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## **Special Treatment and Policy Space for the Developing Economies in the Multilateral Trade Regime**

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The contemporary multilateral trading system comprises members ranging from high-to very low-income countries; this range has a bearing on the operations of the multilateral trade regime. Presence of a large number of low-income members is the new systemic reality. Special and differential treatment (SDT) has operated for the developing economies, principally for the small, low-income ones, for many decades. The concept of SDT grew in three basic stages, on which this article elaborates. Theoretically this concept was meaningful and significant, but in reality it has not engendered substantial benefits to the intended beneficiary groups, the developing economies. The Uruguay and the Doha Rounds of multilateral trade negotiations (MTNs) reaffirmed faith in SDT. The Doha Development Agenda (DDA) was clear about reaffirming the importance of SDT to the multilateral trade regime and referred to it as an integral part of the WTO Agreement. During the Fifth Ministerial Conference in Cancún and the subsequent WTO meeting in Geneva in July 2004, small developing countries held together as the Group-of-Ninety (G-90). They made their presence felt in the Hong Kong Ministerial Conference as well. As SDT has not spawned large benefits for the target groups of countries, there is a pressing need to refine the concept. Academics and policy makers have debated over what future shape SDT should take so that it will be able to meet the expected goals. Taking these concerns into account, this article presents a comprehensive set of recommendations.

Keywords: developing economies, Doha Round, multilateral trade regime, policy space, special and differential treatment

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Patience and perseverance have a magical effect before which difficulties disappear and obstacles vanish.

—John Quincy Adams

## 1. Introduction

This article dwells on the diversity-driven special treatment of the developing economies in the multilateral trade regime. The concept of “special and differential treatment” (SDT) materialized early during the General Agreement on Tariffs and Trade (GATT) period. During the lifetime of the GATT the concept of SDT developed in several stages. Developing countries were given non-reciprocal preferences under SDT by the industrial economies. Being on the lower rungs of the economic ladder, they also need some policy space. This consideration has been a part of the multilateral trading system for decades. Whether the target economies have benefited from the SDT, and if they have by how much, remains open to debate. The developing economies have used SDT for *inter alia* securing preferential access to the markets of the industrial countries. SDT has taken varying forms and been related to different trade issues. Numerous categories of preferential market access schedules have been given to developing countries under different agreements and arrangements. In recent years SDT has intensified for low-income developing countries, and the least-developed countries (LDCs)<sup>1</sup> were granted preferential market access by the industrial economies under the Generalized System of Preferences (GSP), a large category of market-access schedules. The Doha Development Agenda (DDA) had definite objectives in this area, and the possible new shape of SDT was deliberated during the Doha Round of multilateral trade negotiations at length before its collapse, which followed a prolonged stagnation.

Section 2 of this article traces the concept of SDT and its intellectual origins, while section 3 focuses on various beneficiary-country groups. The issue of hierarchies of beneficiaries is the focus of section 4. What sort of new shape SDT is likely to take under the Doha Round is analyzed in section 5. Many small and low-income developing countries are concerned that trade liberalization under the Doha Round will erode their preferences. Section 6 analyses whether this apprehension is justified. Section 7 concludes and summarizes.

## 2. Special and Differential Treatment

The members of the WTO range from very high-income to very low-income countries. In terms of stages of growth, institutional development, resources and capacity constraints they cover a large spectrum. The WTO does not have a definition

of developing economies, although some supranational institutions, for example the World Bank, provide closely worded definitions not only of developing economies but also of various subgroups among them. In the case of the WTO, it is the member that decides and announces its status itself; that is, members declare whether they are “developed” or “developing” countries. However, other members can challenge the decision of a member to make use of provisions available to developing countries. Due to the fact that members represent a wide diversity in economic and institutional resources, their ability and willingness to incur costs associated with implementation of new multilateral trade rules varies significantly. So does their ability to derive benefit from such rules. The implementation and adjustment costs associated with new regulations are almost always borne by the developing economies, because these rules essentially represent the status quo in the mature industrial economies and are passed on to the developing economies as the best practices.

Over the decades, the traditional approach in the multilateral trade system for the developing economies has been to seek benefits under SDT. This was a part of the process of evolution of the multilateral trade regime. It goes back to the period when negotiations for the International Trade Organization (ITO) were going on in 1946 and 1947 (Narlikar, 2006). What does the term SDT precisely entail? It captures the GATT/WTO provisions that (i) allow high-income countries to grant preferential access to their markets to some developing economies, (ii) allow the developing economies the right to limit reciprocity in multilateral trade negotiations (MTNs) to levels “consistent with development needs”, (iii) give them exemption from some WTO obligations, many of which are transitory and some permanent, (iv) give them extra time periods to comply with obligations, (v) allow developing economies greater freedom to use otherwise restricted trade policies and (vi) provide technical assistance and help in institution building so that WTO obligations can be fulfilled and negotiated decisions implemented. The basic philosophical premise behind the provisions of SDT is simple and logical: the developing economies are provided SDT on the premise that their industrial development depends on assistance for some time in both their home markets (by way of protection) and in their export markets (by way of preferences in the form of lower tariffs and fewer non-tariff barriers).

