Understanding developing country resistance to the Doha Round

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ABSTRACT

The Doha Round negotiations at the World Trade Organization have come to a halt. The vast majority of analyses of the (at least temporary) demise of the Doha Round have focused on the lack of the United States and the European Union to reach consensus on the agricultural proposals that were tabled during the round. Relatively little attention has focused on explaining the rationale for why a large part of the developing world would not agree to proposals on the table as well. Many developing country negotiators claim that the potential benefits of the Doha Round were relatively small while the potential costs in terms of a loss of sovereignty to deploy effective development policies were significant. This paper argues that developing countries took a respite from the negotiations because the possible gains from market access were not large enough to trade for giving up domestic policy space for development policy.

KEYWORDS

WTO; developing countries; development policy.

1. BACKGROUND: POLICY SPACE FOR WHAT?1

The Uruguay Round negotiations were completed in 1994 and culminated in the establishment of the World Trade Organization (WTO) in 1995. When the developed world proposed another round of global trade talks in 2001 in Doha, Qatar, developing countries agreed to negotiate only on condition that development was the centerpiece of the negotiations. The round is thus commonly referred to as the ‘Doha Development Round’ (DDR).

During the DDR many developing countries rejected numerous proposals on the grounds that such proposals further constrained their policy space to deploy adequate development policies (South Centre, 2005).
Policy space has become a Geneva buzzword, but is rarely defined. For the purposes of this paper, policy space is defined as the flexibility under trade rules that provides nation states with adequate room to maneuver to deploy effective policies to spur economic development. More often than not it is referred to as space that allows developing countries a relatively larger role in economic development policy than is permitted by developed countries but that developed countries deployed during earlier stages of development. In essence, some developing countries are concerned about their sovereign ability to deploy certain policies. Thus, ‘policy space’ is used interchangeably in this paper with ‘development sovereignty’.

The case for policy space is often made on both theoretical and empirical grounds. The persistence of market failures in the global economy, especially rife in developing countries, is cited as the theoretical justification for governments to play a supporting role in the development process. On the empirical level, the experience of many of the East Asian tigers such as Taiwan, South Korea, and contemporary China is pointed to as testimony that state-facilitated development policy can be a success. Both justifications are not without their critics.

When markets stray from ideal conditions, market ‘failures’ emerge that distort the real functioning of the economy against the ideal result, creating or sustaining inequalities, environmental stress, and technical stagnation or regress. Although it has brought considerable benefit, the recent wave of globalization has integrated vastly different economies at vastly different levels of development. Developed and developing countries alike are rife with market failures. Integration can lead to the globalization of market failure – in other words, economic distortions – in many cases (see Gallagher, 2005).

Economic theory states that when the market fails, policy instruments should be deployed to correct the distortions created by private markets (Lipsey and Lancaster, 1956). This theory is referred to as the ‘second best’ theory, and states that government policy can offset market failures.

There are four categories of market failures that are most prone to being ‘globalized’ during the economic integration process: market failures related to imperfect competition, externalities, and technological dynamism. Economists have shown that liberalizing trade in one country that uses second best policies to correct for market failures and another that does not correct for distortions can accentuate the distortions that were occurring in the first place (Kowalcyk, 2002). Common market failures in today’s global economy that developing countries face are:

- **information externalities** where the private sector lacks the information about opportunities to make productive investments;
• **coordination externalities** where profitable new industries will not develop unless ‘upstream and downstream’ industries are developed simultaneously;

• **imperfect competition** where highly concentrated sectors make entry into the industry and technological change extremely difficult; and

• **environmental externalities** where the environmental costs of production and consumption are not reflected in prices and lead to the under or over production of certain goods and services.

For instance, if a nation liberalized trade in a sector where its firms are forced to compete with global monopolies or oligopolies, the imperfectly competitive firms can wipe out the local firms and then sell their products at higher prices than they would in a competitive environment. Or in the terms of externalities, when trade is liberalized between two countries and only one of them produces with second best policies to protect the environment, production can increase in the more environmentally destructive country. Economists have also argued that the WTO has focused on reducing tariff rates, rather than economic distortions – reducing rates can simply maintain existing distortions and even exacerbate such distortions. The policies outlined above therefore can be justified as ‘second best’ approaches to correct the distortions created by the globalization of market failures.

Some countries have been successful at deploying state-led policies for economic development, namely, Taiwan, South Korea and more recently China. Today’s developing nations look to these success stories as possible models for twenty-first century policy.

Table 1 exhibits average annual growth rates in GDP per capita for selected regions of the world from 1970 to 2004.

East Asia experienced 4.5 percent annual per capita income growth from 1971 to the present – one of the most impressive growth trajectories on record. What’s more, such growth has also corresponded with reduction in inequality and improvements in many other social indicators. It is beyond the scope of this paper to explain in detail the literature on development in these nations, but experts attribute East Asian growth to four general

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<tr>
<td>East Asia</td>
<td>5.2</td>
<td>4.4</td>
<td>3.9</td>
</tr>
<tr>
<td>Latin America</td>
<td>3.3</td>
<td>−0.8</td>
<td>0.7</td>
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<tr>
<td>US</td>
<td>2.2</td>
<td>2.4</td>
<td>1.6</td>
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<tr>
<td>World</td>
<td>1.8</td>
<td>1.4</td>
<td>1.1</td>
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*Source: World Bank (2005).*

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categories of policies (for useful full-length treatments of development in this region and the use of state policy tools, see Amsden, 2001; Kim and Nelson, 2000; Wade, 2004; World Bank, 1994):

• targeted industrial policy with reciprocal control mechanisms where nations selectively secluded certain industries where they wanted to gain dynamic comparative advantages;
• loose intellectual property rules where nations encouraged learning from foreign nations through government R&D efforts and at times reverse engineering good from foreign counterparts;
• the movement of people across borders for higher education and temporary work. The best students were sent to the US and Europe to earn degrees in science, mathematics, and technology then came home to work in targeted industries or government; and
• investment in human capital and public infrastructure where governments invested heavily in education and provided infrastructure such as roads, ports, and so forth.

