



The benefits of trade liberalization

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Economies

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Outline

- Trade and protection in agri-food products post-Uruguay Round
- The gains-from-trade arguments
- Key reason why trade barriers remain
- What the WTO can contribute
- Model-based evaluations of DDA
- Conclusions

The OECD

A forum where the governments of 30 member countries work together to address the economic, social and environmental challenges of globalisation, and engage in dialogue with 70 other countries, based on analysis, information and policy advice

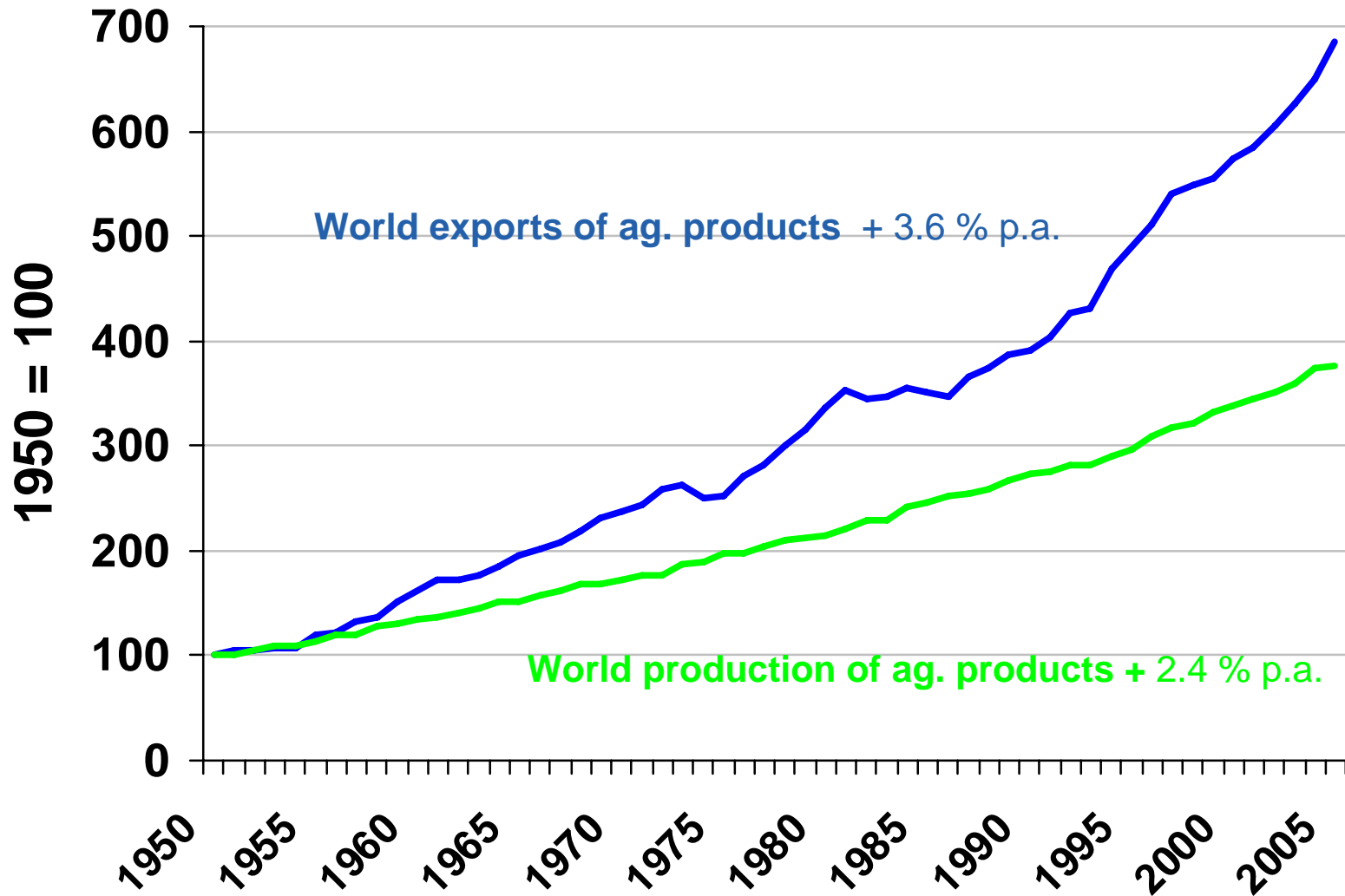
OECD work on food and agriculture...

Provides comparative economic and policy analysis, information and advice to support government efforts to improve the domestic and international performance of their food and agricultural policies

...which specifically includes

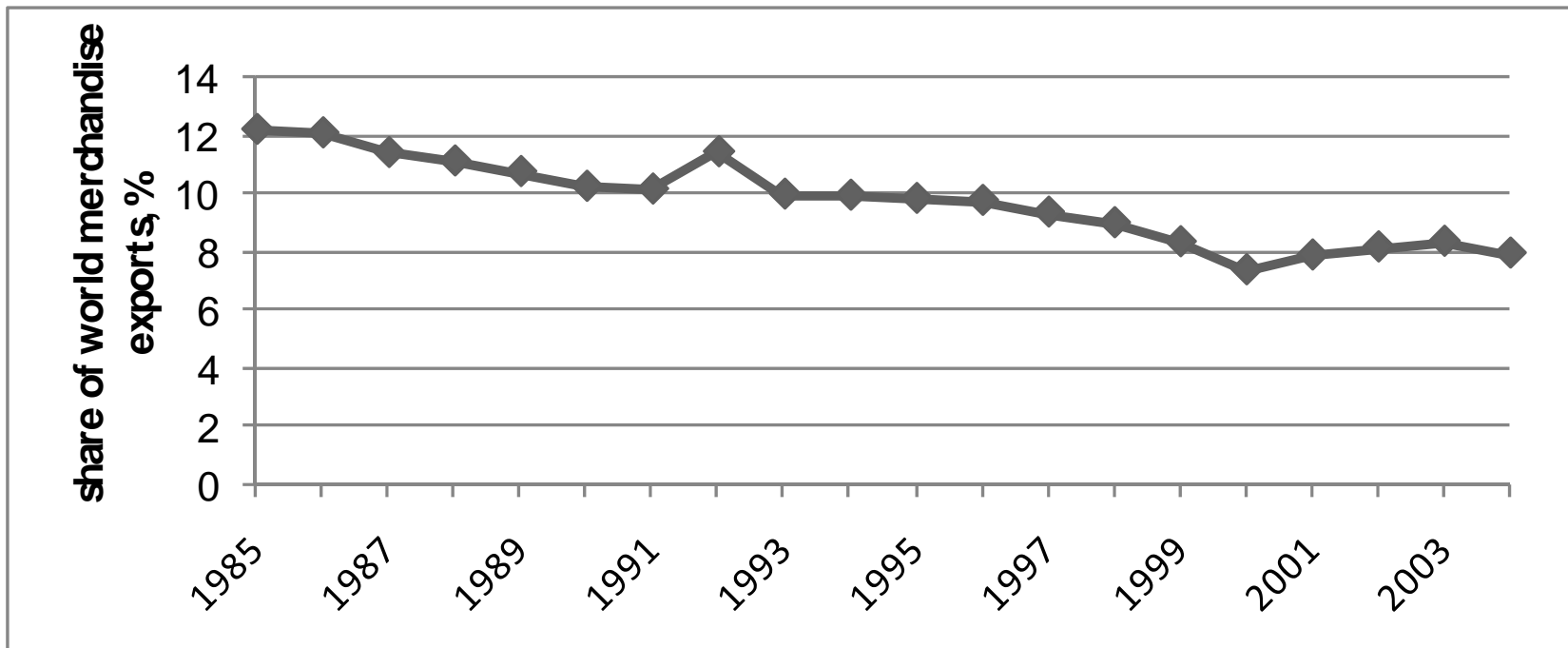
- Monitoring & evaluation of agricultural policies
- Generating outlook for agricultural markets
- Analysing key policy developments
- Quantifying domestic & trade policy impacts
- Defining characteristics of good policy design
- Talking with policy-makers and wider public

