



The Challenge of Subsidies and Trade Barriers

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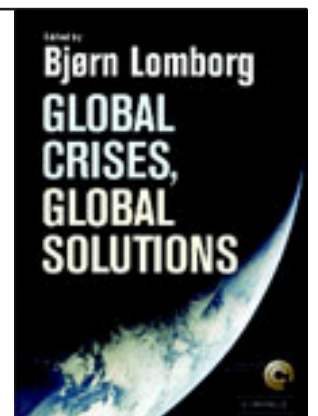
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Subsidies and Trade Barriers: a comment.

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Opponent paper to *Subsidies and Trade Barriers*, Challenge Paper prepared by Kym Anderson for the Copenhagen Consensus project, to be presented at a roundtable in Copenhagen, 24-28 May, 2004.

In his paper *Subsidies and Trade Barriers* Kym Anderson argues that phasing out wasteful subsidies and trade barriers should be given first priority, for three reasons:

1. the direct economic costs are low and the benefits in terms of trade expansion and economic growth are high,
2. trade liberalization and reform would enable the world to allocate resources more efficiently and would set resources free in order to meet other pressing needs (including the challenges addressed in the Copenhagen Consensus),
3. in addition to this indirect contribution to the alleviation of other challenges, trade liberalization and reform would also directly address these other challenges, including poverty (and poverty related issues in the fields of education, health, water and nutrition), environmental degradation, climate change, governance (conflicts, corruption, financial instability) and migration.

I will argue that the first two reasons are valid, but that their relevance requires further scrutiny of the political options. The third reason, in my view, is only true if specific conditions are met, outside the realm of trade itself. I will call them sustainability conditions. Meeting them requires political action in other fields than trade. Not meeting them is also jeopardizing the political opportunities to make better use of the potential of trade liberalisation and economic reform.

The challenge.

Anderson defines the challenge as a global one: to rid the world of wasteful and anti-poor distortionary trade policies. In order to keep the task manageable he limits the consideration of the policy instruments to those trade-related ones over which a government's international trade negotiators have some influence. Limiting oneself to trade distortions at national borders and trade-distorting production subsidies for reasons of measurement and comparison is fully understandable. During the last two decades an impressive global data base has been developed that includes data on trade tariffs, taxes and subsidies, on quantitative restrictions and technical barriers to trade as well as on trade-distorting production subsidies. Building and refining the data base for about eighty countries and country groups, together spanning the world, and about sixty sectors, spanning the entire economy is an important accomplishment. In the early eighties, in UNCTAD, when I had the responsibility for a smooth functioning of a number of specific multilateral trade negotiations, we were still lacking such a comprehensive data base. We had to limit ourselves to simple world models and multi-sectoral national and regional models that were complemented by sectoral and national cost-benefit analyses of alternative trade policies. Using global multi-sectoral computable general equilibrium models is a great step forward in the analysis of different scenarios. It provides policy makers with much more insight into the effects of possible alternative policies

Amongst these policy makers trade negotiators play an important role. In the practical reality of international trade negotiations they take crucial decisions. However, behind them there are the governments themselves. They give the instructions. They are accountable vis a vis the population and the business sector for the results or non-results of the negotiations. The governments, not the trade negotiators, are responsible for the overall economic, social, financial and budgetary policy of a country. That includes decisions concerning taxation, public expenditure on infrastructure, social welfare, the environment as well as health and education. Consideration of this category of policy measures has been excluded from the analysis. This is understandable because there is not yet a comprehensive global data base that includes the data concerned and because corresponding world models would become unmanageable. However, an analysis of the challenge to redress distortionary policies and opportunities to free resources in order to meet social and

economic needs and to alleviate poverty - as intended in the Copenhagen consensus - should not be limited to a consideration of trade policies. In practice governments are managing their economies with the help of all policy instruments at their disposal and they try to harmonize them. That implies also harmonization between trade measures and domestic policies. Trade policies do affect the economic and social perspectives of people and business. Domestic policies will either positively or negatively influence the social, economic and political capacity of a country to commit itself towards more free trade. Examples of such policies, that can boost or retard the ability and willingness of a government to engage itself into a speedy trade liberalisation, are the facilitation of production capacities, investments in research and education, the establishment of social safety nets and measures to avoid environmental pollution and a deterioration of the biodiversity. In a consideration of opportunities to alleviate major challenges confronting the population of the various nations of the world, it is up to (democratic) governments to assess the alternatives. Governments, more than experts or bureaucrats responsible for specific sectors, have the duty to weigh the various objectives. More than anybody else they can influence, directly as well as indirectly, the allocation of resources and the application of all relevant policy instruments concerned. For this reason a consideration of trade policies should go hand in hand with a consideration of domestic policies.