There is considerable debate regarding the extent to which these policies were the key drivers of growth in some countries. Nevertheless, at this point there is widespread agreement that these policies did have some positive effect on economic performance. The debate now centers on what level of effect that was (World Bank, 1994). It is not the purpose of this paper to enter that debate. Nor is it the purpose of this paper to judge the value of those policies for development. Rather, based on the evidence that such policies have had some positive effect, this paper examines whether developing countries are still given (or keeping) the choice to deploy them under existing and proposed WTO rules.

Table 2, in the next section of this paper, outlines the major policy measures that were deployed by these countries to fulfill the four objectives presented above.

Whereas the East Asian nations – such as South Korea and Taiwan – managed their integration into the world economy through gradual liberalization and some degree of government involvement, nations in Latin American in the Caribbean (LAC) rapidly liberalized their economies in a short period of time – along the lines currently being advocated in the Doha Round. As we see in Table 1 for LAC, income growth since liberalization began in the 1980s has been barely one percent annually.

Many economists have expressed caution over advising other developing countries to follow the same path as East Asia. First, governments can be pathetic in picking ‘winners’ for industrial policy. Many governments have tried to adopt pro-active policies and have failed miserably – in other words, meeting market failures with government action often leads to government failure. Governments have been criticized for not being able
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to pick winning sectors to focus on. Indeed, there are many examples of governments picking ‘losers’. South Korea and Taiwan are often cited as success stories but Indonesia, Nigeria, and Brazil have had failures that have received relatively less attention in scholarly circles. (Burton, 1983; Evans, 1995). In addition, subsidization and government involvement has been shown to accentuate ‘rent-seeking’ behavior that make it additionally difficult for developing country governments to let go of projects that aren’t going well or that have already reached maturity (Krueger, 1996).

These critiques are quite valid. Of course, without the proper policies in place, government intervention can create more problems than they correct for. However, the most successful cases (discussed in the next section of this paper) in large part circumvented these problems because governments by designing policies where corrective instruments were indeed close to market failures, where state actors were ‘embedded’ in the private sector and where the state enforced discipline on the private sector.

To circumvent the rent-seeking problem, political scientists have shown that successful industrializers have had states that were ‘embedded’ in the private sector while maintaining ‘autonomy’ from sectional elite interests seeking rents. State agencies that are charged with correcting market failures have to maintain constant communication and input with the private sector (Evans, 1995). Perhaps most importantly, the problem of picking winners problem has been circumvented by having a good deal of discipline for private actors. Alice Amsden (2001) has referred to the need for ‘reciprocal control mechanisms’. A control mechanism is ‘a set of institutions that disciplines economic behavior based on a feedback of information that has been sensed and assessed’ (Amsden, 2005). For the East Asian success stories, the key principle behind their use of control mechanisms was ‘reciprocity’:

Reciprocity disciplined subsidy recipients and thereby minimized government failures. Subsidies were allocated to make manufacturing profitable – to convert moneylenders into financiers and importers into industrialists – but did not become giveaways. Recipients of subsidies were subjected to monitorable performance standards that were redistributive in nature and result-oriented. The reciprocal control mechanism thus transformed the inefficiency and venality associated with government intervention into collective good. (Amsden, 2005: 222)

In other words, firms have performance requirements that when they aren’t met are no longer supported. The most successful industrializers were able to abandon projects that were not performing whereas others where perpetuated because bureaucrats became hijacked by business interests who
became dependent on the state. The next section discusses how well such performance requirements and other measures performed in developed and developing countries.

In summary, it should be underscored that policy space alone will not develop economy. It takes domestic political will, reciprocal control mechanisms and perhaps a lot of luck.

2. DEVELOPMENT SOVEREIGNTY AND THE URUGUAY ROUND: A CRITICAL ASSESSMENT

This section of the paper presents a critical review of the literature on the loss of policy space in the WTO, particularly the results of the Uruguay Round (UR). Most of the literature on this subject has been somewhat void of looking at these ‘costs’ of the round in their full political economic context. Focusing solely on what was ‘lost’ in the round falls short of acknowledging two things. First, that there were also benefits to the UR, and second, that the losses were exchanged as part of a grand bargain where developing countries gained access to developed country markets. The first part of the section outlines that literature that shows how indeed developing countries surrendered significant amounts of development sovereignty under the UR. However, the second part shows that such losses were incurred in exchange for significant benefits (for many developing countries).

2.1. The loss of policy space in the UR

There is a fairly large literature that shows how, when looked at in isolation, developing countries surrendered a great deal of development sovereignty in the UR. Table 2 outlines the majority of the key policy instruments used by successful late industrializers and lists indicates whether or not such measures are still permitted under the WTO and under what agreement. An ‘X’ depicts whether a measure is permissible under UR is derived from the literature. A ‘*’ depicts whether the measure was permissible under the final proposals at the DDR and is the author’s original analysis. This latter analysis will be presented in the next section of the paper.