### ***2.1 Intellectual Foundation of Special and Differential Treatment***

SDT is an obvious departure from the all-important most-favoured nation (MFN) principle of the GATT/WTO. The history of SDT is as old as the GATT/WTO system itself. Not only has it existed since the inception of the GATT, it also had a significant history in the multilateral trading system. Raul Prebisch and Hans Singer were the

intellectual fathers of the concept. They argued that during the 1950s and 1960s the exports of the developing economies were concentrated in the area of primary products and commodities, which were characterized by volatile prices and steadily deteriorating terms of trade. Therefore, they (along with Ragnar Nurkse) propounded the strategy of import-substituting industrialization (ISI), supported by high rates of protection for the infant domestic industries in the developing economies. The rationale that infant industries needed protection from international competition is reflected in the “policy space” argument, which posits leeway in the implementation of WTO for the developing economies. Although the infant industry argument is accepted by economic theory, this group of economic theorists applied it a little too comprehensively and indiscriminately. Consequently, in the economies that followed the ISI strategy, the infant industries remained infants for decades – until many of them touched their middle ages. South Asian and Latin American economies avidly followed the ISI strategy in the 1950s and beyond. The second premise behind SDT was that trade liberalization under the MFN clause was not enough for the small and low-income developing countries to be able to expand their trade and thereby accelerate their growth rates. These low-income economies needed preferential market access in the industrial countries’ markets through instruments like SDT. To that end, various programs under the auspices of the GSP were considered necessary.

In international fora such as the United Nations General Assembly and subsequently in the United Nations Conference on Trade and Development (UNCTAD) the developing economies lobbied for equitable outcomes in the GATT system, rather than merely equitable processes, so that preferential treatment could be institutionalized for them. As the GATT did not have institutional mechanisms like majority voting and coalition building, these efforts had to take place outside the GATT. These lobbying efforts achieved some measure of success in the form of Article XVIII of the GATT-1947.<sup>2</sup> In the initial stages SDT was limited to the provisions of Article XVIII, which both allowed developing economies to void or renegotiate their commitments and limited infant industry protection. A modification that took place in 1954-55 was inclusion of Article XVIIIb, which allowed the developing countries use of quantitative restrictions (QRs) for balance-of-payments reasons.

Developing economies continued their endeavours to have the objective of growth and development included in the agenda of the supranational institutions. The 1960s was designated as the UN Development Decade. This turned out to be a fruitful period for the developing economies, during which they achieved more successes. The second defining moment in the development of the concept of SDT came during the Kennedy Round (1962-67), when Part IV on the benefits to and obligations of the

developing economies was introduced in the Articles of Agreements of the GATT-1947. Added in 1965, Part IV of the GATT was devoted to trade and development. It provided for discriminatory “advantages” for developing countries during the MTNs. The Committee on Trade and Development (CTD) was established. It is noteworthy that much of the language of Part IV suggested good intentions rather than obligations. The developing economies were explicitly relieved of any requirement to reciprocate the benefits provided by the industrial economies. Recognition of the principle of non-reciprocity by the industrial economies was an unprecedented measure. Article XXXVI of Part IV acknowledged the wide income disparities between the developing and industrial economies and emphasized the need for rapid economic advancement in the developing economies by means of “a rapid and sustained expansion of the export earnings of the less-developed contracting parties.” In 1971, a waiver was adopted to temporarily legitimize the GSP under the GATT system. These were significant epistemic and institutional developments, and for the first time the developing economies were able to introduce a concept of fairness in the GATT system.

## ***2.2 Enabling Clause***

The third important period in the life of SDT came during the Tokyo Round (1973-79). What SDT entails was further clarified and made a formal element of the multilateral trading system in 1979, when the Enabling Clause was introduced. It established that the developing economies were exempted from Article I, the MFN clause of the GATT-1947.<sup>3</sup> The Enabling Clause legally established the principle of non-reciprocity in trade negotiations, in turn facilitating more favourable treatment and preferential market access for the developing countries in the mature industrial economies. In negotiations in different rounds of MTNs, reciprocity for them was limited to levels “consistent with development needs”, as specified in the Enabling Clause. In addition, they were provided with greater freedom to use trade policies than the GATT rules otherwise permitted. SDT also entailed the cost of implementation of WTO agreements. The Enabling Clause effectively made GSP a permanent feature of the multilateral trade regime and further extended discriminatory preferences to the UN-designated LDCs group.