There is a second reason. The distribution of the fruits of trade amongst countries as well as within countries will be unequal. Trade is not the culprit. Trade takes place in the context of a given degree of inequality between nations and population groups. The allocation of production factors, their remuneration and the distribution of costs and benefits amongst market partners will reflect that inequality. Whether the resources set free by open and more efficient trade relations will be used to address the challenges concerned, will depend on their allocation, and thus on a combination of market forces and public policies.

A third reason why we should not limit our attention to the potential benefits of trade expansion is that trade is not an aim in itself. The ultimate objective of economic policy making is not to expand trade, but to increase income and welfare. Trade is an instrument. Its expansion should be assessed against the objectives. It is always the relationship that matters: trade and growth, trade and welfare, trade and development, trade and the environment. And because the objectives are manifold trade should also be seen in relation to other intermediary instruments and policies: trade and investment, trade and finance, trade and competition, trade and labour, trade and technology..

The arguments

In chapter 2 of his paper Anderson presents the well known arguments for free trade: static economic gains resulting from an optimum allocation of resources in a world characterised by competition, plus dynamic gains, because openness contributes to investment, knowledge, innovation, productivity and growth. This is classical theory, more and more refined in the latter half of the previous century. It has been substantiated by econometric studies and empirical evidence.

The author mentions two caveats. First, ascribing causality is not easy, because parallel to trade many other factors influence economic growth. Though recent developments in the theory of economic growth have provided us with more insight into the relative importance of factors explaining growth, we will never be certain about the causality and the mutual relations between those factors in specific circumstances. However, as is also argued by Anderson, economic history shows that open economies grow faster and that autarkic economies tend to stagnation. So, policy makers and governments can safely assume that openness is better. However, that does not mean that openness is enough. There is a second caveat, also mentioned by the author: trade openness is a necessary, but not a sufficient condition for sustained economic growth. In order to make good use of openness a country needs good institutions, functioning markets and macro-economic and political stability.

These are important conditions. What if the domestic conditions are not fulfilled? Is more openness and more free trade always good under such circumstances? Moreover, do these conditions determine trade or does trade also affect the conditions? In other words: could more and open trade not result in a weakening of institutions, less stability and a deterioration of market relations?

That complete openness is not always necessary is shown by the example of the Asian Tigers. The newly industrializing countries of East Asia in the 1970s did experience unprecedented trade expansion and high economic growth with the help of much public intervention, aggressive policies, managed trade, gradual opening of markets.

Fast market reforms can also create problems. For a long period already China has witnessed two digit growth figures, amongst others facilitated by a massive and speedy access to world markets. But within China this unprecedented growth rates give rise to economic and environmental distortions. Pollution is enormous, jeopardizing people's health. Easy lending has resulted in a huge overhang of bad loans, threatening the banking system, financial stability and people's confidence. Moreover, in the world outside China Chinese competition on the basis of its comparative cost advantage may lead to an increase in unemployment that cannot easily be matched by increased exports to China. Without a comprehensive international approach, integrating policies concerning trade, investment, finance and money, this could violate the stability of trading partners and of the world economy

That a gradual and conditional opening of markets can be a wise policy is shown by the European Union. Long negotiations had to take place in order reach agreement with the accessory countries. These negotiations dealt with the consequences of the European expansion for markets in both the old and the new Europe: agriculture, transport, internal migration, competition, environmental legislation. Nobody dared, for instance, to argue in favour of a prompt establishment of a fully free agricultural market within the enlarged European Union. Countries were willing to further liberalise agriculture, because everybody realized that the allocation of resources was highly inefficient and that subsidies could not be sustained. But at the same time there was fear for social consequences, as had also been the case during the negotiations to enlarge the then old Europe with Spain, Greece and Portugal. Were those fears not justified? The position of farmers outside Europe is much worse. That alone would justify a removal of the barriers that those farmers have to overcome when they want to export to Europe. But this does not render the fears inside Europe itself irrational. Rural conditions within Europe are not only a burden on the European economy. They also reflect certain values. For similar reasons Austria had been afraid that a free transportation market would irreversibly violate the environment in the Alps. Not everything can be compensated through a reallocation of resources set free by expanded trade.