Global agricultural exports grow dynamically



Source : WTO

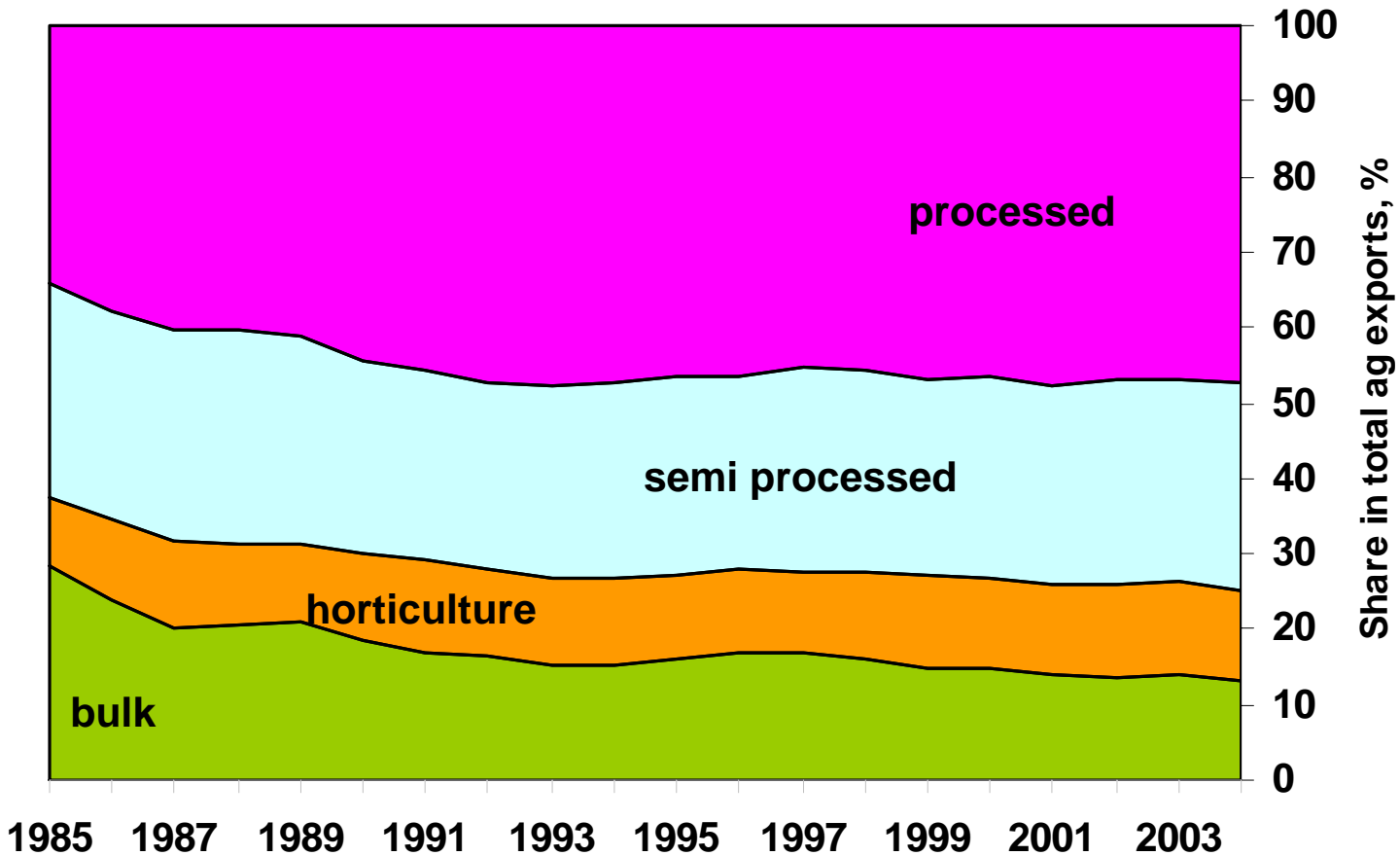
... but share of agriculture in world trade declines



Source : OECD, based on UNCTAD/TRAINS/WITS



... and most 'agricultural' trade is
in processed products



Source : OECD, based on UNCTAD/TRAINS/WITS

Bilateral trade patterns in agri- food, 2001

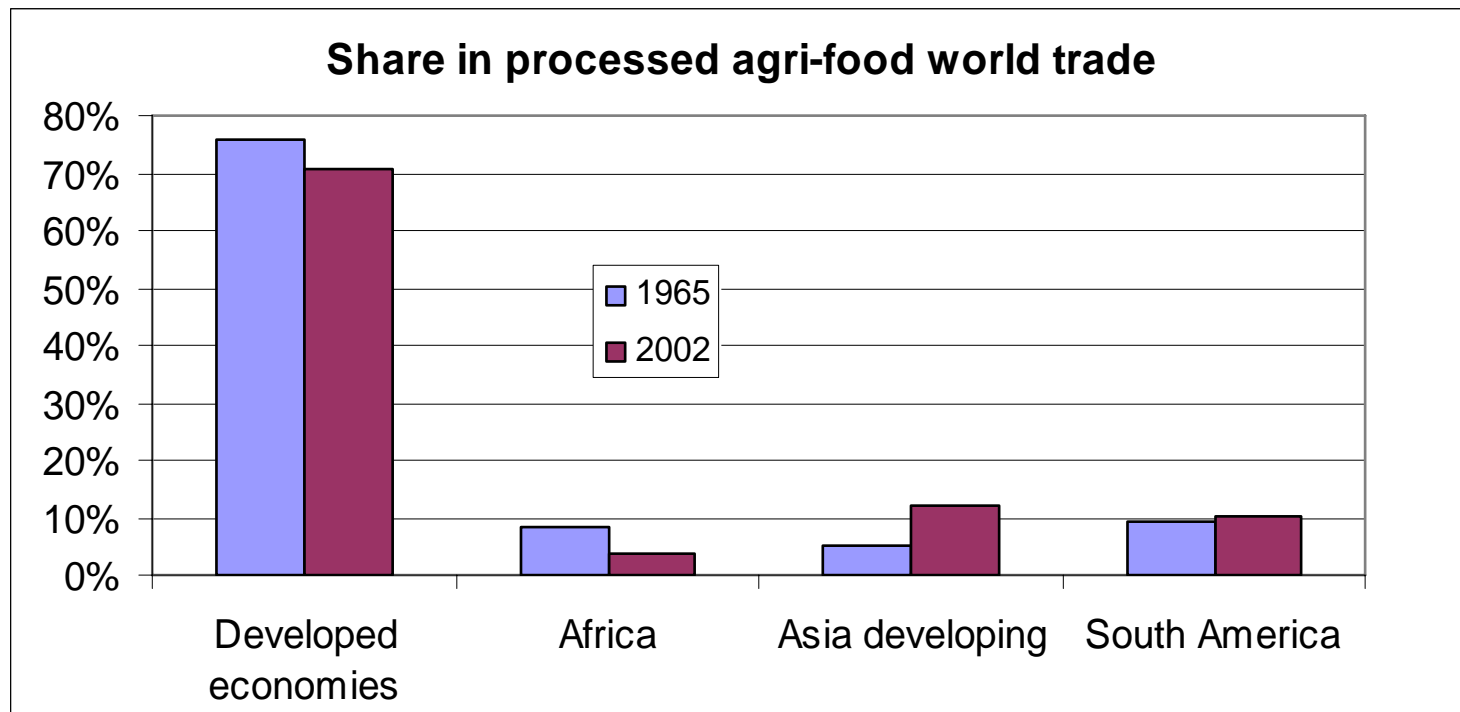
from / to	Developed economies	CEEC & CIS	Africa	Asia developing	South America	Total
Developed economies	77%	4%	7%	7%	6%	100%
CEEC & CIS	48%	34%	11%	6%	1%	100%
Africa	58%	5%	28%	7%	1%	100%
Asia developing	58%	3%	10%	28%	1%	100%
South America	62%	5%	9%	9%	16%	100%
Total	71%	5%	9%	10%	6%	100%

Source: GTAP v6,

Who is in business?

Africa and South America have declining or constant shares in the high growth processed markets.