The Enabling Clause had a “graduation principle” associated with it. This was an important qualification, which made it clear that the developing countries enjoying the benefits of GSP are to go off the GSP list when they move up the ladder of economic growth. The Enabling Clause was to be understood as an impermanent measure devised for a specific objective. Its graduation principle clearly implied that the developing economies are to assume their normal reciprocity in multilateral trade

liberalization when the time comes to do so. The MFN and reciprocity were the fundamental principles of the GATT; their waivers were granted only to support the economic growth process.

Thus, development objectives were covered by Article XVIII of the GATT-1947 and, subsequently, the GATT-1994. Conceived in a considerate manner, Article XVIII not only permits the developing economies to use their trade policies in pursuit of economic development and industrialization, but also imposes a weaker discipline on them than on the industrial economies in several areas of GATT/WTO regulations. It also exhorts the industrialized countries to take into account the interests of the developing economies in the application of GATT disciplines. The Enabling Clause made SDT an essential element of the GATT system and disciplines. With prescience, the Enabling Clause also required that, as economic development gathers momentum, the developing economies would try to improve their capacity to gradually reciprocate concessions. This was christened the process of “graduation”. Subsequently, several preferential trade agreements (PTAs) have been created under the Enabling Clause.<sup>4</sup>

### ***2.3 Discriminatory System of Preferential Market Access***

The SDT is a system of preferences; it is, by definition, discriminatory. Historically, efforts to operationalize SDT essentially centred on preferential market access through the GSP. To this end, there has been a long-standing trend of unilateral discriminatory liberalization, which was operationalized through offering tariff- and quota-free market access for the small and low-income developing economies, particularly the LDCs. This group comprises economically vulnerable countries. If fully implemented, the discriminatory liberalization schemes could certainly make SDT more effective than it has been in the past.

Unilateral market access could not be offered to the developing economies that do not fall under the LDC category, because to do so would be a political impossibility in the industrial economies.<sup>5</sup> Therefore, the absolute poor of the global economy cannot benefit from SDT because a large proportion of them live in South Asia and Sub-Saharan Africa. While all of these economies come under the category of developing economies, not all of them are LDCs. This means that the absolute poor can only benefit if trade liberalization proceeds multilaterally, in a non-discriminatory manner.

## **3. Beneficiaries of Special and Different Treatment**

Over time, non-reciprocal trade preferences became a part of the relationship between the developing and industrial economies in the multilateral trade regime. The SDT principle has operated for the developing economies, principally for the small and low-income ones, for many decades. In the recent period such

preferences have deepened, particularly for the LDCs and the African, Caribbean and Pacific (ACP) economies. Noteworthy among the SDT schedules are the Everything-But-Arms (EBA) initiative by the European Union and the parallel U.S. initiative, the African Growth and Opportunity Act (AGOA). The SDT schedules usually exempt certain products from tariffs. Exports of bananas, rice and sugar are not covered under the EBA. As many as 144 developing countries and customs territories presently benefit from the GSP schedules of the Organization for Economic Cooperation and Development (OECD) countries (IMF, 2006).

Theoretically this concept is meaningful and significant, but in reality it has not engendered substantial benefits for the intended beneficiaries. There are several reasons for this failure. The preferential market access schedules under SDT were designed voluntarily by the industrial economies, which chose both the eligible countries and the products for their respective schedules. It has been observed that, first, the selected countries and products generally lacked capacity to export and, second, countries and products with export potential were excluded from the schedules. Third, when the market preferences were granted, the preference schedules were laden with restrictions, product exclusions and administrative rules in the form of documentary requirements.

Schemes like the EBA and AGOA could potentially have a good deal of favourable impact on exports from the beneficiary economies, but those benefits depend primarily upon the supply-side capabilities in these economies. Supply-side constraints have seriously limited potential use of SDT schedules. Second, documentary requirements by the preference-granting countries for ascertaining the origin of exports, or the so-called rules of origin (ROO) requirements, tend to work as a real administrative barrier and reduce the utilization rate of the GSP schedules. This applies particularly to some of the large export sectors, such as textiles and apparel. Third, most LDCs have failed to benefit from the GSP schedules because of costs and uncertainties created by product exclusion (Brenton, 2003). Fourth, the strategy of granting non-reciprocal market access to LDCs under various GSP schedules has not turned out to be effective. Preferences are not enforceable commitments under the WTO. Consequently, many of these schedules have worked merely as exhortations. They did not go beyond “best endeavor” promises that were subjected to numerous restrictions.