Many fears are related to specific interests. They can be addressed with rational economic counter-arguments. However, are all such fears irrational? Can all arguments for protectionism "found wanting in almost all circumstances in that a lower-cost domestic policy instrument is available to meet each of those objectives"? [Anderson, 2004, p.6] Anderson argues that the most compelling explanation for their persistence is a political economy one. Indeed, but that does not render them irrational or inferior. Anderson points out that the source of resistance to policy reforms is that "the expected losses in jobs, income and wealth are concentrated in the hands of a few who are prepared to support politicians who resist protection cuts, while the gains are sufficiently small per consumer and export firm and are distributed widely as to make it not worthwhile for those potential gainers to lobby for reform." I agree that this is often the case. However, resistance to reforms often also is based on more general considerations, instead of specific group interests. Anyway, whether the resistance would be socially justified or not, it is a political fact, related to questions of distribution. To address such resistance would require a broad analysis of all relevant factors, perhaps with the help of models that include political variables and equations. Anderson seems to admit this himself, when he concludes the paragraph concerned with the statement that "the observed pattern of

protection in a country at a point in time may well be an equilibrium outcome in a national political market for policy intervention”. [Anderson, 2004, p. 6]

If so, then the policy measures suggested in para 2.4 are not adequate. Better information dissemination concerning the potential benefits from reducing trade distortions will not be sufficient. Many parties, consumers, labourers as well as producers, do not see these feature as trade distortions, but as mechanisms to restore, protect or sustain a socio-economic and political balance in the economy or in the nation. To inform them about the costs involved, for them as well as for others, and thus about the potential benefits of removing the costs, will not suffice. They will envisage the removal of the trade distortions as paving the way for other distortions and as a possible source of uncertainty and instability. They will therefore weigh the costs and potential benefits differently. Is that irrational? Sometimes, but not always, because the initial situation preceding trade reform and before more freedom is introduced on markets, is one of inequality in welfare as well as in political power.

Will technological change and the unilateral opening up of markets abroad contribute to a different understanding and weighing of the benefits and costs? Yes, in so far as trading costs are lowered and economic gains to be reaped come near by. Anderson rightly points out that this is happening in the present era of globalisation. However, at the same time the perceived uncertainties and threats come close by. Financial and monetary instabilities increase with globalisation, economic inequality as well. Foreign control of investments and thus of production, commercial and trade systems and sales also increases with globalisation. This may retard the willingness to actively contribute to a further opening up. Because of the inequalities mentioned earlier, such reluctance is not irrational. Even when it is clear that further liberalisation will contribute to growth and will help creating more resources, it is uncertain who will reap he benefits and whether inequalities might not increase. It is too simple to conceive of this in terms of an “alarmist lobbying of protectionists” [Anderson, 2004, p. 7] alone. Such lobbies exist and do harm. However, there are also legitimate fears that cannot be taken away by merely more and better information. Such fears can only be countered through a serious and comprehensive approach that goes beyond creating expectations and beyond promises.

International trade agreements, as widely representative for all the interests concerned as possible, would be the most credible way to begin addressing the fears. They form the best opportunity to bargain and exchange access and opportunities. Anderson rightly points out that the chances of success are greater the larger the number of countries involved and the broader the product and issues coverage of the negotiations. But here again it will not be simple. Like all other modalities of trade policy making multilateral negotiations take place in a context of both international and national inequality. Inequalities at home imply rigidity in the position of the negotiation partners. They may fear instability at home resulting from a different assessments and weighing of the outcome of the negotiation amongst various groups at home. For this reason they cannot afford to be very flexible in the negotiations. Their governments can try to prevent or compensate this by means of specific domestic economic and social policies. However, these policies are costly and will have to be financed out of the economic gains resulting from the expanding trade opportunities. Sometimes these opportunities have a different time frame. Often they cannot easily be taxed. All this will mean that the governments will be rather cautious in their instructions to their trade negotiators and that the negotiators themselves will exercise restraint.

This will add to a cautious approach that the same governments will choose because of the other inequality, namely that between the negotiating countries themselves. It is self-evident that this inequality leads to a lengthy negotiation process. The fact that previous rounds of negotiation have led to quite unequal results for the trading partners – the OECD countries did benefit much more than most developing countries – and also the fact that many commitments and promises resulting from these negotiations have not yet been implemented will add to the reluctance to engage themselves in further rounds of talks, not to speak of new

negotiations. Even if new rounds more or less objectively could be considered as beneficial to the world economy as a whole, weaker negotiation partners will stay reluctant. This, for instance, is the case for negotiations concerning services and investment. The reluctance of weaker developing countries to engage themselves in the MAI negotiations and in talks concerning the so-called Singapore issues is understandable in the light of the above.

It is also understandable that other countries are eager to speed up negotiations and action. They want to expand trade and boost the opportunities for growth and they are less afraid for an unequal distribution of the results. Because in their view multilateral negotiations become more and more cumbersome, they increasingly choose a different path: bilateral and regional negotiations, with free trade areas involving only a subset of countries. Anderson rightly warns against such an approach. Trade may be diverted from lower cost developing countries, worsening situation for non-participants in these talks. Therefore it is meaningful to analyse empirically the likely gains from different types of prospective agreements. This is done in chapter 4 of Anderson's paper, where he presents results of a variety of empirical studies. The usage of the term empirical is a little misleading, however. It remains a theoretical exercise, with the help of quantifiable data and empirically tested models that by their very nature cannot reflect political realities. The outcome of the scenario exercise remains an abstract possibility. Whether it can be turned into a reality will depend on many factors outside the limits of trade policy alone.