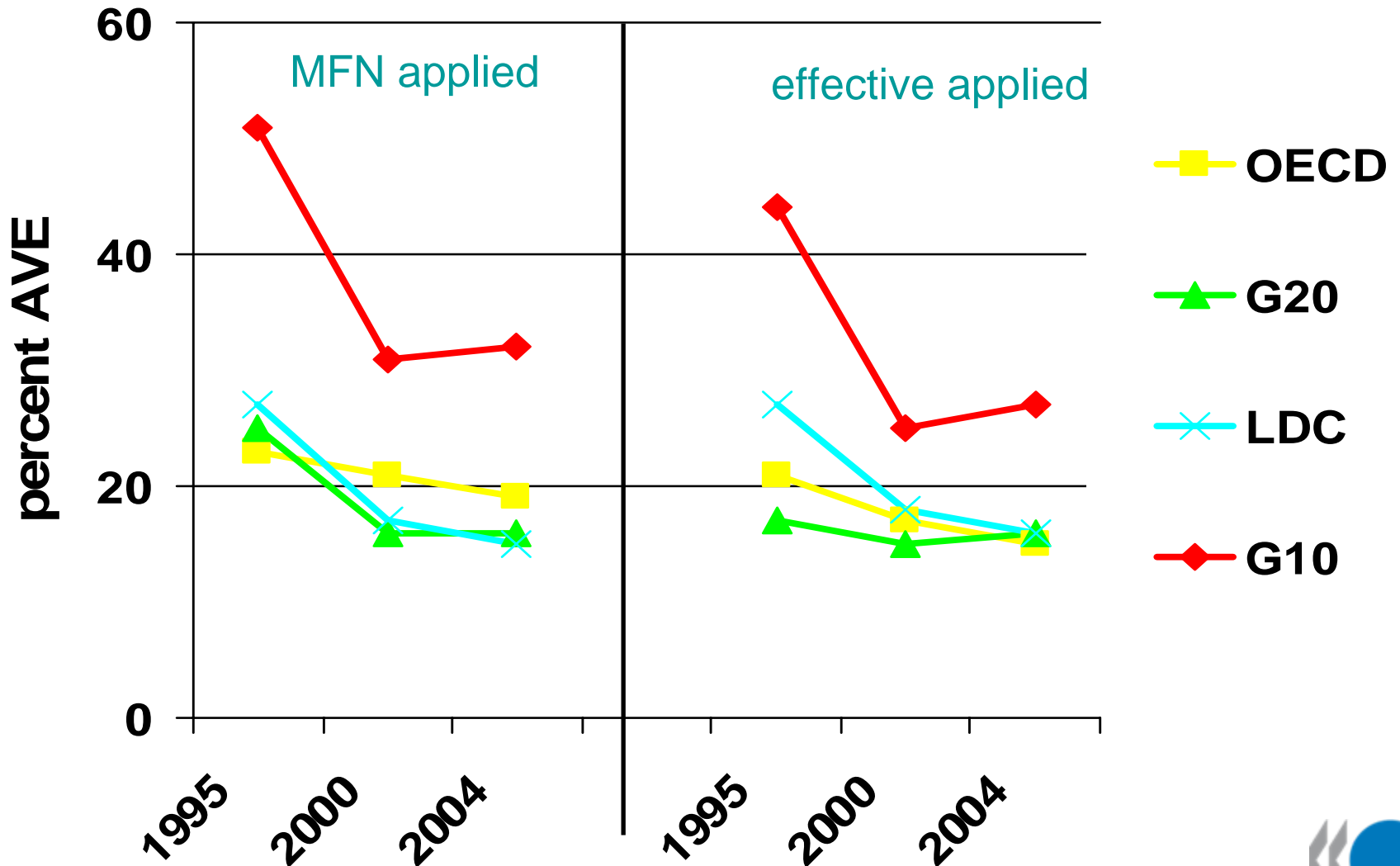
Asian developing countries diversify more in recent years



Source: GTAP v6,

Tariffs declined

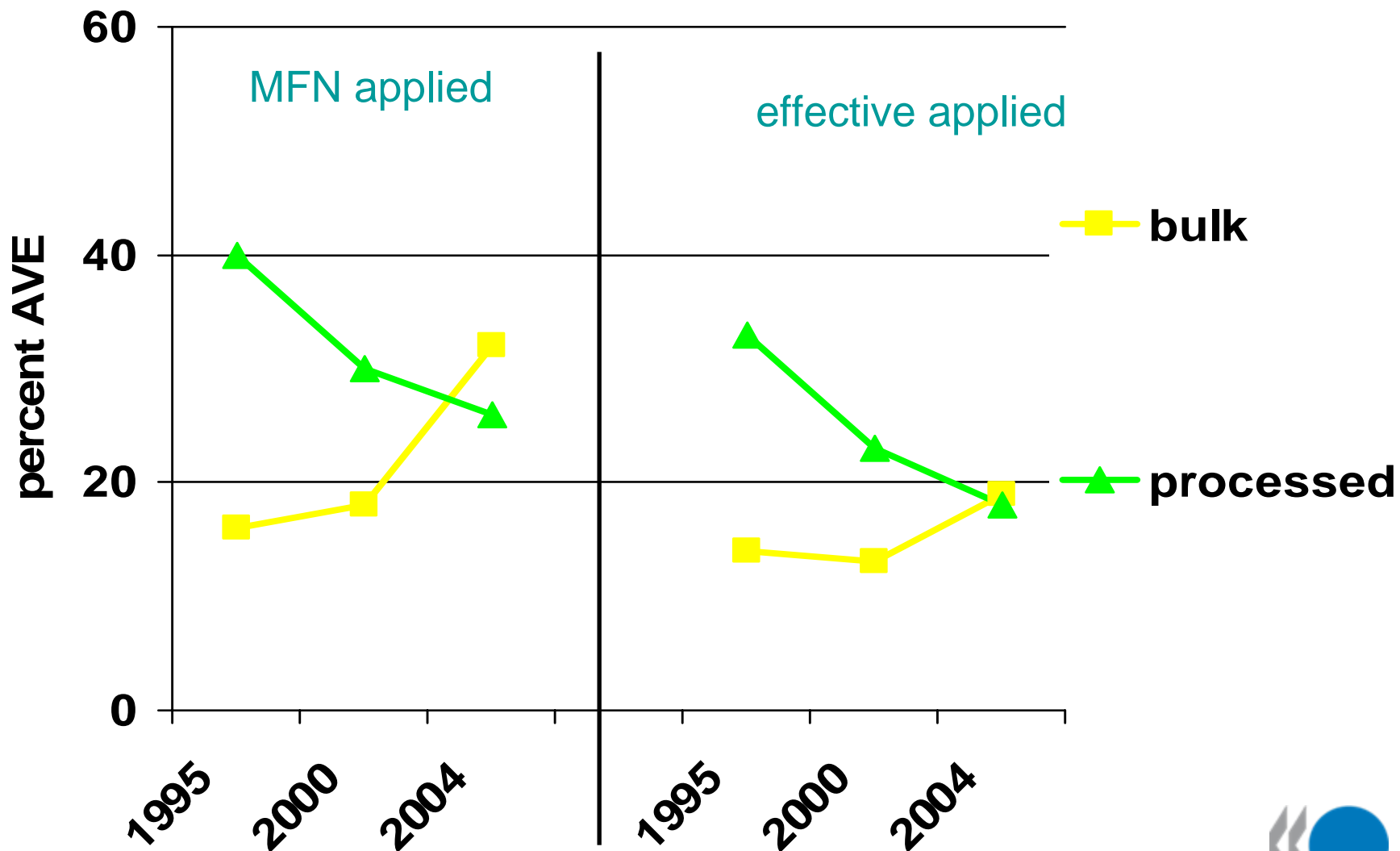
Simple average of all agricultural products



