

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT



## **G-24 Discussion Paper Series**

# **The Potential Impact of the Aid for Trade Initiative**

**Sheila Page**

*No. 45, April 2007*



UNITED NATIONS



**UNITED NATIONS CONFERENCE  
ON TRADE AND DEVELOPMENT**

**INTERGOVERNMENTAL  
GROUP OF TWENTY-FOUR**

***G-24 Discussion Paper Series***

**Research papers for the Intergovernmental Group of Twenty-Four  
on International Monetary Affairs and Development**



**UNITED NATIONS**  
New York and Geneva, April 2007

## Note

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

\*

\*                      \*

The views expressed in this Series are those of the authors and do not necessarily reflect the views of the UNCTAD secretariat. The designations employed and the presentation of the material do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area, or of its authorities, or concerning the delimitation of its frontiers or boundaries.

\*

\*                      \*

Material in this publication may be freely quoted; acknowledgement, however, is requested (including reference to the document number). It would be appreciated if a copy of the publication containing the quotation were sent to the Publications Assistant, Division on Globalization and Development Strategies, UNCTAD, Palais des Nations, CH-1211 Geneva 10.

UNITED NATIONS PUBLICATION

---

UNCTAD/GDS/MDPB/G24/2007/3

---

Copyright © United Nations, 2007

All rights reserved

## **PREFACE**

The *G-24 Discussion Paper Series* is a collection of research papers prepared under the UNCTAD Project of Technical Support to the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development (G-24). The G-24 was established in 1971 with a view to increasing the analytical capacity and the negotiating strength of the developing countries in discussions and negotiations in the international financial institutions. The G-24 is the only formal developing-country grouping within the IMF and the World Bank. Its meetings are open to all developing countries.

The G-24 Project, which is administered by UNCTAD's Division on Globalization and Development Strategies, aims at enhancing the understanding of policy makers in developing countries of the complex issues in the international monetary and financial system, and at raising awareness outside developing countries of the need to introduce a development dimension into the discussion of international financial and institutional reform.

The research papers are discussed among experts and policy makers at the meetings of the G-24 Technical Group, and provide inputs to the meetings of the G-24 Ministers and Deputies in their preparations for negotiations and discussions in the framework of the IMF's International Monetary and Financial Committee (formerly Interim Committee) and the Joint IMF/IBRD Development Committee, as well as in other forums.

The Project of Technical Support to the G-24 receives generous financial support from the International Development Research Centre of Canada and contributions from the countries participating in the meetings of the G-24.



# **THE POTENTIAL IMPACT OF THE AID FOR TRADE INITIATIVE**

**Sheila Page**

*Senior Research Associate  
Overseas Development Institute, London*

**G-24 Discussion Paper No. 45**

April 2007





## *Abstract*

*The Aid for Trade initiative was revolutionary in the acceptance by international consensus of a role for the World Trade Organization (WTO) in aid and of the limitations of trade. The general case for aid for trade is that while trade can be a tool for development, countries need infrastructure, institutions, technical capacity, investment, etc., in order to trade, and in particular to respond to new liberalization under the WTO. The case for WTO-related Aid for Trade (AfT) is that although many in developing countries will gain from a WTO settlement, there are costs to some developing countries and some have little to gain from multilateral trade liberalization. The first responses proposed to the WTO dilemma were trade measures, more or better preferences. But this would not work for countries with exports that are either highly dependent on preferences or whose other exports are already relatively free from barriers. And preferences were increasingly being challenged by the non-preferred countries and by those who feared that they obstruct multilateral liberalization.*

*Aid for Trade emerged as an issue within the Doha Round, first driven by the need to find benefits for all countries in the negotiation, and thus “as a complement, not a substitute” for the Round. By the time the Round stalled, it had acquired sufficient support from the aid community as well as the trade community to go forward independently of the Round. When it was part of the negotiations, there was pressure to define a new structure for trade aid, outside normal aid mechanisms and parallel to those for other international concerns such as health or the environment. Without the need to secure developing countries’ support for a trade settlement, however, there is now a risk that it will be absorbed into normal country aid programmes, and be governed by the wishes of the international financial institutions*

*There may be an increase in aid for improving the trading and productive capacities of developing countries. But there will be no way to ensure that the direction of that aid will be determined by the priorities of the international trading system. The WTO and its members retain the potential to influence the allocation of funds through monitoring, analysis, and debate. But the leadership has now shifted to the World Bank and the International Monetary Fund. To ensure that the implementation of Aid for Trade reflects the decisions that they have made in the WTO, therefore countries must act there to require that these institutions now act coherently to accept a priority for trade that has been determined by another international institution, the WTO. This may require greater voice for developing countries.*



## *Table of contents*

	<i>Page</i>
<i>Preface</i> .....	<i>iii</i>
<i>Abstract</i> .....	<i>vii</i>
<i>Abbreviations</i> .....	<i>xi</i>
<b>1. Aid and trade</b> .....	<b>1</b>
<b>2. The analytic rationale behind proposals for using aid to support trade</b> .....	<b>2</b>
2.1 Trade is an important activity in developing countries .....	2
2.2 Trade is essential to development .....	2
2.3 Trade and poverty .....	4
2.4 Future trends mean countries will need more aid in order to trade .....	5
2.5 Aid is needed to ensure that all groups and all countries gain from trade .....	6
2.6 Practical arguments in the current context .....	7
2.7 What is not in the rationale for Aid for Trade .....	7
<b>3. Evolution of support for Aid for Trade in the WTO negotiations</b> .....	<b>7</b>
3.1 Background to the presence of aid as an issue in the Doha Round .....	7
3.2 How Aid for Trade emerged in the Doha Round .....	8
3.3 The Aid for Trade Task Force .....	15
3.4 Aid for Trade separates from the Doha Round .....	17
3.5 What Aid for Trade is needed and what the Task Force proposed .....	18
<b>4. Financial issues</b> .....	<b>20</b>
4.1 Predictability .....	20
4.2 Grants or loans .....	20
4.3 Conflicting approaches to conditionality and to country-based priorities .....	21
4.4 How much Aid for Trade is needed? .....	23
4.5 Pledges for Aid for Trade .....	24
4.6 Allocating Aid for Trade: criteria, constraints, and eligibility .....	27
4.7 High aid makes trading harder (Dutch Disease) .....	28
<b>5. Suggestions for the architecture of Aid for Trade</b> .....	<b>29</b>
<b>6. The future for Aid for Trade</b> .....	<b>32</b>
<i>Notes</i> .....	<i>34</i>
<i>References</i> .....	<i>35</i>



## *Abbreviations*

AfT	Aid for Trade
ACP	African, Caribbean and Pacific Group of States
AGOA	African Growth and Opportunity Act
EBA	Everything But Arms (access to EU for LDCs)
EC	European Commission
EPA	Economic Partnership Agreement (between EU and ACP regions)
EU	European Union
G20	Group of Twenty
GATT	General Agreement on Tariffs and Trade
GTAP	Global Trade Analysis Project
HIPC	Heavily Indebted Poor Country
ICTSD	International Centre for Trade and Sustainable Development
IF	Integrated Framework
IMF	International Monetary Fund
ITC	International Trade Centre
LDC	Least Developed Country
MFN	Most-Favoured Nation
NFIDC	Net Food Importing Developing Countries
ODA	Overseas Development Assistance
OECD	Organisation for Economic Co-operation and Development
OECD-DAC	OECD-Development Co-operation Directorate
PRSP	Poverty Reduction Strategy Paper
SPS	Agreement on Sanitary and Phytosanitary Measures (WTO)
SVE	Small and Vulnerable Economy
SWAp	Sector Wide Approach
TBT	Agreement on Technical Barriers to Trade (WTO)
TIM	Trade Integration Mechanism (IMF facility)
TPR	Trade Policy Review
TRIPS	Trade-Related Aspects of Intellectual Property Rights (WTO)
TRTA	Trade-Related Technical Assistance
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNIDO	United Nations Industrial Development Organization
UR	Uruguay Round
WTO	World Trade Organization



# THE POTENTIAL IMPACT OF THE AID FOR TRADE INITIATIVE\*

Sheila Page

## 1. Aid and trade

The Mandate for Aid for Trade derives from the WTO Hong Kong Ministerial Declaration on Aid for Trade, paragraph 57 (WTO, 2005a):

We welcome the discussions of Finance and Development Ministers in various fora, including the Development Committee of the World Bank and IMF, that have taken place this year on expanding Aid for Trade. Aid for Trade should aim to help developing countries, particularly LDCs, to build the supply-side capacity and trade-related infrastructure that they need to assist them to implement and benefit from WTO Agreements and more broadly to expand their trade. Aid for Trade cannot be a substitute for the development benefits that will result from a successful conclusion to the DDA, particularly on market access. However, it can be a valuable complement to the DDA. We invite the Director-General to create a task force that shall provide recommendations on how to operationalize Aid for Trade. The Task Force will provide recommendations to the General Council by July 2006 on how Aid for Trade might contribute most effectively to the

development dimension of the DDA. We also invite the Director-General to consult with Members as well as with the IMF and World Bank, relevant international organizations and the regional development banks with a view to reporting to the General Council on appropriate mechanisms to secure additional financial resources for Aid for Trade, where appropriate through grants and concessional loans.

This was revolutionary in the acceptance by a consensus including all developed and most developing countries of any role for the World Trade Organization (WTO) in aid and of the limitations of trade measures alone. It rejects exaggerated claims that trade can only have benefits.

At its September 2006 meeting, the Group of Twenty-Four welcomed “recent proposals regarding the ‘aid for trade’ agenda” (Group of Twenty-Four, 2006). This paper will discuss how the initiative arose, in the two contexts of development policy and international negotiations, explore the decisions that now need to be taken, and ask if it will mark a significant change in the aid or trade regimes.

---

\* This work was carried out under the UNCTAD Project of Technical Assistance to the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development with the aid of a grant from the International Development Research Centre of Canada.

There have been two strands of discussion of Aid for Trade (AfT), helping countries to increase their productive and trading capacity and helping countries meet the costs of WTO-related changes. The arguments for them are different; the costs are very different in magnitude; and one is much more closely related to the WTO.

The arguments for the first type of AfT are that countries need infrastructure, institutions, technical capacity, investment, etc., in order to trade, in general and in the specific case of new liberalization under the WTO. In the past, which countries should be eligible and for how much have been settled by aid, not trade, criteria. What is new and controversial is how far the WTO should have a role in this type of aid. One role which it has already had is in shifting aid agencies' attention back to trade.

The case for WTO-related AfT is that there are additional costs from a WTO settlement (implementation, preference erosion, food prices ...). Many countries provide adjustment assistance internally; transferring money to countries which lose is in principle the same, especially if it is a transfer from the "rich" to the "poor". Alternatively, there is the external economy argument, for example, for regional aid, building a road across a coastal country for the benefit of a landlocked country; spending money in a preference-losing country to permit greater trade liberalization may benefit a non-preferred country.

The potential for aid and trade to work together to help developing countries might seem obvious, but there has been a history of mistrust and apparent conflict between them (Page, 2006). Aid agencies in developed countries and finance ministries in developing are normally entirely separate from trade ministries, so that there is rarely an institutional spur to consider the possibility of using trade measures. On the trade side, although there has been much study of how trade can contribute to development, this has come mainly from the schools of economics that mistrust government planning and intervention. These economists have not had an interest in looking at how aid decisions are made and how aid is allocated. The new interest on both sides, therefore, seems to offer the potential for increasing the effectiveness of both trade and aid policy through greater coordination, although the discussion of AfT has shown that the division remains wide.

## 2. The analytic rationale behind proposals for using aid to support trade

### 2.1 Trade is an important activity in developing countries

Developing countries have particular difficulties in trading. Exporters face all the difficulties inherent to a developing country, of poor infrastructure, thin product chains, lack of familiarity with standards or ability to meet them, and weak public and private institutions, but, unlike suppliers to the home market, they must compete with exporters in developed countries without these disadvantages. They are more likely to need to change to new products and markets (this is the essence of development). They need to increase their exports exceptionally rapidly in order to be able to import the physical and technological inputs they need to develop.

### 2.2 Trade is essential to development

Trade was first considered a central element in countries' development strategies in the 1950s and 1960s. It owed its new significance partly to the experience of the developed countries in the 1930s, when restrictions on trade had had serious effects on many, partly to the experience of countries which had seen their economies transformed during World War II by changes in trade patterns, and partly to new ways of analysing the choices facing developing countries. In the 1950s and early 1960s, there were no examples of countries that were still clearly "developing", but competing against "industrial countries" through producing competitive exports in some industries. Therefore, it seemed that the only strategy open to them was to continue to specialise in primary products for export, but concentrate on increasing production of other goods for home consumption. In terms of trade policy, this meant a concentration on policies to control imports.

Then came the first generation of successful Asian economies. They showed that it was not necessary for a country to develop an integrated national industry before competing with developing countries in manufactures. They showed that developing countries *could* export manufactures, and that this



was closely *associated with* very rapid growth and structural change. So the obvious, if not the logical, conclusion was that exports *led* to development. There remained disagreement about whether an initial period of import substitution was necessary as a preparation, but agreement that export opportunities are sooner or later essential. The important change in what could be identified as conventional views was from emphasis on the efficiency role of trade to a view that there were dynamic effects.

*Conventional theory.* In traditional terms, opening trade should raise a country's income (welfare) by permitting it to change the composition of its output to a more efficient structure, that is, permitting it to specialize according to comparative advantage. Even if the principal effect of trade is merely the comparative static one, to increase income and average productivity through reallocation of resources, this could lead to prolonged growth as a result of a sequence of one-off changes because of the great number of new possible markets and types of production, and in some countries, of high barriers and substantial potential for structural change. This could be sufficient to justify concluding that helping developing countries to trade more effectively would be a useful tool for development.

There is also a straightforward demand argument. If there is unemployed capacity, but there are administrative reasons or foreign exchange constraints that mean that there are no ways of increasing domestic sources of demand, then raising exports will be the only way to stimulate growth.

*Export-led growth.* But much of the literature on the role of the external sector moved beyond these efficiency effects (e.g. Krueger, 1983). The apparent association between high and rapidly growing exports and rapid growth of manufacturing and of total output suggested that a policy of opening an economy to external influences (liberalization) or perhaps even a policy of deliberately biasing growth towards exports (export promotion) could improve investment and growth, and raise efficiency not only from reallocation of resources and increases in aggregate demand, but by increasing the dynamic efficiency of the economy. The strong argument is that exposure to competition, from imports and in export markets, increases the efficiency of firms, not simply by providing information or access to technology (these can be done without trade), but because

the threat of losing markets (and profits) is more of an incentive to change than the potential to increase them. This represents a particular view about the nature of incentives (that sticks are more effective than carrots) which is not adopted in other economic theory. It was this type of analysis, often associated with the World Bank (see section 3.1) which strongly influenced the view that increasing the opportunities for developing countries to export (through the Doha Round) could have a significant effect on their development. But, unlike the other reasons for expecting exports to help growth, this theory is not entirely consistent with a view that offering increased international demand (a carrot) will promote development.

Even if we accept that there is substantial evidence of an association between successful exporters and successful development, the implications of such arguments for aid are not clear. The very market-orientated arguments for how trade works do not suggest a direct role for aid, but they may reinforce the traditional argument for aid to create the conditions to trade. Such aid could make a country better able to respond to opportunities.

As well as supporting aid to help trade, the arguments for trade's role in development have in the past been used to justify direct intervention in trade to help developing countries.

*Special and differential trade policies.* The earliest measures encouraged an import substitution strategy, while the offer of special access provided some encouragement to exports. From 1947, Article XVIII of the General Agreement on Tariffs and Trade (GATT) allowed developing members to protect imports and use domestic policy to develop particular sectors. Countries could also continue to offer special access to colonies or other associated countries. The provisions were reinforced and consolidated by the adoption of Part IV in 1966 (GATT, 1994).

The export side was strengthened from the 1970s, as exports became more central to thinking on development. In 1971 GATT authorised preferences as an exception to MFN treatment through a waiver. The access arrangements were implemented by individual developed countries, not by any general reduction in the tariffs notified to the WTO. In 1979, following the Tokyo Round, the Enabling Clause (GATT, 1979) was adopted to allow not only

preferences for developing countries, including further flexibility in the application of rules, but additional special treatment for Least Developed Countries (LDCs) (the first differentiation among developing countries), and this remains the basic WTO statement of principles for SDT.

The Uruguay Round (UR), in contrast, attempted to move toward ending all permanent differentiation: agriculture and textiles were brought under normal rules; all countries had to sign all agreements; as in the Kennedy Round, there were formula tariff reductions, a de facto shift away from the differentiation allowed by sectoral negotiations. The differentiation still allowed in agriculture, through a combination of average and minimum cuts, applied to all Members. The remaining differences allowed for developing countries were partial or delayed compliance. The “declaration” on food importing countries did imply structural differentiation, but it was not accompanied by any provision for implementation. The Uruguay Round did not, however, formally change GATT Part IV or the Enabling Clause; these continue to allow (and advocate) special treatment, and were reinforced by the Decision of December 1993 in favour of LDCs, which encouraged more rapid implementation of tariff cuts on products of interest to LDCs.

*Do preferences help?* The vast literature on this can be summarised as “sometimes”. Some countries that have had preferences increased trade particularly rapidly and especially in the preferred sectors. Some countries have used preferences and the associated economic rents from one product to develop through diversification into another. Such countries, and some analysts, attribute their success to the preferences. Some countries with preferences have failed to benefit because they were not in the right commodities (they faced protection for agriculture and clothing) or because they received preferences at the wrong time (countries with severe structural problems and supply constraints cannot use additional access). Preferences always offer countries’ principal objective in traditional trade negotiation terms: access to markets on more favourable terms than other suppliers.

There are systemic arguments against them. Countries with preferences may attempt to preserve these by obstructing liberalization. For most countries, dependent on preferences for some exports, but on the general trade regime for others, this is

unlikely to happen. But a few are so dependent on preferences that they do have an interest in preserving the current system.