This table reveals that there was a loss of policy space in goods trade, intellectual property rules, subsidies, investment rules, and services. However, when looked at as a whole (which has not been done in the literature), I conclude that there was still considerable policy space left for developing countries if they so chose to use it. Each of these is discussed in turn.

Goods trade. Industrial nations and East Asian success stories after them relied on relatively high tariffs in order to sequence the integration of select industries into the world economy (Amsden, 2001; Chang, 2005). The
Table 2 Policy space for development and the WTO

<table>
<thead>
<tr>
<th>Policy instrument</th>
<th>Permitted</th>
<th>Agreement</th>
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<tr>
<td>Goods trade</td>
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<tr>
<td>Tariff sequencing</td>
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<td>GATT</td>
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<td>Tax drawbacks</td>
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<tr>
<td>Intellectual property</td>
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<tr>
<td>Selective permission for patents</td>
<td>X</td>
<td>TRIPS</td>
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<tr>
<td>Short patent timelines with exceptions</td>
<td>X</td>
<td>TRIPS</td>
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<tr>
<td>Compulsory licenses</td>
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<tr>
<td>Subsidies</td>
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<tr>
<td>Export</td>
<td>X</td>
<td>SCM</td>
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<tr>
<td>R&amp;D</td>
<td></td>
<td>SCM</td>
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<tr>
<td>Distribution</td>
<td></td>
<td>SCM</td>
</tr>
<tr>
<td>Environment</td>
<td></td>
<td>SCM</td>
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<tr>
<td>Cost of capital</td>
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<td>FDI</td>
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<tr>
<td>Local contents</td>
<td>X</td>
<td>GATT, TRIMS</td>
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<tr>
<td>Trade balancing</td>
<td>X</td>
<td>TRIMS</td>
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<td>Joint ventures</td>
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<tr>
<td>Technology transfer</td>
<td></td>
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<tr>
<td>R&amp;D</td>
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<tr>
<td>Employment of local personnel</td>
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<tr>
<td>Tax concessions</td>
<td></td>
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<tr>
<td>Other</td>
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<tr>
<td>Human capital</td>
<td></td>
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<tr>
<td>Administrative guidance</td>
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<tr>
<td>Movement of people</td>
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<tr>
<td>Provision of infrastructure</td>
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Source: See Gallagher (2005); Shadlen (2005a).

Uruguay Round and the subsequent establishment of the WTO took a bite out of the ability to use such measures, but left significant room for nations to use tariffs as a means to foster industrial development. Under the WTO nations had to convert their non-tariff measures such as licenses and quotas to their tariff equivalents and had to bind (place ceilings on) many tariff categories. Many developing countries left their bound limits fairly high upon entry into the WTO and entered the WTO with relatively higher average industrial tariff rates than developed countries – 12.5 percent versus just over 4 percent. In addition, developing countries did not have to bind all their tariffs. On average, developing countries bound only 61 percent of their tariff lines. Some nations such as Mauritius, Zimbabwe and others chose to only bind 10 percent of their tariffs (Martin and Ivanic, 2005).

Article XVIII of the WTO allows nations to further use import controls as safeguards to protect themselves against foreign export competition that is
due to unfair competition, import surges, or that disrupts their balance of payments. Whereas the GATT allowed unlimited limits on the duration of safeguards however, the WTO limits their use to eight years. Developing nations have been working to shield themselves from unfair competition from developed countries by filing anti-dumping claims at the WTO. In the 1980s developed countries were the major filers of anti-dumping suits; by the late 1990s developing countries filed two-thirds of all claims (Amsden, 2005).

**Intellectual property rules: Trade Related Intellectual Property Rights (TRIPS).** Developed countries hold 86 percent of all patents in the world and receive 97 percent of all patent royalties. This makes it very difficult for developing countries to enter the innovation process or at least very expensive in terms of licensing such patents (UNDP *et al.*, 2003). To address these asymmetries developing nations – especially those in East Asia – relied on considerably loose intellectual property rules.

In order to facilitate domestic firms’ capabilities for adapting to and improving on foreign innovations, many late industrializing nations simply refused to grant patents for key products and limited the ability of permitted patent holders to exclusively hold patents for a long period of time (Correa, 2005; Shadlen, 2005a). Such strategies are now considerably more difficult under TRIPS. The agreement states that nations have to grant patents in all fields of technology and that patent holders may have exclusive rights over patents for 20 years.

The economic costs of TRIPS under the Uruguay Round have been significant. First, costs have incurred from using patentable knowledge. Second, there are welfare costs for consumers who subsequently have to pay higher prices for patented goods. As shown in Table 3, World Bank estimates of

<table>
<thead>
<tr>
<th>Country</th>
<th>Millions of 2000 dollars</th>
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<tr>
<td>US</td>
<td>19,093</td>
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<tr>
<td>Germany</td>
<td>6,768</td>
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<tr>
<td>Japan</td>
<td>5,673</td>
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<tr>
<td>France</td>
<td>3,326</td>
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<tr>
<td>UK</td>
<td>2,968</td>
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<tr>
<td>Switzerland</td>
<td>2,000</td>
</tr>
<tr>
<td>Australia</td>
<td>1,097</td>
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<tr>
<td>Netherlands</td>
<td>241</td>
</tr>
<tr>
<td>Ireland</td>
<td>18</td>
</tr>
<tr>
<td>Total</td>
<td>41,184</td>
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*Source: World Bank (2002).*
the amount of South-to-North profit transfers due to the WTO are $41 billion annually, higher than some of the estimates for the benefit of the round as a whole (Weisbrot and Baker, 2004). Because virtually all forms of technology now have to be patented under TRIPS, TRIPS increases the price of patentable knowledge and thus increases the flow of rents from South to North (Correa, 2005).