Source : OECD, based on UNCTAD/TRAINS/WITS

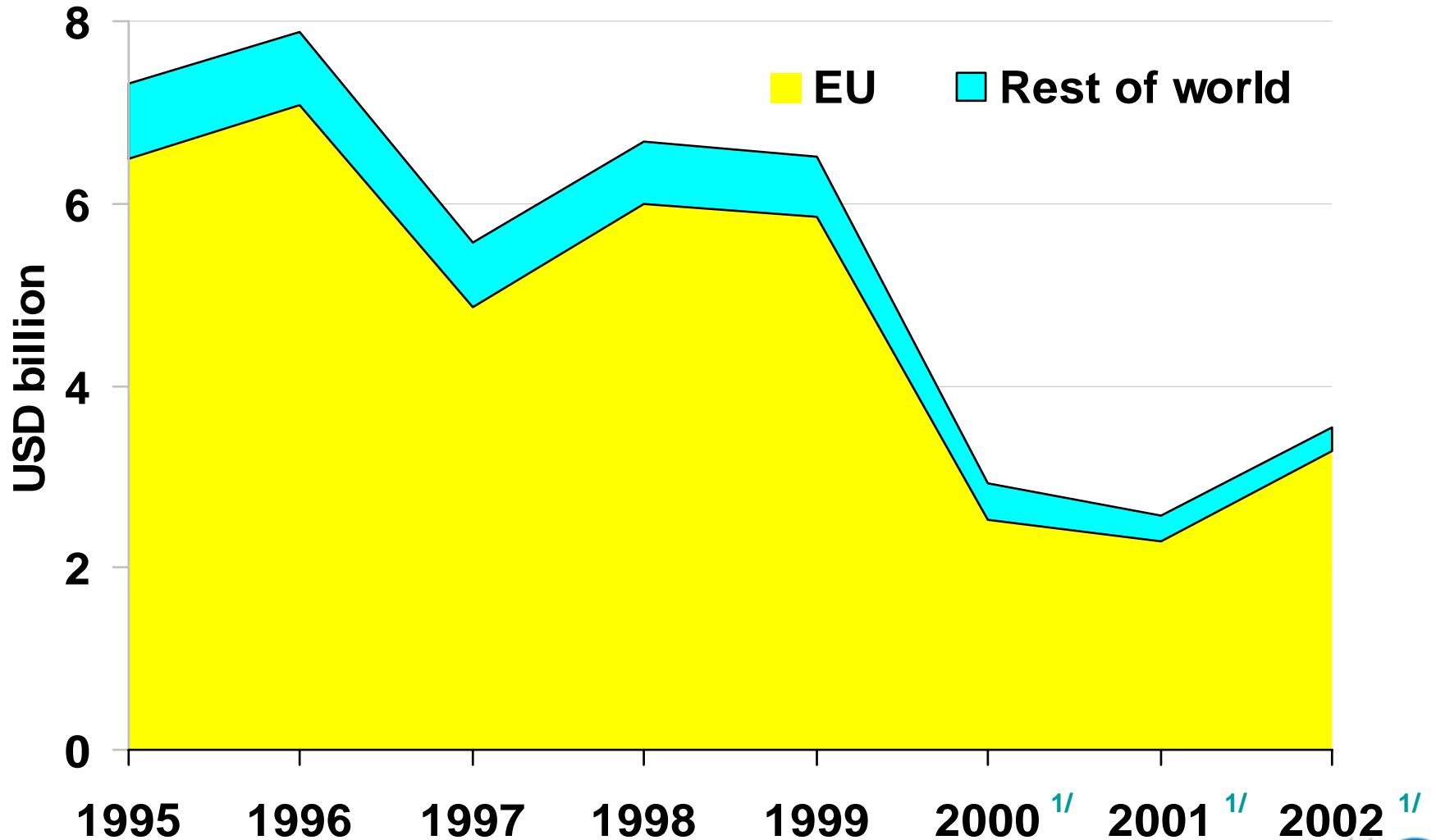
... but more so for processed products

Average of OECD countries



Source : OECD, based on UNCTAD/TRAINS/WITS

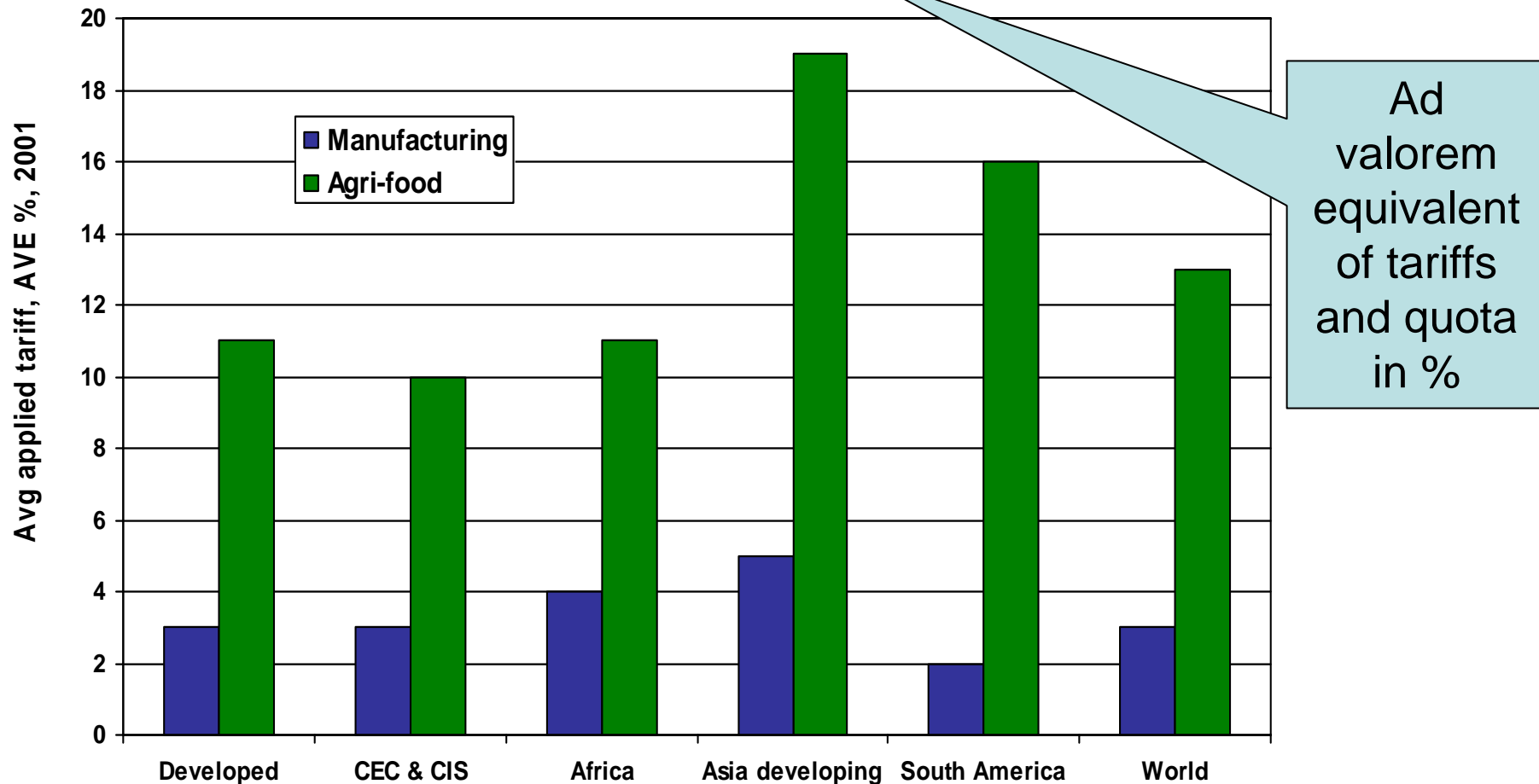
Direct export subsidies declined



^{1/} Not all countries have notified as yet for this year

Source: ERS calculations from WTO notifications

Manufacturing trade less restricted than agri-food trade, AVEs 2001



Source: GTAP v6

Outline

- Trade and protection in agri-food products post-Uruguay Round
- The gains-from-trade arguments
- Key reason why trade barriers remain
- What the WTO can contribute
- Some research results
- Conclusions

Arguments for removing trade barriers and subsidies

- Standard gains-from-trade argument: allows nation's resources to be used to exploit its comparative advantages by specializing its production in what it does best
- That in turn can increase (esp. in small economies):
 - scope for exploiting economies of scale,
 - capacity to deal with natural disasters
 - competitiveness of domestic markets,
 - variety of products available to producers and consumers,
 - enhanced learning and technological catch-up (esp. via FDI)
 - less wasteful rent-seeking lobbying activities by protectionist groups

Arguments for removing trade barriers and subsidies

(continued)

- Empirical evidence: there are many examples of reformed economies that have boomed
 - and none of booming closed economies
- Not to say openness is *sufficient* for sustained rapid economic growth, but it is a *necessary* condition
 - Other necessary conditions include:
 - macroeconomic and political stability,
 - rule of law and establishment of property rights,
 - efficient provision of public goods (incl. safety nets), and
 - absence of distorting domestic policies

Developing countries' arguments for retaining agric protection

include ...

- Stabilize food prices
- Provide food security/self sufficiency, esp. in the case of food-deficit countries
- Offset terms of trade deterioration
- Slow the depopulation of rural areas

BUT, all those policy objectives can be achieved more efficiently by means other than protection from import competition, none of which are prevented by WTO

So why do most governments still retain protectionist policies?

- Because some workers and owners of some productive resources, and less-competitive farmers, fear that they will lose from reform, and that social safety nets will not fully compensate them
 - Any losses would be concentrated in the hands of a few, while gains will be small per capita for the many benefitting firms or consumers,
 - so the latter have less incentive to counter the former's lobbying
- A political equilibrium can involve protection

What can alter the political equilibrium level of protection?