There are reasons why preferences may be of more limited usefulness than in the past, especially for the Least Developed Countries which are now the ones at which preferences are being most targeted. The more multilateral barriers are reduced, the less valuable are preferences. Rules of origin which require a high level of vertical integration of industry always create obstacles for small countries with limited industrial capacity, and rules in preference regimes are becoming more restrictive. Most current exports by LDCs to developed countries are primary commodities which would enter duty free or at low tariffs even if they were on Most-Favoured Nation (MFN) terms. Supply factors are an increasingly well-recognized barrier to using preferences, even in non-LDC countries. And LDCs are precisely the countries where the supply constraints on using preferences may be most serious.

Preferences affect other developing countries, which do not receive the same preferences. In many cases, developed countries have transferred the “cost” (in protectionist terms) of liberalizing their trade with the favoured developing countries to the less favoured by choosing those imports which compete with other developing countries, rather than those that compete with developed countries’ own production.

The benefits of preferences mean that countries will only accept change if they receive something in exchange. But the disadvantages, especially the risks to the system, suggest that the WTO needs to find alternative ways of helping developing countries to export, if trade is indeed a significant factor in development.

### 2.3 Trade and poverty

That trade reduces poverty was a popular theme during the 1990s emphasis on poverty reduction as the most important goal for development assistance, but the direct links are less important than the traditional path from trade through development to poverty. Trade theory argues that increasing the openness of an economy (if it is done in a non-distorted way) improves the return to those factors of production which are less scarce in the country

than in the world as a whole (their prices relative to other factors move closer to the ratios found in the rest of the world). For countries with scarce capital and abundant labour, the conventional model of a developing country, this is likely to mean an improvement in income distribution towards wages and towards the poor.

But this simple relation need not lead to the conclusion that trade is the best tool for reducing poverty (Bird, 2004; Conway, 2004). First, the economic relationship will have a different result in countries where natural resources, whether agricultural, mineral or (for tourism) scenic are the principal advantage. There, trade may shift the distribution towards returns to holders of resources, and thus to profits and rents. Even if there is an increase in the share of labour income, this may not have a direct effect on the least skilled and poorest. If trade reduces the cost of imports, some consumers will gain, and some of these may be poor, but the size of the effect cannot be easily related to the change in trade. Growth in incomes definitely increases the potential to reduce poverty; it does not itself reduce poverty. Increased national income permits increased social spending, although if the increase in trade comes in part from lower taxes on trade, this can only be realised if the government successfully finds alternative sources of income.

There are also potential negative effects directly from trade to poverty, so the final effect depends on policy choices. The poverty literature views both shocks and structural changes less favourably than the growth literature, often appearing to put a higher weight on losses than on gains in analysing the net effects of a policy. It also puts more weight on the short-term effects and on direct effects. This substantially reduces the expected benefits from trade. The poverty argument for trade must therefore be mainly based on the development one that trade increases income. Complementary policies to do with aspects other than trade (e.g. transport infrastructure, education or safety nets) may be critical in maximising the benefits and minimising the losses that the poor experience from trade liberalization.

As long as the poverty and Millennium Development Goal (MDG) focus continues, advocates of the potential benefits of coherence between aid and trade policy must accept that some will argue that it is trade policy which should be subordinated to aid policy and its poverty reducing objectives. Those

who argue that aid should be designed to assist trade objectives need to face this. To the extent that trade itself contributes to development, the link from development to poverty is an argument. But trade is not the only way to promote development so in aid terms a policy of deliberately targeting aid at a trade need could not be justified without weighing the importance of trade against the other priorities of the country (or the donors). There are possible reasons to justify this, outside aid priorities, as is discussed below in considering the aspects of trade which can be considered public goods.

The same type of argument holds in reverse. Any deliberate targeting of gains from trade at aid objectives must be judged against all the objectives of trade. The international trade regime is intended to increase world income and to promote sustainable development, but it is also intended to give to both developing and developed countries the benefits of a consistent and predictable environment in which to trade and make investment plans.

There are choices of priorities to be made, and the questions are what should guide these choices, and who should make them.

#### ***2.4 Future trends mean countries will need more aid in order to trade***

An argument against applying past evidence on the benefits of trade to countries which are now starting their development is that they are different in their potential for trade: a much higher proportion of those which remain poor are land-locked, and therefore facing much higher costs of trading. They have mainly similarly poor neighbours, and thus lack easy markets. They are small, with low-skilled labour, so lack both natural resources and labour as an advantage in entering developed country markets. High costs and low returns might suggest that such countries would be expected to trade less, for a given resource endowment or level of development, than the countries observed in the past. But they may also be less suited to the alternative, import substituting, mode of development, because their small size limits the size of the market. Aid, rather than trade, might help them to find new development strategies.

In the last forty years, developing countries have greatly increased their shares of world output

and of world trade. From about 20 per cent in the 1970s, their share in trade rose to 25 per cent in the early 1980s. After a slow rise in the 1990s (with the decline in commodity prices), it reached a third by 2005. But the actual change in the structure of the world economy was even greater, because these data include at each point in time only those countries which were then defined as “developing”. Some, for example Spain and Portugal, became “developed” during the period, so that the performance of the remaining developing countries is even more impressive. As a result, most countries, developed as well as developing, now have a high share of their trade with countries which are currently “developing countries”.

The World Bank has recently published (World Bank, 2006) its projections for the next twenty-five years. In its interpretation of them, it asserts that “Developing countries, once considered the periphery of the global economy, will become main drivers.” It claims that their share of trade will rise to almost 45 per cent (World Bank, 2006: x), while their share of global output will rise to a third. But this interpretation relies on defining “developing countries in 2030” as those countries which were “developing” in 2006. This is misleading. As the Bank report notes, by 2030 incomes in what it calls the developing countries will average (using constant prices) \$11,000, “roughly the level of the Czech Republic and the Slovak Republic today”, while “countries as diverse as China, Mexico, and Turkey would have average living standards roughly comparable to Spain today” (World Bank, 2006: x). But countries which are at or above that level in 2030 will, like “Spain today”, not be developing countries, either in the economic sense in which we use the words today or in their own perceptions. As the report notes elsewhere, what we are seeing is a shift to a world dominated by a “global middle class”. It is therefore possible to take a diametrically opposite interpretation, that we are moving from a world where developing countries (in the normal sense of the word) are a significant force to one where most of the larger countries (led by China) will have moved above the line. There will remain a small and declining share of increasingly marginalised countries. They will be mainly in Africa.

In the last twenty years, while developing countries as a group increased their share of world trade, this was based principally on rises for Asia, but also included Latin America. These more than offset falls

for Africa and the Middle East. In the 1980s, the share of Africa and of low income countries in world trade declined. By 1998, the share of Africa in world exports was 2 per cent, having fallen from 2.7 per cent in the late 1980s and 4.4 per cent in 1983. In the next twenty-five years, the pattern will continue, as East Asian average incomes as a share of high income countries’ average income double to 35 per cent. Latin American incomes still hover around 27–28 per cent, but African income is expected to fall slightly from its current 5 per cent. “Africa, now home to one-third of the poorest people, is likely to see its share of the lowest tenth double by 2030” (World Bank, 2006: xiii).

The international trading system will need to adjust to a world in which trade is once again mainly among developed countries (now including China), while most African and a few other countries see both their income and their importance in the international economy fall further behind. There are clear risks to those left behind: their power to demand assistance, whether financial or in favourable policies, will be eroded. There are also political risks to a world economy with such marginalized members, as there are in nation states which have a class of the permanently poor. And there are implications for trade institutions. In these, as in markets, developing countries have become strong, and therefore have been able to promote their interests increasingly effectively in recent years. The changes in preferences and regions are in part the result of this change in power. The nature of decision making in the WTO has adapted to the presence of a large number of developing countries with a stake in the system and participating actively. A change back in the balance may provide comfort for the developed countries, although this, of course, will be a different group with new members. But there is an increased risk that some will be left behind.

## *2.5 Aid is needed to ensure that all groups and all countries gain from trade*

The arguments that are used for aid for trade are all based on a view that trade is basically beneficial to developing countries. But some accept, to varying degrees, that it may have costs, to some groups or to some countries, temporary or permanent. The benefits will outweigh these costs (for example, the costs to those within a country who

may lose because of new competition from imports will be less than the gains to others from increased income or the costs to some countries of preference erosion will be less than the gains from liberalization for the non-preferred). But aid to the losers, particularly if it is used to help them adapt to be able to benefit from trade, is desirable to ensure that there are not serious costs to poor people or poor countries in promoting a generally beneficial policy. A more general argument is that aid may be needed to help countries to have the potential to benefit from trade, to improve their ability to supply goods or services that match the opportunities to trade.

## 2.6 Practical arguments in the current context

To these developmental arguments were added two practical ones. There have been large recent increases in aid, and promises of much greater increases. Spending more on existing programmes may be difficult, and there is the financial problem that large inflows of foreign currency drive up the exchange rate (new aid is like a commodity price boom). Programmes offering specific stimulus to trade help to solve these aid problems. And second, as long as there seemed a chance that the Doha Round would succeed, it was necessary to find something to offer those countries who feared that they would lose from proposed liberalization.

## 2.7 What is not in the rationale for Aid for Trade

There is no place in the standard Aid for Trade literature or in the current implementation of the WTO proposals for arguing that aid is needed because trade liberalization is happening outside developing countries' control and is imposing (net) costs on them, i.e. that trade is to be considered a cost to avoid. Such a belief would, obviously, not be consistent with offering aid to help countries trade more effectively, and is not consistent with the national policies of most developing countries now, as they have lowered their tariffs and barriers to services trade much more than required by WTO agreements. Developing countries still have substantial "space" within WTO rules to use trade or domestic policy for development (Page, 2007). Other types of agreement,

notably bilateral or regional arrangements, have imposed more constraints on countries, but aid for trade in the multilateral context is not designed to meet problems caused by other agreements.

## 3. Evolution of support for Aid for Trade in the WTO negotiations

### 3.1 Background to the presence of aid as an issue in the Doha Round

*Problems from the Uruguay Round.* Most analyses of "the results of the Uruguay Round" had ignored the existence of preferences in calculating the potential export gains for developing countries (e.g. during the Round: GATT, 1993; after it: Martin and Winters, 1996), and the most commonly used general equilibrium model for calculating the effects of changes in trade policy did not include these until 2003. Some unofficial analyses of the Uruguay Round (Page and Davenport, 1994) had found negative effects for Least Developed and other preference-receiving countries, in both agriculture and textiles and clothing. In the late 1990s the very limited results of the Uruguay Round became recognized. Countries feared that the gains in the Doha Round might also be small. Countries like Bangladesh, Mauritius, and Sri Lanka were beginning to express concern that the end of controls on textiles and clothing exports by developing countries (at the end of 2004) would damage them because they had replaced some of the quota-constrained countries. As the Doha Round began, there was little expectation that these countries would have major gains on services, and areas like trade facilitation and public health were likely to offer small effects.

There was another "hangover" from the Uruguay Round. The extension of international rules to new areas like intellectual property and the tightening of rules on areas like customs administration led to complaints that these had high costs of compliance for developing countries, and therefore that they needed assistance in order to avoid being disadvantaged. Some observers took the position that the new agreements were of no benefit to developing countries, and therefore that all costs incurred should be considered as "excessive", but even an alternative position, that the benefits were less for them, would lead to a belief that aid was needed to meet the ex-

cess costs. The two fears, of limited benefits and potential costs, led many developing countries to declare that a Round had little to offer them.

*Newly powerful developing countries.* Preferences depended on acceptance that trade rules could be informal and that developed countries could decide whom to prefer. It was accepted that developed countries would offer better treatment to traditional trading partners or those that they wanted to assist. The lack of constraints on interventions in agriculture until the Uruguay Round had allowed arrangements like the sugar and banana regimes which gave preferred access and favourable prices to particular classes of countries for specific commodities. And even if any of these “special and differential” treatments had been considered contrary to GATT rules, the GATT dispute mechanism had no teeth: disputes could be dragged out and all countries (including the loser in a dispute) had to approve any action to implement a decision. The increasing power and skill of developing countries in trade negotiations has meant that this type of policy is no longer acceptable. The extension of preferences to more (in some cases all) products from Least Developed Countries helped to focus attention on the losses to countries which are not LDCs, while the increasing effectiveness of the WTO dispute mechanism has offered non-preferred countries ways of challenging preferences. It became clear that any trade concessions would have to be limited to the permitted categories: tariff reductions for recognized groups of countries (for developing or for LDCs). This is not a sufficiently flexible tool for aid.

*The move from poverty.* A final change that would contribute to acceptance of directing aid towards trade was the change starting in about 2005 away from the 1990s emphasis on poverty as the most important target of aid. The emphasis of the Millennium Development Goals, the official United Nations targets for aid, had been on social spending. In analytic terms, the focus had been on results (attaining the targets) not on means (what can promote sustainable development). There is now a return to looking at the means.

*In place of preferences.* As giving developing countries extra opportunities to trade has helped some of them to develop, it is not possible for the WTO (especially if it accepts a development obligation) simply to reject preferences as no longer useful and unfair without offering an alternative. The

obvious one is to provide finance to help countries to achieve the necessary developmental pre-conditions for trading. Finance also is an alternative to exports in directly alleviating the external constraint on development. Helping developing countries through aid rather than other trade concessions was a major new initiative for the WTO, and one that could seem inconsistent both with its role as a trade agency and with other funding by developed countries, through their aid programmes and the international financial institutions. As the Doha Round evolved, however, AfT was suggested because the other proposals for dealing with the problem seemed more unsatisfactory and more difficult. Suggesting that countries find other ways to increase their exports, perhaps through alternative preferences, would not work for countries with exports that are either highly dependent on preferences or whose other exports are relatively free from barriers, and would perpetuate the problems for the system and for countries outside preference schemes.

### 3.2 *How Aid for Trade emerged in the Doha Round*

*Recognizing the problem.* There was no mention of Aid for Trade in the Doha Declaration. Like many settlements coming out of the Uruguay Round, it mentioned the need for technical assistance for countries to comply with new rules, and stated that “technical cooperation and capacity building are core elements of the development dimension of the multilateral trading system” (WTO, 2001), but only committed to maintaining the existing value of WTO technical assistance, along with supporting coordination with other donors. There was no suggestion that this should be a negotiating condition of the Round. The commitments to Least Developed in the Doha Declaration concentrate on market access (paragraph 42) and technical assistance, and there was no recognition of the problems that market access for others could cause.

It did not envisage any losses from trade liberalization, so did not consider whether such losses might need compensation. Indeed, the concept of a “development round” was based on the explicit belief by many commentators that liberalizing trade would provide significant benefits for all developing countries and an assumption that it could not be harmful.

This was perhaps the final appearance of the view that trade was the most important input into development so countries needed “trade not aid”. This slogan was based not only on attributing the success of the East Asian countries entirely to trade, but also on an assumption that aid could not be increased and a comparison of the magnitudes of trade and aid flows. Aid flows had been falling in the 1990s, and were expected to continue to do so, whether from aid fatigue or for more specific reasons such as the end of the Cold War. Therefore trade was the only tool available for helping developing countries. Aid flows, however, are now rising.

It is important to note that from the point of view of a developing country the comparison of benefits should not be between the value of an increase in aid and the value of the alternative trade flow because aid is a straight transfer of resources while exports by the developing country use both national and imported inputs, and unless all these were unemployed and unemployable there is a cost. This reduces the net value to national income of exports to a (possibly small) fraction of the traded value.

Even if the net value of trade is correctly calculated, there are fundamental distributional differences. The developing countries which can increase their exports, and in particular those which are so competitive that they face barriers in the developed countries, are in general not the ones most dependent on aid. In developed countries, the distributional consequences might be better from a welfare point of view (ending protection hurts profits in dying industries, although it may also hurt labour; reducing aid spending would permit either higher domestic spending by the government or lower taxes, which might benefit all the population).

In developing countries, aid and trade encourage the growth of different sectors. Aid could be used to support the activities that are normally in the private sector, to establish market-oriented industries or services, directly or through subsidies, but this is now rare. It is likely to fund general government activities, health and education spending, transportation and communications infrastructure, sometimes energy or water infrastructure. It may provide social services, research or housing. In contrast, trade increases the demand for the production of goods and services normally found in the private sector.

As countries began to analyse their prospects in the Round and prepare their positions, it became

clear that the optimistic view that a successful liberalizing round would have major positive development effects was over-optimistic, and some began to fear that the effects might be negative. In July 2002 (WTO, 2002: 2), the LDCs suggested that:

... supply side constraints in developing countries and their need to retain the flexibility of being able to adopt pro-development policies and options should be addressed. This can be done in several ways, including: (i) exemptions from obligations for developing, particularly least-developed countries, if those obligations would constrain or prevent developing countries from adopting policies or measures required for their economic and social development, and (ii) obligations on the part of developed countries to assist developing countries to build their supply-side capacity to foster national production capacity as well as export supply capacity.

And there was a need (WTO, 2002: 3) to “Provide temporary financial compensation for fall in export earnings resulting from a reduction of MFN tariff rates in the case of products whose share in the total export earnings of an LDC exceeds 50 per cent”, the first explicit proposals on obligatory aid for costs and for preference erosion.

Then, in 2003, the IMF (IMF, 2003a) in an official submission to the WTO accepted the argument that preference erosion would have significant costs, and that:

In any assessment of the balance of payments need in the context of program discussions, Fund staff should take into account the potential losses from preference erosion as one of the elements that affect the external environment facing a country’s exports.

It explicitly criticized the methodology of previous studies, e.g. Ianchovichina et al. (2001), Hoekman et al. (2001), and even an UNCTAD study by Bora et al. (2002), which had looked at total LDCs or total African countries for effects of preference erosion, and found very small numbers. “The GTAP general equilibrium model on which these simulations are based is not able to estimate the impact on individual LDCs.” The studies “do not fully take into account the EBA and AGOA.”

