trade Organization (WTO) that have received considerable attention in recent years is one that the WTO has restricted or threatens to restrict developing countries' policy space and (implicitly and explicitly) that the WTO, as a result, has harmed or threatens to harm the growth and development prospects of the developing countries. The 'policy space' critique of the WTO has received most influential, academic support from Dani Rodrik. His argument is in two parts (See, for example, Rodrik, 2004). Firstly he argues that most (if not almost all) successful cases of development in the recent past (citing China, India, South Korea, Taiwan and Vietnam) have been based on the adoption of distinctive and often heterodox policy stances. Given this, he argues that developing countries in general need to resist the constraining of their policy space (through for example allowing encroachment of WTO disciplines) so as to be able to adopt similar (or dissimilar, but equally distinctive and heterodox) policies. Similar criticisms can be found also in the international policy community. United Nations Conference on Trade and Development's (UNCTAD's) Trade and Development Report (2006) argues, for example, that:

“...the rules and commitments of the international trading regime restrict the de jure ability of developing countries to adopt national development policy.” (UNCTAD, 2006:167)

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By contrast less attention has been given to the potential role of the WTO in enhancing developing countries' trade and trade-related policy space, both in terms of the extent and quality of that policy space. By lowering tariff and non-tariff import barriers or constraining the use of contingent protection instruments in export markets, WTO membership seeks to increase the scope and effectiveness of developing countries' own reforms aimed at promoting exports. The extension of WTO disciplines to the opening of markets to services as well as goods is another potential source of policy space enhancement. In turn the quality of the developing countries' trade policy space may be enhanced through 'aid for trade' initiatives which increase the capacity to undertake and implement trade reform and increase the effectiveness of trade reforms by improving their trade-related infrastructure and institutions.

A range of positive and normative issues are embodied in both the policy space-constraining and space-enhancing views of the WTO's role in the development of the developing countries. The aim of this paper is identify and evaluate the issues involved, and to offer an overall assessment of the competing arguments. The remainder of the paper is organised as follows:

Section 2 reviews the potential influences on policy space associated with WTO membership, while Section 3 offers an assessment of the actual influence on policy space to-date. The prospects for WTO membership affecting developing countries' policy space in the future are examined in Section 4. In Section 5, the balance of constraining and enhancing influences of WTO membership are assessed, while in Section 6 the case for strengthening the enhancing influence of the WTO through 'aid for trade' measures is examined. Finally the paper's overall conclusions are set out in Section 7.

II. POTENTIAL WTO INFLUENCES ON POLICY SPACE

Two contextual points are worth making at the outset. First, we concentrate here on trade and trade-related aspects of policy space. Other non-trade policy aspects of developing countries' policy space may be influenced by other international agencies and rules, but they are not within the domain of the WTO. Second, it should be emphasised that trade policy space is (potentially and actually) influenced and substantially so by other than the multilateral commitments and negotiated agreements associated with WTO membership. WTO members constrain, modify and enhance their trade policy space through unilateral actions (e.g. structural adjustment loan-induced reforms agreed with the World Bank), and as a result of bilateral (e.g. Economic Partnership Agreements negotiated by groupings of African Caribbean and Pacific countries with the European Union (EU), or the Africa Growth and Opportunity Act (AGOA) arrangements between the United States of America (USA) and African countries) and regional trade agreements (which are extensive among developing countries). These additional and substantive influences on developing countries' trade policy space are invariably subject to WTO rules and disciplines, but they are not in general imposed or required by WTO membership.

A) Potential Sources of Constraint?

The WTO has a number of dimensions: a set of trade rules, a negotiating forum and a vehicle for settling trade disputes. All of these dimensions are ultimately directed at creating a freer international trading regime. To the extent that less liberalised international trade is sought by member states, then WTO membership must by definition offer the potential to constrain or restrict policy space. The core rules or disciplines on transparency, non-discrimination and reciprocity are formulated so as to bind tariffs and encourage the lowering of tariffs, and to restrict national government's capacity to differentiate between trading partners and between foreign and domestic producers and products. Similarly the rules seek to

encourage predictability and fairness by preventing or restricting the use of particular trade policy instruments, encouraging the use of tariffs rather than non-tariff measures in general, outlawing the use of specific non-tariff measures (e.g. voluntary export restraints), and constraining the use of export subsidies. Indeed through negotiation and agreed institutional change (from the GATT to the WTO), there has been an intensification and extension of the rules-based nature of the world trading system. This has extended the product or sector coverage of rules (from goods to services) and from border, trade policy measures to beyond the border, trade-related measures (with the introduction of new disciplines for instance on trade-related investment and intellectual property issues).

The above constraints on national policy action are not necessarily, however, uniform across member states. There are exemptions to the rules, which allow for example the offering by industrial countries of preferential market access terms to exports from developing countries. Indeed there is differentiation within the rules to allow developing countries to use trade policy to support infant industries or support the balance of payments, and to subsidise exports. Combined with the allowed use of safeguard measures and the scope for the protection of national interest through the dispute settlement mechanism (and through the forum for negotiations offered by the WTO), the WTO-structured, rather than controlled, international trading regime should not be viewed as being monolithic, inflexible or highly constraining by design or intent.

B) Potential Sources of Enhancement?

One can think of the constraining of policy space as a two-sided coin; the constraining of policy actions by one country offering the scope for enhancing, qualitatively at least, the policy space of another or others. The lowering of import barriers in any (or all) WTO members as a result of WTO rules or negotiations will increase the effectiveness of export-promoting trade policies of the member's trading partners (and incidentally including the liberalising economies). Furthermore in a

multilateral context the scope for reciprocity, and therefore for enhancing the effectiveness of trade reform and trade facilitation in promoting exports is magnified, both because the number of reciprocating trading partners is maximised and because there is greater scope for creating coalitions of countries who can lobby/negotiate for improved export market access.