- Wider dissemination of information on the gains from trade
- Technological innovations that lower trade costs (e.g. ICT revolution), or increased openness abroad, both of which increase the incentive for exporters to lobby for reduced protectionism by their home government
 - such globalization forces raise the rewards from good economic governance -- and raise the cost of poor economic governance (e.g., via FDI)
 - more countries are looking to open up, and that is easier if done when others do likewise

Why WTO trade negotiations make reform easier

- They offer scope for exchange of market access
 - And more so the larger the number of countries taking part in a negotiating round and the broader the product and issue coverage
 - ➔ Hence, WTO negotiations offer far more scope than regional or bilateral negotiations

What else does WTO offer?

- Exporters receive MFN treatment in markets abroad
 - A major improvement for those now facing sanctions
- Access to WTO's dispute settlement process
- Opportunity to 'bind' tariff commitments so as to avoid future policy back-sliding
- Requirements to make policies more transparent
- All of which reduce business uncertainty and so encourage more investment

What was different about the 1980s that brought agric to the Uruguay Round?

- CAP-generated surpluses led to disposal via EU export subsidies
- US (& Canada) retaliated in kind
- Pushed real food prices in int'l markets to century's lowest level by 1986
 - which more than doubled the welfare costs of agricultural protection over the 1980s (Tyers and Anderson 1992)

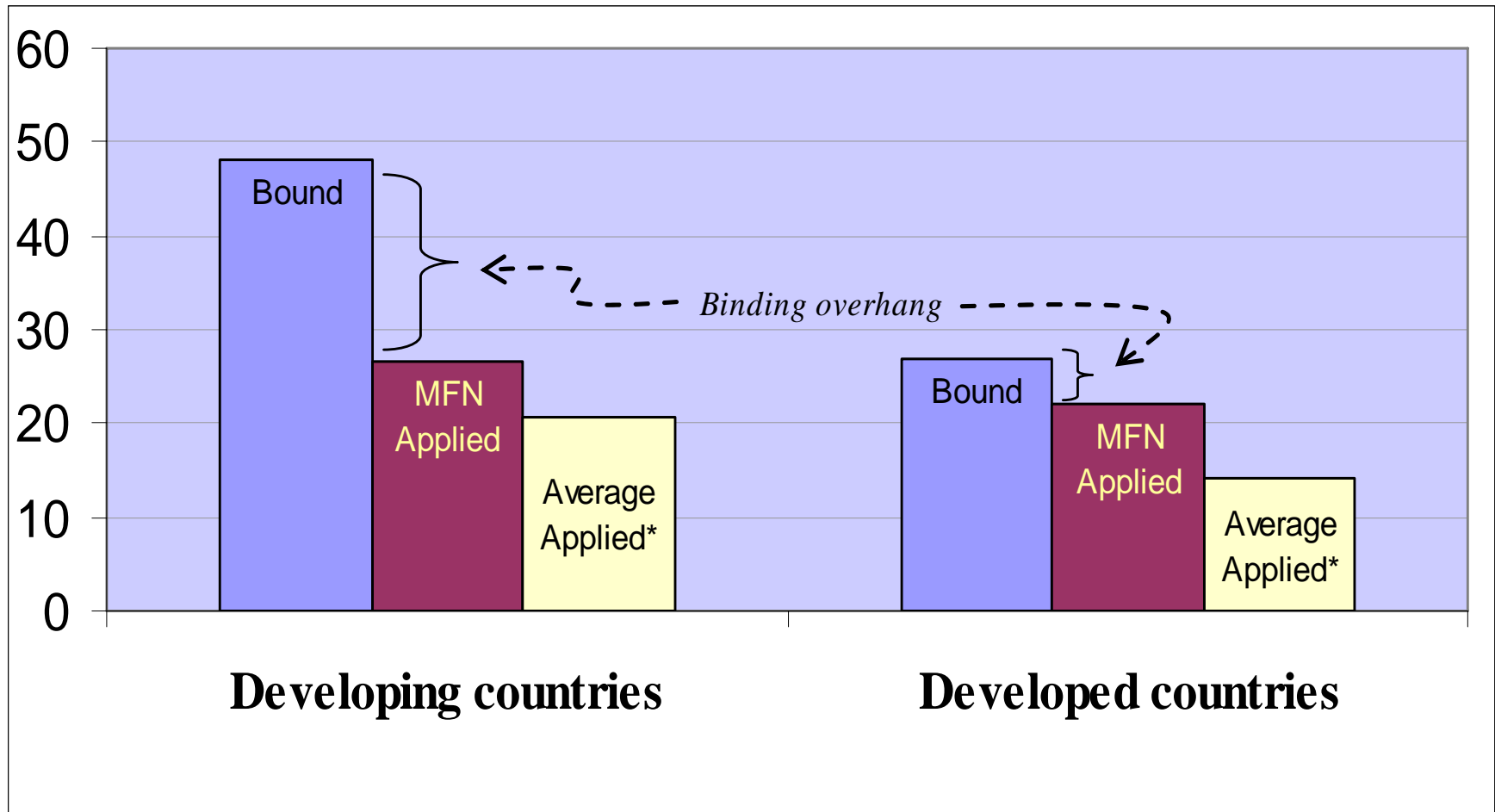
Who brought agriculture into the UR?

- US farmers were hurt more by EU policies than EU farmers were by US policies
- Australia/NZ and food-exporting developing country farmers were affected hugely
 - led to formation of Cairns Group in 1986, whose sole aim was to keep agriculture high on UR agenda

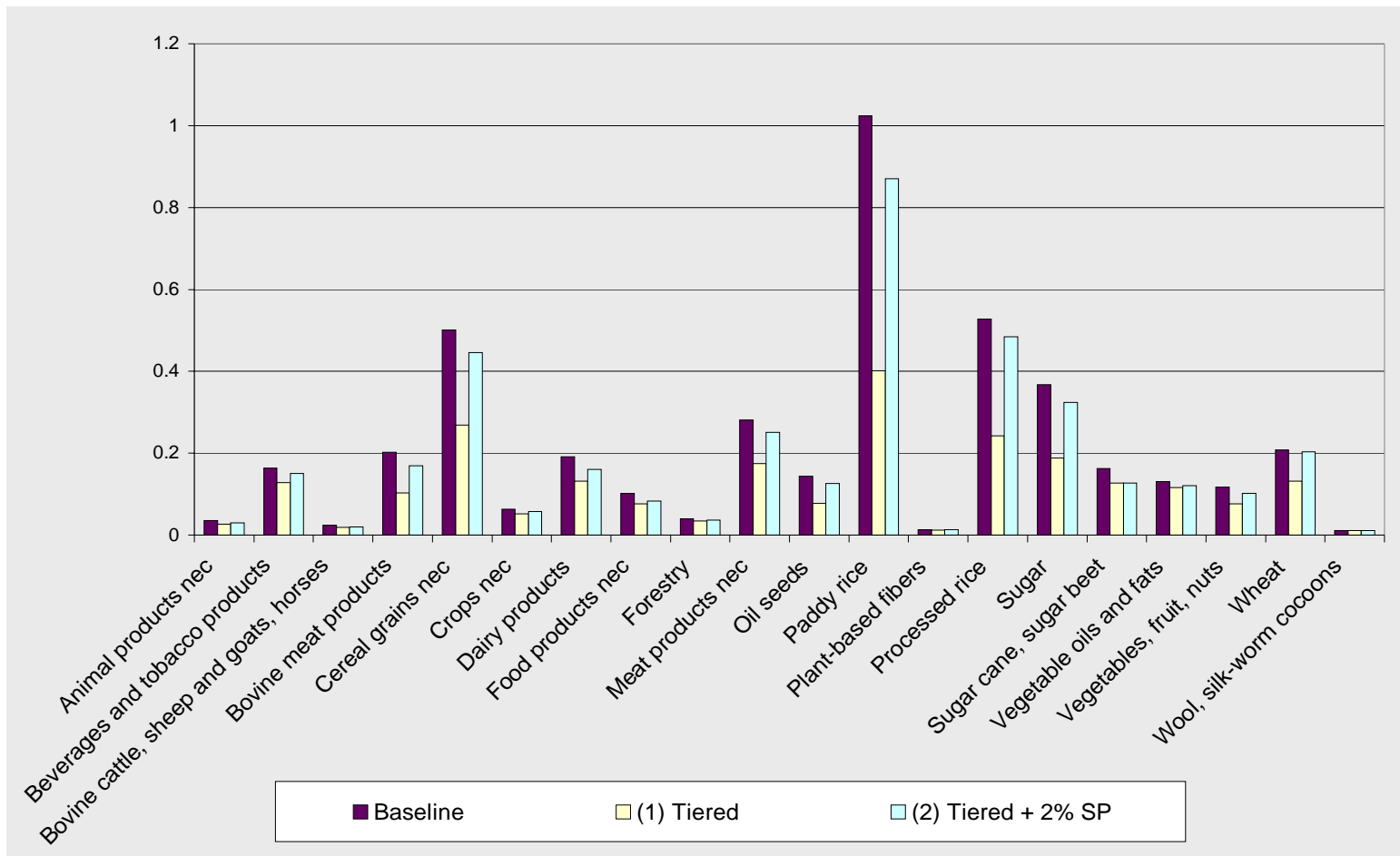
Current protection pattern

- Unilateral reforms by developing countries since the 1980s have reduced their export taxes and other negative incentives for farmers
- But some developing countries have ‘overshot’ and become protectionist towards farmers
 - or could do in the future, because of their much higher bound than applied tariffs