Fifth, overall coverage of these schedules applied to only a tiny portion of exports of small and low-income developing economies. Experiences under various GSP schedules reveal that the eligible countries are able to utilize only a small part of the preference granted to them. Their utilization rate is quantified. The exports of eligible countries under various preferential schemes form a very small part of EU and U.S.



imports. Over the past three decades they have ranged between 0.9 percent and 0.4 percent of total annual imports of the EU and the United States (WB, 2004). Sixth, the preference schedules are characterized by trade diversion; that is, they divert trade with the ineligible developing countries. Finally, preferential market access schedules do not benefit the target groups of population referred to as the absolute poor of the world.<sup>6</sup>

While there are a large number of eligible recipients of the benefits of SDT, not all of them have benefited. Numerous studies have shown that while some developing economies have benefited from non-reciprocal preferences to a significant degree, others have not benefited at all (Ozden and Reinhardt, 2003; Grossman and Sykes, 2005). With regard to which developing economies have benefited, the foremost group is a small subset of relatively more advanced developing economies of Asia, which have gradually acquired the status of emerging-market economies (EMEs). The supply-side scenario in this small group is better developed than in the other small, low-income developing economies. Also, they put to good use the export revenues generated. This group not only has the wherewithal to export the products but also efficiently meets the administrative requirements – preparation of documents required by the preference-granting countries. This subset of economies has not allowed ROO to become an effective barrier. It was observed that liberal ROO were a critical factor for eliciting a strong response from the potential beneficiary economies, particularly in products like textiles and apparel.<sup>7</sup>

According to statistics compiled by the World Bank (2004), in 2001 130 countries were eligible for SDT. According to the International Monetary Fund this number was 144 in 2006 (IMF, 2006). Of these, 10 countries accounted for 77 percent of U.S. non-oil imports under its GSP. The same 10 countries accounted for 49 percent of all GSP imports to all the industrial countries that were providing GSP. Occasionally a small developing country did benefit substantially from preferential market access where domestic prices were raised above the world market prices by tariffs, subsidies or other trade-distorting mechanisms. For instance, Mauritius, which exports sugar and enjoys preferential access to the EU markets, benefited a good deal from this opportunity. However, these benefits to Mauritius came at a high cost to the EU taxpayers and consumers (WB, 2004).

A comparison of beneficiary countries that were eligible for the U.S. GSP and those that were recently graduated from it revealed that the latter category outperformed the former in terms of export performance. Countries that were no longer on the GSP eligibility list had higher export-to-GDP ratios, as well as higher export growth rates in real terms. One explanation for the success of the countries that graduated from the U.S. GSP-eligible list that seems rational is that it appears that the

GSP provided a stimulus to their export industries. While care must be taken in attributing causality, GSP seemingly helped the graduating countries to engender supply-side capabilities, which strengthened with the passage of time and turned these small developing economies into successful trading economies. The flip side of the coin is that mere GSP eligibility cannot turn them into successful exporters. Reform of their macroeconomic policy structures must have played a decisive role.

#### **4. Hierarchies of Beneficiaries and Preferential Market Access**

**I**n the hierarchy of beneficiaries from preferential market access, the most preferred countries are those that are part of a regional integration agreement (RIA) with the preference-granting economy. Trade partners in an RIA commonly have close trade and economic ties. This trade relationship is usually reciprocal in nature. The LDCs, which enjoy unilateral preferences or free market access, come next in terms of importance. Other small developing economies with which the preference-granting economies have a GSP relationship are the last. GSPs are unilateral in nature and are devised for large country groups of beneficiaries.

Several unilateral preferential market access programs were devised as GSPs by the industrial economies as well laid out, structured and customized programs that were intended to be carefully implemented. Each one of them had characteristic features regarding eligibility criteria, product coverage and administrative rules in important areas such as ROO. Together these criteria determine which developing countries are excluded and which can benefit from the customized unilateral preferential market access schedule. The programs devised and implemented by the United States include the AGOA, the Caribbean Basin Initiative and the Andean Trade Promotion Act, as well as several unilateral and reciprocal trade agreements with Israel and Jordan. The principal EU programs include the Cotonou Convention, which includes the African, Caribbean and Pacific (ACP) countries, and the EBA initiative targeting the LDCs. The EU has also entered into a large number of unilateral and reciprocal trade agreements with the North African, Middle Eastern and Mediterranean economies.<sup>8</sup>

The characteristic features of unilateral and reciprocal trade agreements differ from GSP schemes in several important respects. For instance, some sectors (such as textiles and apparel, processed foods, etc.) are treated as “sensitive” items and usually excluded from the GSP. These sensitive sectors of trade are included in some unilateral and reciprocal trade agreements. For instance, by 2009, the EBA initiative will cover *all* the exports of the target group of countries. All protectionist measures will be eliminated for imports into the EU economies from the 50 LDCs. However, an

unseen restriction in this is that the products that matter most to LDCs (rice, sugar and bananas) were not to be liberalized until after 2006. Their liberalization begins in 2007 and will become complete in 2009. Second, under the unilateral and reciprocal trade agreements, administrative requirements tend to be more relaxed in comparison to the more comprehensive GSP schemes, particularly regarding the ROO.