On the import side too, WTO membership offers a scope for improving the capacity of countries to deal with disruptive and unfair trade (relative to a non-membership status). Defensive trade measures (anti-dumping and countervailing duties) against unfair (dumped or subsidised) trade may be more easily and effectively used, especially by small countries, in the context of a rules-based system where there is redress also to a dispute settlement process. But enhancement in qualitative terms may come not only by constraining the actions of other governments, but by constraining a country's own policy actions. Not all policy actions are desirable ones in terms of efficiency or equity (or both criteria). There is a clear ranking on efficiency grounds of import policy instruments, for example, with tariffs being superior to non-tariff measures. In which case the WTO disciplines on the usage of non-tariff measures constrain the use of less efficient (and usually less equitable) instruments, and thereby offer the potential for enhancing, qualitatively, the trade policy space of WTO members.

III. ACTUAL WTO IMPACT ON DEVELOPING COUNTRIES' SPACE

In order to move from potential to actual implications of WTO membership for developing countries' policy space, we need to distinguish between the effects of becoming a member from those associated with being a member for a period of time. The distinction is necessary because there is some evidence to suggest that the conditions of membership ('joining the club') have become more substantive and binding in recent years. Indeed if the distinction does matter it suggests

that there is a heterogeneity of impact across countries, and that there may be a prospect of increasing WTO influence.

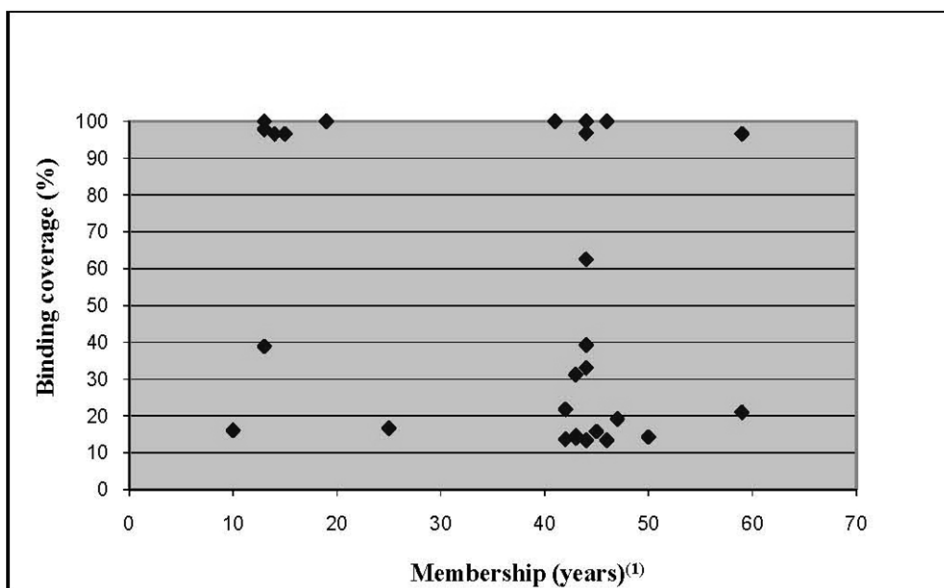
A) Being a WTO Member?

One of the major impacts that one might anticipate WTO membership to have is on the border import measures of member states. This is certainly the case for the industrial countries, which have bound their tariff rates and progressively reduced them through rounds of negotiated tariff reductions. These countries also dismantled most of their non-tariff import barriers in the post-second world war period, with some sector restrictions (e.g. textiles, agriculture) and some policy innovations (e.g. voluntary export restraints) requiring subsequent further actions to prevent their use. In the case of developing country members, it is much less evident that General Agreement on Tariffs and Trade (GATT) or WTO membership has had a major influence on their import policies.

To support this argument, we first consider the extent of binding coverage, i.e. the percentage of tariff lines for which there is a bound Most Favoured Nation (MFN) rate. We do so in Figure 1 for all the sub-Saharan African countries that are WTO members, matching up the overall binding coverage with the numbers of years membership of either GATT or the WTO.¹ Although there are some countries (5 out of 27) that have bound all their tariff lines, the majority of the countries (15 out of 27) have bound no more than 40% of their tariff lines. More importantly for the present purpose, the degree of binding is wholly uncorrelated with the length of GATT/WTO membership, there being both long term and non-long term members in both the 'binders' and 'non-binders' groupings. Indeed twelve of the countries have been members for over forty years and the majority of their tariff lines remain unbound!

¹ The information is provided for this set of developing countries for illustrative purposes, but the debate and issues are of relevance for developing countries in general. The policy space debate and search for improved export performance is, however, of particular relevance to sub-Saharan African countries.

Figure 1. Binding Coverage and GATT/WTO Membership (Sub-Saharan African countries)



Notes:⁽¹⁾ up to 2007

Consider also in Figure 2 the level at which these same countries have bound their (bound) tariffs, and how these compare with the tariffs they actually apply. The majority (15 out of 27) of these sub-Saharan African countries have average (simple) bound tariff rates in excess of 50%, with three countries having average bound import duties in excess of 100%. By contrast all of these countries have an average (again simple) applied MFN tariff (on bound and unbound tariff lines) below 20%. This is certainly indicative at least that WTO commitments on the level at which these countries' MFN tariffs are bound do not have much leverage on actual tariff setting. Of course there is a risk that averaging is obscuring greater leverage at the detailed level, especially when we may be comparing the average of a subset of tariffs (i.e. bound ones) with that of the total set of (bound and unbound) tariffs. To confirm the assessment based on the average data, we report therefore in Table 1 on the bound and applied tariffs for a country from our sample that has bound all its tariff lines. We can see from this table that Rwanda has average bound

tariff rates in excess of 60% and average applied tariffs below 30% in every product group (except dairy products).