Agricultural Tariffs in Developing and Developed Countries



Market access sectoral impact, tiered formula and sensitive products (2% of tariff lines)



Only 2% of tariff lines 'sensitive' greatly limits impact on market access

Source: Jean, Laborde and Martin, 2004

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Model-based evaluations of DDA round

- All models are wrong – but some are useful
- Several large scale studies published 2002-05
- Results differ in some nuances, but all agree that agricultural reforms could bring substantial gains
- OECD: sectoral and household effects

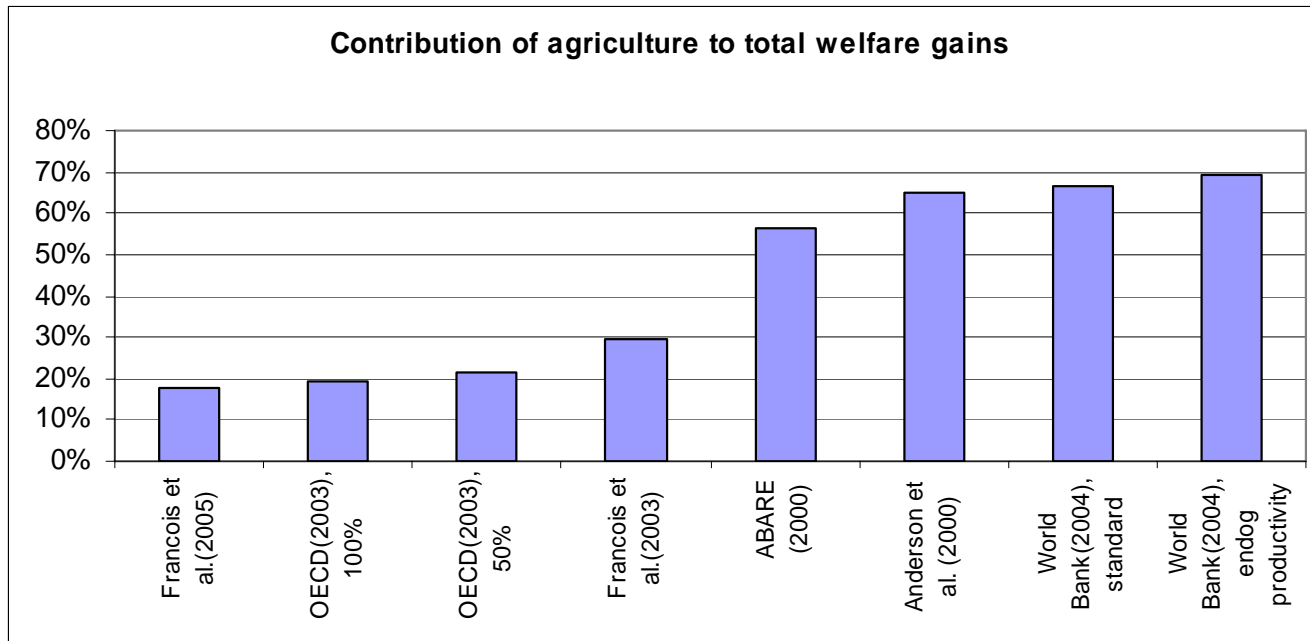
Distribution of gains

- Results can be presented by country and by sector.
- Results should also be analysed at the household level, but requires other models
- Distribution is important:
 - not all countries gain
 - within a country, not all sectors gain
 - within a country, not all households gain

Adjustment and compensation

- More detailed analysis at the household level is needed to have a complete picture
- Important for good policy design:
 - to facilitate adjustment that follows reform
 - to compensate those who lose
- Safety nets and adjustment assistance, rather than exemptions from trade commitments or delayed reform

The contribution of agriculture



The contribution of agriculture to total gains differs

Modelling assumptions are crucial

Francois et al: include services and trade facilitation

ABARE and World Bank: projections into future -> share of agriculture in DCs high

Agri-food sector: liberalisation and adjustment pressures

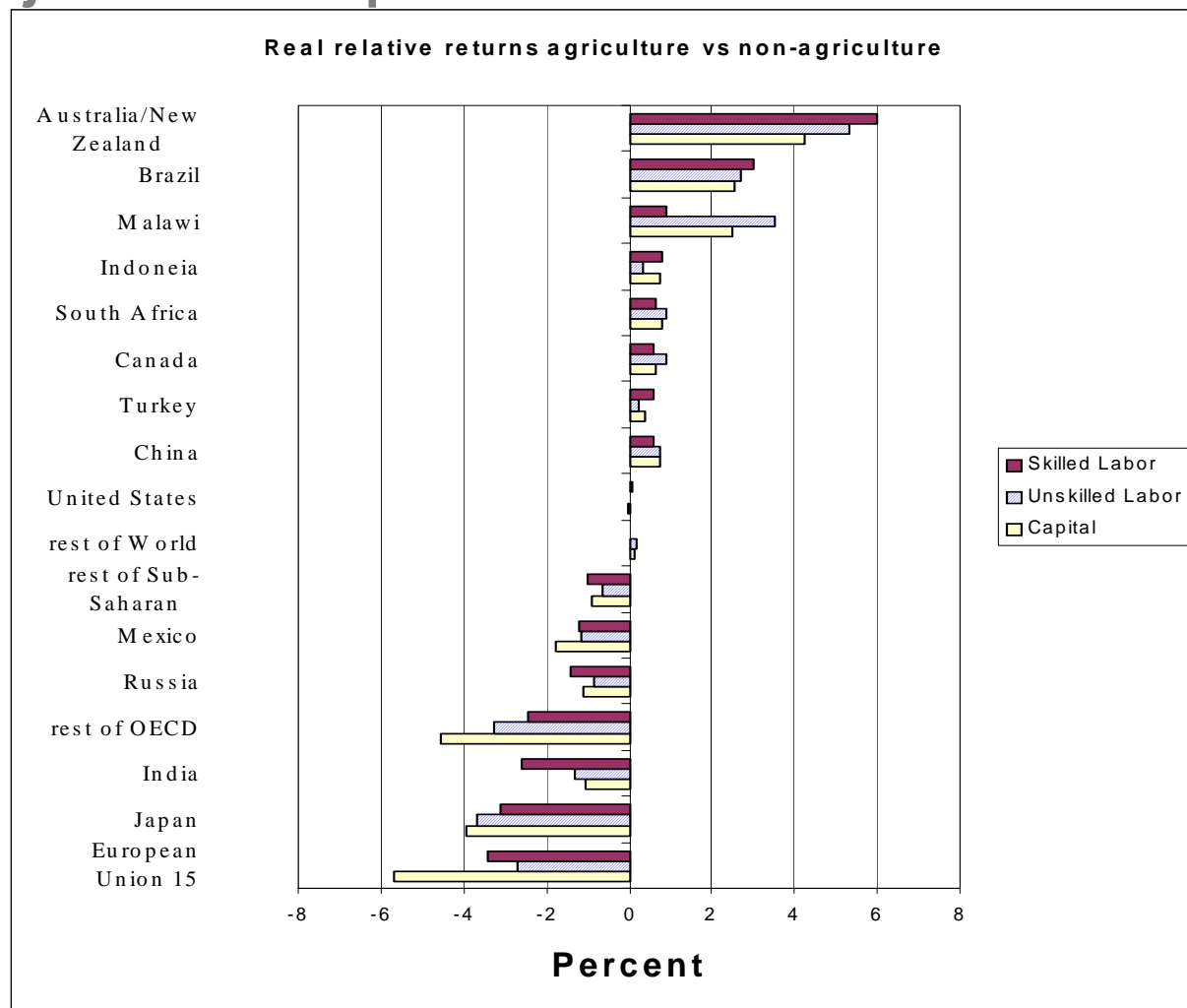
Relative factor returns agri/non-agri

Countries which provide large support see drop in factor returns in agric.