Other researchers have estimated the welfare effects of the TRIPs agreement. One area of considerable research has been the welfare effects of the TRIPS agreement and pharmaceuticals – which can be as much as six times the patent transfer costs. A study of quinolones in India found that the annual welfare losses to the Indian economy were $450 million. Eleven percent of those losses accrued to domestic producers and the rest to Indian consumers. In contrast, the profit gains to foreign producers were only $53 million per year (Chaudhuri et al., 2004). Another study found costs of a similar magnitude for Argentina in terms of pharmaceuticals. Based on the differences between prices charged by foreign pharmaceutical firms in markets with and without patent laws, it was estimated that the transfer from Argentine consumers to foreign drug firms will be $425 million on an annual basis (Nogues, 1993).

TRIPS however, still does permit nations some exceptions to exclusive patent holdings, as in the case of compulsory licenses. Compulsory licenses are when the government steps in and allows a domestic firm (or government agency) to patent without the patent holder’s consent. Although TRIPS does limit the conditions under which nations can issues compulsory licenses, there is still significant leeway for their use (Correa, 2005). Compulsory licenses are restricted to be of limited duration, be predominantly for the domestic market, and that compensation is paid to patent holders. It is important to note, however, that the TRIPS agreement does not specify conditions on the grounds of compulsory license use – nations can issue a compulsory license for whatever reason they deem necessary (Shadlen, 2005a). However, in regional and bilateral trade agreements developed nations are refusing to grant developing nations this policy space (Shadlen 2005a; 2005b).

**Agreement on subsidies and countervailing measures (SCM).** The SCM agreement has limited the options for subsidizing industry under the WTO. Subsidies have a clear economic justification, but have to be allocated in a disciplinary manner. Subsidies are one tool for correcting market failures. Indeed, without the proper policies in place, government subsidies can create more problems than they correct for. A framework for ‘smart’ subsidies has been termed ‘reciprocal control mechanisms’ (discusses above) and was deployed by the most successful East Asian economies (Amsden, 2001, 2005).
The agreement clearly defined a subsidy and introduced the concept of a ‘specific’ subsidy. Specific subsidies are supports made solely to an enterprise, industry, or a group of enterprises. The agreement only applies to specific subsidies when they take the form of domestic or export subsidies. SCM separates subsidies into three categories: prohibited, actionable and non-actionable. SCM covers agricultural goods as well as industrial products, except when the subsidies are exempt under the Agriculture Agreement’s ‘peace clause’. The SCM prohibits the subsidies directly linked to exports (export subsidies) which were key control mechanisms for many developing countries.

All forms of export subsidies are prohibited under the SCM and therefore constrain the ability of nations to help their firms break into global markets. However, there is some indication that nations may subsidize firms to the point that they become strong enough to export. Canada challenged Brazil’s subsidies to the aircraft giant Embraer. Brazil has a subsidy program to help firms access capital in credit scarce Brazil. Canada won the case and Brazil modified its subsidies to Embraer but kept the program intact for smaller firms. Presumably then these subsidies could remain in place (or under the radar screen) until recipient firms became strong enough to inflict ‘damage’ on foreign firm and thus become prey to WTO suits (Schrank and Kurtz, 2005).

Under Article 8 of the SCM, three types of subsidies were permitted ‘green light’ subsidies – assistance for R&D, assistance to disadvantaged regions, and assistance to promote the adaptation of existing facilities to new environmental regulations. These subsidies remained non-actionable until 2000, giving countries significant policy space. Re-establishing such subsidies was under negotiations at the DDR and will be discussed in the next part of the paper.

Investment rules: Trade Related Investment Measures. Like TRIPS, the agreement on Trade Related Investment Measures (TRIMS) was forged during the Uruguay Round. As part of targeted industrial policies East Asian nations strategically relied on foreign investment as part of their strategy to gain dynamic comparative advantage in higher value added economic activity. The TRIMS leaves a significant amount of policy space for developing countries. In addition, developing countries were successful in keeping deeper measures in investment rules off the negotiating agenda for the Doha Round.

Nations such as South Korea and Taiwan, and now China, encouraged foreign investment in certain sectors but required that the majority of the firm be owned by nationals, that certain percentages of local suppliers be used, that technology and R&D be transferred and conducted in the host country, and that a certain percentage of nationals be employed in such processes. Because oligopolistic foreign firms can crowd out local
competition, such policies are justified on economic grounds and have worked well for many countries when the proper control mechanisms and when government enjoyed embedded autonomy in the private sector (Kumar, 2005).

The TRIMs agreement makes it more difficult to selectively choosing foreign investment in host countries and also restricts the ability of nations to deploy local content standards. TRIMS also constrains the ability to impose trade balancing requirements (which make foreign firms use domestic inputs rather than foreign imports) (Kumar, 2005; Shadlen, 2005a). Such rules have contributed to the crowding out of domestic investment in some areas of the globe. In Latin America, a region that received large amounts of foreign investment in the 1990s, total investment has been on the decline. Indeed, gross fixed capital formation as a percentage of GDP has been a mere 19 percent during the 1990s. In contrast East Asian economies have experienced investment levels of 40 percent of GDP (Agosin and Mayer, 2000).

Although many measures are not permissible, significant space remains: requiring R&D, requiring joint ventures and technological transfer – remain intact (Kumar and Correa, 2004).