Opportunities.

Anderson present estimates for four different categories of trade liberalization: 1) a world free of trade barriers and subsidies, (2) non-preferential legally binding partial trade liberalisation, (3) reciprocal preferential legally binding trade liberalization, and (4) non-reciprocal preferential trade agreements. The potential benefits of full trade liberalisation are tremendous, though their estimates widely diverge, depending on the assumptions made. The author carefully mentions the assumptions underlying the estimates: the definition of the baseline scenario (full implementation of the commitments made in the Uruguay Round, with or without the completion of the accession of China to the WTO and of the EU eastern enlargement), constant returns to scale versus economies of scale, perfect versus monopolistic competition, with or without trade in services in addition to trade in goods, static versus dynamic efficiency gains. Possible benefits resulting from the lowering of barriers to international capital and labour movements and from the lowering of subsidies outside the sector of agriculture, notably the energy subsidies are generally excluded in most of the scenario's. There are also different assumptions concerning the extent to which the liberalisation of agricultural markets would draw resources from other sectors in the economy. The wide divergence between the outcomes strongly reflects different combinations of the assumptions underlying the various models. However, some general conclusions can be drawn. First, trade liberalisation by developing countries is very important, in particular in the framework of South-South trade. This conclusion reflects the predominance of protection in developing countries themselves. Second, liberalisation of the services sector, including both capital services, foreign direct investment and labour migration will offer many opportunities for growth, though the precise magnitude of the effects is still uncertain. Third, trade facilitation, an area that is often neglected, deserves more attention. This last conclusion can be interpreted as an indication that non-tariff barriers are an even greater barrier to trade and more difficult to handle than tariffs and subsidies. Examples of such non-tariff barriers, other than customs clearance, are health and sanitary regulations and safety measures. These trade measures are not so easily quantifiable and comparable as tariffs and subsidies and not easily manageable in negotiations that require a bargain. But have become quite popular and increasingly replace traditional trade barriers.

There is no reason to dispute the outcome of the computations. They represent state of the art. The question is not whether the estimates are right, but whether they are relevant. After all, also without the help of global modelling in the period following the Second World War policy makers knew that the macro economic

benefits of trade liberalisation could be enormous. They knew that also before the war. There was ample economic literature making a convincing case for trade liberalisation. Before the war and in particular after the Crash of 1929 policy makers had not listened well. After 1945 they had learned their lesson and gradually embarked on a mutual removal of barriers to trade. The result was a series of multilateral negotiations, though not world-wide. Experience with the trade rounds is not bad. Governments were serious. They knew what was at stake [Cairncross, 1982] In the course of half a century many tariffs were substantially reduced. Though there are still rather high tariff peaks and tariff patterns discriminating against processing of raw materials and intermediate products in countries where they have been produced. But increasingly countries that had shown a clear preference in favour of protectionism and import substitution became willing to liberalize trade and to implement market reform. At first this was a by-product of adjustment policies that were more or less imposed upon them by financing institutions, but later this tendency became more endogenous. There is, however, a mixed reading of that experience. Some authors claim that developing countries have shown a substantial willingness to unilaterally opt for reform. [Whalley, 1989] Others, like Bhagwati, were much more sceptical. [Bhagwati, 1991]

Negotiations were limited to tariffs and to the manufacturing sectors. These limitations constrained the capacity to liberalise fully amongst all countries, but they also made the negotiations manageable. During the Dillon Round, the Kennedy Round and the Tokyo Round the low hanging fruit had been reaped. These negotiations also helped to counter inclinations to return to protectionism. But protectionist tendencies still had their way in the form of non-tariff barriers and restrictive business practices. Moreover, commodities and agriculture still were outside the scope of these rounds. These subjects were dealt with in different international gremia. The Uruguay Round, negotiators reached the limits of what was possible within the prevailing trading system. No wonder that after about half a century it was deemed necessary to broaden the scope. GATT was turned into WTO, which meant that investment, services and agriculture got a prominent place on the agenda, next to trade in goods. It also implied a broadening from tariff barriers to all barriers to trade. And it meant a widening of the partnership in the negotiations: with the former Soviet Union and with China as well as with developing countries. The latter had been followers of what basically were West-West negotiations. The entry into force of WTO as the successor of GATT increased their chances to become equal partners in the talks. Formally that was the case, but it had to be given shape and content in the negotiations that would follow.

No wonder that since the early ninety nineties the broadened negotiation process did slow down. The reason was not that countries had become more protectionist. Governments had not become less aware of the potential benefits of trade liberalisation, such as the benefits estimated in macro terms by economists that built the GTAP database and variations of the CGE model. However, they found it more difficult than before to cope with the institutional intricacies of globalisation and with the uncertainties resulting from globalisation. They had to learn to deal with the complications resulting from the multiple broadening of the negotiations, as reflected in the mandate and the composition of the new WTO.