Despite recent improvements in the implementation of these programs, as mentioned earlier the overall imports into the industrial economies under various preferential schemes have remained diminutive, almost insignificant. (The textile and apparel exports from small African economies that came under the AGOA to the United States represent an exception; these exports recorded significant gains.) In 2001, imports by the Quadrilateral (or Quad) countries<sup>9</sup> from the GSP-beneficiary economies amounted to \$588 billion, of which \$298 billion were subject to normal trade and non-trade restrictions while \$184 billion came under various preferential trade programs. That is, the coverage of these programs was 38.9 percent of the eligible exports, which in turn received market access preference. In 1991, this proportion was 51.1 percent. Thus the proportion of coverage of eligible exports declined during the decade of the 1990s (Inama, 2003). A similar quantitative study by Haveman and Shatz (2003) produced comparable, although slightly different, evidence of coverage.

## **5. Special and Differential Treatment in the Doha Round**

Subsequent rounds of MTNs (the Uruguay and Doha Rounds) have reaffirmed **S** faith in SDT. The DDA was clear about reaffirming the importance of SDT to the multilateral trade regime and referred to it in the Doha Communiqué as “an integral part of the WTO agreement” (paragraph 44). SDT figures in several places in the Doha Communiqué. The objective of the DDA in this area is clearly laid down in paragraph 2 of the Communiqué as “... we shall continue to make positive efforts designed to ensure that developing countries, and especially the least-developed among them, secure a share in the growth of world trade commensurate with the needs of their economic development. In this context, enhanced market access, balanced rules, and well targeted, sustainably financed technical assistance and capacity-building programmes have important roles to play” (WTO, 2001).

Recognizing that SDT had not succeeded in imparting large benefits to the target group of beneficiaries, participating members called, in paragraph 44, for a review of the SDT schedules so that their provisions could be strengthened, “making them more precise, effective and operational” and enabling SDT to fulfill its objectives (WTO, 2001). As the benefits of SDT were to be provided through enhanced market access,

balanced rules, and well targeted, sustainably financed technical assistance, a good case exists for rethinking all three channels so the benefits can be more precisely targeted for the groups that need them most. Affirming the good intentions of the negotiators, the Doha Communiqué provided (in paragraph 14) a deadline of March 2003 for reestablishing the new modalities of SDT. The deliberations and dialogues on this issue continued all through 2002 and 2003.

Notwithstanding the upbeat commitments expressed in firm language in the Doha Communiqué, during these deliberations WTO members not only were deeply divided on important SDT matters, but also had opinions that were significantly far apart from each other. They could not approach a consensus or an agreement of any kind. The deep division among WTO members on the scope and design of SDT was indubitably a reflection of their wide diversity in terms of income levels, stages of growth, capacity and institutional constraints, national policies and investment priorities. The foregoing sections have pointed to differences in each member's ability and willingness to bear the burden of cost associated with implementation of WTO rules, as well as the payoffs they are likely to receive from these rules.

### ***5.1. Official Commitments to Special and Differential Treatment***

After the failure of the Fifth Ministerial Conference in Cancún, the so-called July Framework Agreement was arrived at during the last day of July 2004. In this agreement the General Council of the WTO reaffirmed that provisions for SDT are an integral part of the WTO agreements. The council not only reaffirmed the DDA objective of strengthening them, but also recommended making them more "precise, effective and operational". The Committee on Trade and Development (CTD) began a review of SDT. The council instructed the CTD to expeditiously complete the review of all the outstanding agreement-specific proposals regarding SDT and report to the General Council, with clear recommendations for a decision, by July 2005. The CTD, within the parameters of the Doha mandate, was asked to address all other outstanding work, including on the cross-cutting issues, the monitoring mechanism and the incorporation of SDT into the architecture of WTO rules. However, the CTD after several meetings failed to make concrete recommendations to the General Council. Members continued to have strong and fundamental disagreements on several issues.