The IMF found (IMF, 2003a: 12) that: “significant losses will be confined to a few countries. For

26 out of the 46 LDCs, export losses from preference erosion are estimated to be less than two per cent, and for another 15 countries less than five per cent. Thus, only five countries may face losses exceeding five per cent of exports. These are Malawi (11.5 per cent), Mauritania (8.8 per cent), Haiti (6.4 per cent), Cape Verde (6.3 per cent) and Sao Tome and Principe (5.2 per cent). In absolute value, the largest likely losers are Bangladesh (\$222 million), Cambodia (\$54 million), Malawi (\$49 million), Mauritania (\$40.4 million) and Tanzania (\$29 million).” The IMF paper was the first by an international institution to do the calculations on a country basis.

At the same time, a study for the African Union (ILEAP, 2003) found similar results, using a slightly different methodology. It had been commissioned to find what benefits African countries could expect from increased access for agricultural products under the current proposals in the Doha Round, reflecting the expectations at the time. It first found that most African agricultural exports did not pay MFN rates, so that there would be virtually no gains, and then suggested that preference erosion would be a major problem, and found that Malawi (at 17 per cent of exports), followed by Uganda and the United Republic of Tanzania would be the major losers on its assumptions about liberalization. It was probably these two studies (which were communicated to the African group, and to Malawi in particular, during the summer of 2003, before the Cancún Ministerial Conference) which helped to convince a large number of LDCs and African countries that they had little to gain and (for some) much to lose in the Doha negotiations unless they received financial compensation.

The ILEAP study concluded that the main potential gains for African countries could come from pressing for substantial reduction in subsidies to agriculture in the developed countries as these were depressing prices. This had also been noticed by the cotton producing countries of West Africa. Also in 2003, four West African countries, Benin, Burkina Faso, Chad and Mali cited the cost to them of subsidies, notably by the United States, and placed this as a separate item on the agenda for Cancún. Cotton is between 5 and 10 per cent of their GDP, and more than 60 per cent of exports (Goreux, 2003). They requested, in addition to any changes in subsidies in the Doha context (which could not take effect until at least 2005) not only an interim reduction in subsi-

dies starting in 2004, but, until 2006, compensation for Least Developed cotton producers based on the estimated losses suffered (about \$250 million in direct costs and four times that for indirect, WTO, 2003c; 2003b). This would be paid by the countries subsidising their cotton. The proposal was targeted principally at the United States, whose subsidies are quantitatively the most important, although the European Union (EU) and China also have subsidies which may be damaging to some exporters.

One main group of beneficiaries from preferences, those who had sugar quotas at two to three times the market price for their exports to the EU and the United States, had also recognized the problem by 2003, with a paper to the WTO from Mauritius (Mauritius, 2003).

One problem with these calculations, and those that followed, e.g. by the IMF for the middle income countries (Alexandraki and Lanke, 2004), the WTO (Low et al., 2005; 2006), World Bank (Nielson, 2006), and UNCTAD (2005), is that there is no generally accepted way of calculating the gains from preferences (and hence the losses from erosion), partly because of lack of consensus on the purpose of preferences. They may provide increased volume of exports, a production effect accompanied by an income effect; new opportunities for a particular type of exports (e.g. new manufactures), an industrial structure effect; improved terms of trade, an income effect. Only the income effects are amenable to direct calculation of values. But the limitations caused by this should not be exaggerated. All trade negotiation calculations depend on challengeable assumptions. Most of the calculations have identified roughly the same major losers and the same commodities where changes in tariffs were most likely to cause losses.<sup>1</sup>

*Identifying solutions.* From the beginning there were two approaches to dealing with this problem, to create some mechanism to deliver aid within the WTO or to leave it to the normal processes of aid. Broadly speaking, those from the trade community favoured the first, while those from donors, including the World Bank and the IMF, favoured the second, or simply assumed that this was the only possibility, as there is no existing mechanism within the WTO.

Losses as a result of trade policy change have always been recognized as suitable for compensa-



tory action in the WTO. When a regional trade area is formed, for example, non-member countries which lose market access can ask for compensatory tariff reductions in other areas. Similarly, if countries win a dispute, and the “offending” country does not change its policy, they can take trade measures against it. There is, however, no WTO provision for monetary compensation. But for preference erosion, it became clear that trade compensation was not possible.<sup>2</sup>

Financial compensation has been proposed in the disputes procedures, where there are no obvious retaliatory actions to take (or where the country entitled to them does not want to damage its own welfare by restricting imports). It was implied in the agreement in the Uruguay Round that Net Food Importing Developing Countries (NFIDC), who were expected to be hurt by a rise in food prices as a consequence of the agricultural reforms, should get special consideration. Some expected the international financial institutions to offer adjustment assistance. In practice, no action has been taken on this, by either the WTO or financial and donor institutions, principally because of the lack of clear allocation of responsibility for taking any action, but also because it has not been clear that the reforms had clear consequences for prices.

The normal WTO negotiation answer to meet the consequences of preference erosion would be to expect the countries requesting a reduction in tariffs, in this case principally the non-preferred developing countries, such as Brazil and the Group of Twenty (G20), along with some efficient developed country producers, like Australia and the Cairns Group, to make an offer that will secure agreement. They could either offer to fund adjustment in the losers themselves or demand that the developed countries, which created the problem by combining high protection with deep preferences, compensate the losers. The evolution of Aft, as long as it was within the Doha Round, corresponded to the latter.<sup>3</sup>

The IMF (2003a: 14–15) instead attempted to analyse the question in terms of its principles for aid. This difference in approach between the aid approach, of assuming consensus on criteria and goals, and the trade approach, of negotiating to find a balance between different interests, has remained a fundamental stumbling block in all the discussions of Aid for Trade. Should the distribution of compensation follow development criteria or be related

to the size of any trade costs? There is also the question of how to offset private losses (to export revenue) by means of transfers to governments, without raising the same issues which are being contested in the context of the allocation of anti-dumping duties in the United States.

The IMF concluded:

... it could be argued that preference erosion represents an adverse exogenous shock similar to those arising from reductions in prices of commodities ... But there are at least three differences with commodity shocks that are germane to the design of any financing arrangement. First, shocks from preference erosion are likely to be permanent ... Second, shocks from preference erosion can be anticipated ex ante. Third, they are likely to be spread out over time because of the phased nature of MFN tariff reductions.

The first distinguishing feature – the permanent nature of the shock – suggests that adjustment needs to be an integral part of any response, including financing, to preference erosion. There would therefore be a presumption that any financing of losses from preference erosion should be within the context of adjustment facilities and program financing by the international financial institutions, which ensures that appropriate adjustment actions accompany any financing.

In the case of commodity price shocks, the point has been made that disbursement needs to be quick, rendering financing under a Fund arrangement, which can typically be time-consuming, unwieldy and inappropriate. The second and third distinguishing features – the predictability and the gradual nature of the shock – make this critique less valid. Because preference erosion can be anticipated well in advance and the actual loss from it is spread out, a medium-term adjustment facility might well be the most appropriate way of combining the financing and adjustment. Since such facilities already exist, and given the limited nature of the likely losses, it would not seem necessary to create new financing facilities.

This is quoted at length because it remains the fundamental argument of those who favour using existing aid instruments. But the IMF itself, during 2003, increasingly realised that the existing facilities were not appropriate for the problem. Immediately before Cancún, the IMF and World Bank offered assistance to “developing countries with trade-related

adjustment needs in the Doha Round". A joint letter from the World Bank President and IMF Managing Director (IMF, 2003b) said that they "appreciate that adjusting to a more liberal trade environment may impose costs on some of our member countries – albeit temporarily – as a result of preference erosion, the loss of tariff revenue or other factors". They offered to help members "to assess the nature and magnitude of any adjustment need", to "assist in designing policies" to adjust, "to use and tailor our lending authority to respond to the specific challenges posed by the Doha Development Agenda", and "to provide support in mobilizing donor resources". At Cancún the IMF (Krueger, 2003) offered "a new trade initiative ... specifically tailored to address temporary external imbalances that might result from the multilateral trade reforms." It held discussions with the countries it had identified as potentially most seriously affected. In 2004, it extended its initial analysis of LDCs to Middle Income countries (Alexandraki and Lanke, 2004), and created the promised new facility, the Trade Integration Mechanism (TIM) (IMF, 2004) for balance of payments problems arising from trade liberalization. It has been used by three countries.

In contrast, the World Bank has always been more sceptical about whether the problem existed, and about whether special measures were needed. It (World Bank, 2003) emphasized that most poor in developing countries were not in the preference dependent countries or LDCs, so that measures to help these did not meet the major needs (World Bank, 2003: 306). It thought that preference erosion could be largely compensated by expansion in other exports,<sup>4</sup> and judged that trade facilitation and more liberal rules of origin would "attenuate the impact" (World Bank, 2003: 218). It noted the problems of food importers if food prices rise (World Bank, 2003: xvii), but again expected other improvements to balance this.

Following the increasing IMF interest during mid-2003 and the suggestion in the United States/EU/Canada position paper on non-agricultural market access (WTO, 2003d) that these major countries supported action "to address adjustment needs of Members whose exports are significantly affected by erosion of preferences", there was a temporary reversal of the World Bank position when it joined the IMF offer of support pre-Cancún. The World Bank (Zhang, 2003), however, presented its proposals more as an extension of existing programmes, for example on trade logistics, than a new facility.

The WTO, in comments by the then Director General Supachai, additionally raised the issue of those who would need to adjust to the end of the Multi-Fibre Arrangement.

The cotton producers had suggested one mechanism to give a formal link between the costs imposed by cotton subsidies and a source of funds. It was not immediately clear, however, how this could be extended to the other "losers" in the negotiations, even if the principle of allowing a financial arrangement in a trade agreement could be accepted. For the cotton case, those subsidising are clearly taking measures that would not normally be considered legitimate interferences with trade, and they are high income developed countries, so direct compensation seemed possible. But in the case of normal trade liberalization, many of the gainers are developing countries with large numbers of poor people, and are not responsible for the damage to the losers.

It is the previous system of high trade barriers and preferences, set up by the developed countries, which is responsible for the vulnerability to loss. Transfers from the developed countries would be appropriate to prevent reductions in income, to meet the long term developmental objective of helping the losers increase their exports without dependence on preferences, and to provide a substitute for the preferences which have been presented as forms of assistance to developing countries.

Various groups considered possible solutions before Cancún. Most position papers suggested other types of trade access or postponing or avoiding the liberalization that might cause the problems. The second draft proposals on agricultural access, for example, suggested maintaining "to the maximum extent technically feasible" nominal margins of tariff preferences (WTO, 2003a). As the impracticality (and injustice) of these proposals were recognized, after June 2003, some groups moved into asking for compensation payments as well. The Least Developed (WTO, 2003e) suggested "the establishment of compensatory or other appropriate mechanisms, including measures that promote exports of LDCs", and the ACP (WTO, 2003f) repeated this, and also asked that "Technical and financial assistance should be provided [*sic*: it did not attempt to say by whom or how] to ACP States for improving infrastructure, productivity and diversification, and for development of facilities and systems to achieve compliance with ... SPS and TBT requirements".

Following the collapse at Cancún, which was attributed in part to the fears by some developing countries that they would lose from the proposals then on the table and the concerns by a great many more countries that they had little to gain, there was more pressure on both developed and developing countries to find new solutions.

On one point, the cost of implementing new WTO rules, there was clear progress in 2004. Developing countries had requested a binding commitment to provide additional funding required to meet rule changes. This was not accepted, but the July 2004 framework for WTO negotiations (WTO, 2004) moved in that direction. In the one new area included, Trade Facilitation, there was, as well as clauses like the much-criticized “best endeavours” commitments on technical assistance in the Uruguay Round Agreement, in addition for the first time in a WTO agreement an acceptance that “in cases where required support and assistance for such infrastructure is not forthcoming, and where a developing or least-developed Member continues to lack the necessary capacity, implementation will not be required.”

In the United Kingdom, the International Development Committee of the House of Commons (IDC) recognized “moral, historical, and legal responsibilities” of the EU to the African, Caribbean and Pacific (ACP) countries that have received preferences or benefited from subsidies, and drew the analogy of compensation for expansion of the EU (IDC, 2003: 36). In 2004, a study was commissioned for the Swedish Government to find new forms of special and differential treatment that could offer developing countries real gains in trade (Kleen and Page, 2005). It concluded that:

... some countries will have a measurable negative outcome from any significant liberalisation of trade because their losses from preference erosion will be greater than their gains from other parts of the agreements, so that only financial assistance can give them a positive outcome. Compensating them through a fund, rather than other trade concessions would be a major new initiative for the WTO, and one that could seem inconsistent both with its role as a trade agency and with other funding by developed countries, through their aid programmes and the international financial institutions. The reason for suggesting it is that the other proposals for dealing with the problem of preference erosion are more unsatisfactory

and more difficult. (Kleen and Page, 2005: 100–101)

In particular, it noted that :

Asking aid donors to treat it as a special aid problem is unlikely to work well because aid agencies have other priorities (in some cases, formally established).

Also in 2004, the Government of the United Kingdom commissioned studies to estimate the costs to sugar and banana exporters of changes in the preference regimes for these (Gillson et al., 2004), which helped to motivate action by the European Commission (EC). Its Action Plan (EC, 2005) would be widely seen as a possible precedent for AfT in the WTO. In January 2005, the EU recognized the principle that countries which had benefited from preferential trade because of EU policies on sugar should be “supported” to adjust to changes in these. In presenting its Action Plan, it noted that “Several ACP economies are significantly dependent on sugar exports to the EU”. They have made investments and development plans based on expectations about these. It suggested combining “trade and development measures” to meet the “challenges”. In proposing that the assistance be used to improve the competitiveness of countries’ sugar sectors, to promote diversification away from sugar, and to assist adjustment more generally, it directly substituted development assistance for preferences.

From the end of 2004 to the first half of 2005, a group of experts chaired by Ernesto Zedillo examined what developing countries could gain from the Round, and concluded that Aid for Trade was an essential part of a package to rescue the Round and ensure that developing countries gained (Zedillo, 2005): “A significant increase in ‘aid for trade’ – that is, development assistance dedicated to increasing the recipient country’s capacity for trade – would help to ensure that more countries benefit from trade opportunities, including those that derive from unilateral reforms.” It also argued for “Adopting an approach to negotiations that helps governments of developing countries to put in place the policies and undertake the investments they need to benefit from implementation of WTO rules.” It suggested that two essential conditions for substantial liberalization were internal mechanisms to compensate losers and “In the case of losses from the erosion of trade preferences, preference-granting countries should take bilateral actions to offset these losses.”

It explicitly rejected the alternative approach, of finding new preferences: "Seeking to address preference erosion concerns *within* the trade negotiating agenda is likely to be counterproductive." The consultations leading to this paper had involved unofficial representatives of the World Bank and the IMF, of some major EU donors, and of African negotiators, as well as academic experts. It helped to define the terms in which AfT would be discussed in the WTO's Task Force in the first half of 2006.

The WTO research department had also started to calculate the costs of preference erosion (Low et al., 2005; 2006).

At the April 2005 meetings of the IMF and the World Bank (World Bank and IMF, 2005a), these organizations were instructed to consult with others on AfT before the September 2005 meetings. They asked two ambassadors to the WTO, from Sweden and Rwanda, to consult the ambassadors there on "the need for aid for trade". Ambassadors Mia Horn af Rantzien (who had organized a meeting on the report to the Swedish Government on special and differential treatment and who would later chair the WTO Task Force on Aid for Trade) and Valentine Rugwabiza (who would, as Deputy Director General of the WTO, lead the drafting process to put AfT on the Hong Kong agenda) attempted to identify areas of consensus on possible solutions. They identified "three pillars" for Aid for Trade (World Bank and IMF, 2005b):

- (i) enhancing the in-country trade development agenda (in broadest sense) via the Integrated Framework (IF) approach;
- (ii) creating a multilateral fund with the aim of providing more predictable and credible financing to respond to the prioritised trade-related needs assessment; and
- (iii) a separate "window" for specific adjustment issues affecting certain countries arising from MFN liberalization (notably on preference erosion, but also other issues could be considered, including loss of fiscal revenues).

Assistance under all pillars is envisaged as taking more the form of grants and other forms of assistance, as opposed to loans, over a 10 year period.

They saw the first pillar as an enhanced version of the Integrated Framework, and in an interesting precursor of the emphasis that the Task

Force would place on regional needs, quoted a programme by the Inter-American Development Bank (IADB) as a precedent. They saw a need for a new fund because: "the first pillar does not provide an assurance that ... [the] priorities [it identifies] will be met. Developing countries have frequently expressed concern that donor follow-up to the identified supply-side priorities has been insufficient."

The IMF and World Bank responded in September 2005. They accepted the need to help countries trade and the argument that promoting trade could be an international public good. They accepted the arguments for an enhanced Integrated Framework, but rejected the proposals for a separate fund and a separate window for adjustment. They argued that "full and faithful implementation" of the IF would make a new fund unnecessary with the possible exception of funding for regional needs. For these, it agreed to look at the possibility of a new fund. But they had "serious misgivings about the desirability and effectiveness of a separate fund to address adjustment, given the availability of existing mechanisms and the need to consider adjustment as part of an overall package of domestic policy reforms and economic planning." This effectively rejected both the criticisms by the Geneva based ambassadors (and others) that the "existing mechanisms" neglected trade and the argument that there was a need to provide designated trade funding in order to ensure that countries agreed to trade liberalization. By saying that any support for adjustment would follow "analyses of adjustment impact" by their staffs, and should not be directly tied to WTO shocks, but considered in the context of other policies, they rejected the arguments for predictability.

Following this, Zambia (the country which would lead the LDCs at the Hong Kong Ministerial Conference) denounced the World Bank and IMF reaction as "totally inadequate" and presented an LDC proposal on Aid for Trade (Patel, 2005). This accepted the three pillars of the Geneva proposal, and added a fourth: support to deal with debt. It accepted liberalization as an objective, but argued that improving supply capacity and finding alternative sources of revenue were essential prerequisites. It made detailed proposals on how to identify productive and infrastructure needs and the adjustment financing required.