... others see increase

Land returns even more dramatic changes

Source: OECD 2006



Regional impact: participation pays off

	Developing countries liberalize	Developed countries liberalize	All countries liberalize	Share of total gains
Gains to developing countries	74%	24%	100%	35%
Gains to developed countries	12%	79%	100%	65%
Gains to all	34%	60%	100%	

Average % breakdown of welfare gains calculated from 5 studies

Three quarters of the gains depend on own actions.

What You Give is What You Get (WYGIWYG)!

Developing country share of the global gains is about 35%

The contribution of the 3 pillars

- All studies show that:
 - Market access is most important pillar
 - Export subsidies are relatively less important, and reductions may hurt some food importers
 - But elimination will effectively limit domestic policies and future export subsidisation
 - Domestic support reforms mainly beneficial to reformers themselves (decoupling etc)

Conclusions

- More openness offers opportunity for many to trade their way out of poverty
- Multilateral negotiations offer more scope for trade-offs than bilateral deals
- Broad consensus:
 - Ag liberalisation contributes about 30%-50% of total gains from a broad multilateral reform
 - Gains from domestic agricultural reform fall mainly on OECD countries (efficiency gains)
 - Market access is most important issue on the Doha agenda
 - Developing countries potentially benefit most relative to GDP (but not in absolute terms)
 - Continued

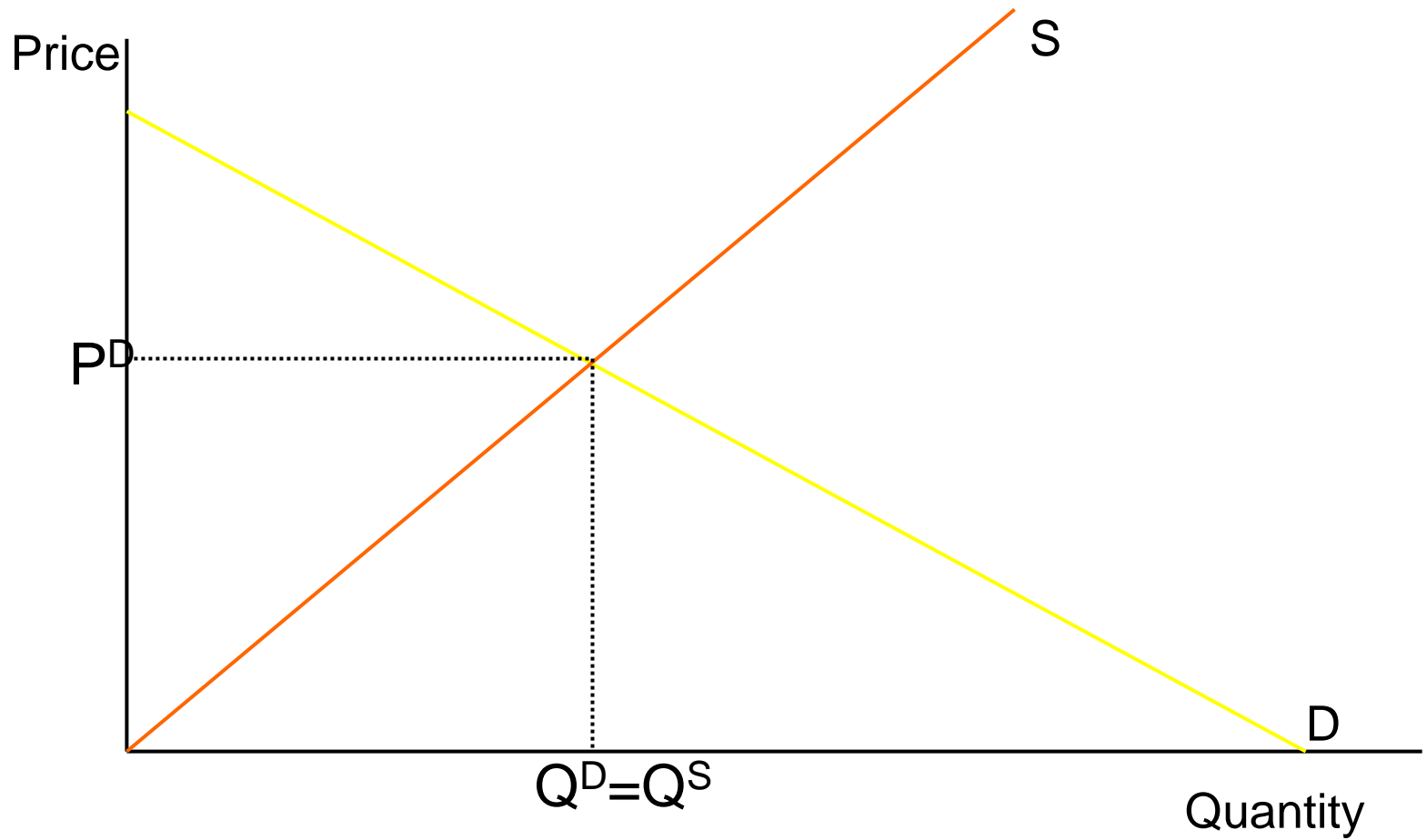
Conclusions -II

- ... but if they choose not to participate, their gains disappear
- A country's own policy reforms contribute most to its own potential gains: What You Give is What You Get.
 - Non-agricultural liberalisation is important for developing countries.
 - South-south trade can be an important source of growth for developing countries.
 - 'Sensitive' products limit effective market access improvements
 - Trade reforms should be part of policy package, including adjustment assistance for those who lose from reform

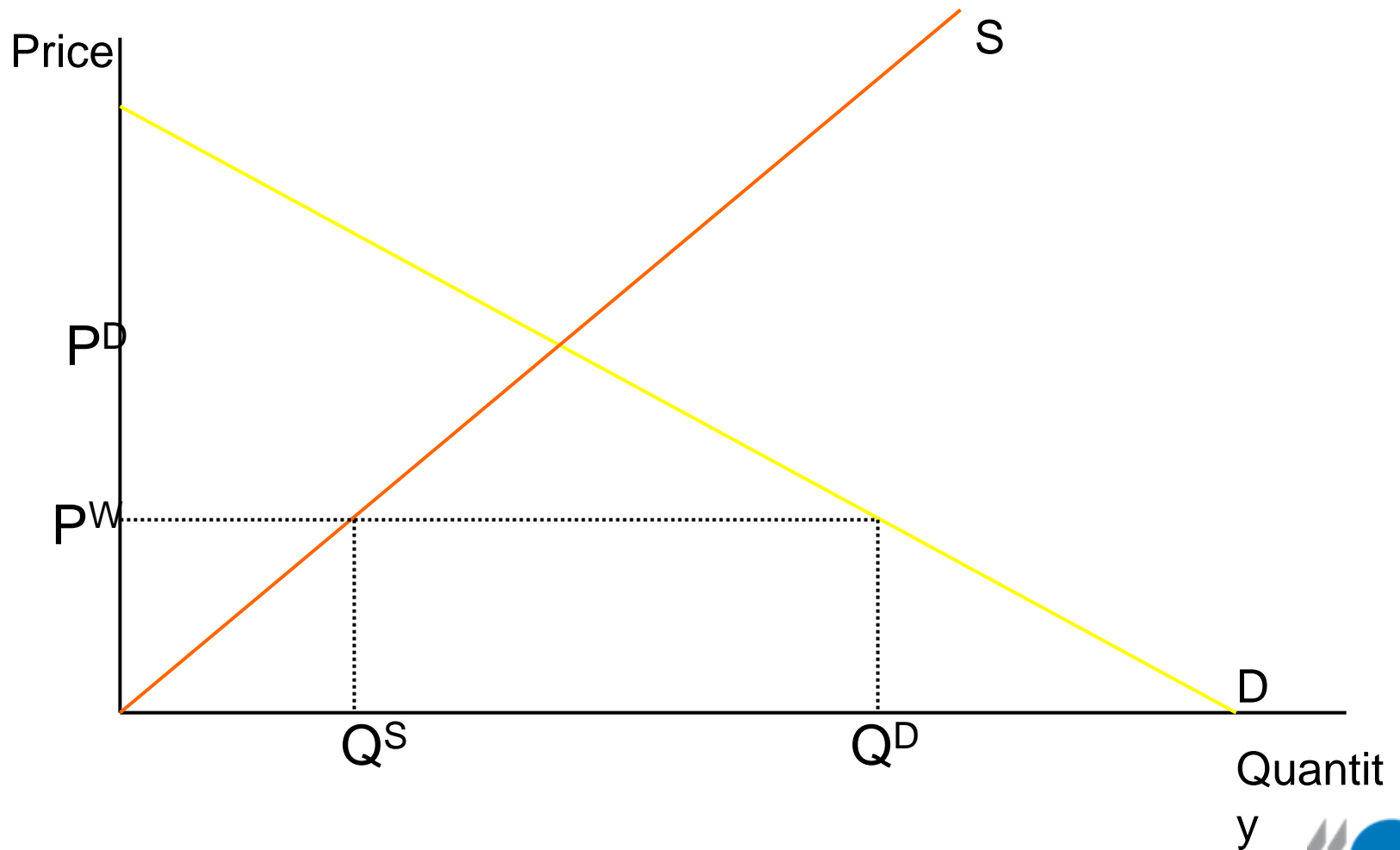
Supplementary material

- Graphical analysis of effects of a tariff in a small economy
- CGE Models and measurement of welfare effects: Equivalent variation