General Agreement on Trade in Services. The General Agreement in Trade and Services (GATS) is at the same time one of the most flexible and constraining WTO agreements. On the one hand the GATS has a ‘positive list’ approach where nations only have to liberalize those service sectors that they wish rather than liberalizing all but sensitive sectors. In addition, when a nation does list a sector they may put ‘limitations’ on such liberalization. For instance, in Chile’s liberalization of some sectors they have required that foreign firms control only 49 percent of the firm’s equity and that foreign firms employ a certain amount of local employees.

However, the GATS came at considerable cost for some developing countries. It has been shown that when key service sectors are liberalized, private foreign firms often do not have the incentive to provide equitable access and low prices, and some citizens are even denied services (Bifani, 2004). One study examined the impact of financial services liberalization on the rural poor in four African countries: Kenya, Malawi, Lesotho, and Uganda. In three out of the four countries the result was a decrease in access to rural credit. The exception was Uganda, who coupled liberalization with regulation focused on access and poverty reduction (Mosley, 1999).

This exposes the fact that the GATS, unlike the GATT, does not have safeguard provisions. In the GATT, nations are permitted to temporarily suspend their liberalization commitments during or in response to a threat of an import surge that would result in serious injury to domestic industry. The GATS does not have such provisions. In the GATS case nations would be allowed to suspend liberalization during or in response to
foreign investment that was wiping out local investment as in the African case outlined above.

In summary, indeed the UR took a large bite out of the development policy set deployed by some developing countries. However, it is often overlooked that many options for policy space still remain under the WTO. Investing in human capital, providing marketing support to firms, supplying public infrastructure are all key elements of late industrialization that continue to steer clear of WTO rules. More specifically, what is clearly WTO legal at this writing is the ability to fund human capital and public infrastructure, offer tax concessions to foreign firms, and provide marketing services to domestic firms.

2.2. The other side of the table: Policy space for market access in the ‘grand bargain’

While the loss of policy space discussed above is significant, it should not be viewed in isolation. Developing countries knowingly surrendered such policy choices in exchange for something else. The outcome of the UR negotiations has been dubbed by many as a result of a ‘grand bargain’:

it was essentially an implicit deal: the opening of OECD markets to agriculture and labor intensive manufactured goods, especially textiles and clothing, for the inclusion into the trading system of trade and services (GATS), intellectual property (TRIPS), and (albeit to a lesser extent than originally demanded) investment (TRIMS). (Ostry, 2000: 4)

The developed world brought (to a limited degree) agriculture into the trading system, agreed to the Agreement on Textiles and Clothing agreement to phase-out of northern textiles and clothing. Although developing countries were initially very opposed to inclusion of new issues beyond goods trade, the south ultimately agreed to surrender policy space in terms of TRIPS, TRIMS, and GATS in return for these northern concessions (Odell, 2006).

Ten years after the UR and WTO went into affect, some developing countries felt that the UR result was lopsided in favor of developed world. However, according to the majority of economic estimates the net benefits to the developing world were fairly significant under the UR, most putting the benefits in the 50 to 100 billion dollar range (see Stiglitz and Charlton, 2004; Weisbrot and Baker, 2004). Nevertheless, there were winners and losers of the UR. Although the net benefits for developing countries were positive, some regions were worse off. The 48 least developed countries were worse off by $600 million, and sub-Saharan Africa was worse off by $1.2 billion (UNDP, 1997). Moreover, many of the nations that demanded liberalization of textiles and apparel had not anticipated China’s entry into
the WTO – which resulted in China capturing most of the non-agricultural developing country gains from the UR. Finally, many countries were not aware of the ‘costs’ in terms of policy space that are outlined here. For these reasons and others, many developing demanded that any subsequent new round would have to address the needs of the poorest countries.

3. ANALYSIS: DEVELOPMENT SOVEREIGNTY AND THE DOHA ROUND

This section of the paper presents an original analysis mirrored on the framework presented in the critical literature review above. From a political economy perspective, this analysis examines the extent to which proposed measures under the DDR would have further constrained development sovereignty in developing countries but juxtaposes such ‘costs’ with estimates of the potential benefits of the deal on the table. That deal was cuts in agricultural tariffs and subsidies in the developed world for cuts in manufacturing tariffs and services regulation by the developing world. This sets up the ability to ask the question of whether or not there was the means for a grand bargain analogous to the UR where developing countries could further surrender policy space in exchange for further access to developed country markets.

3.1. Policy space in the DDR proposals

Relative to the UR, proposals under the DDR would not present major new constraints on development sovereignty for poorer countries – especially when the DDR is looked at during its full period, 2001 to 2005. From 2001 to 2003, negotiations covered further deepening of investment and IPR rules, in addition to new negotiations in competition policy. The ‘final’ deal consisted of cuts in agricultural tariffs and subsidies in the developed world for cuts in manufacturing tariffs and services regulation by the developing world. Such proposals by the developed world on these issues were rejected by the developing world. To what extent were cuts in manufacturing tariffs and services regulations constraining developing country policy space? They are presented in Table 1 above and discussed below.

Goods trade. The proposals in the Doha Round, from Hong Kong until talks collapsed in the summer of 2006, would have made some nations suffer major losses of government revenue and made it much more difficult to use tariffs for selectively fostering industry. For instance, in the Non-Agricultural Market Access (NAMA) negotiations developed countries proposed binding all tariff lines, lowering average tariffs by at least 30 percent, with such reductions on a tariff line by tariff line basis under a Swiss formula. Under a ‘likely’ scenario this would lower the average
developing country tariff from 12.5 percent to 5.9 percent for existing tariff lines, or from 12.5 percent to 9.2 percent if all lines became bound (de Cordoba and Vanzetti, 2005).