In spite of the official views of the World Bank, its Geneva office organized in July 2005 a confer-

ence at which researchers and international organizations presented evidence on preference erosion (ODI database). In one of the papers a member of its research department, with an official of the United Kingdom, Department for International Development (Hoekman and Prowse, 2005: 8), reviewed the evidence on the likely risks of preference erosion, and concluded that “‘Less preferred’ countries are increasingly concerned about the discrimination they confront, while ‘more preferred’ developing countries worry that WTO-based liberalization of trade will erode the value of current preferential access regimes. This tension suggests there is a political economy case for preference-granting countries to explicitly address erosion fears. We argue that the appropriate instrument for this is development assistance. The alternative of addressing erosion concerns through the trading system will generate additional discrimination and trade distortions, rather than moving the WTO towards a more liberal, non-discriminatory regime.”

In Geneva, there was still support among negotiators (from developed and developing countries) for a separate fund for AfT, in spite of (virtually the same) countries’ formal acceptance of the World Bank and IMF rejection of it. In the final stages of preparation for the Hong Kong Ministerial, the WTO convened an informal group of ambassadors, under the former Rwanda ambassador, now Deputy DG, Rugwabiza, to consider what could be included in the Hong Kong deliberations on this.

A draft proposed before the Hong Kong Ministerial was considered in informal meetings at the Hong Kong Ministerial and amended to give a clear process: a Task Force to prepare a report to the General Council on “operationalizing” AfT and instructions to the Director General to identify what donors could do, before a discussion in the General Council. The concern of many countries that AfT might be considered a replacement for liberalization in the Doha Round led to the constant repetition of the phrase seen in the Horn of Rantzien, Rugwabiza report in 2005 (World Bank and IMF, 2005b): it is a complement to, not a substitute for, a successful round.

The World Bank continued to state its opposition to a special facility for trade at the Hong Kong Ministerial (WTO, 2005b). Once it became clear following the Hong Kong Ministerial that AfT would have an official existence, however, the Bank actively participated in discussions and clearly wanted

an implementing role similar to the one it has acquired in the Integrated Framework.<sup>5, 6</sup>

### 3.3 *The Aid for Trade Task Force*

*The work of the Task Force.* Following the Hong Kong conference, a Task Force<sup>7</sup> was appointed by the Director General. From a WTO governance point of view, it is interesting to note that the members were chosen to include the major countries, developed and developing, plus the chairs or representatives of the various informal groups of developing countries (Africa, LDCs, ACPs, Small and Vulnerable Economies). The risk of this system is that countries which are not members of prominent groups are neglected. Following protests in the General Council about the original proposed composition, two additional members were added, Colombia and Thailand, middle income countries which, although not normal aid recipients, might expect to be included in a trade-related facility. (Colombia had been a member of the pre-Hong Kong Ministerial drafting group; the current ambassador was also chair of the Trade Policy Review Mechanism committee.) Prior to the meetings of the Task Force, the WTO secretariat drafted a Concept Paper on Aid for Trade (WTO, 2006a), but the Task Force took the Hong Kong Ministerial paragraph as its Terms of Reference. The plan then was for the Director General to issue a report on his consultations with donors in May, for discussion in June, thus before the Task Force Report in July (WTO, 2006a).

The Task Force had to reach consensus among a range of different views. Developed countries do not agree on AfT. The EU has supported it in principle, expecting the IMF or World Bank to implement it. Within the EU, however, some development ministries tend to take the same position as the World Bank. There is support on the trade side, and its Action Plan for sugar has many of the elements now proposed for AfT, of allocation to countries according to adjustment need, and with the possibility of using the funds to provide support either for those incurring losses or for new products. Internally, the EU has accepted the need for “cohesion funds” and for transfers from those who gain from integration to those who lose, and it has schemes to compensate farmers both in the EU and in the ACP countries who will lose income because of changes in the sugar regime.

Those who believe that it is mainly the preferences offered by EU which are the problem do not see any obligation to share in any cost of compensating for these. The United States has been anxious to avoid any transfer of the costs of erosion of EU preferences to international funding. It has accepted a special responsibility for helping the cotton countries of West Africa.

The World Bank in its input into the Task Force (WTO, 2006d, the inputs to the Task Force; see also the summaries in WTO, 2006c; International Centre for Trade and Sustainable Development (ICTSD), 2006; and ODI, 2006) identified three areas where there was insufficient trade-related funding, on the IF, on regional and cross-country issues, and for assessing (*sic*: not for meeting) adjustment needs. But (WTO, 2006d: 5) it has an interesting comment on a need “to have a clear commitment from all donors to assist countries where the adjustment costs are deemed to be significant” so there does now seem to be support for including adjustment costs even from former opponents. It also noted that there was a problem for trade initiatives of “lack of ownership at the country level (by both donor agencies and country authorities)”.

One country, Mauritius, had already started negotiating with the World Bank for Aid for Trade funds in 2006. The Bank mentioned this as an example, but did not note that this illustrated a problem with its preference for “country-led” approaches: that funds may go preferentially to the countries that are most skilled at identifying their needs and packaging them to fit new aid programmes.

The IMF position was similar to that for the World Bank, with perhaps even less belief in a need to increase funding. Again, it thought that existing mechanisms were adequate.

In its submission (OECD, 2006) the Organisation for Economic Cooperation and Development (OECD) argued that AfT was already increasing (“The aid volume is not the issue”), and could be expected to continue to do. The problem is to make it more effective through local accountability, where “local” is taken to include donors. (It did not share the World Bank’s concerns about donors.) It has consistently argued that there are “compelling reasons to refrain from creating a new institutional mechanism for the financing and allocation of aid-for-trade” because this would “separate the trade-

related agenda from the broader economic growth agenda”.

Three of the contributions came from organizations for which trade is a central interest, and their expertise and experience were clear. The International Trade Centre (ITC) made a strong case that there was inadequate attention to trade because policy makers were not convinced of its importance, and in particular there was insufficient attention to “developing entrepreneurial activity and trade-enabling environments”. It had detailed suggestions for involving the private sector. The United Nations Industrial Development Organization (UNIDO) looked particularly at the need to work on standards and to work with the private sector, what it called “the technical infrastructure”. It provided lists of what countries need, in contrast to the approach that says that donors should wait for countries to identify their needs. It thought it more important to identify what could make developing country exports competitive than to do more calculations of preference erosion etc. The Inter-American Development Bank described its own experience of trade support, and argued that there has been neglect of supply side capacity. It set up a separate unit to deliver trade-related technical assistance and actively encouraged integrating trade into countries’ development programmes. It also argued that a lack of “grant funding for trade-related assistance to middle-income countries is a serious challenge”, and that what is available is not predictable because it is budgeted annually. It joined the others in citing the lack of regional finance, but also saw a lack of a “flexible ‘rapid response’ facility” (a problem first mentioned in IMF, 2003a), a contrast to the long-term programming suggested by the Bank and the Fund.

The other international organizations were less original, repeating the principles of aid or describing existing programmes.

The Small and Vulnerable Economies (SVE) (with a seat on the Task Force) stressed the general “trade challenges” that they face (high transport costs, high trade dependency, high infrastructure costs, etc.), rather than any specifically related to the WTO or the Doha Round. They also argued that AfT should be mainly through grants to avoid increasing debt. For administration, it wanted an extension of the IF process to other countries, and argued that “another added advantage is that the United Nations Development Programme (UNDP) is the Trustee of

IF funds, rather than one of the Bretton Woods financial institutions. This would avoid the introduction of those institutional conditionalities in this context.” This distrust of World Bank as the lead institution was not confined to the SVEs. The ACP also mentioned the need for grant support and cited the IF as a good model. The EC paper dealt specifically with how to involve the private sector in AfT.

Brazil (a member of the Task Force) stressed that resources should be additional and unconditional, to facilitate adjustment. It defined separate areas for coordination by the World Bank and the IMF, rather than seeing a single central role. AfT should not be “a bargaining tool”. Colombia, supported by Ecuador and Peru, like Brazil and the specialized agencies, supported a project-based approach. It particularly stressed that it should not be necessary to assess needs *ex ante* because these would depend on the course of the negotiations. This approach wants AfT to meet specific needs, rather than as part of a general development strategy. As such aid is likely to be a much smaller proportion of middle income countries’ budgets than in the countries where the Bank normally intervenes, it is important to be aware of this different approach.

Zambia, for the LDCs, again suggested Value Chain analysis as a tool for identifying needs and also of involving the private sector. This falls between the approach of AfT in the context of a full national development programme and the project-based approach.

*What the Task force recommended* (for full text see WTO, 2006e). The Task Force defined the scope of what could be funded under AfT as “activities ... identified as trade-related development priorities in the recipient country’s national development strategies.” It listed those that it thought would qualify, partly by reference to the OECD/WTO database on past trade-related aid which covers mainly training and institutional support, but it added infrastructure and more general spending on adjustment which could include creating productive capacity.

It did not recommend a new agency to administer AfT, but made clear its dissatisfaction with the existing mechanisms. It criticised donors for neglecting trade and failing to understand its needs, leading to inadequate support for infrastructure and meeting the costs of adjustment, and for inadequate attention to regional needs. Without formally pro-

posing new institutions (its rather odd phrasing was “A National Aid-for-Trade Committee could be established” and: “Explore the merits of establishing a Regional Aid-for-Trade Committee”), it did recommend better coordination mechanisms at country, regional, and multinational level. The principal role for the WTO would be to monitor the overall and country performance of other agencies.

It did not deal in detail with either the quantity or the nature of financing, as these were (under the Hong Kong mandate) the responsibility of the WTO Director General. The Recommendations of the Task Force state that they are dependent on the provision of “substantial additional targeted resources” (section C), but they do not set up a mechanism to secure this either in the immediate future or in the long run. There is no recommendation that donors should bind the funds that they have announced, even in terms of each agency rather than under WTO rules.

### 3.4 Aid for Trade separates from the Doha Round

The Hong Kong mandate implied a strong link between it and the Doha Round: it was to “contribute to the development dimension of the DDA” and be complementary to trade changes. But it also argued that AfT should aim to help developing countries “more broadly to expand their trade”, and in spite of the suspension of negotiations, WTO members have agreed that AfT should go ahead. By the time the Task Force reported in July, it was clear that negotiations might stall, so while it repeats the mantra that AfT should be complementary to the Round, not a substitute for it, it also stretched the ordinary meaning of words to produce a variant on this: “Aid for Trade is a complement to the Doha Round, but it is not conditional upon its success.” It urged that it begin “as soon as possible”.

In October 2006, the WTO General Council accepted the Task Force’s report, and endorsed the recommendations. At its December 2006 meeting, the WTO Director General emphasized the WTO’s role in “promoting coherence” (WTO, 2006g) through monitoring AfT. This would largely use the existing OECD/WTO data base, but the WTO could also use direct reports to the Committee on Trade and Development by development agencies and country-based monitoring. There is an intention to

include assessments of AfT for donors and recipients in Trade Policy Reviews and to hold an annual debate in the General Council starting autumn 2007, following up two of the Task Force recommendations, and to establish a committee of donor agencies.

In September 2006, the IMF and the World Bank agreed that there should be improved coordination of regional aid, but rejected any new institutions (World Bank and IMF, 2006).

### 3.5 *What Aid for Trade is needed and what the Task Force proposed*<sup>8</sup>

The Task Force tried to ensure that AfT met WTO-related and general needs. Funding countries to implement commitments made in the Doha Round had already been recognized as a potential cost of a Doha settlement in the July 2004 decision. And funds for implementation of the commitments in the Uruguay Round were a basic demand of developing countries. This includes commitments under the Marrakech Declaration for the costs imposed by agricultural liberalization on Net Food Importing Developing Countries. But any targeted assistance causes problems in normal aid terms. While implementing WTO agreements may benefit a country in the medium term, and it may benefit its trading partners, some of which will also be developing countries, it is not necessarily a country priority for a cash-constrained government; accepting the commitment is therefore a “cost” of entering the WTO agreement. It would be based on targeted project assistance, not be part of a country proposal. Helping countries to adjust to higher food prices could be close to aid objectives, if it is part of a development programme.

The costs of adjusting to preference erosion or to the fiscal costs of liberalizing a country’s own imports would raise serious problems for normal aid funding. The absence of a Doha agreement means, of course, that there will be lower costs than originally anticipated. But the fact the Round is stalled does not mean that there will be no erosion of preferences: some special schemes will be ended or reduced (sugar, bananas); unilateral and bilateral liberalization will reduce the value of preferences; existing preference schemes may be modified.

On the non-WTO-related needs, the developmental case is clear, so there is less need to modify

aid criteria: that countries need infrastructure, institutions, technical capacity, investment, etc., in order to trade, both in general and in the specific case of new liberalization under the WTO. Trade capacity building includes “mainstreaming” trade into Poverty Reduction Strategy Papers (PRSPs) (many of which had ignored trade, Gillson and Hewitt, 2003) and development plans, assistance in and training for trade negotiations, and other capacity building relevant to trade-related policies. There are different problems here. Within this, assistance to negotiate, which has been a very conspicuous part of trade-related aid, including under the IF, may be particularly difficult to incorporate into a WTO-related programme. Emphasizing the donor-recipient relationship can distort trade negotiations.

A second problem comes from the need to build up the capacity of governments to link domestic policy ministries and trade ministries (Vitalis, 2006). This approach sometimes leads to a government policy model that gives great weight to consultation networks with “civil society”, and less weight to constitutional representative bodies. While this is a potential problem in all types of aid, it may be particularly serious in trade because of the well-established risk that the benefits from trade are dispersed and the costs concentrated, so that vocal interest groups may not be representative.

Support for institutions that improve capacity to trade, not only at country, but at regional and/or other country group level (e.g. regional banks or The Advisory Centre on World Trade Law) is clearly aid-eligible as capacity building, but there have been problems in getting support for multi-country projects. If it is not directly tied to current negotiations, it is less likely to be subject to conflicts of interest.

Support for infrastructure and other measures to build countries’ ability to trade may be also being needed at regional as well as country level. There is a particular need for infrastructure based on regional needs because the country-based nature of most aid programmes makes it difficult to identify and fund cross-country projects. This can include regional facilities such as ports or bilateral arrangements such as a road from a land-locked country to a port. Again, there have been problems in adapting country-based aid programmes to regional needs.

Finally, there is a need for support for the supply side in the sense of building up private sector



enterprise in new export (or import replacing) areas. Arguably this is normal adjustment to changes in trade opportunities (or to current opportunities), so it does not necessarily require a special aid programme. It is difficult to reconcile aid to the private sector, which might involve picking some companies to benefit, with current fashions in aid or development theory which distrust “picking winners”, but the specialist agencies have experience in this.

AfT could cover any or all of these categories. But it is not appropriate to estimate the needs (or the supply of funds) by adding them together. The categories of adjustment costs from food prices, preference erosion, and fiscal losses identify needs for support, but they do not define what the funds would be used for. While a purely trade negotiation approach would imply offering countries cash payments to replace their gains from low food prices or preferences, the nature of aid relations and the delinking of AfT from the negotiations suggest that the payments will be conditional on their use for a need identified from the non-WTO-related list.

Another way of classifying the needs identified here is the range from low cost specific projects to major infrastructure investment. These are likely to require different types of organizations and programmes to meet them. Needs that are small and easily defined (for example: assessments of new circumstances or institutional reform to meet particular implementation needs, often to a deadline) require an organization able to offer quick disbursement, probably with a minimum of conditionality or planning. Others require longer term and more considered programmes, to ensure that building the supply capacity to trade is well integrated into a country’s (and perhaps a region’s) development programme.

The Task Force recommendations (WTO, 2006e) could be interpreted as covering all the needs identified here. It categorizes them, drawing on the OECD/WTO data base classification as (section D):

- Trade policy and regulations
- Trade development

- Trade-related infrastructure
- Building productive capacity
- Trade-related adjustment
- Other trade-related needs.

The “adjustment” category could include adjustment to preference erosion, higher food prices, and loss of tariff revenue as the objectives include helping countries to “adjust to trade reform and liberalization” (section F.1). There was no formal coordination between the work of the Task Force and negotiations on Agriculture or non-agricultural market access to allocate some or all responsibility for dealing with preference erosion or food costs to AfT.

The Task Force recommendations follow the Hong Kong Declaration in specifying that AfT is for “developing countries, particularly LDCs”. They do not suggest any categories other than this. They do not suggest any *a priori* allocation by country.

Their recommendations would be consistent with either a project-based or a programme allocation, but they show a preference for defining trade needs through a general country or country/donor planning process (section F.5.1). This contrasts with the emphasis on targeted, quick-disbursing funds in some vertical funds (see below) or in successful precedents for trade-related aid by the regional development banks. They emphasize the need for donors to reform their mechanisms to meet the demand for trade-related assistance more effectively.

The Task Force places particular emphasis on the need to consider regional needs, and thus directly meets one identified gap in current aid (sections F.3, F.5.2). It does not explicitly mention the problem that some of the needs closely related to WTO agreements (for example the costs of implementing trade facilitation requirements) or some adjustment costs might not fit the mandates of aid donors, because their immediate purpose is to meet international obligations, not to promote a country’s development in accordance with a nationally adopted plan. It deals with it by implication by providing for “clearing house functions” to meet unfunded needs.

## 4. Financial issues

### 4.1 Predictability

The Task Force stated that “Additional, predictable, sustainable and effective financing is fundamental for fulfilling the Aid-for-Trade mandate.” As long as there was a link to the negotiations, there was an argument that countries would need sufficient confidence in the aid pledges made in 2006 to sign up to any Doha agreement with the assurance that their costs and adjustment needs will be met. Therefore, there would have to be a formal agreement (in aid programmes, if not in the WTO) on the level and allocation of financing. This negotiating need, however, is no longer relevant and the fact that trade-related aid has increased in recent years, without a “Global Trade Fund” could suggest that donors now agree that there is a need to spend more on trade, and therefore that a specific “trade” fund is not needed. But the history of aid flows shifting from one priority to another suggests that those who support more AfT may justifiably feel a need to ensure that the increased shares to trade are sustained.

The history of disappointment in the implementation of “best endeavours” commitments in both trade and aid pledges means that the current generation of aid donors faces demands for stronger commitments because of the failures of the past. The fundamental argument for a multilateral trade system, that it provides certainty and predictability, suggests that assistance to help countries take advantage of it should also have those qualities. There is also increasing support in aid theory for providing predictable flows of funds, and the Initiative for Highly Indebted Poor Countries (HIPC) had some success in offering funds tied to broad areas, such as education and health.