No wonder, also, that many governments resorted to alternatives to real multilateral negotiations at a world scale. The nineties saw a preference for regional reciprocal or non-reciprocal trade liberalization areas. Governments choose such options not because they had become less oriented to free trade, but because they wanted to combine more free trade with more speed than would be possible in a fully multilateral framework and with more certainties than would be possible in a fully global context.

One could explain the efforts emerging towards the end of the millennium in two different ways, either as tendency towards more protectionism, or as trade liberalisation in stages. The failure in Cancun to further the implementation of the Doha commitments, the harsh language used by the EU as well as the US and the newly established group of bigger and more advanced developing countries, and the regional approaches chosen by the US as well as the EU (combining regional free trade areas with trade measures against non-

members) can be conceived as a return to protectionism. The estimates of the benefits of various regional approaches towards trade expansion, as summarised by Anderson, indicate that, to a great extent, these benefits are achieved to the detriment of third parties. Harmful trade diversion may arise from the establishment of a Free Trade Area of the Americas as well as from the EU 'Everything But Arms' initiative to provide duty- and quota-free access to exports of all least developed countries.

However, are these examples of a conscious choice in favour of protectionism or are such policy steps meant to be a gradual approach towards a further liberalisation of markets? Recent developments in trade policy can also be explained as an effort to follow a two track approach, parallel or in stages: a slow WTO process in combination with an intensification of bilateral and regional trade negotiations, both with the objective to enlarge trade, but in such a way that the economic and social consequences of that enlargement can be managed. The problem, however, as has been made clear by many authors, is that the second track renders the first track less and less feasible, because it undermines the rule based character of a global system, eroding the principles which in earlier stages had been agreed by all countries. It is not enough to address such a tendency by highlighting the wonders of trade liberalisation or by investing, as suggested by Anderson, one or two billion dollars per annum in research and advocacy, in order to counter the lobbying of entrenched protectionist forces and to change public opinion. I agree with Anderson that in present circumstances a policy choice has to be made in favour of what the author calls 'a multi-pronged approach': unilateral reform at the national level and multilateral reform at the WTO level, supplemented by regional support for both, in a form of open MFN regionalism. I consider this politically feasible, because I interpret recent developments not as a tendency towards protectionism, but as a preference for a double track approach. I also agree with Anderson that in such a multi-pronged approach there is no place for an expansion of regional preferential trade arrangements. These would harm third parties, erode an efficient allocation of resources at home and undermine efforts to achieve a better multilateral agreement later. It is my personal experience from trade negotiations that temporary preferential treatment, enjoyed by initially less developed countries and granted to them on the basis of infant economy considerations in order to overcome time bound handicaps, turns out to stay. It is difficult to reduce preferences, let alone to remove them, because beneficiaries see them as established rights. It is nearly impossible to replace them by other measures intended to assist the integration of the country into the world economy at equal footing.

However, to choose in favour of a multi-pronged approach is more easily said than done. It certainly cannot be confined to trade measures only. More information dissemination regarding the benefits of free trade is not sufficient. Advocacy is not enough. Policy-makers are already aware of the potential effects. They are weary about the uncertainties. Vos, for instance, has shown that since 1980 trade liberalization in Latin America has resulted in import dependence rising more strongly than the capacity to export. As a result, for these countries capital flows have become more important to sustain a growth path built on this combination of increasing reliance on exports and a structural rise in the trade deficit. Moreover, as Vos found out, these capital flows reinforced this pattern by pushing up real exchange rates, cheapening imports and squeezing profits for exporters in the short run. [Vos, 2004]

A multi-pronged approach should therefore be constructed in such a way that the real impediments can be removed: unequal treatment, social instability, transition costs, financial constraints, increasing foreign debt. Impediments to trade should be dealt with in conjunction with other macro-economic constraints. The answer to the fears lies in elaborating a world trading system that (1) is truly rules based, (2) guarantees equal treatment of all partners, (3) is comprehensive and in tune with the world financial system and vice versa, and that (4) ensures sustainability. After the end of the Cold War and in response to the international economic stagnation and adjustment of the ninety eighties the world trading system has been reformed, in order to render it more adequate to address the needs could not be taken care of by GATT. [Pronk, 1987] However, the new impetus to globalisation since then demands a further reform of the world economic system, without which claims to further open up economies will not easily be honoured by all participating

countries. This would require, amongst others, a further reform of WTO in relation to a reform of the Bretton Woods system and of international debt management procedures. [Sampson, 2000] [Carlson, 1995]