‘Swiss formulae’ are scenarios that would allow higher tariffs to be cut more than lower tariffs. The formula is represented as follows:

\[
t_1 = \frac{a \cdot t_o}{a + t_o}
\]

where \(t_o\) is the initial tariff, \(a\) is the tariff ‘coefficient’ that sets the highest possible tariff in the new schedule, and \(t_1\) is the new tariff. Negotiators are currently negotiating over the coefficients for developed and developing countries (Martin and Ivanic, 2005). Figure 1 illustrates how coefficients of 6 and 25 for developed and developing countries, respectively (the coefficients plausible under a ‘likely scenario’) would work.

In Figure 1 the horizontal axis is the initial tariff \((t_o)\) and the vertical axis is the final or Doha tariff \((t_1)\). Applying the Swiss formula with coefficients of 6 for developed countries and 25 for developing countries, the figure shows how higher tariffs are reduced more than lower tariffs. For developing countries, tariffs that were 101 percent are reduced to 20 percent \((25(101)/25+101)\), whereas for developed countries, where the coefficient would be 6, tariffs that were 101 percent would be reduced to just over 5 percent.

As shown in Table 4, the fiscal costs of these tariff reductions will be significant. The coefficient under discussion during the summer of 2006 was

\[
Figure 1\ Application\ of\ Swiss\ formula\ for\ NAMA\ negotiations.
\]
Table 4 Estimates of NAMA tariff losses

<table>
<thead>
<tr>
<th></th>
<th>Billions of 2001 US dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td>Developed</td>
<td>38.0</td>
</tr>
<tr>
<td>Developing</td>
<td>63.4</td>
</tr>
<tr>
<td>Selected developing regions</td>
<td></td>
</tr>
<tr>
<td>Middle East and North Africa</td>
<td>7.0</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>1.7</td>
</tr>
<tr>
<td>Latin America and the Caribbean</td>
<td>10.7</td>
</tr>
<tr>
<td>Selected countries</td>
<td></td>
</tr>
<tr>
<td>Brazil</td>
<td>3.1</td>
</tr>
<tr>
<td>India</td>
<td>7.9</td>
</tr>
<tr>
<td>Mexico</td>
<td>0.4</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>0.04</td>
</tr>
</tbody>
</table>

Source: Author’s calculations based on de Cordoba and Vanzetti (2005).

a coefficient of 22. The United Nations Conference on Trade and Development (UNCTAD) predicts that the losses in tariff revenue for developing countries would be approximately $63.4 billion. If all tariffs were eliminated under full liberalization, the losses would be $135.5 billion.

If such a scenario was accepted, the Swiss formula approach would have made tariff sequencing more difficult because higher tariffs would be cut deeper than lower tariffs. In a recent paper, Yılmaz Akyüz (2005) describes how many nations sequence tariffs for technological development.

Tariffs are introduced once a particular line of industry is entered, and kept at their initial (maximum) levels for a certain period before being brought down at a constant rate as the industry matures. For the reasons already noted, technology-intensive industries have higher initial levels of protection and support than resource-based and labour-intensive manufacturing. As technological capacities are built successfully, subsequent shifts to more advanced sectors become relatively easier than the earlier move from labour-intensive to technology-intensive activities. (Akyüz, 2005: 26)

Binding at a line-by-line basis and reducing tariffs under a Swiss formula would make such sequencing much more difficult because nations would not be able to maintain relatively low average tariffs while having high tariffs in some lines and zero tariffs in others. Some developing nations, such as Brazil, India, Pakistan, and others, have proposed NAMA reductions using a Swiss formula that sets a coefficient equivalent to the nation’s average tariff. Brazil currently has an average tariff of 30 percent, India 19 percent, and Pakistan 11 percent (de Cordoba and Vanzetti, 2005). That
would make numerous formulae possible, and allow nations to vary more – but very high tariffs would be difficult to maintain by the nature of the formula. Finally, the economic costs of lost tariff revenue, as shown earlier in the paper, could be quite significant. There have not been proposals to change the safeguard mechanisms under the current round.

More than developed countries, the developing world relies on tariff revenue for a large share of government revenue and expenditure. Slashing tariffs may not only restrict the ability of developing countries to foster new industries so they may integrate into the world economy, it could also prohibit them from obtaining funds to conduct industrial policy and to maintain social programs for the poor. Least developing countries rely on tariffs for more than one quarter of their tax revenue. For smaller nations with little diversification in their economies, tariff revenues provide the core of government budgets. In the Dominican Republic, Guinea, Madagascar, Sierra Leone, Swaziland, and Uganda tariff revenues are more than 40 percent of all tax revenue in their countries (South Centre, 2004).

*Services.* The proposal regarding services that was tabled in 2006 was that developing nations liberalize significantly more services sectors, especially financial services in places like Brazil and India. Developing nations were not necessarily opposed to this, indeed Brazil and India indicated as much in Hong Kong. However, developing countries argued for an emergency safeguard mechanism that was rejected by developed countries.