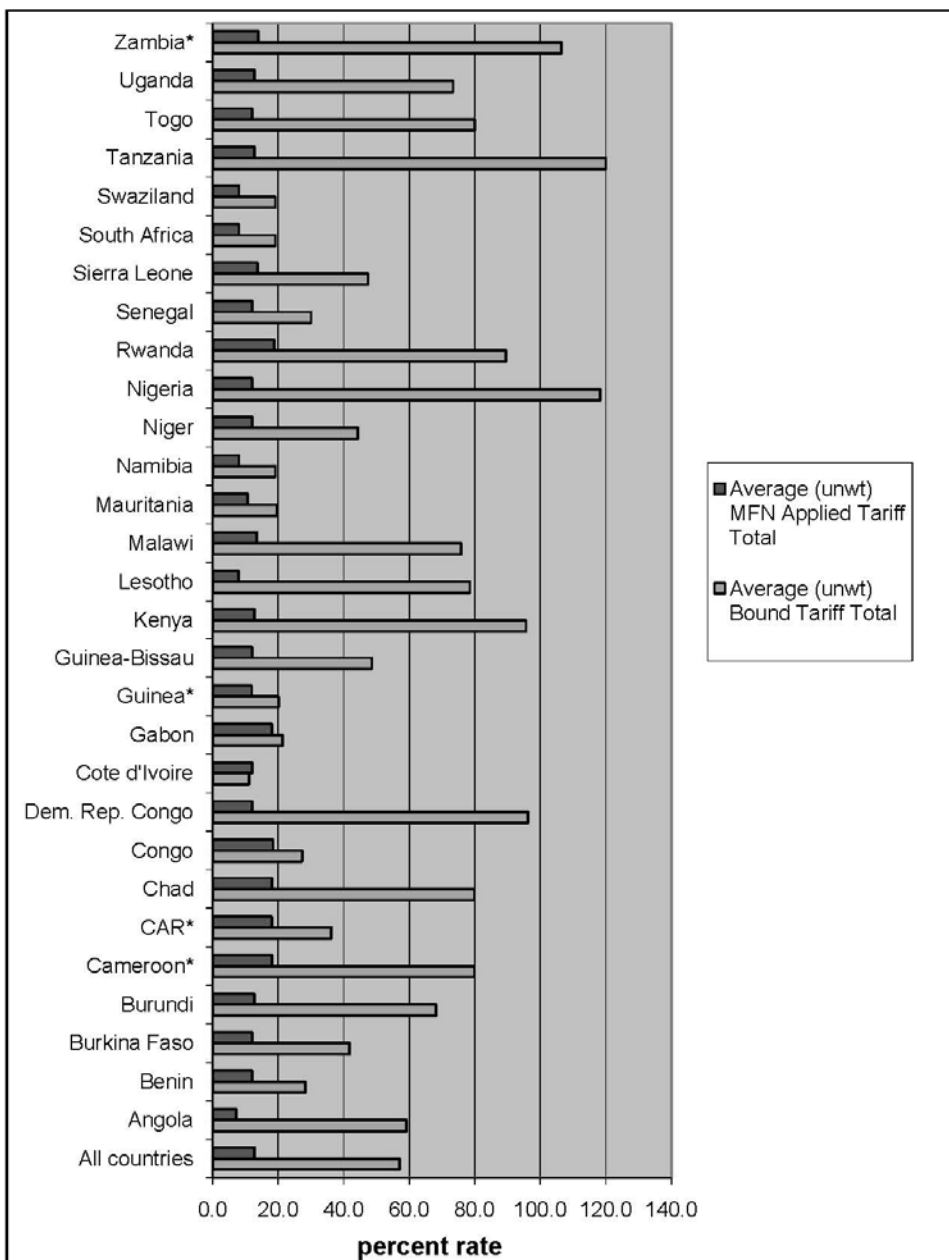
Table 1. Bound and Applied Tariffs: Rwanda (2006)

Product groups	Final bound duties				MFN applied duties		
	AVG	Duty free in %	Max	Binding in %	AVG	Duty free in %	Max
Animal products	80.0	0	80	100	14.3	0	30
Dairy products	16.0	80.0	80	100	24.8	0	30
Fruit, vegetables, plants	75.6	0	80	100	11.5	0	30
Coffee, tea	80.0	0	80	100	21.1	0	30
Cereals & preparations	72.8	6.1	80	100	19.2	0	30
Oilseeds, fats & oils	79.5	0	80	100	15.2	0	30
Sugars and confectionery	69.0	3.1	80	100	28.1	0	30
Beverages & tobacco	67.5	0	80	100	27.9	0	30
Cotton	80.0	0	80	100	7.0	0	15
Other agricultural products	76.7	0	80	100	8.1	0	30
Fish & fish products	87.6	11.2	100	100	16.3	0	30
Minerals & metals	97.9	0	100	100	18.2	4.4	30
Petroleum	100.0	0	100	100	13.3	0	30
Chemicals	92.9	1.3	100	100	16.3	3.6	30
Wood, paper, etc.	95.5	0	100	100	18.5	4.1	30
Textiles	65.3	0	100	100	18.2	0.8	30
Clothing	98.2	0	100	100	29.9	0	30
Leather, footwear, etc.	95.1	0	100	100	23.5	0	30
Non-electrical machinery	97.0	0	100	100	12.9	38.1	30
Electrical machinery	98.7	0.4	100	100	26.7	5.5	30
Transport equipment	96.9	0	100	100	22.5	0	30
Manufactures, n.e.s.	96.3	0.1	100	100	26.1	2.8	30

Source: Tariff Profiles (WTO)

The above evidence would not surprise anyone who has researched or observed trade policy developments in Africa over recent decades. GATT and WTO commitments on tariffs have been very limited as far as this set of developing countries is concerned. The main source of both tariff and non-tariff reform of import policies have been outside of the multilateral arena. Reforms have been unilaterally or regionally-inspired, that has often been conditionally-attached to World Bank structural adjustment lending or membership in the many regional trading arrangements that have been spawned during this period.