Benefits and costs

Provided that such a comprehensive, multi-pronged approach could be followed, then the estimates of the gross economic benefits from reducing subsidies and trade barriers by 2010, as summarized in table 3 of Anderson's paper, would not only have a strong theoretical basis but could also become politically realistic. In that table a wide range of estimates has been presented, again with different assumptions. I agree with the author that it would be justified to assume that the comparative static gains could lie somewhere between the extremes presented in the table, because one can assume that many sectors are characterized by oligopolistic market relations and by economies of scale. It would also be justified to assume that the liberalization of markets of goods would be accompanied by services trade reform. In addition to this I agree with Anderson's expectation that the additional dynamic gains from trade will be much higher, in particular for developing countries. So, I have no reason to dispute the summary estimates presented by the author in para 4.1.7 of the paper. Anderson calls these estimates – GDP growth in 2015 of 2.7 % for developed countries, 4.6% for developing countries and thus 3.2% for the world as a whole – conservative. They are indeed conservative in the light of recent experience of reformers such as China, India, Korea and Chili. They are also not overly ambitious when compared with the internationally agreed policy targets for GDP growth of developing countries that since 1960 were laid down in the subsequent Strategies for the United Nations Development Decades. However, though they are conservative and not too ambitious, they will not easily be achieved.

Why not? There are three reasons. First, the benefits are not distributed equally amongst trading partners. The positions taken by various country groups during the first phase of the Doha Round and in particular at the Cancun mid term review, show that countries are aware of this and act correspondingly. To a certain extent this is due to a lack of experience of negotiators in a new setting. This can be overcome. However, there are also substantial differences. Francois et al show that agricultural liberalization offers a mixed set of results, even against expectations: positive for Europe, Asia and Northern Africa, negative for Sub-Saharan Africa, potentially negative for the Asia-Pacific region and North America, neutral for Latin America. The same authors also show that China will be hurt by a liberalization of manufacturing. It will meet stiffer competition from other developing countries and experience a decreasing terms of trade. [Francois, 2003, 2003] Vos, with the help of CGE models for Latin American countries, has found that, unlike the Asian experience, export-led growth in Latin America has proved so far to be anything but a development miracle. He shows that for some Latin American countries free trade under WTO or FTAA will have a negative impact on agriculture which is not compensated by sufficient employment and income growth in other sectors. [Vos, 2004] These are examples only. The results of the calculations depend strongly on the assumptions made. Some assumptions are less realistic than others. Will liberalized and expanding agricultural sectors (with constant returns to scale) really draw substantial resources from modern industry that is characterized by increasing returns to scale? But the examples make clear that, for good reasons, different negotiation partners will have different expectations. This cannot easily be solved, neither in negotiations of a rather limited scope, nor in the framework of negotiations which are fully representative for all interests concerned.

The second reason is that the benefits per country are also distributed unequally. The benefits of international trade policies so far were utterly unequal. These policies were a combination of free trade and protectionism, a la carte, selective, characterized by a fair amount of arbitrariness in the granting of preferences and the mix between reciprocity and non-reciprocity. The benefits were bought at the cost of many poor countries and many poor people, within both more and less advanced economies. Europe, for instance, in combining ACP free trade with the continuation of its Common Agricultural Policy, has done much harm to farmers both

within ACP countries and in other developing countries. Poor farmers world-wide have suffered from the functioning of international commodity markets (sugar, banana's, cotton, rubber, cocoa and others) with decreasing terms of trade, overproduction, subsidies to commodity producing farmers in the USA and the EU, preferential treatments, unilaterally set rules of origin, market speculation and the development of technologically new substitutes. International talks to remove all of these and other barriers will create a new perspective to the victims of these practices. But the winners of today will be the losers of tomorrow and it is not only a matter of rich versus poor. It is much more complicated and this explains why negotiations in the field of trade will have to be complemented by internationally harmonized domestic policies that can result in a fair balance in all countries.

The third reason is that for all negotiation partners there are costs involved. These costs are higher than often is assumed. Anderson, referring to studies in particular of manufacturing in the US and Europe, argues that the costs involved - private costs of adjustment for firms and workers and social costs in the form of social safety nets, unemployment schemes and retraining and reintegration - are minor. They are one-off costs, transitional and should be weighed against the non-stop flow of economic benefits from reform. Anderson does not want to overstate the net gains from trade and therefore presents an estimate of the costs amounting to one third of the gross static benefits, for a period of no more than five years. In my view, however, the costs are much higher. For a number of traditional sectors one cannot speak of one-off costs. The costs involved will have to be born by a full generation consisting of people that can no longer be retrained and reintegrated in the economy. The next generation, the children of workers laid off in extractive industries or in traditional manufacturing enterprises that are downsized or closed, will also be affected. In agriculture the cost will even be born by many more people, not only in the less productive agricultural sectors in Europe and the United States, but above all in developing countries. For many of these people small-scale subsistence agriculture is more than an economic activity. It is a means to survive, a living, a culture, a way of life. Some of these people can be hired as farm laborers, others as unskilled laborers in industry. Many would be fully uprooted, they themselves as well as their families and the next generation. The economic, social, psychological and cultural costs are neither minor, nor one-off or transitional. They are long term, structural and major.