Developing nations proposed that an emergency safeguard mechanism (ESM) be inserted into GATS, but developed nations have had a lukewarm response to such proposals. Developed countries have been reluctant to liberalize along mode 4 (movement of natural persons). Free trade in labor markets is estimated to bring large gains to the developing world, as we will see in the next part. Instead, developed nations, led by the European Union (EU), proposed that developing nations quantify the number of service sectors they have and commit to liberalizing a minimum level of sectors – 50 percent of all sectors (developed countries would reduce 80 percent of their sectors). In the mode 3 negotiations (for foreign investment in services), the EU is pushing for 51 percent foreign equity holdings in domestic service sectors.

*Subsidies and countervailing measures (SCM).* Although not a major piece of the negotiations, some policy space was up for grabs under the SCM. As mentioned earlier the SCM allows for some subsidies that correct for market failures. These non-actionable subsidies are arguably more justified in economic terms because they can be used in second best settings to correct distortions in domestic and international markets (Hoekman and Kostecki, 2001). The door to deploying such subsidies may be closing in the current negotiations.
There are numerous examples of nations that have been using this policy space, yet the full potential of the Article 8 provisions are yet to be realized. However, ability to use such subsidies was “sunseted” and set to expire in 2000. Negotiating reinstatement is part of the DDR but little progress has been made (Aguayo and Gallagher, 2005).

3.2. The political economy of the DDR

Part 1 has shown that developing countries stood to give up relatively less in terms of policy space under the final proposals tables under the DDR. It should be underscored that relatively little space would have become constrained. Indeed, Part 1 outlined how NAMA and services proposals would have further constrained development sovereignty. Relative to the considerable number and significance of the instruments traded away during the UR, and the fact that developing countries were able to reject proposals on deepening investment and IPR rules in addition to new negotiations on competition policy, just deepening NAMA and services were major losses in policy space. Nevertheless, they are sometimes considered the final nails in the coffin and are therefore seen as being of a very high magnitude.

This part of the analysis asks the question: if developing countries did not stand to lose much in terms of policy space, why then were they not willing to exchange it for the cuts in agricultural tariffs and subsidies offered by developed countries? Here I show that the reason at least in part lies in the fact that the economic benefits of agricultural tariff and subsidies cuts by developed countries were strikingly small – nowhere near the size of the benefits during the UR. Such small benefits did provide the means for a bargain across the developed and developing world. Second, the relatively small losses in policy space under the DDR are seen to be cumulatively large by the developing world.

Projections of the economic benefits of the DDR were not considerably large. The World Bank estimated the potential welfare gains at just $287 billion in the year 2015. However, these estimates are for a scenario of ‘full’ global trade liberalization. In other words, the models assume that all tariffs and non-tariff trade barriers are completely eliminated in the world economy. Such a scenario was highly unlikely in the DDR from the beginning. To be more attune to the possibilities in the DDR negotiations, the World Bank conducted projections for a ‘likely Doha scenario’ of partial liberalization. The ‘likely’ scenario according to these models is for agricultural tariff rate reductions in developed countries of 45, 70, and 75 percent within three bands of existing tariffs, and reductions in developing countries of 35, 40, 50, and 60 percent within four bands of tariffs; the least developed countries are not required to make any reductions in agricultural tariffs. For non-agricultural tariff bindings the scenario calls for 50 percent cuts in developed countries, 33 percent in developing countries, and zero in the
least developed countries. This scenario is approximately what was on the
table in Hong Kong, but more ambitious than what was on offer in the
summer of 2006 (Anderson et al., 2005a).

The ‘likely’ Doha benefits are exhibited in Table 5. Under this scenario,
where the gains accrue in 2015, global gains are just $96 billion, with only
$16 billion going to the entire developing world. The developing coun-
try benefits are 0.16 percent of GDP. In per capita terms that amounts to
$3.13, or less than a penny per day per capita for those living in develop-
ing countries. Although the lion’s share of attention in these negotiations
has been focused on agriculture, developing country gains from ‘likely’
agricultural reforms amount to less than 0.1 percent of GDP, just $9 billion.
Likely gains from Northern subsidy reduction are projected at barely $1
billion (Anderson et al., 2005a).

Of the benefits that will flow to developing countries, only a few coun-
tries will receive those benefits. The majority of all the benefits to develop-
ing countries (just $22 billion) are expected to flow to just eight countries:
Argentina, Brazil (which stands to receive 23 percent of the developing
country benefit), China, India, Mexico, Thailand, Turkey and Vietnam.

Another major area of negotiation in the Doha Round was services ne-
gotiations. Services trade has been growing faster than goods trade since
the 1980s. Developed countries pushed for developing countries to open
up their services markets – especially in the financial and telecommunications
sectors – in exchange for market access in agriculture. The World Bank
also put together models for services trade benefits but ended up deeming
them too ‘highly speculative’ to publish in their Doha Round publications.
Services trade itself is very hard to quantify, and since ‘tariffs’ in the sector
don’t exist they need to be extrapolated for modeling purposes (Hertel and
Keeney, 2005: 17–18).

Like the estimates in goods trade, services trade liberalization was ex-
pected to yield relatively small benefits where the majority of those bene-
fits go to developed countries. Under a full liberalization scenario the total
benefit for the world would be $53 billion. Only 34 percent of those bene-
fits would go to the developing world, amounting to a one time increase
of 0.31 percent of GDP, or a penny per day per capita. The authors’ likely

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**Table 5** Benefits of ‘likely’ Doha Round scenario

<table>
<thead>
<tr>
<th>Beneficiary region</th>
<th>High income</th>
<th>Developing</th>
<th>World</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total amounts, billions of dollars</td>
<td>80</td>
<td>16</td>
<td>96</td>
</tr>
<tr>
<td>Per capita, dollars per person</td>
<td>79.04</td>
<td>3.13</td>
<td>15.67</td>
</tr>
<tr>
<td>Percentage of GDP</td>
<td>0.24</td>
<td>0.16</td>
<td>0.23</td>
</tr>
</tbody>
</table>

Source: Ackerman (2005); Anderson et al. (2005a).
scenario of partial liberalization (50 percent reduction in services trade barriers) would yield only $6.9 billion for the developing world, or 29 percent of the total and amount to significantly less than a penny per day for one year. In both scenarios, India, South Africa, and China were set to receive more than half the total benefits for developing countries (Francois et al., 2003).