**Figure 2. Bound and Applied Tariffs Compared: Sub-Saharan Africa
(all products, 2005/2006)**



These 'other than multilaterally-inspired' import liberalisations and privatisations have reduced substantially the implicit subsidisation of domestic production, especially that which is oriented toward import-substitution. Accordingly, the desire or incentive to use more explicit means of subsidisation to support infant or export production may well have increased. One might argue, therefore, that it is in this range of the policy space (rather than import border measures) that the WTO constraint on policy space has tightened. But it is in general not the GATT articles that are the major constraint in this sphere – there is some scope within WTO rules for the use of production subsidies for development and infant industry purposes by developing countries and they are also exempted from the general ban on export subsidies. Although the tone of the 'special and differential' (S&D) provisions within the GATT articles indicate a flexibility towards the use of subsidies for development purposes, there is a debate in the policy literature about the appropriateness and adequacy of the provisions. Arguably the provisions might be too lenient and imprecise regarding the use of trade-distorting subsidies, in particular in the case of the implicit subsidies associated with the use of Export Processing Zones (EPZs) to promote exports (Table 2 reports the high incidence of EPZs, even in a fiscally-constrained region like sub-Saharan Africa). On the other hand, there are critiques of the WTO subsidy rules that argue that they are too stringent and restrict developing countries' ability to meet their development objectives. The argument that it is the multilateral rules that have been the major constraint to date in practice is not, however, a convincing one. It is rather the national, fiscal constraint on the use of subsidies, and the bilateral or regional pressures from trading partners to avoid retaliatory action (whether or not the countries are WTO signatories), that have been the major constraint in practice on developing countries' policy space.

Table 2. Export Processing Zones in Sub-Saharan Africa

Country	Multiple Zones	No. of Firms	Zone Exports as % of total exports (*)
Cape Verde		9	n.a.
Cameroon		29	33
Cote d'Ivoire		n.a.	n.a.
Gabon		144	80
Ghana	✓	n.a.	70
Kenya	✓	68	87
Lesotho	✓	n.a.	80
Malawi		n.a.	n.a.
Mali	✓	343	80
Mozambique		65	85
Namibia		n.a.	41
Nigeria		n.a.	75
Senegal		57	n.a.
South Africa	✓	1538	n.a.
Sudan	✓	46	n.a.
Togo		61	n.a.
Zimbabwe	✓	73	80

Source: ILO database on export processing zones (Boyenge, 2007)

Notes: (*) presumably of manufacturing goods, but not defined by database. n.a. denotes not available from database

✓ denotes incidence of multiple zones

B) Does Becoming a WTO Member Restrict Policy Space?

It is the case that many of the Sub-Saharan African developing countries we have considered thus far were either founding members of the WTO (having previously been GATT members) or joined fairly soon after the WTO's creation. It is widely recognised that the focus of pre-WTO, GATT negotiations had been on and determined by the industrial countries, and relatively limited demands were made of or attention given to the commitments of the developing countries. With the creation of the WTO there has been a greater monitoring role (e.g. through the Trade Policy Review mechanism) and greater attention given to the role of the newly

exporting countries specifically and of the developing countries in general in the world trading system. It is suggested therefore that the WTO's influence on recent new member's policy space has been more evident and significant than on existing developing country members.

Table 3. Recent (post-2004) WTO Members and Accessions

a) Recent Members	Date of Membership
Cape Verde	(23 July 2008)
Ukraine	(16 May 2008)
Tonga	(27 July 2007)
Vietnam	(11 Jan 2007)
Saudi Arabia	(11 Dec 2005)
b) Accession in Progress	
Afghanistan	Lebanese Republic
Algeria	Republic of Liberia
Andorra	Libya
Azerbaijan	Montenegro
Bahamas	Russian Federation
Belaries	Samoa
Bhutan	Sao Tomé and Principe
Bosnia and Herzegovina	Serbia
Comoros	Seychelles
Equatorial Guinea	Sudan
Ethiopia	Tajikistan
Iran	Uzbekistan
Iraq	Vanuatu
Kazakhstan Democratic	Yemen
Lao People's Republic	

In Table 3, the recent (post-2004) new WTO members and those countries in accession negotiations with the WTO are listed. (Note the strong Middle East, Central Asian and Eastern European presence in this list, and the limited number of sub-Saharan countries still outside of the WTO.) To illustrate the impact of becoming a WTO member, we concentrate on Cape Verde.²

² For an assessment of the impact of WTO accession on Eastern European transition economies, see Bachetta and Drabek (2002).

The pre-membership structure of applied (MFN) tariffs is summarised in Table 4. Membership does involve a commitment to comprehensive binding of tariff rates, but with some bindings involving reductions phased in over a period up to 2018. The ceilings committed to on bound rates range from 0% to 55%, with an average bound tariff of about 20% on agricultural products and 15% on industrial products. But these commitments on bindings do not appear to involve substantive restriction of the import policy space relative to what Cape Verde wished to do prior to membership. Compare the average bound tariffs above with average (simple or weighted) applied tariffs in 2004 or 2005 recorded in Table 4. This comparison may in part be inappropriate to the extent that there has been pre-membership tariff reform/liberalisation taking place in preparation of membership. But it emphasises to show that any constraints on the use of tariffs can be phased in over a long time period, and that membership is something that these countries wish to achieve. Cape Verde, like the other recent members and aspiring members of the WTO, are voluntarily negotiating for and willing to concede some policy space in order to enhance the effectiveness of policy in other directions.³