The General Council reviewed and recognized the progress that has been made since the beginning of the negotiations of the Doha Ministerial Conference in expanding trade-related technical assistance (TRTA) to small and low-income developing countries and economies in transition. In furthering this effort the council affirms that such countries, and in particular the LDCs, should be provided with

enhanced TRTA and capacity-building assistance to increase their effective participation in the negotiations, to facilitate their implementation of WTO rules and to enable them to adjust and diversify their economies. In this context the council welcomed and further encouraged improved coordination with other agencies, including under the Integrated Framework (IF) for TRTA for the LDCs and the Joint Integrated Technical Assistance Program (JITAP) (WTO, 2004). This did give an impression that SDT is being taken up for serious review and at the end of the Doha Round should emerge stronger than ever.

The Hong Kong Declaration of December 18, 2005, once again reaffirmed that the provisions for SDT are an integral part of the WTO agreements (WTO, 2005). In paragraphs 35 through 38 of the Hong Kong Ministerial Communiqué members expressed their determination to fulfill the DDA mandate spelled out in paragraph 44 of the Doha Ministerial Declaration as well as in the July Framework Agreement, that all SDT provisions would be reviewed with a view to “strengthening them and making them more precise, effective and operational”. Official recognition was given to “lack of progress” in the Hong Kong Declaration; accordingly, the CTD was again instructed to “expeditiously complete the review of all outstanding agreement-specific proposals and report to the General Council, with clear recommendations for decision”, this time by December 2006.

### ***5.2 Refining and Strengthening the Concept of Special and Differential Treatment***

In view of the fact that SDT has not spawned large benefits for the target groups, academics and policy makers have debated over what future shape SDT should take so that it will be able to meet the expected goals.<sup>10</sup> In their various official pronouncements, the ongoing Doha Round negotiations have given additional importance to this debate, because this is *inter alia* being seen as an opportunity to refine the SDT system. As alluded to above, while WTO members have found agreement on SDT elusive, there is some degree of agreement among analysts and researchers on the new shape of SDT. Their recommendations are thoughtful and comprehensive and are summarized as follows. First, a bold unilateral measure such as a general reduction by 2010 in all MFN tariffs in the industrial economies to 5 percent on labour-intensive exports from the small and low-income developing economies, and to 10 percent on their agricultural exports, will indeed reduce impediments such as the ROO-related documentation requirements. The target date for achieving Millennium Development Goals (MDGs) is 2015. By this time all tariffs on exports of manufactured products from the developing economies should be eliminated.

Second, as with the first recommendation, industrial economies need to unilaterally expand market access for LDCs and simplify the ROO requirements. This will circumvent some of the problems presently related to the GSP schedules.

Third, in keeping with the spirit of the first and the second recommendations, developing economies, on their part, should slash their tariff barriers on the basis of an agreed formula-based approach. Such action would amount to their reciprocation to the measures taken by the industrial economies. It will help in keeping the multilateral trade regime balanced.

Fourth, paragraph 2 (d) of Article I of the GATS refers to international trade in the supply of services through the presence of natural persons in a foreign country when both the country of origin and the recipient country are members of the GATS. Such provision of services is known as Mode-4. Industrial economies should make binding commitments to expand temporary access of service providers by a specific proportion of the workforce, say, 1 percent. Judged by the present level of temporary access, this indeed is a large measure and will realistically take some time to implement in a phased manner without disturbing the domestic economies in the industrial countries.

Fifth, acceptance of the principle of policy space for the small and low-income developing economies under WTO discipline would go a long way in helping many of these economies. They may be permitted to decide whether or not to implement a new set of WTO rules, as long as their non-implementation does not significantly impair the trade interests of other WTO members.

Sixth, the developing economies, on their part, need to accept the core discipline of WTO on market access, including undertaking liberalization commitments. This may, however, be done in a differentiated manner across the entire spectrum of developing economies.

Seventh, the multilateral trade system needs to explore feasible channels for meeting the special institutional development needs of low-income developing economies and LDCs.

Eighth, the industrial economies need to meet the trade-related technical assistance needs of the small and low-income developing economies.<sup>11</sup>

None of the above proposals are novel and revolutionary; these or similar expansion of SDT have been discussed in the past. However, if they are deliberated, promoted and adopted during the Doha Round, the final outcome would indeed be supportive of development in the small and low-income developing economies and the LDCs. The name DDA would then ring true.

## **6. Erosion of Non-reciprocal Preferences**

As mentioned earlier, a large number of developing economies are eligible to receive benefits from one GSP schedule or the other. These developing economies, particularly WTO members from the ACP group and LDCs, have an additional concern about the erosion of non-reciprocal trade preferences during the Doha Round. As the industrial economies slash their tariffs on imports from all of their trading partners under MFN-based multilateral trade liberalization, the value of trade preferences previously granted to these country groups will erode decisively, adversely affecting the competitiveness of their exports.<sup>12</sup> To that extent, these small and low-income developing countries believe that the MTNs render them vulnerable. To be sure, loss due to preference erosion – which will drive down competitiveness enjoyed exclusively due to the GSP – will be partly offset by expanding multilateral market size and higher world prices. However, some of these economies fear serious loss of their export markets and expect setbacks in their export revenues. They have become indifferent to general MFN trade liberalization by lowering tariffs and elimination of quotas and have begun resisting and resenting the MFNs. This conflict has pitted a small number of low-income and some medium-income economies against the interests of the other developing economies.