The experience since the Uruguay Round also shows the need for formal commitments. While small costs, particularly those easily tied to a need for specific spending (customs rules, for example) did attract additional aid, those which require a macroeconomic approach both to calculate them and to find a way of meeting them (adjustment needs following on the terms of trade change in agriculture) were left to one side. Another reason for commitments to be important is the problem, discussed above, that some donors question whether implementation costs should receive aid money.

This means that there may be a need for new funds, with new criteria, either as designated parts of individual donors’ programmes (the EU Action Plan for Sugar, for example) or in a new multilateral form (HIPC, the vertical funds in health). Even if countries cannot require certainty through a WTO agreement, they can ask for it through aid mechanisms. The WTO arrangements as currently proposed (see section 4.5) do not provide this.

### 4.2 Grants or loans

Although any financing provided on the basis of the adjustment costs of trade liberalization might be used for purposes and in countries that would normally expect loan, not grant terms, the fact that countries need this additional finance for reasons of benefit to others and as a replacement for previous transfers suggests that there is a need for at least some of this to be on concessional terms. Countries which lose preferences need non-repayable support in order to be able to make the investments in physical and human infrastructure and in productive capacity to permit alternative production, adapted to the new trading conditions. The Trade Integration Mechanism of the IMF (IMF TIM) is not the answer to a permanent loss of income, and more debt is the last thing such countries need. Both equity (the countries themselves do not gain from the cost) and financial considerations (there is no identifiable return) suggest that the financing should be on grant terms for any developing country incurring significant costs. Hong Kong paragraph 57 suggests that AfT should be “where appropriate through grants or concessional loans”.

For other needs, whether loans or grants are appropriate should be decided in the context of normal aid criteria. It will depend on the income level of the country and on the use of the funds. For assistance to private sector production or infrastructure of a type which can recover its costs, there may be a clear source of returns to repay a loan. For assistance to government capacity to negotiate or to build new institutions, there can be expected to be a return to the country as a whole, but not an identified income stream.

Public goods arguments provide another reason for grants. They tend to be under-supplied if left to the market because some of the benefits cannot

be captured by the provider of the good. This problem can be met by rules requiring their provision, but, particularly in developing countries, there is likely to be a need for subsidy, and therefore for some financing not to be on fully commercial terms. Many trade needs for aid have at least some characteristics of public goods or goods with strong external effects. The generally recognized types of public goods are governance, knowledge, health, security and environment (te Velde and Morrissey, 2005). Broader definitions would include transportation and communication (at least in part), while some types of production have important external effects (the arguments for the effects of industrialization or clusters of activities, for example). Of the types of trade assistance identified as in need of aid, trade policy and regulations contribute to governance in both national and international trade rules, and research on these contributes to knowledge. Training in trade also contributes to knowledge, while infrastructure could contribute to the broadly defined public goods. Aid to help countries to adjust could, if it makes it easier to secure international agreements, contribute to any public good benefits from a more well-governed and more liberal international trading system. The World Bank and IMF have argued that “Overcoming coordination and capacity problems is not an agenda that lends itself to debt-finance” (World Bank and IMF, 2006), suggesting that grant finance may be a necessary pre-condition to developing the demands for specific projects, even if these are themselves suitable for loan-finance.<sup>9</sup>

Most aid for both the OECD/WTO database categories “Trade Policy and Regulation” and “Trade Development” has been channelled through grants over the period 2001–2004 (Cali et al., 2006). Around 92 per cent of \$3 billion spent on the former category and 85 per cent of \$6.9 billion spent on the latter category were channelled as grants by the donors. In contrast, most infrastructure has been in loans. For implementation needs, therefore, there seems to be evidence that donors are willing to treat this aid as meeting pure costs from which recipient countries do not gain, and from which they cannot make repayments. If the other types of adjustment costs were also treated as appropriate for grants, but if the spending of those adjustment funds was to be on adapting, rather than compensating (as defined above), it would be necessary to *increase the share of infrastructure funded by grants*. The share did increase in 2004 (although entirely because of the high share of spending in Iraq and Afghanistan) from

about 30 per cent in 2001–2003 to 49 per cent. If the other adjustment costs were about \$2 billion a year, about 40 per cent of the increase planned in Aft would need to be in grants.

### 4.3 *Conflicting approaches to conditionality and to country-based priorities*

The discussions of Aft have reflected broader conflicts in aid between targeting specific areas for help and taking a broad view of a country’s development process, and between donor or internationally determined priorities and country priorities. In 2005, aid donors signed up to principles on harmonization, alignment and ownership and these were cited in the Task Force recommendations (WTO, 2006e, section F.2) (OECD, 2005). They include:

- *Ownership*, to respect the right – and responsibility – of the partner country itself to establish its development agenda, setting out its own strategies for poverty reduction and growth.
- *Alignment*, align development assistance with the development priorities and results-oriented strategies set out by the partner country and to progressively depend on partner countries own systems.
- *Harmonisation*, to streamline and harmonise donor policies.

But if there are public good or externalities reasons for aid, neither donors nor recipients should have complete freedom to decide how aid funds are used, just as countries have chosen to give up some of their rights to determine their own trade policies in return for the benefits of an international system.<sup>10</sup> As well as being inconsistent with the principles of the multilateral trading system (or, indeed, any multilateral obligations), seeing aid only as a means of providing general support for all of a country’s needs, with choices made within this by the country (or donor) in response to its own identification of priorities, suitable for that country at a particular time, is directly in conflict with the premise behind both the donor commitments of increased trade related aid and the inclusion of paragraph 57 in the Hong Kong Declaration, that there has been insufficient aid for trade, not just because of general constraints, but because it has had too low a priority in donor

and country programmes. The existing vertical funds for environment, health, and other needs show that trade is not the only area where those outside the aid process have identified a need for more aid, and show both the advantages and the disadvantages of solving the problem by providing finance “tied” to a particular sector. There is increased knowledge; clear identification of needs; concentration of resources; but also distortion and negative effects on other programmes. There is now an additional problem: once some vertical funds exist, there is an argument that other general needs need their own vertical fund in order to avoid being “crowded out” by the subjects which have their own facilities.

The conflict may, however, be not between country-determined agendas and international priorities, but rather one between the priorities of the international aid community and those of other international interests, in trade, but also in health, the environment, and other areas. In practice, the degree of intervention by donors to assist countries to prepare their national assessments, to guide recipients in their choice of projects, and to limit recipients by specifying their own priorities and what they are willing to fund means that there is still donor intervention to influence the allocation of aid among sectors.

The Task Force report reflects the inconsistent trade and aid approaches. Its recommendations formally accept aid principles, and emphasize the need for a “country-driven” approach based on the Paris Principles. But the emphasis on ensuring that there are clear definitions of what is to be included under AfT and its provision for agencies to identify cross border needs suggest that it supports designating funds for trade needs. Its compromise is summarized in two apparently inconsistent recommendations (section F.4), that donors and agencies should:

- (i) move towards a programme/sector/budget approach, if country owned, if mainstreamed in national development strategies and if a robust system of financial accountability is in place;
- (ii) make targeted funds available for building infrastructure and removing supply-side constraints – over and above capacity building and technical assistance – perhaps as co-financing with multilateral development banks.

In particular, it does not resolve the problem of whether AfT should be offered to countries which

are identified as needing particular types of spending by some external process, rather than in national processes. In regional or multi-country programmes, action by one country may be needed to help another to trade. The importance given to regional needs, and in particular to the regional development banks, may imply a less country-programme based approach.<sup>11</sup> Both the Inter-American Development Bank and the Asian Development Bank (ADB) have experience in such lending, and have been less committed to the PRSP/country strategy approach. They and the International Trade Centre emphasized this type of assistance in their presentations to the Task Force.

There is a long tradition of international aid having a special responsibility for funding international public goods, both because they are not likely to attract sufficient private funding (for the reasons outlined above) and because of the role of international identification of needs and funding in areas such as the environment (the Global Environmental Fund is an interesting precedent). If there is international agreement (as demonstrated by WTO commitments) that countries and their economic actors should be able to participate on an equal basis in international trade, then funding the necessary pre-conditions should have a claim on aid funds and, equally important, countries should be expected to use available funds to make the necessary investments. This is, of course, a very different model from the wholly country-based one of the Paris Declaration, but it is one more consistent with the recognition (implicit in the founding of GATT and then the WTO) that countries cannot have complete freedom to follow any trade policies, regardless of the effects on other countries. The Zedillo (2005) report argued that multilateral liberalization itself was a public good, and therefore if dealing with preference erosion was a necessary condition for this, funding this could be considered support for international public goods. It considered this public good argument sufficiently important to give trade objectives priority over aid principles:

Experience demonstrates the need for a mechanism that provides dedicated funding to address the identified constraints on a nation’s trade competitiveness and to help offset the adjustment costs of reform. Although the earmarking of development assistance is generally not efficient, we support it in the case of the trade agenda on the basis of the global public good argument made earlier.

#### 4.4 How much Aid for Trade is needed?

It is necessary to look in detail at the WTO-related costs to determine if there are new needs. For other aid, it would be desirable to look at countries' own (or external) assessment of their needs to trade effectively. This type of evaluation could be similar in spirit to the diagnostic trade integration studies carried out under the Integrated Framework, but extended to identify additional priorities, from the point of view of the trading system and the trading needs of its developing country members. This could permit setting some minimum requirements under each type of assistance that is identified as appropriate, with priorities above this to be determined by other processes. Possible considerations might include identifying those areas where there is no or inadequate current funding, as the Task Force found for regions, those where the needs are largest, and those countries where the needs seemed greatest.

Given the lack of consensus on an appropriate methodology, this section does not attempt this; rather it estimates how much of past aid has been channelled to trade-related activities in order to provide a base against which to judge recent pledges (OECD/DAC Database). This is a substitute for the "baseline measurement" proposed by the WTO which has not yet been calculated. That will use 2002–2005 flows as a base (WTO, 2006f). (For further details on possible quantification, see WTO and OECD, 2005; Cali et al., 2006.)

*Estimating WTO-related costs.* The calculation is necessarily arbitrary, because of the assumptions that must be made, and because non-WTO changes, such as countries' internal reforms and new bilateral and regional arrangements will also be affecting costs of trade and the value of preferences. It is impossible to have a "right" number. What matters (as in other WTO rules) is to have an agreed calculation that gives a "good enough" number to separate countries into those which are significantly affected and others.

There are no good estimates of the additional costs imposed by Uruguay Round rule changes. An early, widely quoted, World Bank estimate (Finger and Schuler, 1999) that they would cost LDCs the equivalent of a year's development budget was based on assumptions, not evidence, as the most costly requirements, on Trade-Related Aspects of Intellectual Property Rights (WTO-TRIPS), are still not in

force. (They were originally to be required by 2006; this deadline has now been postponed to 2015.) One estimate for a non-LDC developing country, Jamaica (Hoekman et al., 2002) found that implementing the additional TRIPS rules would cost about \$6 million; implementing the Sanitary and Phytosanitary Measures, another \$6 million (mainly to establish an Agriculture Health and Food Safety Authority), and new rules on customs valuation, about \$1 million. In the same year, 2002, Jamaica received \$24 million in official assistance (OECD/DAC, 2004). The total cost is a significant additional burden in the short term, even if lower than the high estimates (see also Sweden National Board of Trade, 2004). These are once-off, not continuing, costs. Many countries which are members of regions may be already making reforms of this type, so the additional cost imposed by the WTO may be less than the full cost. If half these costs are taken to be directly attributable to the WTO and about 60 countries are affected, the total cost is about \$0.4 billion.

To calculate the costs of past agricultural liberalization to Net Food Importing Developing Countries (NFIDC), there a recent World Bank study (Mitchell and Hoppe, 2006). If there is no further liberalization, the cost could be \$0–0.3 billion. There are many estimates of preference erosion available, but if there is no settlement, only the planned changes in the banana and sugar regimes need to be included; these are about \$0.6 billion (Gillson et al., 2004). The cotton exporters estimated that the United States and EU subsidies cost them \$250 million in direct costs and \$1 billion in indirect costs (WTO, 2003c). These and the costs to NFIDCs are annual, so these estimates add up to \$2 billion annual costs to the perhaps \$0.5 billion in one-off costs (if we make some allowance for costs of implementation of any changes in rules in the Doha Round). Assumptions about the speed and skill of adjustment increase the uncertainty of estimates. The countries most seriously affected by implementation costs will be those who are furthest from the new standards and those least likely to have instituted reforms because of regional commitments.

These estimates do not include the fiscal costs of liberalizing a country's own imports because even if there is a Doha settlement, for LDCs the cost would definitely be 0 (as they are not expected to reduce their tariffs) and for most other developing countries, the cost will probably also be 0 (bound tariffs are sufficiently high that any reduction will merely

remove some water in the tariffs, not reduce revenue). For those which will need to reduce their applied rates, the cost to national income is still close to 0. There is a transfer from the government (reduction in import tax revenue) to those purchasing imports. To restore the previous position, the government would need to incur some administrative costs in finding alternative revenue, but it is wrong to count the revenue lost as a national cost.

*Estimates of past aid for general trade.* The OECD estimates (OECD, 2006) that in 2004 total AfT on the broadest definition was \$22.7 billion, of which \$2.5 billion was for technical assistance and capacity building, \$12.9 billion for infrastructure (or about \$9 billion if United States aid to Iraq and Afghanistan is excluded as a special case),<sup>12</sup> and \$7.3 billion for productive capacities. It estimates that this was about a quarter of total official development assistance excluding debt relief. Spending on Uruguay Round implementation costs has been around \$0.4 billion per annum, close to the estimates above.

The value of capacity building has fluctuated around \$0.2 billion, representing the category with the lowest AfT spending. This may be explained by the nature of training activities. Support for institutions that improve capacity to trade has been about \$1.1 billion a year.

Many donors (bilateral and multilateral) have announced their intention to increase aid for infrastructure. Support for building up private sector enterprise has also increased, from about \$0.5 billion in 2001 to \$0.9 billion in 2004.

All major donors have either maintained or increased their spending on trade related assistance over the period 2001–2004. The United States (because of spending in Iraq and Afghanistan) was the country with the highest contribution in AfT in 2004. (For a recent detailed analysis of the United States AfT see Langton, 2007.) Australia, Belgium, Denmark and France have also increased their spending. Japan was the largest donor over 2001–2004, mainly due to its large assistance in infrastructure investments. The EC is the largest donor in the categories more strictly related to trade (Trade Policy and Regulation and Trade Development), with a relatively lower spending on infrastructure (though the level of aid for infrastructure is still high) (te Velde et al., 2006).

An examination of aid by recipient (table 1) shows that the funds are fairly equally spread across regions, with Asian regions (Far East, South and Central Asia and Middle East) all receiving over \$3 billion in 2004, the same amount as sub-Saharan Africa. However the Far East has enjoyed stable inflows, while flows into sub-Saharan Africa have increased only recently. The largest recipient countries were all Asian: Viet Nam, India, Indonesia and China. The top sub-Saharan recipient, Ethiopia is in the 12<sup>th</sup> position, confirming a different (less trade related) model of development assistance for sub-Saharan Africa compared to Asia.

Low-middle income countries (LMIs) and non-LDCs low income countries (OLICs) have received the highest share of trade related funds over 2001–2004 (table 2). LDCs receive the lowest level of spending in trade-related assistance relative to total aid among the large aid recipients. There is only one LDC (Bangladesh) in the first ten recipients of past AfT. These figures are a cause for concern as LDCs and African countries are among those most likely to need support to trade.

#### 4.5 Pledges for Aid for Trade

In the second half of 2005, including at the Hong Kong Ministerial, and then again in 2006, “increases” in trade-related aid were announced by several donors. They do not seem represent an acceleration of recent spending on trade aid. The EU announced at the G8 Conference in 2005, repeated at the Hong Kong Ministerial and (Bounds, 2006) in 2006, a total of 2 billion euro, half from the Commission and half from national governments. This is restricted to trade policy and regulations and institutional support, not infrastructure. This appears to mean 1 billion euro a year from 2007 from the Commission and 1 billion euro a year from 2010 for members. (Within this, the United Kingdom has offered £100 million, about 150 million euro.) Japan offered at the Hong Kong Ministerial a total of \$10 billion, all to “trade, production, and distribution infrastructure” (WTO, 2005c), apparently over three years. The United States offered \$2.7 billion at the Hong Kong Ministerial, apparently for both trade policy and infrastructure (Wilska and von Bonsdorff, 2006). For all these it was not stated how much is additional.