Table 4. Cape Verde's Pre-Membership (2005) Applied Tariff Structure

Frequency distribution	Duty free	0-5	5-10	10-15	15-25	25-50	50-100	>100	Max.	Average applied tariff	
										Simp.	Trade-Weigh. ^(**)
Tariff lines (in %)											
Agricultural products											
MFN applied	32.2	22.1	9.9	0.1	21.0	14.7	0	0	50%	11.7	17.0
Non-ag. Pro.											
MFN applied	45.5	13.1	11.2	0.1	14.0	16.0	0	0	50% ^(*)	10.2	10.2

Source: Tariff Profiles (WTO)

Notes:^(*) except for electrical machinery where the maximum was 320%

^(**) For 2004

³ Cape Verde had no agricultural export subsidy programmes and all its existing domestic support programmes are 'green box' in nature. There were, however, commitments made as part of the membership process on improving market access in services.

IV. FUTURE WTO INFLUENCES ON POLICY SPACE

On the basis of the preceding discussion, one may well conclude that membership in the GATT and the WTO has not in general had a major influence on developing countries' policy space, but that WTO influence has increased somewhat for recent members. It is natural therefore to consider whether WTO influence can be expected to increase in future.

A) Broadening of WTO Disciplines

The shift from the GATT to the WTO and the progressive broadening of the negotiating framework has broadened the sector and policy coverage of the international trading rules – from goods to services, embodying the sensitive sectors of agriculture and textiles/clothing, and covering trade – related issues such as investment Trade Related Investment Measures (TRIMS) and intellectual property Trade Related Intellectual Property Rights (TRIPS). But this broadening of influence has involved possible enhancing as well as restricting features. The scope for more effective promotion of activities of comparative advantage in many developing countries has been increased by increasing opportunities for market access in agriculture, textiles and services. Developing countries may also be concerned with the protection of local intellectual property.

The extension of WTO disciplines to beyond the border issues such as TRIPS and TRIMS, and the possible extension of this agenda during the latest Doha Round of negotiations to wider trade and investment issues, and to trade and competition policy and trade and environment issues, may be interpreted as increasing the reach of WTO disciplines. Indeed earlier in the negotiations, there was disquiet among the developing countries about the proposed extension of the so-called 'Singapore issues,' including trade and labour issues. But therein lies a key message. Any future broadening of WTO disciplines is the outcome of a negotiation process, within which the developing countries have increasing influence (both in agenda-setting and outcome terms). The exclusion or narrowing of some of the 'Singapore

issues' was an expression of that increased influence, as is the failure to reach a negotiated outcome to the Doha Round in general. Note further that the return of any of these issues to future negotiations does not necessarily mean that any negotiated agreement will *only* restrict policy space. There may well also be sources of enhancement, especially if there is scope allowed for differentiation or for slower implementation for developing countries.

B) Stricter Monitoring and Enforcement of the Rules

The fact that recent membership of the WTO has been subject to more conditionality, and the establishment of a formal monitoring mechanism (the creation of the Trade Policy Review Mechanism—TPRM) as a result of the Uruguay Round of negotiations, point to greater policing of the international trading rules. But it is not obvious why better monitoring and enforcement of the rules is necessarily any more restricting of policy space than it is enhancing. A policing mechanism is in principle symmetrical across countries; it constrains your trading partner's actions as much as it does your own, and as a consequence increases the effectiveness of your policies that depend on access to export markets and fair trade.

In practice one may argue that stricter enforcement of the rules is actually asymmetrical across countries by having the implication of altering the behaviour most of the larger, more powerful (economically and politically) countries. The smaller and weaker developing countries in particular stand likely to gain more in terms of the enhancement of their policy space, if their more powerful trading partners are required by better policing and more effective dispute settlement mechanisms to offer more open markets and to trade more fairly. Indeed there are further built-in asymmetries in the TPRM mechanism, because the review process is more frequent for the developed country members of the WTO.

C) More Ambitious Future Negotiations

The information cited earlier on the impact of WTO membership on tariff bindings and tariff levels was by implication backward-looking. The limited

impact identified for most sub-Saharan African countries may well have reflected some mixture of indifference and benign neglect towards them by the industrial country GATT members as far as multilateral trade policy was concerned. With the emergence of more newly industrialising and exporting countries and the intensification of globalisation processes, the attitude of industrial country trade negotiators towards developing countries may well be changing. Indeed during the current Doha Round of negotiations, this change of attitude is evident, with greater pressures from industrial countries for reciprocal liberalisation by developing countries (as part of both the industrial and agricultural market access negotiations). Further, although the principle of differentiation for the least developed countries was recognised by their exemption any from tariff-cutting formula agreed, there was pressure for these countries to substantially increase the coverage of bound tariffs and to reduce the difference between bound and applied tariffs (by reducing bound rates).

Both of these aspects of the Doha agreement offer scope for restricting policy space. The application of a tariff-cutting formula would lower the tariffs (over some agreed time period) of the developing countries, while the binding of tariffs for the least developed countries (again over some agreed time table) may constrain the ability of these countries to raise applied tariffs (and in the future may lead to the lowering of applied tariffs if subjected to some future tariff-cutting requirement). The extent of this future constraint would depend in part on the nature of the tariff-cutting formula (including the degree of differentiation for developing countries), and on the level at which currently unbound tariffs are bound. But it would also depend in part on the extent to which countries might want to raise their applied tariffs above their current levels or above their newly bound levels. If past experience is to go by, then it is not evident that developing countries take advantage of the shorter term flexibility created by the 'water' between their bound and applied tariff rates. Administrative and regional commitments appear to constrain this in which case the key future issue for the developing countries is the extent to which they wish to exchange improved market access to their own markets in return for

improved access to the markets of their trade partners. Again it is a trade-off between your own and other's constraints, but one that is established through negotiation.