They will be complemented by costs for the environment because traditional production techniques in harmony with the natural environment and with available scarce natural resources will get lost. There will also be a possible loss in terms of the landscape and the biodiversity. All this may easily translate into political costs: more poverty, less cohesion, turmoil. In theory policies to redress and compensate all this ought to be financed out of the benefits resulting from reform. However, as argued above, these benefits often accrue to population strata that cannot easily be taxed by the government, in particular because the reforms take place in the framework of an economic philosophy that emphasizes the market and demands a retreat of the public sector. Moreover, not all such costs are of an economic character, lending themselves for specific forms of compensation. And they last much longer than a transition period of five years. All this explains a reluctance of governments to engage themselves in opening up their economies. The reason is not only, as argued by Anderson, that the losses in jobs and asset values are concentrated, whereas the gains in terms of new jobs and investment opportunities are thinly spread, and are less attributable to trade reform, taken up by people other than those losing from the reform. For many countries and sectors this is a relevant political analysis, not only in the western industrialized countries, but also in developing countries such as India, where the middle class is benefiting from new opportunities due to the opening of markets such as in information services. However, in many sectors and countries, in particular in agriculture in less advanced Northern economies and in the Third World, it is the other way around: the losses are widely spread and cut deeply into the existence of people while the initial concrete benefits are concentrated in the hands of a new class. Whether there will be also long term benefits in the form of structural employment opportunities for many people is often uncertain, also because new industries, often financed with foreign capital, disregard the comparative advantage of the countries involved and choose rather capital intensive production

technologies. Especially nowadays, in a more and more globalised economy, the ample availability of labor becomes a relatively less important factor in decisions of enterprises to invest and to choose a particular location. The resulting uncertainty is for governments an additional reason to go slow with reforms.

For these reasons I am less positive than Anderson about the relation between trade reform and poverty alleviation. Trade reform can reduce the income gap between developed and developing countries, provided that it takes place within a comprehensive approach. In doing so trade reform will enhance the capacity and help increasing the resources necessary to implement pro poor policies within poorer countries. Trade reform also will contribute to higher economic growth within developing countries. Whether the increased capacity will be used for that purpose, however, will depend on the policies pursued and on the economic and social structure of the country. Market reforms can also lead to new distortions and new inequalities, to the detriment of the poor people, and to more rather than less poverty. As has been documented by many studies, since the early nineties inequalities have widened both within and between countries. That phenomenon took place at the same time that, parallel to increasing trade and a strong emphasis on economic liberalization and market reform, world economic growth was very high and sustained for a long period, without precedent. The conclusion is warranted that the world has never been so rich as in the period just before the end of the Millennium. Foreseeing this after the end of the Cold War, in 1992 at the World Summit on Environment and Development, governments had promised to use the additional resources, which would be set free by reforms and growth, for the implementation of policies to reduce poverty. Commitments were made to increase international income transfers to poor countries and to carry out specific anti-poverty programs in the fields of water, health, education and food and agriculture. A decade later we must admit that this promise has not been kept. International assistance went down, anti-poverty programs stagnated, inequalities increased and the number of poor people in terms of income poverty as well as human poverty is as high as it used to be. No wonder that poor countries are suspicious with regard to the promise that new trade negotiations after Doha will lead to less poverty. Some market liberalization in the field of agriculture, for instance, will lead to increased consumer prices in food importing developing countries. Other reforms will result in upsetting traditional agrarian systems and land use patterns, depriving the poor from the use of essential resources. Market reforms aiming at price liberalization, a retreat of the public sector and more incentives for private enterprise in essential sectors such as health and education have similar consequences. It not only a matter of good governance along the lines set out in studies such as the ones by Dollar and Kraay that could countervail this. [Dollar and Kraay, 2002] Criteria of good governance accompanying market reform, as advocated since 1990, and applied in international policies concerning trade, finance, aid and debt have often produced a counterproductive effect. Governments were more or less forced to diminish public efforts to decrease poverty. [Pronk, 2001, 2003] Expectations similar to the ones quoted by Anderson on the basis of recent studies and estimates concerning the number of poor people in rural areas which could find a better living after reforms, because there would be an increased demand for both farm products and their off farm labor have also have been raised fifteen years ago. They have not been fulfilled. China was an exception, but in Africa and in South Asia urban and rural poverty increased, despite a certain degree of liberalization. [UN, 2003] One could perhaps say that these reforms did not go far enough, but those who realize how much policy change has been implemented since 1980, first as a necessity due to adjustment policies, later on the basis of the universally applied Washington Consensus, will understand the skepticism regarding the acclaimed future speed and depth of further reforms.