Table 1

<b>AID FOR TRADE BY RECIPIENT COUNTRY/REGION AND YEAR</b>						
<i>(USD '000)</i>						
	<i>2001</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2001–2004</i>	<i>Rank<sup>a</sup></i>
<b>Total Aid for Trade</b>	<b>11,151,490</b>	<b>11,216,131</b>	<b>12,312,349</b>	<b>17,798,386</b>	<b>52,478,356</b>	
<i>1. Far East Asia</i>	<i>3,247,649</i>	<i>2,982,697</i>	<i>2,958,317</i>	<i>3,474,778</i>	<i>12,663,441</i>	
Viet Nam	716,339	992,886	767,227	1,066,953	3,543,405	1
Indonesia	464,332	123,506	1,143,825	1,242,666	2,974,329	3
China	1,005,238	655,597	606,128	382,171	2,649,134	4
Philippines	668,005	595,666	110,687	116,406	1,490,764	6
Thailand	47,018	393,344	18,791	427,664	886,817	11
<i>2. Sub-Saharan Africa</i>	<i>2,556,546</i>	<i>1,587,703</i>	<i>2,723,313</i>	<i>3,246,941</i>	<i>10,114,503</i>	
Ethiopia	179,886	247,894	197,040	234,745	859,565	12
United Rep. of Tanzania	392,666	34,741	47,909	356,105	831,421	13
Mozambique	278,741	98,145	218,876	170,992	766,754	15
Kenya	128,781	5,066	113,660	447,553	695,060	17
Ghana	275,816	56,870	193,050	104,017	629,753	18
Uganda	340,422	62,900	72,657	148,960	624,939	19
<i>3. South and Central Asia</i>	<i>1,330,671</i>	<i>2,123,079</i>	<i>2,406,415</i>	<i>3,108,523</i>	<i>8,968,688</i>	
India	319,768	710,666	801,953	1,353,725	3,186,112	2
Bangladesh	151,804	355,547	598,291	324,103	1,429,745	7
Afghanistan	378	40,424	271,584	771,716	1,084,102	-
Sri Lanka	288,434	429,116	220,819	107,642	1,046,011	9
<i>4. Europe</i>	<i>1,647,466</i>	<i>2,307,528</i>	<i>1,340,546</i>	<i>1,975,460</i>	<i>7,271,000</i>	
Russian Federation	276,060	522,627	396,987	630,673	1,826,347	5
Serbia and Montenegro	88,038	148,814	200,497	360,486	797,835	14
Romania	339,378	128,648	20,257	211,770	700,053	16
<i>5. Middle East</i>	<i>152,742</i>	<i>96,491</i>	<i>173,027</i>	<i>3,396,974</i>	<i>3,819,234</i>	
Iraq	4	5	60,828	3,257,910	3,318,747	-
<i>6. North Africa</i>	<i>497,575</i>	<i>834,683</i>	<i>803,957</i>	<i>710,042</i>	<i>2,846,257</i>	
Egypt	93,221	204,883	456,164	292,520	1,046,788	8
Morocco	174,648	171,970	276,884	268,777	892,279	10
<i>7. Central America</i>	<i>576,907</i>	<i>281,135</i>	<i>393,600</i>	<i>558,451</i>	<i>1,810,093</i>	
Nicaragua	123,104	38,130	36,038	146,744	344,016	29
<i>8. South America</i>	<i>233,253</i>	<i>295,186</i>	<i>290,723</i>	<i>227,447</i>	<i>1,046,609</i>	
Bolivia	11,688	103,367	106,259	46,269	267,583	38
<i>9. Oceania</i>	<i>154,170</i>	<i>60,476</i>	<i>113,454</i>	<i>290,460</i>	<i>618,560</i>	
Papua New Guinea	59,190	8,626	34,747	159,261	261,824	39

Source: OECD/WTO database.

<sup>a</sup> Countries are ranked according to the cumulative 2001–2004 spending.

Table 2

**DESTINATION OF AID FOR TRADE BY INCOME GROUP,  
SHARES IN TOTAL AND SPECIALIZATION INDEX**

	2001	2002	2003	2004	2001–2004
LDCs (share, <i>per cent</i> )	22	16	26	21	21
LDCs (index)	1.07	0.70	1.04	0.83	0.88
Other Low Income Countries (share, <i>per cent</i> )	25	24	29	28	27
Other Low Income Countries (index)	0.84	1.00	0.97	1.30	1.04
Low-Middle Income Countries (share, <i>per cent</i> )	28	35	23	35	31
Low-Middle Income Countries (index)	1.09	1.34	0.92	1.15	1.14
Upper-Middle Income Countries (share, <i>per cent</i> )	3	3	3	1	2
Upper-Middle Income Countries (index)	1.00	0.84	0.69	0.39	0.59
Others and unallocated (share, <i>per cent</i> )	21	22	19	15	19
Others and unallocated (index)	1.00	0.94	1.23	0.74	0.97
Total Aid for Trade (US\$ million)	11,151	11,216	12,312	17,798	42,507

**Source:** OECD/WTO database.

**Note:** The index is obtained by dividing the share of an income group in total aid for trade over the share of the income group in total ODA; an index greater than 1 means that a country is receiving aid for trade more than proportionally with respect to ODA.

The total G8 commitment, confirmed at the 2006 meeting, is still stated as \$4 billion annually for AfT (G8, 2006), in total, not the increase, and including the Enhanced Integrated Framework. Even taking the most limited OECD definition, \$2.5 billion for trade related technical assistance, this would be an increase of only 60 per cent, and compared to the higher estimates of around \$23 billion (OECD, 2006) it implies an increase of less than 10 per cent. If it includes the Japanese pledge, it includes some infrastructure, so it may be no increase. This would mean a fall in the share of AfT in total aid, given the promises made in July 2005 by the G8, confirmed by the Finance Ministers, December 2005 (AITIC, 2006) to double aid to Africa. It is substantially less than assumed in the WTO's Concept Paper (WTO, 2006a) for the Task Force which expected a doubling of AfT, an extra \$2 billion by 2007, rising to "an additional \$5–6 billion by 2010", about 10 per cent of the additional aid promised of \$50 billion, so a total of \$10–12 billion. (These seem to use an estimate of \$5 billion for current spending.) Even the most conservative (OECD) estimates for what

was needed were a 67 per cent increase, to preserve its share of total projected aid, with \$4.3 billion for trade related technical assistance alone, and \$33.7 billion including infrastructure (OECD, 2006: 41–42).

These apparent inconsistencies of definition and of the pledges should have been clarified by the WTO Director General under his Hong Kong mandate to consult on additional finance, but there has still been no report on these consultations except for his comment (WTO, 2006g) that "all of the key donors have confirmed to me that they remain committed to following through with their Hong Kong pledges."

The original demand by developing countries, notably the LDCs, was that AfT be additional to planned increases in total aid, in order not to divert resources from other areas. All statements by donors have refused to accept this, arguing that the large increase projected for total aid (\$50 billion more per year by 2010) was designed to allow for any new demands, and therefore for AfT. The targeting of these amounts, however, dates to the Monterrey con-



ference of 2002, before the recognition of the costs of WTO implementation and the Doha negotiations, and they were accepted by the G8 in July 2005, before any formal discussion of AfT, so this is disingenuous. If some of the financing required is for international public goods, whether to support the international trading system or more particularly to achieve success in the Doha negotiations, the fact that “most DAC members have already made commitments for their total aid levels to at least the year 2010” (OECD, 2006: 41) is not a convincing reason to reject the possibility of increased spending on non-aid purposes.<sup>13</sup> But even accepting the overall limit, it is difficult to argue that commitments for AfT are “additional”, as demanded by the Task Force, if the value is either stagnating increasing more slowly than in the past and they are a falling share of total aid.

#### 4.6 *Allocating Aid for Trade: criteria, constraints, and eligibility*

In the early discussions of AfT, it was important to find needs that could be justified as related to WTO obligations or negotiations because the intention was to use the negotiations to obtain the money. This remained true up to and including the phrasing in the Hong Kong Declaration. Now the position is different. The principle of spending more on trade has been secured, but the negotiations have failed. It is now important to ensure that spending can be justified even in the absence of a Round. This is reflected in the rephrasing of the objectives in the Task Force Report. One risk (from a multilateral point of view) is that spending to promote other types of trade, notably regional or bilateral arrangements, which may damage prospects for multilateral agreements, will be accounted for as AfT. The EU, for example, has announced that it will spend what it has pledged on AfT on support for the ACP in their negotiations of Economic Partnership Agreements (Bounds, 2006).

Some projects might be related to regulations or adjustment or new opportunities that are the result of a regional or bilateral agreement. If these are only slightly related (improving infrastructure for regional trade), it would be impossible to exclude them, and probably wrong to do so. But if they were specifically the result of that agreement (for example assistance in negotiating or setting up a regional organization or enforcing a regional set of standards),

it would probably be wrong to include them in the WTO monitoring of spending.

One way suggested to extend the categories covered from those directly part of trading, while keeping a trade-related focus, is a “value-chain” approach. This was suggested by the LDCs (Patel, 2005; WTO, 2006d) and was developed in a paper by Wilksa and von Bonsdorff (2006). They argue that “There can be many relevant AfT needs that are crucial for enhancing export competitiveness of an economic sector, but may not have immediate connection to cross-border trade.” (Wilksa and von Bonsdorff, 2006: 11) They give examples both of necessary productive inputs (including infrastructure) and required institutional or governmental inputs (including investment and competition policy, as well as trade policy).

The question of which countries should be eligible for any special treatment is sensitive in both aid and trade. The only classification in current use that is the same is Least Developed Countries. This is the determinant of eligibility for the Integrated Framework and is used to offer more special treatment in the WTO both in WTO rules (compliance with TRIPS, lack of obligations to make offers on goods in the Doha Round, etc.) and in WTO-permitted derogations such as preferences. That these countries should be included in AfT is already determined in the Hong Kong statement. Beyond this, while aid agencies can determine their own differentiations among recipients and define groups, the WTO can only differentiate by consensus of all members. The WTO gives special status in a few agreements to “developing countries”; it specifies this as a condition for allowing preferences. Although this is conventionally described as “self-selecting”, in practice the list is not open to all: countries can be strongly encouraged to graduate themselves (for example, countries which have joined the EU), and countries joining the WTO have had to negotiate details of their rules, even if they have been allowed to call themselves developing.

An alternative approach has been to list countries other than LDCs that may be eligible for particular treatment (e.g. the NFIDCs in the agreement on agricultural subsidies in the Uruguay Round) or excluded from it (e.g. the agreement on importing pharmaceutical products of 2003). In legal terms, any modification of the group “developing countries” for AfT in the WTO would have to follow this model.

The controversy over membership of the Task Force suggests that countries will not exclude themselves. As some AfT is likely to be for international institutions, for example the Advisory Centre on World Trade Law, or to meet regional needs, excluding some developing countries could restrict its usefulness. In the absence of a Doha settlement, there would be no legal way to change the coverage from “developing countries”.

#### 4.7 High aid makes trading harder (Dutch Disease)

Aid inflows are a positive flow in a country’s balance of payments. They therefore have potentially the same effect as exports of increasing the supply of foreign currency to the country. Like any increase in supply, this results in a fall in price. Therefore there is an upward revaluation of the value of the domestic currency. For exporters (or those competing with imports), the change in the exchange rate reduces the return that they can expect, measured in their own currency.<sup>14</sup>

In the case of a permanent change in trade (for example if a country discovers a sufficiently large source of oil so that it can expect high income into the indefinite future), this negative effect on other producers is exactly what is needed, as the economy has to restructure itself (at least in relative terms) away from what it was previously producing and trading. In the case of a permanent flow of funds, for example from a relatively prosperous part of a country to a poorer, the same argument might hold.

The situation where the export or the inflow of capital is expected to be temporary is different.<sup>15</sup> There are adjustment costs, both to shifting away from the existing pattern of production and, once the flow stops, towards a different pattern. Therefore the correct development strategy is more uncertain, because policy makers will want to maximize the temporary benefit without incurring unnecessary costs of adjustment. Aid to assist trade must take account of both the immediate negative effects which the aid itself will have (through the exchange rate) and the medium term ones on incentives to move into export production if the aid inflows are expected to remain high into the medium term.

It is important not to exaggerate the problem. If the “temporary” is more medium term than short

term, and if the economy would in any case have found it necessary to move out if its existing production pattern in order to develop, the “Disease” may not impose significant additional adjustment costs. The benefits will always be greater than any costs, unless all revenue is wasted.<sup>16</sup> This may be particularly true of a very poor country where the temporary increase from aid may reduce serious poverty.

There are also potentially damaging government effects from large inflows of aid which are relevant to AfT. Large aid inflows potentially affect the political development of the country, and create a clear inconsistency with the aid principle of country ownership. If the single most important, or even the majority, source of both finance and policy is external, the question of the accountability of the government must be raised. In some African countries, it has been over a half of government expenditure. Even if donors use the language of partnership, they have their own priorities and cannot avoid advocating them. A strong government may be able to override donor wishes and take its priorities from its electorate and legislature, but many developing countries have weak political systems. If aid donors try to deal with this by finding alternative ways of consulting public opinion, for example direct contacts with interest groups, this may further weaken the system and attenuate the accountability of the government.

Even if the government and the donor do negotiate on trade as if there were no aid relationship, the perception in the developing country will be affected by the aid relationship. A government is expected to take account of national interests in forming its trade position. In a non-aid dependent country, this means listening to the major economic interests, traders and those competing with traded goods and (although often neglected) consumers. One way that these interests make their importance felt is as taxpayers. In an aid-dependent country, the most regularly consulted “interest group” is probably the donors. They are also a, perhaps the, major source of government revenue. Normal economic actors may feel that their interests are unlikely to be taken into account. This pessimism may reduce their expected returns from trading and investing, damaging development. If a developing country official knows that his country is heavily dependent on the trading partner for aid, he is unlikely to forget this when pressing for a trade concession or when trying to ensure that a trading partner keeps its trade agreements.

If there is an even more direct relationship, because of AfT, in particular direct support for negotiating capacity or in trade disputes, this intensifies the problem. Learning to use trade negotiations and institutions effectively is important for countries trying to improve their trade performance, and donors have helped to build capacity and have directly funded some of the costs of participation (aid for salaries, travel to meetings, costs of representation). But if a negotiator has his salary paid by a trading partner country, and has travelled to a negotiation with that country on a ticket paid for by that country, it may be difficult for him to disregard this when in the negotiation.

There is evidence that the aid relationship can be a problem in trade negotiations where there is a direct role for aid. The EU has had a combined aid and trade relationship (Lomé agreements) with its associated ex-colonies, the African, Caribbean and Pacific (ACP) countries. The ACP have been much less effective in negotiations with the EU than in the WTO. As the same people were involved in both sets of negotiations, lack of capacity or inexperience cannot be the answer. The main reason for the difference appears to be that the role of the EU as donor is constantly emphasised as part of the same negotiation (Page, 2004).

Like “Dutch Disease”, aid dependency syndrome need not make trading impossible, and it is unlikely to make either the trading or the negotiating performance of the country actually worse than they would be in the absence of aid. But it can reduce the benefits. The implementation of AfT should be designed to avoid or minimise the risks from political dependency.

## 5. Suggestions for the architecture of Aid for Trade

The different purposes and the large scale of what donors are now calling AfT, as well as the unwillingness of both donors and recipients to rely on a single existing institution, suggest that the way in which AfT will work will be mainly through existing funds, multilateral and bilateral. In some cases the changes in scale may require new administration and new types of spending. It is possible that some of the needs identified here will be so far from what donors and their rules of operation recognize

as official development assistance that new funds or new sections of funds will be needed.

The need for AfT has been formally accepted by the WTO through consensus of its members. *Others involved in aid, in particular the World Bank and the IMF which are intended to act in coherence with the WTO, must therefore accept that trade now has a special claim on aid, equal to other international commitments, such as the Paris Principles.*

In 2005, countries acting as members of the World Bank and the IMF rejected the call for a new approach to AfT while, at the same time, as members of the WTO, they accepted it in the Hong Kong Declaration. *Countries acting in the international financial institutions will need to support the interests that they have identified as members of the WTO.*

One obvious difference between trade and most other aid subjects is that it always crosses borders. Some aid projects (for example, in energy, water, etc.) have had to deal with regional problems, but the normal model is country-based. The potential share of regional or international spending in trade-related spending will be higher than in existing aid. There may be a need to *increase the share in new aid of those institutions which are already better able to deal with regions* (e.g. regional development banks, a few donors) and to encourage *reorganization of aid administration in the others.*

For some donors, using or allocating funds on the basis of trade-related needs, rather than poverty or other criteria, may be not only unfamiliar, but contrary to the legal requirements of their aid programmes. For these, it may be *necessary to establish new funds* (as in the EU sugar Action Plan and the IMF TIM).

The organization of AfT funding could be either on the basis of *ex ante* assessments of countries' needs or by setting up definitions of the potential scope of coverage, and allowing countries (or regions) to apply for funds. Programmes such as the IF provide assessment of trade needs, separately from programmes to fund the needs. The evidence is that this does not work. The country has no guarantee that they will be funded, and therefore the initial assessment is not taken seriously, and perhaps merely repeats “what everyone knows”; the result is that assessments become even less likely to be used. If the assessment is by a different agency, the needs

must be re-assessed by the funding agency. *The Integrated framework experience demonstrates that there is a need for a mechanism to ensure that all projects put forward are considered by some agency, and assigned priorities by it.*

If the implementation of AfT is through existing programmes, then the rules of each donor and programme will constrain what is offered to whom. As there is a strong argument for accepting that existing systems will work best if they work in their normal mode, and with their normal recipients, this may be effective for those needs and those countries which are covered. But this suggests that *the Task Force's suggestion of a Clearing House Function to identify gaps, and find ways of filling them, will be very important.*

Past experience of country-based initiatives suggests that if AfT is left to these, there will be inadequate spending on trade. The Aid for Trade Task Force asked all the international organizations which it contacted if "trade has been adequately addressed in countries' development plans and poverty reduction strategies". All (World Bank, IMF, ITC, UNIDO, UNCTAD, UNDP) agreed that it had not, whether because of lack of interest or lack of capacity (WTO, 2006d).

The models for the project approach are largely from outside trade, but are found in other funds which have emerged out of international conventions, rather than specifically from aid programmes, e.g. the Global Environment Fund (GEF); and in terms of country aid, in the offering of support to country budgets under HIPC debt relief or the Sector Wide approaches. *These provide support for a specified type of spending in a country, so they are between project and unspecified aid.*

There might be some rigidity and potential distortion with vertical funds, but where an issue has been neglected by donors imposing rigidity and reversing past distortions may be required. In the case of the Montreal Protocol, quick agreement was found to fund a specific problem, the elimination of certain greenhouse gases according to certain timetables. Some issues require global coordination and involvement of a pool of expertise. UNCTAD relies on expertise in the area of trade negotiations, the Global Fund to fight Acquired Immunodeficiency Syndrome (AIDS), Tuberculosis and Malaria relies on health expertise, Global Alliance for Vaccines and

Immunisation (GAVI) for vaccines brings funders and private sector expertise together.

It may be that a compromise between special funds and general assistance is to ensure that the special funds have broad aims (e.g. HIPC) and align their rules with the government and with other programmes. One example of such a compromise is the Sector Wide Approach (SWAp), a process where donors give significant funding to a government's comprehensive sector policy and expenditure programme. It might focus aid on the trade sector, broadly defined, without tying it to a narrow range of projects. It is hard to assess the possibility of adopting a SWAp to AfT. The major obstacle to that is inherent into the definition of AfT. A broad definition of needs may be too broad to fit within one ministry-based SWAp.