V. REVIEWING ALTERNATIVE POSITIONS ON THE POLICY SPACE ISSUE

It may well be clear from the arguments offered and conclusions already reached what judgment is being offered on the 'policy space' debate namely that there are net benefits associated with constraining the use of some potential national policy space in return for the opportunities for enhancing policy space through the reciprocated actions of one's trading partners. The constraints on policy space include constraints on the inappropriate use of policy and use of inappropriate policy instruments. This encourages greater openness and outward-orientation, with associated opportunities for a range of static and dynamics gains. Where this also reduces opportunities for using trade and trade-related policy interventions to remedy market failures, there are more than offsetting benefits from the enhancement of policy that comes from improved export market access and from disciplines on trading partners. In reaching this assessment or position, alternative positions have been rejected. For completeness reasons we consider them now.

A) Is More Trade Policy Choice Always Better?

This 'straw-man' is considered, because on occasions it appears that this is how the policy space debate is represented in policy circles; the WTO rules constrain the use of particular trade policy instruments and by definition therefore are harmful because they restrict the policy choices that developing countries can make. To reject this position, one merely needs to recall how trade policy can be used, and not necessarily for the better, in a less constrained environment.

Recall pre-trade reform conditions in sub-Saharan Africa. Trade regimes in the region, even for members of the GATT, were typified by complex

taxation of imports (multiple taxes, multiple rates and considerable discretion in the application of taxes), extensive use of non-tariff barriers (NTB), highly regulated market entry conditions for domestic firms, and extensive (implicit and indirect) taxation of exports and exportable production. Table 5 provides some evidence on pre-reform NTB coverage and the associated black market exchange rate premia in a range of sub-Saharan countries, while Table 6 captures the variability of protection or incentives across and within sectors that resulted from these types of regimes, with evidence taken from Burundi. The result of these types of policy choices and actions was typically a lack of transparency, costly rent-seeking activity, substantial under-utilisation of capacity, and random and systematic distortions to resource allocation.

Table 5. Selective SSA Information on Pre- and Post Reform NTBs and Exchange Rate Distortions

Country	Pre-Reform ^(*)		Post-Reform ^(**)	
	NTB Coverage	Black Market Premium (average)	NTB Coverage	Black Market Premium (average)
Cameroon	hundreds	–	hundreds	–
Cote d'Ivoire	38%	–	38%	–
Ghana	100%	985%	2%	17%
Kenya	71%	16%	0%	9%
Madagascar	100%	37%	0%	13%
Malawi	100%	51%	Few	12%
Mali	58%	–	0%	–
Nigeria	100%	210%	17%	27%
Senegal	–	–	15%	–
South Africa	55%	0%	23%	3%
Tanzania	100%	242%	100%	119%
Uganda	–	303%	5%	79%
Zaire	100%	71%	100%	9%

Source: Dean (1995)

Notes: (*) Various years, usually 1980s

(**) Various years, usually early 1990s

Table 6. Effective Protection by Sector: Burundi (1984)

SECTOR	RANGE OF RATES % (*)
Agricultural Products	-2 → 4
Food, drink and tobacco	86 → 2017
Leather and footwear	-4 → 102
Textiles	12 → 124
Wood and paper products	43 → 7896
Metal products	16 → ∞
Chemicals	9 → ∞
Pharmaceuticals	1 → ∞
Construction goods	63 → 72

Source: Greenaway and Milner (1991)

Notes: (*) The weighted average rate of effective protection in domestic and export sales.

∞ denotes negative value-added at world prices.

With unconstrained policy choices comes the option to choose poor (costly and distorting) policies (Krueger, 1990). Restricting or constraining the policy space so as to reduce the scope for adopting poor policy choices may restrict national political autonomy, but may well be attractive on economic efficiency and equity grounds. As argued earlier, sub-Saharan countries became more constrained in their trade policy choices, not because of GATT/WTO membership, but because of constraints from other external sources (IMF and World Bank). But interestingly, WTO membership in the 1990s that preceded 'unilateral' reform by some sub-Saharan African countries was seen by these countries as anchoring their reforms and demonstrating their commitment to the future constraining of trade policy space.

B) Do WTO Rules Restrict Heterodox Options With Harmful Effects?

Besides the harmful trade policy options outlined above, it is possible that the WTO rules restrict the use of helpful ones as well. This is certainly the basis of those who interpret the success of the newly industrialising countries (NICs) not in terms of the benefits of liberal trade policies but rather as being due to unorthodox or heterodox industrial policies (Singh, 1994; Lall and Theubal, 1998) and due to selective, interventionist industrial policies, further, that tended to be overlooked or tolerated by the pre-WTO international trading arrangements of the GATT (Hudec, 1987; DiCaprio and Gallagher, 2006).

The constraining of the current developing countries, in particular the least developed countries, from the use of active and effective industrial measures by the WTO policies, is overstated by the critics of the WTO and often the developing countries themselves. Non-trade instruments such as the subsidising or taxing of the consumption or production of goods, services and factors are not in general constrained by WTO rules, and S&D treatment of developing countries gives even more scope even where the distortion of trade flows is involved. The greater constraints are associated with fiscal, human and institutional capacity, especially in the low income developing countries of sub-Saharan Africa or in the case of many of the small, remote and island developing countries. The dangers of picking inappropriate infant or export industries and of providing inappropriate levels of support are considerable where there is limited domestic entry and competition in industrial markets, and where institutional, technical and administrative capacity is limited. These dangers do not mean, however, that industrial policy should necessarily be eschewed or minimalist. Economists such as Rodrik rightly point to the need for industrial policy to be directed towards the correction of market and information failures associated with underdeveloped market conditions in many developing countries. It is about the nature and extent of market intervention that is the point of departure between heterodox and other economists.