It was pointed out in the preceding section that, first, not all the developing countries have gained a lot from the GSP schemes that were devised for them. Second, the high degree of apprehension related to preference erosion due to MFN-based liberalization is not supported by empirical research. A comprehensive study of the non-reciprocal preference-recipient countries inferred that these countries as a group did not lose from preference erosion following MFN-based trade liberalization in the Doha Round, although significant gains and losses underlie the estimates of the average (Low and Piermartini, 2005). Low and Piermartini's research (using a Swiss formula, with a coefficient of 10) showed that the beneficiaries of GSP schemes of the Quad countries plus Australia enjoy a net gain of \$2 billion in terms of the value of adjusted preference margins on non-agricultural products. Almost all LDCs either lose from preference erosion, or they are unaffected by it because their exports are MFN tariff-free. Their loss was estimated at \$170 million, not high by any normal standard. However, a significant effect of preference erosion was found for LDCs exporting textiles and apparel.

Using elaborate cross-country analysis, Alexandraki and Lankes (2004) quantified the impact of preference erosion and inferred that it is a source of vulnerability for a small set of countries that have enjoyed deep preferential access to the markets of the Quad and that have an undiversified export base and a heavy export dependence on the Quad markets alone. The ability to absorb the impact of preference erosion will

necessarily depend upon an economy's competitiveness in the affected sectors and upon its macroeconomic robustness. Alexandraki and Lankes's calculations revealed that the magnitude of potential shock in a realistic, realizable scenario was small. It ranged between 0.5 percent and 1.2 percent of the total exports of the countries for the sample countries, and was dependent upon the elasticity of export supply. This small impact of preference erosion was also spread over time, in accordance with the liberalization schedule established under the Doha Round. Nevertheless, for a small subset of economies the shocks of preference erosion could be significant. Estimates show that small island countries that enjoyed deep preferences in the Quad markets due to historic, cultural or geo-political reasons in the EU (in the case of banana and sugar exports) and the United States (in the case of sugar exports) have suffered most under the MFN liberalization under the Doha Round.

## **7. Conclusions and Summary**

**I**t is a significant fact that the members of the multilateral trade regime presently range from very high-income to very low-income countries. This reality of global economic life has a bearing on the operations of the multilateral trading system. Given the large variation among members in terms of their economic and institutional resources, their ability and willingness to incur costs associated with implementation of new multilateral trade rules also varies. So does their ability to derive benefit from new rules. Over the decades, the traditional approach of the developing economies, which were at lower income levels, has been to seek benefits from the industrial economies under SDT. This was a part of the process of evolution of the multilateral trade regime.

The concept of SDT grew in three basic stages. In the first stages SDT was limited to the provisions of Article XVIII of the GATT-1947, which allowed developing economies to void or renegotiate their commitments. The second defining moment in SDT came during the Kennedy Round, when Part IV on the benefits to and obligations of the developing economies was introduced in the Articles of Agreement of the GATT-1947. The third important period in the life of SDT came during the Tokyo Round. What SDT entails was further clarified and made a formal element of the multilateral trading system in 1979, when the Enabling Clause was introduced.

SDT has operated for the developing economies, principally for the small, low-income ones, for many decades. Non-reciprocal trade preferences became a part of the relationship between the developing and industrial economies in the multilateral trade regime. In the recent period such preferences have deepened, particularly for the LDCs and the African, Caribbean and Pacific (ACP) economies. Theoretically this concept is meaningful and significant, but in reality it has not engendered substantial



benefits to the beneficiary developing economies. Empirical research on this issue concluded that not many developing countries have benefited from SDT. There are several reasons for this failure. The beneficiaries of SDT, particularly WTO members from the ACP group and LDCs, have an additional concern, that is, the erosion of non-reciprocal trade preferences during the Doha Round. Empirical research on preference erosion has concluded that apprehension related to erosion from MFN liberalization is over-stated.

As sovereign countries, a large number of small and low-income developing economies and LDCs are now members of the WTO. As their number grew, this category of countries acquired a good deal of influence in the multilateral trade system and its decision-making process. During the Fifth Ministerial Conference in Cancún, and the subsequent WTO meeting in Geneva in July 2004, this subgroup of small developing countries held together as the Group-of-Ninety (G-90). This subgroup presently dominates the WTO system – even though they are small trading economies. The new systemic reality of the multilateral trade regime is diametrically opposite to that of the early decades of the GATT system. The evolving multilateral trade regime will need to adapt to the expectations and needs of this country group.