Guaranteeing the funds, i.e., ensuring that the commitments are not only made, but credible, will need to be done through the mechanisms that each agency or fund uses to set its programme, as in the absence of negotiations, there is no way to build this into the WTO. There are legal means within each donor to make long term spending commitments and to alter any restrictions on aid agencies' competences that discourage them from spending on productive activities. The WTO in its monitoring function will need to ensure that such commitments are made. *Its role is to help to identify what these mechanisms are, and then to report, on whether the legal pledges, etc., have been made and whether they continue to be made to replenish funds.* This might fall under the Director General's responsibilities under the Hong Kong mandate.

*Countries which are donors or acting as members of the international financial institutions must ensure that they commit their funds in a credible way.*

The proposed system of WTO monitoring will cover what is being spent, and in what countries, on what projects; and, at the country level, whether countries are getting appropriate levels of funding. To have an effective system of evaluation, *the WTO should identify some set of criteria on which projects could be judged*, such as the return in trade-related terms to the investment, the lack of other ways of funding it, or the poverty of the country. It also needs to use the proposed base-line estimates to *check whether there is additionality.*

The monitoring process will use the reports on overall aid, by categories, and on the performance of individual donors by the OECD-DAC. This will need to be extended to give details of regional programmes and trade-related infrastructure. *The Committee on Trade and Development may need to ask the Secretariat to include in its annual report on trade a chapter on the level, direction, and types of trade-related aid.* This would allow the Committee on Trade and Development (CTD) and the General Council to discuss whether the aid was sufficient and appropriate.

At the level of countries, both giving and receiving funds, the review mechanism is the Trade Policy Review. This could draw on country reports by the OECD, for donors, and by the IMF and World Bank, for recipients. *The current low frequency of TPRs for developing countries might need to be changed or supplemented by interim reports.* It is never the function of the TPR to determine compliance with WTO commitments (whether by the country being reviewed or by any donors which may have made commitments to it), but it is its function to provide the information on which such judgements can be made. *A country being reviewed could use its response to the Secretariat report to draw attention to any gaps in funding relative to what it had identified as necessary.*

An implicit problem in the Task Force's deliberations and in all discussions of AfT is the conflict between the apparent virtues of a coordinated approach and the fear that this will mean in practice domination by the principal donors and especially by the World Bank. The history of the Integrated Framework is, from this point of view, a warning not a precedent. In principle, comprehensive assessment and co-ordination must be considered "good things", and coordination with other agencies is one of the functions proposed for the "monitoring" mechanism. A risk, however, is that this system is basically an aid approach, where the agencies confront the country. The advantage of the WTO over the international financial organizations has been that its structure and the requirement that all countries join a "consensus" for most agreements give developing countries a direct voice in decisions.

The World Bank has an approach to trade liberalization which goes against the basis of the WTO: the economist's approach of seeing the economic welfare advantages of unilateral liberalization rather

than the negotiator's approach of preferring agreed simultaneous liberalization. *The negotiating approach is what has given developing countries a voice in the introduction and design of Aid for Trade.* The criticisms by some observers (e.g. Thomas, 2006) that the Task Force members took insufficient account of existing mechanisms and did not specify a institutional role for the "core" agencies, such as they have in the Integrated Framework, but only asked for greater coordination misunderstands their difficulties. They may or may not have been right to reject them, but they were aware of them. The initial report by Ambassadors Horn af Rantzien and Rugwabiza (World Bank and IMF, 2005b) had had a much clearer recommendation: that they be bypassed.

They suggested that there should be a new fund and "Resources from the fund would be allocated on a project basis, or as budget support for trade-related programs with an overall maximum country allocation set in accordance with criteria to be agreed. ... It would be for the country to decide an appropriate institutional partner with expertise. ... While the intention would be to use the existing IF partner agencies, it may be desirable to extend this to include other multilateral agencies (notably the regional banks, Food and Agriculture Organization of the United Nations (FAO), UNIDO) and also private sector partners."

The WTO "Follow-up on the Aid-for-Trade Task Force Recommendations" (WTO, 2006f) provides for an Ad Hoc Consultative Group of donors and the private sector "to assist in preparing global reviews of Aid for Trade, as well as in providing follow up support in terms of advocacy and fund raising at country and regional level". This is not the same as the Task Force recommendations. The Task Force recommended an Ad Hoc group as an immediate measure to "take forward" its recommendations, but also suggested that the WTO or donors find a way of matching and brokering unfunded Trade-related assistance (TRA) needs and available donor funding for such projects and programmes. [and] Assign responsibility for these functions. The fact that proposals on this were weakened in the course of the Task Force's deliberations and after suggests that any pressure on donors to fund according to trade definitions of need will face resistance. The Task Force followed the aid model of not imposing obligations on donors to fund identified needs rather than the trade model of reciprocal commit-

ments. *A strong role for the WTO in identifying needs in advance as well as monitoring performance ex post could help to counter donors' reluctance to offer predictability.*

If increased AfT will lead to increased aid for directly productive activities or to infrastructure where the needs are defined by those who are engaged in production, then the interests of private sectors are likely to be much more directly involved than in most other aid sectors. Except for the inclusion of private sector representatives in the Ad Hoc group, there is no indication of how aid agencies or recipient governments will take account of private sector interests. *Allocating more aid through the agencies with experience in working with the private sector could be a solution.*

The introduction of Aid for Trade may not mean an end to all preferential trade. A return to a situation where preferences were simple and relatively rare would remove many of the threats to the system and to the interests of non-preferred countries. In a 2030 world of fewer, weaker, developing countries, it would be more difficult for them to demand extensive preferences as a price for their participation in the system. *It will be essential that the WTO and its members avoid neglecting even a weakened developing country group.*

## 6. The future for Aid for Trade

The hopes that the Aid for Trade initiative would mark new approaches to aid and to building the international trade regime may now be in part disappointed because the failure of the Doha negotiations means that it will have to stand alone. It remains a success for developing country participation in the WTO that an initiative where they both identified the problem (that trade liberalization can have negative effects) and the solution (targeted aid) has led to new attention to the linkages between aid and trade.<sup>17</sup> This success has reinforced those in the aid community who believe that it is time to devote more aid to production and trade. The WTO has acquired a responsibility to monitor flows of aid for trade purposes, and acceptance of the Task Force's recommendations on monitoring by the Committee on Trade and Development, an annual discussion in the General Council, and detailed monitoring of donors

and recipients in the Trade Policy Reviews gives it the opportunity to criticise and propose reforms. But the reluctance of the WTO as an organization to challenge the traditional aid agencies, the agencies' refusal to subject their decisions on the allocation or form of lending to external criteria, and the lack of negotiations in which developing countries could demand changes to aid in return for trade concessions mean that although there will be increased flows of funds for trade-related purposes, there will be no way to ensure that these purposes will be determined by the priorities of the international trading system and no certainty that they will be allocated by national trading priorities.<sup>18</sup>

The developing countries that argued for any financial scheme to be completely de-linked from any obligation to accept liberalization have succeeded, while those who wanted it only alongside liberalization on agriculture have lost out. Nevertheless, so far, they have not challenged the introduction of AfT without a trade agreement.

Before and during the deliberations of the Task Force there were serious concerns by developing countries about the principle of compensation. Developing countries with preferences remained divided on whether compensation was a satisfactory substitute. Many preferred trade mechanisms, and clearly continuing existing preferences, perhaps supplemented by new ones, requires less adjustment within countries. For those who believe that it would be possible to maintain some of the special arrangements, this may seem the better option. Those who do not believe that this is possible see compensation as an acceptable second best, but would be concerned if it was allocated according to the normal criteria and with the normal costs of IMF/World Bank arrangements. If offering compensation is to be successful in solving the problem of encouraging liberalization without damaging some poor countries, the details of its design will be important.

Among developing countries which have not been major preference receivers, there was concern that AfT would be considered a sufficient gesture in the direction of a "development round". For countries which are not likely to receive substantial shares of any AfT because they are neither losers nor poor, the suggestion made by some European negotiators that AfT plus assistance to the LDCs constitutes a "development package" is unacceptable. The current European Trade Commissioner suggested first in

October 2005 and then later in July 2006 (Mandelson, 2006) after the collapse of the Doha negotiations that:

**First** we should push ahead with the Aid for Trade package because developing countries' capacity constraints remain unchanged. **Second**, we should continue to put together a new agreement on trade facilitation, which is linked to aid for trade and will be a focus of our trade related assistance in the years ahead. **Third**, we should put in place the new Integrated Framework for technical assistance to trade for the LDCs and get it up and running. **Fourth**, the Hong Kong agreement on duty free quota free market access should be fully implemented outside of the Round and possibly improved. **Fifth**, we should also pursue specific proposals on Special and Differential Treatment on a fast track and stand alone basis, adapting existing WTO agreements in this way. **Sixth**, we should continue to work on making origin rules more development friendly. **Seventh**, we should see if we can put in place improvements on the dispute settlement understanding to make it easier for developing countries to use. This in summary is a seven point action plan for salvaging or extending the development agenda.

This proposal failed even as compensation, as it offered AfT targeted at the poor and small developing countries, but nothing to the major ones whose power in the WTO had increased. This does not support the argument by some opponents of AfT that it is being offered instead of trade liberalization. The offer was to one set of countries to gain their negotiating support against the countries seeking concessions.

The WTO has not yet fully implemented the provisions of the Hong Kong Declaration or the recommendations of the Aid for Trade Task Force. In his report to the December General Council, the Director General of the WTO asserted that the "most important" question for monitoring was "a more focused, country-specific perspective on whether trade needs are being met" and stated that "Aid for Trade is clearly important to a large number of our Members" (WTO, 2006g). This is a retreat from arguments that aid provides international public goods or that it is important to all members because it helps to provide the preconditions for a successful negotiation. There are now procedures to monitor Aid for Trade, but there are no criteria for that monitoring either of quantity or of effectiveness, as the report of the Director General does not mention additionality and does not define what "trade needs"

are to be covered. There has, therefore, been a failure to provide any secure mechanisms on "how to operationalize Aid for Trade" (WTO, 2005a).

It is a success that AfT stayed on the agenda after the collapse of the Round, but there is now no institutional momentum behind it because the WTO has effectively turned it over to the traditional donors, retaining only a monitoring role, while the traditional donors, with a few exceptions in specialised areas, do not want to change their behaviour. And for the first group to present a clear demand for AfT, the West African cotton producers, there have been reviews of the financial assistance available to them, but no special fund or guarantee of funding.

On the figures announced so far, there appears to be little or no increase in total AfT and its share of total aid may fall, so there is no additionality. Some critics of AfT would say that if this is what countries want, it fits the Paris Principles for aid, but there is an international development interest in shifting more aid towards improving the trading and productive capacities of developing countries. And it would be wrong to lose sight of the international trading interest. It seems odd to build an international system of aid based entirely on the needs defined by individual countries with no way of taking account of interests that cross borders. Some are in specific changes, physical and institutional infrastructure. Some are systemic effects on the trading system. But there is also an interest in avoiding an aid system that creates bilateral political dependency. This is bad in itself, and it makes impossible the effective operation of an international trading organization and regime based on the assumption that countries represent only their own interests.

One reason that AfT emerged as an issue, and the main reason why it remained on the agenda in the absence of a Doha settlement is that trade policy makers, in both developed and developing countries, believe that trade is not given sufficient importance in aid programmes, and that this is at least partly because of lack of interest by donors, not only because of mistakes by recipients. Therefore the force behind AfT was about imposing outside constraints on donors. It also imposes constraint on recipients, but all aid programmes do this. The concept of "ownership" in the aid rhetoric is deeply flawed. Beggars can't be choosers. All aid is ultimately a matter of negotiation between the aims of the donors and those of the recipients, with the advantage on the donor side.

The Task Force justifies the role of the WTO in AfT in terms of the “coherence mandate”. It will be important that the international Financial agencies, in particular the World Bank, also take coherence seriously, and recognize that trade can have legitimate priorities. The IMF has done this with its Trade Integration Mechanism, but the World Bank has not yet altered its position that it has no responsibility for WTO-related needs. In 2005, countries were more able to impose a developing country agenda on AfT at the WTO Hong Kong Ministerial Conference, than at the World Bank and the IMF, at the September meetings. But now, as control of AfT has effectively shifted back to the financial institutions, countries will need to use their membership in these if they want to change the approach to aid.

## Notes

- 1 Some analysts assume that the benefits of preferences are captured by importers, not by developing country exporters, but as some of the most important preferences (e.g. sugar) are based on country quotas, which are likely to ensure that countries not importers gain, this is not major limitation. Some results differ because they calculate the net effect (if negative) from all parts of any WTO settlement. i.e. offsetting the preferences lost by any gains on other goods or services, rather than the total losses from preferences.
- 2 Because the largest losses are for exporters of primary products, changes in rules of origin will not resolve all the losses.
- 3 The European Commission (EC), at Cancún and after, has repeatedly suggested that the G20 offer access to the Least Developed countries as compensation for their loss of preferences. This could be regarded as a way of transferring some of the G20 gains to those who lose. But it would not be an economically equitable solution: the developed country importers would also have gains (they would be importing from more efficient producers, i.e. trade would be “undiverted” from those previously receiving preferences), and it would not be a practical one: the reason the preference holders are expected to lose is that they are not competitive with the non-preferred developing countries in export markets. It is therefore unlikely that they will be competitive in the non-preferred countries’ own markets.
- 4 It appeared not to understand that sugar quota holders like Mauritius receive prices higher than world prices, not lower (World Bank, 2003: 216–217).
- 5 It transformed a routine meeting in Geneva in the days following the announcement of the Task Force in February 2006 into a presentation on Aid for Trade and on its role and skills in trade-related aid. The Geneva representative of the Bank argued that Aid for Trade should be administered by an agency with country offices.
- 6 Other organizations also wrote on Aid for Trade (e.g. Stiglitz and Charlton, 2006), but were not early developers of the concepts or influential on the outcome so far.
- 7 The announcement by the WTO (WTO, 2006b) said: “The Task Force will be composed of these 13 members in alphabetical order : Barbados, Brazil, Canada, China, Colombia, the European Union, India, Japan, Thailand, the United States and the coordinators of the ACP, the African Group and the LDC Group. The Permanent Representative of Sweden, Ambassador Mia Horn af Rantzen, will chair this Task Force *ad personam*.” Barbados was also in practice a group representative of the Small and Vulnerable Economies.
- 8 The costs and possible ways of funding these are discussed in more detail in Cali et al., 2006.
- 9 They are supporting grants in the context of encouraging countries to take regional initiatives, but the same argument could be used at national level.
- 10 Questioning whether donors should fund WTO costs, for example, suggests a limited view of what a country’s programme should include, as accepting an external obligation in implicit or explicit return for other benefits from the international trading system could be considered a proper decision for a country to make, not one to be questioned by a donor. This illustrates that donors support “country ownership” of development programmes only insofar as countries’ choices match those of the donors.
- 11 National public goods and international public goods may be closely related: the international good of a well-functioning trading system, for example, may depend on national public goods in the forms of good administration or infrastructure. The cross-national costs and benefits are likely to be particularly large at the regional level, even if there is no firm dividing line between regional and international public goods.
- 12 Infrastructure includes activities in the communication, transport and energy sectors, without separating out non-trade related activities. The accuracy of this analysis is limited by the usual problem of classifying projects that have broad scope and aims as trade related activities.
- 13 It is not a convincing reason even to reject increases in aid as governments can and do alter their budgets.
- 14 This result holds even if the government immediately spends the full amount of the aid on imports. The observable effect on the exchange rate may not appear, but imports will be in higher supply in the economy, and therefore the real return to exports still falls.
- 15 The traditional example is the natural gas resources discovered in the Netherlands, hence Dutch Disease.
- 16 Some analysis of Dutch Disease shares the views of those who support the hair-shirt view of trade: that only hardship leads to efficiency, so the role of trade is to alter the behaviour of comfortable, protected producers.
- 17 The view by some critics of AfT that it should not be a bargaining point, in contrast, takes the view that developing countries should not use their strength to obtain what they want, but rather depend on convincing developed countries that they have a moral obligation to give aid.
- 18 Some new proposals have emerged for how to relate AfT to the negotiations, in particular that by Lawrence and Rosito (2006) to delay (rather than avoid) reducing tariffs on the products where preference erosion is most likely to arise, and use the tariff revenue received dur-



ing this period to support those who will lose preferences. The idea is a clever way of ensuring that the costs of compensation for preference erosion are paid partly by those who have given the preferences in the past and partly (by delaying their benefits) by the un-preferred. But payments of compensation would appear as first income from tariffs and then aid transfers in countries' budgets, so it is not clear that their cost would be as politically invisible as preferences were, and it assumes that both developed countries and the non-preferred developing countries value a Doha settlement highly enough to be willing to offer deferred liberalization to obtain it. Given the current lack of progress in the Doha Round, AfT may have a better chance of success if it is completely de-linked from the Round, rather than brought back into it.