The questioning of the transferability of the East Asian model to the developing countries in general, especially given the prior entry of the Asian economies into world export markets and the general greater competition now in domestic and export markets, is not therefore to argue against the need for S&D treatment for developing or against the strengthening of S&D provisions within the WTO (Messerlin, 2006). S&D provisions do need to be better focused on helping developing countries adopt pro-development policies, ones that can be differentiated accordingly to national development need (See also Hoekman, 2004). The vision of what constitutes pro-development policies does, however, differ between more liberal and more heterodox economists!

VI. ENHANCING POLICY SPACE: ADJUSTMENT AND TRADE DEVELOPMENT SUPPORT

For most of the poorest, often remote and small, developing countries the greatest constraints on policy space are not associated with the trade or trade-related policy options available to them. The greatest restraints are about these countries' limited institutional capacity to support or assist adjustment to increased openness or export orientation, or about the human and physical capital constraints on domestic market development and integration into regional and international markets (see Milner, 2006).

To support both development and greater openness to international competition and trade expansion, developing countries must be able to efficiently absorb capital and intermediate goods, new ideas and new technologies and to produce goods and services that can compete on price and quality in domestic and international markets. Developing these capacities requires greater accumulation of physical, human and organisational capital, as well as enhanced technological capacity. It requires investment in machinery and equipment, but also in domestic infrastructure (e.g. roads, utilities). It covers both public and private investment and goes beyond material capital accumulation to investment

in education, health and skills. It requires incentives for risk-taking and enterprise by firms and individuals. In part this may be encouraged through the development of domestic capital markets and the promotion of foreign direct investment but it also requires additional development finance and reduced debt constraints. It also requires social institutions to protect property rights, especially intellectual property rights, and to foster business formation, investment and risk-taking by individuals.

Trade and trade policy are important for capital accumulation and technological improvement. The expansion of exports alleviates the balance of payments constraint and permits increased imports of capital goods that embody technological improvements. Access to cheaper imported intermediate goods and increases in competition resulting from increased openness can raise returns on investment and increase incentives to invest. However a range of other sectoral, public sector and microeconomic policies are likely also to be required to make trade pro-development.

Utilising increased productive capacity and providing an incentive to increase capacity requires that production can be sold abroad. A country's capacity to access imports efficiently and to deliver exports to foreign markets is influenced, not only by the trade policies of its trading partners and its own import and export policies and procedures, but also by the scale and quality of the infrastructure affecting its international transport and related services such as communications and the quality of its institutions supporting trade. (For evidence of the relative scale of trade policy and non-policy barriers for some sub-Saharan African countries see Milner et al, 2000 and Milner and Zgovu, 2006). The key issue for the present purpose is to emphasise the asymmetrical effect of trade costs associated with 'natural' barriers such as distance or transport inefficiencies on the incentives to produce for domestic and export markets. 'Natural' barriers are an implicit subsidy to import substitution activity, but also a 'tax' on export-oriented production. Table 7 below illustrates this with some information on the average rates

of effective protection arising from trade policy and 'natural' barriers in the Ugandan manufacturing sector, distinguishing between protection in domestic and export sales. Trade policy liberalisation alone will not eliminate this bias against exporting.

Table 7. Average Rates of Effective Protection in Uganda's Manufacturing Sector (1994) %

In Sales to:	Due to:		Overall Rate ^(*)
	Trade Policy Barriers (a)	'Natural' Barriers (b)	
Domestic Market	+91.3	+27.0	+141.6
Export Market ^(**)	-15.6	-88.9	-108.7

Source: Milner (1997)

Notes: ^(*) Equals (a) plus (b), plus the interactive effect between (a) and (b)

^(**) Based on presumed or potential sales to (unprotected) extra-regional export markets

Trade policy reforms in developing countries have been necessary to initiate integration in to the global economy, but they have often not been sufficient. For many countries the costs of imported goods and the competitiveness of their products in export markets depends more on international transport and other natural trade costs than on their own or other countries' trade policies. There is growing recognition that trade policy, narrowly defined, has been overemphasised at the expense of complementary trade-related measures. Such measures include domestic and international transport policy reforms, national or regional infrastructure developments, or a wider range of services (e.g. insurance, banking) affecting the cost of international transactions. Manufacturing is transaction-intensive, and with the growing fragmentation of international production and creation of international production networks, it is important that developing countries have access to competitive trade and trade-related services.

Viewed narrowly, trade facilitation enables the movement of goods and services across national barriers. Improving transport systems by investing in infrastructure or changing policies to increase competition and efficiency are broader facilitation measures. Improving customs clearance procedures, supporting the capacity to meet the technical or health standards in export markets, and strengthening support for marketing export products is also required. Trade facilitation might also extend to the availability and efficiency of financial and other business services. Uncompetitive local conditions and barriers to moving work offshore may allow costly and lengthy administration procedures to persist in the service sectors. The cost of credit, including trade credits, and of working capital can be much higher in developing countries than countries with more developed and competitive service sectors. Many developing countries have made progress in reducing administrative procedures, bureaucracy and corruption. Changing the ethos of institutions and administrative systems and restoring confidence in them, however, is often difficult and slow. There is still considerable scope for improving the business environment in many developing countries and for reducing the costs of doing business.