Trade and environment

A similar line of reasoning would apply to the relation between trade reform, economic growth and the environment, including climate change. I will only briefly touch upon this. The logic of the argument resembles the discussion of the relation between trade reform and poverty alleviation. Rather than assuming that trade does have a direct impact on the environment, be it positive or negative, I prefer to discuss environmental effects as resulting economic activities in the real sphere, such as investment, production and

income growth, transportation, consumption, exploitation of natural resources, including energy. All such economic activities in the real sphere are linked through trade. It is trade that facilitates their combination and provides them with more opportunities to create value added. So, environmental consequences result not from trade in isolation, but from trade in combination with one or more of the other economic categories. For instance, more free trade resulting from a decrease of trade distorting agricultural and energy subsidies, will produce a positive environmental effect because of the reallocation of resources and production following this trade liberalization. In para 4.3.2 of his paper Anderson rightly points out that there are many examples of such win-win relations in the field of trade and environment. I agree with Sampson that, even within the present WTO framework, this offers opportunities which regrettably still seem to be neglected. [Sampson, 2000]

Not all expanded trade in combination with increased investment and production results does have negative consequences for the environment. Anderson refers to the fact that, contrary to fears expressed at the beginning of the new phase of economic globalisation, when international investment started to pick up again, there was no systematic race to the bottom in environmental standards. He also points out that trade, in so far as this does lead to poverty alleviation, can result in less harmful land use patterns (less slash-and-burn agriculture). It may also result in a substitution of non-renewable sources of energy (wood cutting, for instance) by other sources. The same is true for a substitution of coal by environmentally less harmful sources of energy that could result from the removal of coal subsidies.

In my view, however, trade in combination with activities in the real sphere of the economy does have other environmental effects as well: increased energy use, increased use of other scarce natural resources, risking depletion, loss in animal welfare, spread of animal diseases, loss of biodiversity, climate change, depletion of fish resources, over-utilization of water resources, land degradation due to overgrazing and so on. Trade is not the culprit. Production and consumption are. But specific trade policies, including trade liberalization, have consequences for investment, production and consumption patterns, for land use systems and transportation systems. Trade policy rules, as agreed in WTO, to a great extent determine the use of the world's resources. Of course, it is also the other way around: trade and the opportunities for trade policy-making are influenced by developments and decisions in the other areas and by technological change. But this means that the combined effects for the environment cannot be neglected when choices in the field of trade itself are on the agenda. The discussion of environmental consequences of our economic behavior should also be brought within the scope of world trade talks.

Sustainability

Poverty alleviation and environmental concerns, together with food security and access to medication and some other issues, are sometimes called the 'non-trade concerns' in international trade. At the 2002 Johannesburg Summit on Sustainable Development they were high on the agenda. Calls have been made on trade negotiators to broaden the Doha agenda in order to incorporate the so-called sustainability questions into the talks. Within WTO there is still a reluctance to do so.

This is understandable, because the incorporation of other concerns than trade as such would further complicate the process. It is also understandable in so far as negotiators believe that more free trade, next to higher growth, on balance always will result in less poverty, less environmental damage and more sustainability. Empirical evidence as well development theory teach us that this is not automatically the case. Specific conditions ensuring an integrated and comprehensive approach will have to be fulfilled. I have mentioned a few of these conditions above. Many are of a political character. Meeting such conditions is not only a non-trade concern. It would also be in the interest of trade itself. When policy makers are uncertain about specific consequences of trade liberalization, they may refrain from it. When trade liberalization brings about unintended harm for a society, a backlash may result.

For many governments the main challenge is to create new jobs for ever more new young people without unduly destroying jobs for others. Failing to do so will have major social and political consequences, world-wide. When expectations are not met, when aspirations are violated, when unemployed young people are denied a fair perspective, economic instability, social unrest, political strife and violence may result. People, without a stake on the labor market, in particular the young among them, may feel themselves excluded not only from the economic system, but from society as a whole. In reaction to this they may turn against society. To bring openness and fairness into a society is a first responsibility of policy-makers in the economy, including trade.

Presently the process of globalization seems to strengthen economic forces that are in favor of trade liberalization. But there always will be a natural inclination to protect. It is a struggle between entrepreneurship and fear. Where fear prevails, protectionism will be on the rise. Stemming a return to protectionism as an unintended result from a combination of policy reactions - out of fear, or in order to guard specific interests against dangers from outside - is perhaps even more important than to enforce further liberalization. But a defensive approach would not suffice. It is important to keep the economy dynamic and oriented towards innovation. A standstill would easily turn into regress. Rendering trade policy making more comprehensive could be a contribution towards such a dynamic approach.

The question is not whether the stakes are high, or how high they are, but how to translate them into action.

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