## References

- AITIC (2006). Aid for Trade: A Moving Target. Background Note April. Geneva, Agency for International Trade Information and Cooperation.
- Alexandraki K and Lankes HP (2004). The Impact of Preference Erosion on Middle-Income Countries. *Working Paper*, 04/169. Washington, DC, International Monetary Fund.
- Bird K (2004). *A Framework to Analyse Linkages Between Trade Policy, Poverty Reduction and Sustainable Development*. Final draft of report on the DFID Africa Trade and Poverty Programme.
- Bora B, Cernat L and Turrini A (2002). Duty and Quota-Free Access for LDCs: Further Evidence from CGE Modelling. *Policy Issues in International Trade and Commodities Study Series*, 14. Geneva, United Nations Conference on Trade and Development..
- Bounds A (2006). EU to give 2bn a year in aid-for-trade. *Financial Times*. 17 October.
- Calì M, Grimm S, Page S, Phillips L and te Velde DW (2006). *The Financial Architecture of Aid for Trade*. Toronto, Ontario, International Lawyers and Economists Against Poverty (ILEAP).
- Conway T (2004). Trade liberalisation in Poverty Reduction. In: Conway T and Page S. *Assessing the Poverty Impact of the Doha Development Agenda*. Report to DFID. London, ODI.
- European Commission (2005). *The Commission outlines its support to ACP Sugar Protocol countries*. Trade Issues. 24 January.
- Finger JM and Schuler P (1999). Implementation of Uruguay Round Commitments: The Development Challenge. *Policy Research Working Paper*, 2215. Washington, DC, World Bank.
- G8 (2006). *Communiqué*. Trade. 17 July.
- GATT (1979). *Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries (Enabling Clause)*. L/4903. Geneva, GATT.
- GATT (1993). *An Analysis of the Proposed Uruguay Round Agreement, with Particular Emphasis on Aspects of Interest to Developing Economies*. Geneva, GATT.
- GATT (1994). *The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts*. Geneva, GATT Secretariat and later reprints. Available at: [http://www.wto.org/english/docs\\_e/legal\\_e/legal\\_e.htm](http://www.wto.org/english/docs_e/legal_e/legal_e.htm)
- Gillson I and Hewitt A (2003). *A Review of the Trade and Poverty Content in PRSPs and Loan-Related Documents*. London, ODI.
- Gillson I, Hewitt A and Page S (2004). *Forthcoming Changes in the EU Banana/Sugar Markets: A Menu of Options for an Effective EU Transitional Package*. Report to DFID. London, ODI
- Goreux L (2003). *Préjudices Causés par les Subventions aux Filières Cotonnières de l'AOC*. 20 April.
- Group of Twenty-Four (2006). *Communiqué*. 16 September.
- Hoekman B, Ng F and Olarreaga M (2001). Reducing Agricultural Tariffs versus Domestic Support: What's More Important for Developing Countries? *Policy Research Working Paper*, 2918. Washington, DC, World Bank.
- Hoekman B, Mattoo A and English P, eds. (2002). *Development, Trade and the WTO, a Handbook*. Washington, DC, World Bank.
- Hoekman B and Prowse S (2005). Economic Policy Responses to Preference Erosion: From Trade as Aid to Aid for Trade. *Policy Research Working Paper*, 3721. Washington, DC, World Bank.
- Ianchovichina E, Mattoo A and Olarreaga M (2001). Unrestricted Market Access for Sub-Saharan Africa: How Much is it Worth and Who Pays? *Policy Research Working Paper*, 2595. Washington, DC, World Bank.
- ICTSD (2006). Comparative Table of Recommendations, Proposals and Views on Aid for Trade. Geneva.
- ILEAP (2003). Agricultural Products: Modalities. *Negotiation Policy Brief*, 2.
- IDC (International Development Committee, United Kingdom House of Commons) (2003). *Trade and Development at the WTO: Issues for Cancún*. Seventh Report of Session 2002–2003, Volume 1. Toronto, Ontario.
- IMF (2003a). *Financing of Losses from Preference Erosion, Note on Issues raised by Developing Countries in the Doha Round*. Communication to the WTO from the International Monetary Fund, WT/TF/COH/14. 14 February.
- IMF (2003b). IMF and World Bank Announce Plans to Support Developing Countries with Trade-Related Adjustment Needs in WTO Round. Press Release 03/140. Washington, DC, International Monetary Fund. 21 August.
- IMF (2004). Fund Support for Trade-Related Balance of Payments Adjustments. Prepared by the Policy Development and Review Department. Washington, DC, International Monetary Fund. 27 February.
- Kleen P and Page S (2005). Special and Differential Treatment of Developing Countries in the World Trade Organization. *Global Development Studies*, 2. Stockholm, Ministry for Foreign Affairs.
- Krueger AO (1983). *Trade and Employment in Developing Countries 3: Synthesis and Conclusions*. Chicago, University of Chicago.
- Krueger AO (2003). Statement of the First Deputy Managing Director, International Monetary Fund, WT/MIN/(03)/ST/20. WTO, Ministerial Conference, Fifth Session. 11 September.
- Langton D (2007). *Trade Capacity Building: Foreign Assistance for Trade and Development*. Congressional Research Service, order code RL 33628. Washington, DC.
- Lawrence RZ and Rosito T (2006). A New Compensation Mechanism for Preference Erosion in the Doha Round. *Faculty Research Working Papers Series*, RWP06-044.

- Harvard University, John F Kennedy School of Government. October.
- Low P, Piermartini R and Richtering J (2005). Multilateral Solutions to the Erosion of Non-Reciprocal Preferences in NAMA. *WTO Working Paper*, ERSD-2005-05. Geneva.
- Low P, Piermartini R and Richtering J (2006). Non-reciprocal Preference Erosion Arising from MFN Liberalization in Agriculture: What Are the Risks? *WTO Working Paper*, ERSD-2006-02. Geneva.
- Mandelson P (2006). We need to look ahead and rebuild. Statement, following the suspension of the WTO Doha negotiations. 25 July.
- Martin W and Winters LA (1996). *The Uruguay Round and the Developing Countries*. Cambridge, Cambridge University Press.
- Mauritius (2003). *Market Access for Non-Agricultural Product*. TN/MA/W/21/Add.1 #03-3831. Permanent Mission of Mauritius to the WTO. January.
- Mitchell D and Hoppe M (2006). From Marrakesh to Doha: Effects of Removing Food Subsidies on the Poor. In: Newfarmer R, ed. *Trade, Doha, and Development: A Window into the Issues*. Washington, DC, World Bank.
- Nielson J (2006). Aid for Trade. In: Newfarmer R, ed. *Trade, Doha, and Development: A Window into the Issues*. Washington, DC, World Bank.
- ODI (2006). Views on Aid for Trade by Multilateral Organizations. Compilation of inputs to Aid for Trade Task Force.
- ODI Database on Aid for Trade and Preference erosion. Available at: [www.odi.org.uk/iedg/aid4trade.html](http://www.odi.org.uk/iedg/aid4trade.html)
- OECD (2004). Financing Global and Regional Public Goods through ODA: Analysis and Evidence from the OECD Creditor Reporting System. Paris, OECD.
- OECD (2005). *Paris Declaration on Aid Effectiveness*. DCD/DAC/RD(2005)1ORD2. Paris, OECD.
- OECD (2006). *Aid for Trade: Making it Effective*. Paris, OECD.
- OECD/DAC. International Development Statistics online. Available at: <http://www.oecd.org/dataoecd/50/17/5037721.htm>
- OECD/WTO. Trade Capacity Building Database. Available at: <http://tcbdb.wto.org/index.asp?lang=ENG>
- Page S (2004). Developing countries in International Negotiations: How they influence trade and climate change negotiations. *IDS Bulletin*, 35, 1: 71–81.
- Page S ed. (2006). *Trade and Aid – Partners or Rivals in Development Policy?* London, Cameron May.
- Page S (2007). Policy Space: Are WTO rules preventing development? *Overseas Development Institute Briefing Paper 14*. London.
- Page S and Davenport M (1994). *World Trade Reform: Do Developing Countries Gain or Lose?* London, Overseas Development Institute.
- Patel D (2005). LDC Proposal on Aid for Trade. Presented in Letter to IMF, World Bank, WTO, United States and EU trade leaders. 14 October.
- Stiglitz JE and Charlton A (2006). *Aid for Trade*. Report for the Commonwealth Secretariat, March.
- Sweden National Board of Trade (2004). *Consequences of the WTO-agreements for Developing Countries*. Stockholm, National Board of Trade,
- Thomas H (2006). Aid for Trade. Presentation to WTO Forum. Geneva. 26 September.
- UNCTAD (2005). Erosion of Preferences for the Least Developed Countries: Assessment of Effects and Mitigating Options. TD/B/52/4. Geneva. August.
- te Velde DW, Cali M, Hewitt A and Page S (2006). *A Critical Assessment of the EU's Trade-Related Assistance to Third Countries*. Report to the International Trade Committee of the European Parliament.
- te Velde DW and Morrissey O (2005). *Supporting industrial development: overcoming market failures and providing public goods*. Report for UNIDO.
- Vitalis V (2006). Development, Aid-for-Trade and the Doha Development Agenda: Where to Now? Paper for ICTSD Conference. 14–15 November .
- Wilska K and von Bonsdorff M (2006). Aid for Trade as a Vehicle for Enhancing Export Competitiveness. Paper for ICTSD Conference. 14–15 November.
- World Bank (2003). *Global Economic Prospects*. Washington, DC, World Bank.
- World Bank (2006). *Global Economic Prospects*. Washington, DC, World Bank.
- World Bank and IMF (2005a). Aid for Trade: Competitiveness and Adjustment: Joint Note by the Staffs of the International Monetary Fund and the World Bank. Washington, DC. 12 April
- World Bank and IMF (2005b). *Doha Development Agenda and Aid for Trade*. DC2005-0016. Washington, DC. September
- World Bank and IMF (2006). *Doha Development Agenda and Aid for Trade*. Washington, DC. 9 August.
- WTO (2001). *Doha Declaration*. WT/MIN/01/Dec/1.
- WTO (2002). *Proposal by LDCs*. TN/CTD/W/4/Add.1. July.
- WTO (2003a). Negotiations on Agriculture First Draft of Modalities for the Further Commitments, TN/AG/W/1/Rev.1. 18 March.
- WTO (2003b). Draft Decision Concerning Specific Measures in Favour of Cotton with a View to Poverty Alleviation, Communication from Benin, Burkina Faso, Chad and Mali, WT/GC/W/511. 22 August.
- WTO (2003c). Poverty Reduction: Sectoral Initiative in Favour of Cotton, Joint Proposal by Benin, Burkina Faso, Chad and Mali, Proposal on Implementation Modalities, TN/AG/GEN/6. 4 August.
- WTO (2003d). *US/EU/Canada position paper on non-agricultural market access*. JOB(03)/163.
- WTO (2003e). LDC Position Paper, WT/L/521.
- WTO (2003f). ACP Position Paper, WT/MIN(03)/4.
- WTO (2004). Doha Work Programme, Decision Adopted by the General Council on 1 August 2004, WT/L/579 #04-3297.
- WTO (2005a). Doha Work Programme, Ministerial Declaration in Hong Kong, WT/MIN(05)/W/3/Rev.2. 18 December.
- WTO (2005b). Statement by Mr Danny Leipziger, Vice President and Head of Network, World Bank (speaking as an Observer). Ministerial Conference, Sixth Session, Hong Kong, China, 13–18 December 2005. WT/MIN(05)/ST/15#05-5972
- WTO (2005c). Creating an upward spiral of trade and development – Japan's new development initiative for the WTO Hong Kong Ministerial Conference. WT/MIN(05)/6. 12 December.
- WTO (2006a). *Aid-for-Trade Concept Paper and Timeline for 2006*. 17 January.

- WTO (2006b). Composition of Aid for Trade Task Force Announced. Press Release. 8 February.
- WTO (2006c). *Summary of Contributions from Inter-Governmental Organizations: Aid for Trade Task Force*. WT/AFT/W/17.
- WTO (2006d). WT/AFT/W/1-13, Submissions to the Aid for Trade Task Force by:
- IMF
  - International Trade Centre
  - OECD
  - UNCTAD
  - UNIDO
  - World Bank
  - African Development Bank
  - Asian Development Bank
  - Inter-American Development Bank
  - ACP Group
  - LDC Group
- Small and Vulnerable Economies
- Argentina
  - Brazil
  - Colombia
  - EU.
- WTO (2006e). *Recommendations of the Task Force on Aid for Trade*. WT/AFT/1.
- WTO (2006f). *Aid for Trade: Follow-up to the Aid-for-Trade Task Force Recommendations*, JOB(06)/262. 12 December.
- WTO (2006g). *Report on Aid for Trade by Director General to General Council*. 14–16 December
- WTO/OECD (2005). *Report on Trade-Related Technical Assistance and Capacity Building*
- Zedillo E (2005). *Strengthening the Global Trade Architecture for Economic Development: An Agenda for Action*.
- Zhang S (2003). *Address to the WTO General Council Plenary Session*. By Shengman Zhang, Managing Director, World Bank. Cancún, 10 September.

---



---

**G-24 Discussion Paper Series\***

*Research papers for the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development*

---



---

No. 44	March 2007	Injoo SOHN	East Asia's Counterweight Strategy: Asian Financial Cooperation and Evolving International Monetary Order
No. 43	February 2007	Devesh KAPUR and Richard WEBB	Beyond the IMF
No. 42	November 2006	Mushtaq H. KHAN	Governance and Anti-Corruption Reforms in Developing Countries: Policies, Evidence and Ways Forward
No. 41	October 2006	Fernando LORENZO and Nelson NOYA	IMF Policies for Financial Crises Prevention in Emerging Markets
No. 40	May 2006	Lucio SIMPSON	The Role of the IMF in Debt Restructurings: Lending Into Arrears, Moral Hazard and Sustainability Concerns
No. 39	February 2006	Ricardo GOTTSCHALK and Daniela PRATES	East Asia's Growing Demand for Primary Commodities – Macroeconomic Challenges for Latin America
No. 38	November 2005	Yilmaz AKYÜZ	Reforming the IMF: Back to the Drawing Board
No. 37	April 2005	Colin I. BRADFORD, Jr.	Prioritizing Economic Growth: Enhancing Macroeconomic Policy Choice
No. 36	March 2005	JOMO K.S.	Malaysia's September 1998 Controls: Background, Context, Impacts, Comparisons, Implications, Lessons
No. 35	January 2005	Omotunde E.G. JOHNSON	Country Ownership of Reform Programmes and the Implications for Conditionality
No. 34	January 2005	Randall DODD and Shari SPIEGEL	Up From Sin: A Portfolio Approach to Financial Salvation
No. 33	November 2004	Ilene GRABEL	Trip Wires and Speed Bumps: Managing Financial Risks and Reducing the Potential for Financial Crises in Developing Economies
No. 32	October 2004	Jan KREGEL	External Financing for Development and International Financial Instability
No. 31	October 2004	Tim KESSLER and Nancy ALEXANDER	Assessing the Risks in the Private Provision of Essential Services
No. 30	June 2004	Andrew CORNFORD	Enron and Internationally Agreed Principles for Corporate Governance and the Financial Sector
No. 29	April 2004	Devesh KAPUR	Remittances: The New Development Mantra?
No. 28	April 2004	Sanjaya LALL	Reinventing Industrial Strategy: The Role of Government Policy in Building Industrial Competitiveness
No. 27	March 2004	Gerald EPSTEIN, Ilene GRABEL and JOMO, K.S.	Capital Management Techniques in Developing Countries: An Assessment of Experiences from the 1990s and Lessons for the Future
No. 26	March 2004	Claudio M. LOSER	External Debt Sustainability: Guidelines for Low- and Middle-income Countries
No. 25	January 2004	Irfan ul HAQUE	Commodities under Neoliberalism: The Case of Cocoa
No. 24	December 2003	Aziz Ali MOHAMMED	Burden Sharing at the IMF
No. 23	November 2003	Mari PANGESTU	The Indonesian Bank Crisis and Restructuring: Lessons and Implications for other Developing Countries
No. 22	August 2003	Ariel BUIRA	An Analysis of IMF Conditionality

---



---

### G-24 Discussion Paper Series\*

*Research papers for the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development*

---



---

No. 21	April 2003	Jim LEVINSOHN	The World Bank's Poverty Reduction Strategy Paper Approach: Good Marketing or Good Policy?
No. 20	February 2003	Devesh KAPUR	Do As I Say Not As I Do: A Critique of G-7 Proposals on Reforming the Multilateral Development Banks
No. 19	December 2002	Ravi KANBUR	International Financial Institutions and International Public Goods: Operational Implications for the World Bank
No. 18	September 2002	Ajit SINGH	Competition and Competition Policy in Emerging Markets: International and Developmental Dimensions
No. 17	April 2002	F. LÓPEZ-DE-SILANES	The Politics of Legal Reform
No. 16	January 2002	Gerardo ESQUIVEL and Felipe LARRAÍN B.	The Impact of G-3 Exchange Rate Volatility on Developing Countries
No. 15	December 2001	Peter EVANS and Martha FINNEMORE	Organizational Reform and the Expansion of the South's Voice at the Fund
No. 14	September 2001	Charles WYPLOSZ	How Risky is Financial Liberalization in the Developing Countries?
No. 13	July 2001	José Antonio OCAMPO	Recasting the International Financial Agenda
No. 12	July 2001	Yung Chul PARK and Yunjong WANG	Reform of the International Financial System and Institutions in Light of the Asian Financial Crisis
No. 11	April 2001	Aziz Ali MOHAMMED	The Future Role of the International Monetary Fund
No. 10	March 2001	JOMO K.S.	Growth After the Asian Crisis: What Remains of the East Asian Model?
No. 9	February 2001	Gordon H. HANSON	Should Countries Promote Foreign Direct Investment?
No. 8	January 2001	Ilan GOLDFAJN and Gino OLIVARES	Can Flexible Exchange Rates Still "Work" in Financially Open Economies?
No. 7	December 2000	Andrew CORNFORD	Commentary on the Financial Stability Forum's Report of the Working Group on Capital Flows
No. 6	August 2000	Devesh KAPUR and Richard WEBB	Governance-related Conditionality of the International Financial Institutions
No. 5	June 2000	Andrés VELASCO	Exchange-rate Policies for Developing Countries: What Have We Learned? What Do We Still Not Know?
No. 4	June 2000	Katharina PISTOR	The Standardization of Law and Its Effect on Developing Economies
No. 3	May 2000	Andrew CORNFORD	The Basle Committee's Proposals for Revised Capital Standards: Rationale, Design and Possible Incidence
No. 2	May 2000	T. Ademola OYEJIDE	Interests and Options of Developing and Least-developed Countries in a New Round of Multilateral Trade Negotiations
No. 1	March 2000	Arvind PANAGARIYA	The Millennium Round and Developing Countries: Negotiating Strategies and Areas of Benefits

---

\* *G-24 Discussion Paper Series* are available on the website at: [www.unctad.org](http://www.unctad.org). Copies of *G-24 Discussion Paper Series* may be obtained from the Publications Assistant, Macroeconomic and Development Policies Branch, Division on Globalization and Development Strategies, United Nations Conference on Trade and Development (UNCTAD), Palais des Nations, CH-1211 Geneva 10, Switzerland; Fax (+41-22) 917.0274.