A) Aid for Trade and the WTO

The WTO has played a role over the last decade in the greater focus on trade adjustment and assistance issues that is to be found in policy debates.⁴ The WTO Task Force Report (tabled in July 2006 and approved by the WTO General Council in October 2006) has the broad and ambitious objectives of assisting developing countries to increase their exports of goods and services, integrate into the multilateral trading

⁴ An Integrated Framework (IF) for Trade-Related Technical Assistance to Least Developed Countries was set up in 1997 by six multilateral agencies (IMF, World Bank, UNCTAD, UNDP, ITC and WTO). It seeks to bring together these multilateral agencies, with bilateral donors and with the national governments of the LDCs with the aim of establishing a process to integrate trade into national development plans and assist in coordinated delivery of trade-related assistance (identified by the LDCs).

system and benefit from liberalised trade and improved market access. The Report viewed aid for trade (AFT) as involving the enhancement of productive capacity, the improvement of trade-related infrastructure and institutions, and enhancement of the capacity of developing countries to negotiate and implement trade agreements.

A Global AFT Review (undertaken jointly by WTO and the OECD in 2007) reviewed donor commitments on trade-related aid for the period 2002–2005. This data shows that on average, US \$21 Billion (B) of such aid had been committed, broken down as \$0.6 B for enhancing trade policy capacity, \$8.9 B for promoting productive capacity and \$11.2 B for infrastructure development. This is most likely an upwardly-biased estimate, since the infrastructure figure certainly covers more than trade-related infrastructure, although it excludes any general budget support, under Official Development Assistance (ODA) definitions, that goes to trade-related areas and any non-ODA and other low concessional financing. It appears, however, to reverse an apparent long-term decline in such aid, and in the context of a growth in overall ODA since 2001.

Of course adverse global conditions may reduce overall aid provisions in the short-to-medium term. One might also be sceptical about the extent to which the enthusiasm of industrial country members of the WTO for the AFT initiative was driven by the need to encourage developing countries to sign up for a settlement to the Doha (Development) Round. But, whether or not for wholly the right reasons, ‘aid for trade’ is an appropriate focus for the ways in which multilateral and bilateral donors, with WTO support, need to direct the focus of the policy space debate. It offers considerable scope for most low-income developing countries to enhance the effectiveness of their trade policies.⁵ WTO is not, and should

⁵ Of course, the ‘aid for trade’ initiative must recognise the dangers of inappropriate aid provision and use, as in the case of non-trade related aid provision, but that should not undermine the argument for both national (donor and recipient) governments and the multilateral agencies for taking a broad view of trade policy.

not become, a development agency. It can, however, play an advocacy, dialogue and coordination role on such trade-related matters.

VII. CONCLUSIONS

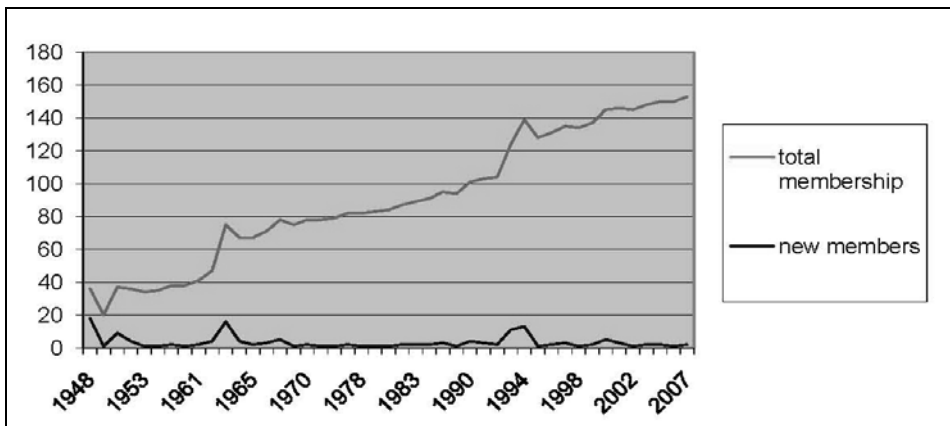
This paper has sought to explore the positive issue of whether the WTO has restricted or threatens to restrict the trade and development policy space of developing countries, and if so whether this is undesirable. It argues that the GATT and WTO have not significantly affected developing countries' policy space to date. The main sources of influence on their trade policy space have thus far been from other than multilateral sources. There are however some indications that this influence on developing countries' space is beginning to increase and may well increase further, as indicated by the stronger commitments required of recent new members of the WTO and the greater focus of recent multilateral negotiations on the trade policies (bindings, reciprocal tariff cuts etc) of the developing countries, although the degree to which this is likely to constrain active trade-related and sector policies in developing countries may well be overstated by the critics of the WTO. The WTO articles allow for differentiation of the rules for developing countries, and any commitments on tariffs, new sectoral disciplines or on trade-related policy instruments are likely to embody this differentiation and be phased in over time. Further the WTO offers a negotiating framework and a vehicle for dispute settlement. It is evident that the developing countries are using their collective influence within the WTO more aggressively. The Doha Round has still not been completed for this very reason!

Any evidence or threat of greater constraint on the WTO's policy space does not in any case have to be viewed necessarily as harmful to the developing countries. Constraining, for example, the use of inappropriate instruments or the excessive use of particular measures is likely to be helpful. Further, reciprocity and policing of the system mean that membership in the WTO imposes constraints on your trading

partners' actions as well, and thereby offers opportunities for enhancing your own policy space. There is the opportunity for sacrificing some policy space in order to benefit in net terms. If the growth of membership (see Table 8) and the queue for membership (Table 3) are anything to go by, then it looks like many developing countries have made a similar, positive net benefit assessment of WTO membership.

A central theme of this paper is in fact that the developing countries and many commentators have tended to overemphasise the importance of trade, trade-related and sectoral (e.g. industrial) policies in promoting development in many of the least developed, smallest and most remote developing countries. Enhancing these countries' policy space depends much more on improving governance, institutions, human capital and infrastructure. The WTO is not a core development agency, but it can play a role in shifting the focus from a narrow concept of trade policy space.

Table 8. GATT/WTO Membership (1948–2007)



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