It is widely recognized that small and low-income developing countries stand to gain in the long term from trade liberalization and integration into the multilateral trade regime. There are short-term macroeconomic adjustments, which in turn lead to immediate adjustment costs. However, the short-term macroeconomic adjustment costs are small relative to the long-term efficiency gains.

Subsequent rounds of MTNs (the Uruguay and Doha Rounds) have reaffirmed faith in SDT. The DDA was clear about reaffirming the importance of SDT to the multilateral trade regime and referred to it as “an integral part of the WTO agreement”. As it has not spawned large benefits for the target groups, there is a pressing need to refine the concept of SDT. Academics and policy makers have debated over what future shape SDT should take that would enable it to meet its goals. A comprehensive set of recommendations has been presented for this purpose.

The small and low-income developing economies need appropriate policy space to accommodate their requirements. They need greater flexibility in trade policy implementation, and they need to be able to pursue policies that would otherwise be subject to strict multilateral discipline. It is prudent to give small and low-income developing countries a choice in the implementation of a specific set of new trade regulations, as long as this measure does not impose significant negative spillovers on other members.

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## Endnotes

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1. In 2006, the United Nations classification of LDCs included 50 countries, of which 30 are members of the WTO and 5 are observers.
2. In discussions of international trade, the two expressions the GATT-1947 and the GATT-1994 are frequently used. The latter is the revised version of the original GATT Agreement of 1947. The text of the agreement was significantly revised and amended during the Uruguay Round, and the new version was agreed upon in Marrakesh, Morocco. Apparently, the GATT-1994 reflected the outcome of negotiations on issues relating to the interpretations of specific articles. In its renewed version, the GATT-1994 includes specific understandings with respect to GATT articles, its obligations and provisions, plus the Marrakesh Protocol of the GATT-1994.
3. Although *most-favored nation* sounds like a contradiction, implying some kind of special treatment to a particular trade partner, in WTO jargon it means non-discrimination, that is, treating all trade partners under the WTO regime equally. Each WTO member treats every other member as its “most-favoured” trading partner. If any country improves the market benefits to one trading partner, it is obliged to give the same best treatment to all other WTO members, so that they all remain “most-favoured”. However, historically MFN did not mean equal treatment.
4. For instance, the Caribbean Basin Initiative (CBI), the Lome Convention, the Cotonou Agreement, the NAFTA Parity Act, the Central American Common Market (CACM) and the CARICOM Common Market are some of the PTAs that were created under the Enabling Clause.
5. The developing economies, according to the World Bank (2006) definition, are divided into various subgroups. These subgroupings are available in *Classification of Economies* on the Internet at <http://www.worldbank.org/data/countryclass/countryclass.html>. Economies are classed according to 2003 per capita gross national income. The groups are as follows: low-income developing countries, \$765 or less; lower-middle income, \$766 - \$3,035; upper-middle income, \$3,036 - \$9,385; and high income, \$9,386 or more.
6. The definition of *absolute poor* is based on subsistence, the minimum standard needed to live. Robert McNamara, who coined this term, defined it as “a condition of life beneath any reasonable standard of human dignity.” There has been a long drawn debate in the discipline regarding whether income or consumption poverty lines should be defined in absolute or relative terms. Most international organizations define the poverty line in an absolute way as the “level of income necessary for people to buy the goods necessary to their survival.” In keeping with this concept, the dollar-a-day line, at 1985 purchasing power parity, is extensively used in academic research and by policy makers (Bourgignon, 1999). However, a broader definition of poverty would be the general lack of the capabilities that would enable a person to live a life he or she values; such a definition would encompass such domains as income, health, education, empowerment and human rights.
7. See for instance Brenton (2003) and Brenton and Manchin (2002).

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8. See Das (2004) for these details, in particular chapter 3, as well as Schiff and Winters (2003).
  9. Canada, the European Union, Japan and the United States are the four Quadrilateral countries.
  10. Some recent studies are those by Oyejide (2002), Hart and Dymond (2003), Hoekman, Michalopoulos and Olarreaga (2003), Hoekman, Michalopoulos and Winters (2003), Hoekman et al (2003), Hoekman, Michalopoulos and Winters (2004) and Hoekman (2005). These recommendations on SDT have been drawn from the studies enumerated here.
  11. Ibid.
  12. Several researchers have addressed these issues. See for instance Hoekman, Michalopoulos and Winters (2003), Messerlin (2003) and Wolf (2003).

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