Adding goods and services trade liberalization together the total benefits for developing countries amount to $123.5 billion under full liberalization (1.1 percent of GDP) and $28.7 billion for a likely deal. A likely deal would bring a one time combined increase in the level of global GDP of 0.28 percent in 2015.

The World Bank created extensions to their models in order to estimate the extent to which the current round will lift many of the world’s poor over global poverty lines. As are the welfare gains, the poverty projections are now smaller. The World Bank estimates that 66 million people would be lifted from poverty under the complete liberalization scenario. The ‘likely Doha scenario’ brings the number to 6.2 million people at the two dollar per day poverty line, 2.5 million people at the one dollar per day level of extreme poverty (out of approximately 3 billion and 1.2 billion total poor, respectively) (Anderson et al., 2005b).

It now becomes more clear why developing countries were less apt to accept the deal that was on the table – it would have been too politically hard to bring home. The benefits would have been small (and negative for some countries), tariff losses would have been high in terms of NAMA, and developing countries were not able to obtain an ESM in services, nor liberalization in the movement of persons (the measure that would have brought the highest level of benefit).

Table 6 presents the likely DDR benefits with the projections of the NAMA tariff revenue losses.

Though not discussed above, the World Bank estimates find that regions such as the Middle East and North Africa, and countries such as Mexico and Bangladesh would be worse off (this has been confirmed by all the major estimates on the DDR; see Bouet, 2006). Though in aggregate developing countries would have been better off by approximately $16 billion.

The tariff losses for NAMA would be four times the benefit. Of course, in formal economic terms it is looking at apples and oranges to compare revenue and welfare. For negotiators, who are representatives of governments, apples and oranges are both fruits. A government negotiator will be interested in whether they will be better off, and by what magnitude. They will also be interested in what losses in revenue will occur (if for no better reason than to understand that new revenue is needed through new tax policy). It should come as no surprise that nations that stood to gain very little (or actually lost) and stood to lose a great deal
in tariff revenue would begin to get skeptical. Add that to the fact that
domestic producers at home who would then have to compete with new
imports would be pressuring them and negotiators would have to come
up with many more benefits to make everyone better off.

Developing countries did indeed have a proposal that would have
yielded many more benefits – for developed and developing countries
alike. Developing countries proposed liberalizing employment services
under the General Agreement in Trade and Services (GATS). This meant
allowing for more visas for professional employees (such as software en-
geers from India) and temporary visas for low-skilled workers (such as
apple pickers from Mexico). Studies have shown that the potential benefits
of such liberalization could range between $150 billion and $300 billion on
an annual basis, depending upon whether temporary work from develop-
ing countries amounted to 3 or 5 percent of industrial country workforces,
respectively (Winters et al., 2004). Another study that looked at the possi-
bility of a 3 percent quota estimated that annual gains could be $200 billion
annually (Rodrik, 2005). The same study stresses the fact that such gains –
which dwarf both the ‘likely’ and full liberalization scenarios – go directly
to those individuals in the developing world who need the funds the most
because much of the gains are transferred through remittances.

4. CONCLUSION

In summary, this paper has two principal findings. First, that the DDR deal
that has had various versions since the Hong Kong Ministerial (after taking
into account the rejection of Singapore Issues in Cancun, and in juxtapo-
sition with the UR) would not have significantly constrained further the
development sovereignty of poorer nations. However, it is also argued that developing nations did not have the will to exchange such policy space for market access in the DDR (as they had in the UR) because the potential gains of the market access deal on the table were relatively small and the cumulative costs in terms of losses of policy space in the UR and the DDR combined were relatively large.

Table 1 shows that many options for policy space still remain under the WTO. Investing in human capital, providing marketing support to firms, supplying public infrastructure are all key elements of late industrialization that continue to steer clear of WTO rules. More specifically, what is clearly WTO legal at this writing is the ability to fund human capital and public infrastructure, offer tax concessions to foreign firms, and provide marketing services to domestic firms. Investment in human capital is indeed an essential component of growth trajectories, and infrastructure provision is also of utmost importance for the facilitation of domestic and foreign markets. Marketing service is also important. Indeed, markets fail at providing adequate amounts of human capital, public infrastructure, and information. Thus, all three of these options are economically justified areas for governments to intervene and are important areas of policy space for the development process. In addition to these measures, before the current round of negotiations began the WTO system provided policy space in the following areas by allowing nations to:

- use average tariffs to sequence certain industries into world markets;
- restrict the liberalization of certain service industries and ‘limit’ the liberalization of other industries to steer liberalization toward development;
- issue compulsory licenses under the TRIPs; and
- require foreign firms to transfer technology, form joint ventures and perform R&D in the host country.

The DDR proposals through September of 2007 could have put much of these openings in jeopardy, with little benefits in return.

**NOTE**

1 The author would like to thank Robert Wade, Kenneth Shadlen, Yilmaz Akyuz, and the anonymous reviewers for useful comments on this paper.

**REFERENCES**


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