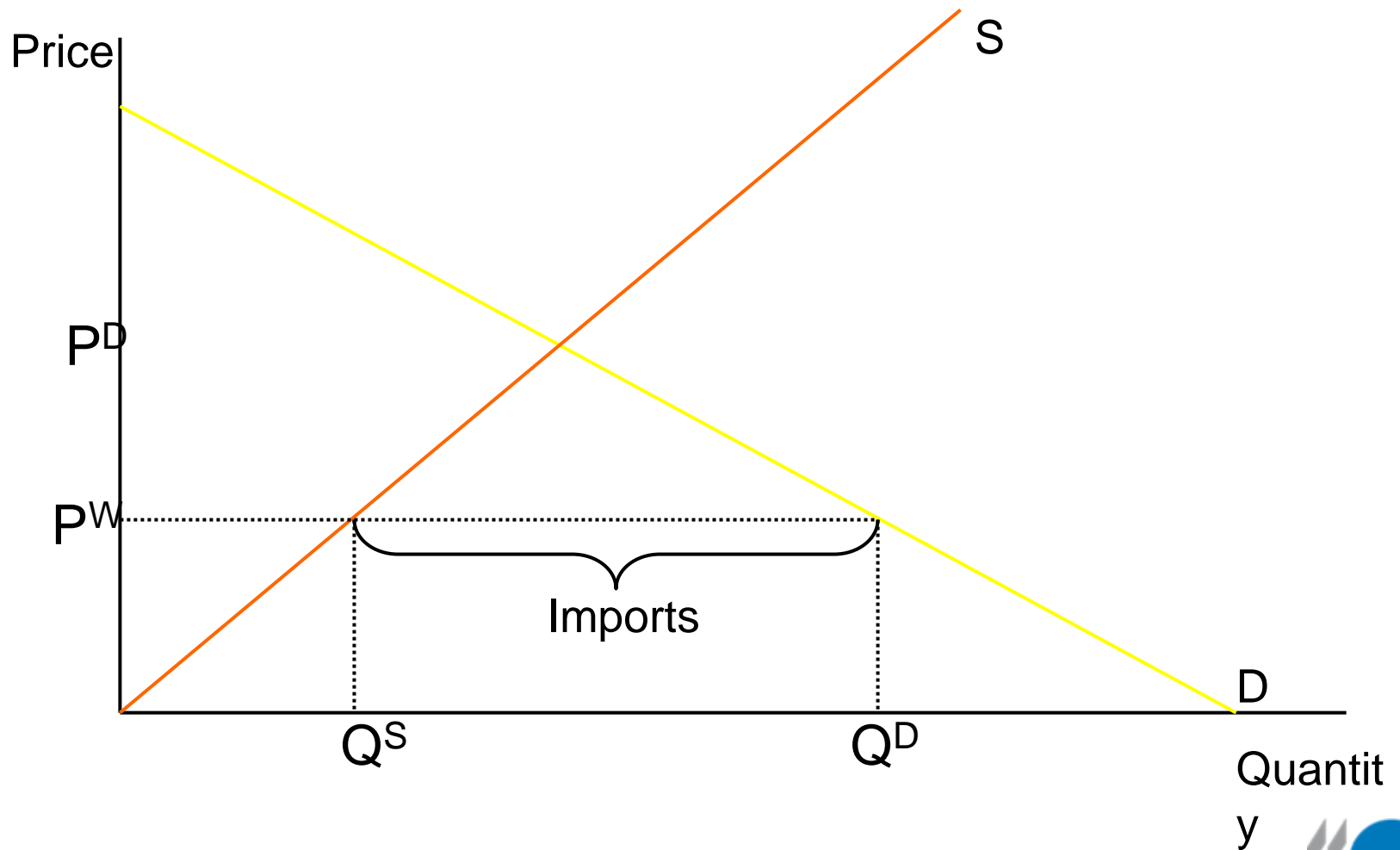
Autarky



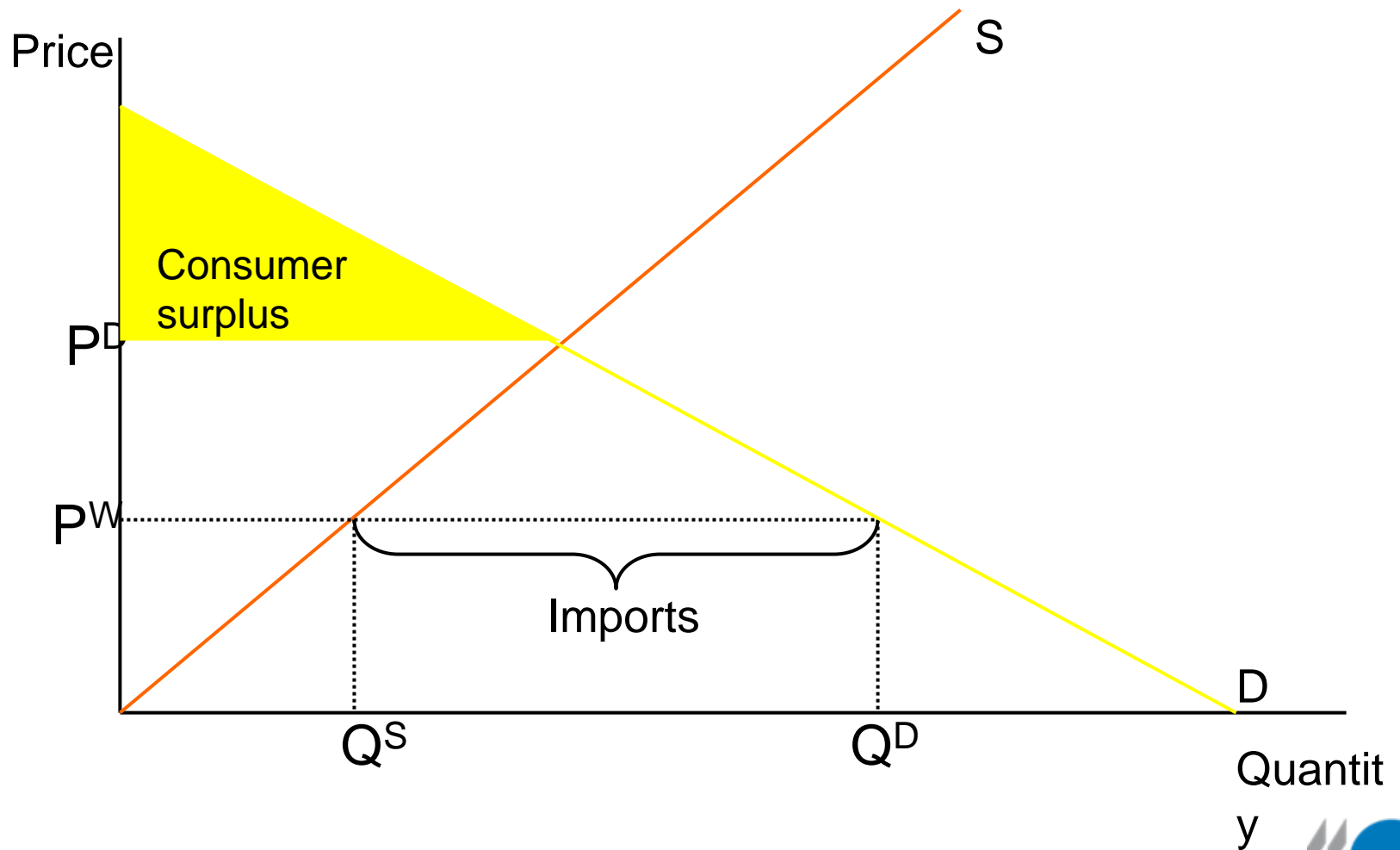
Free trade for a small country



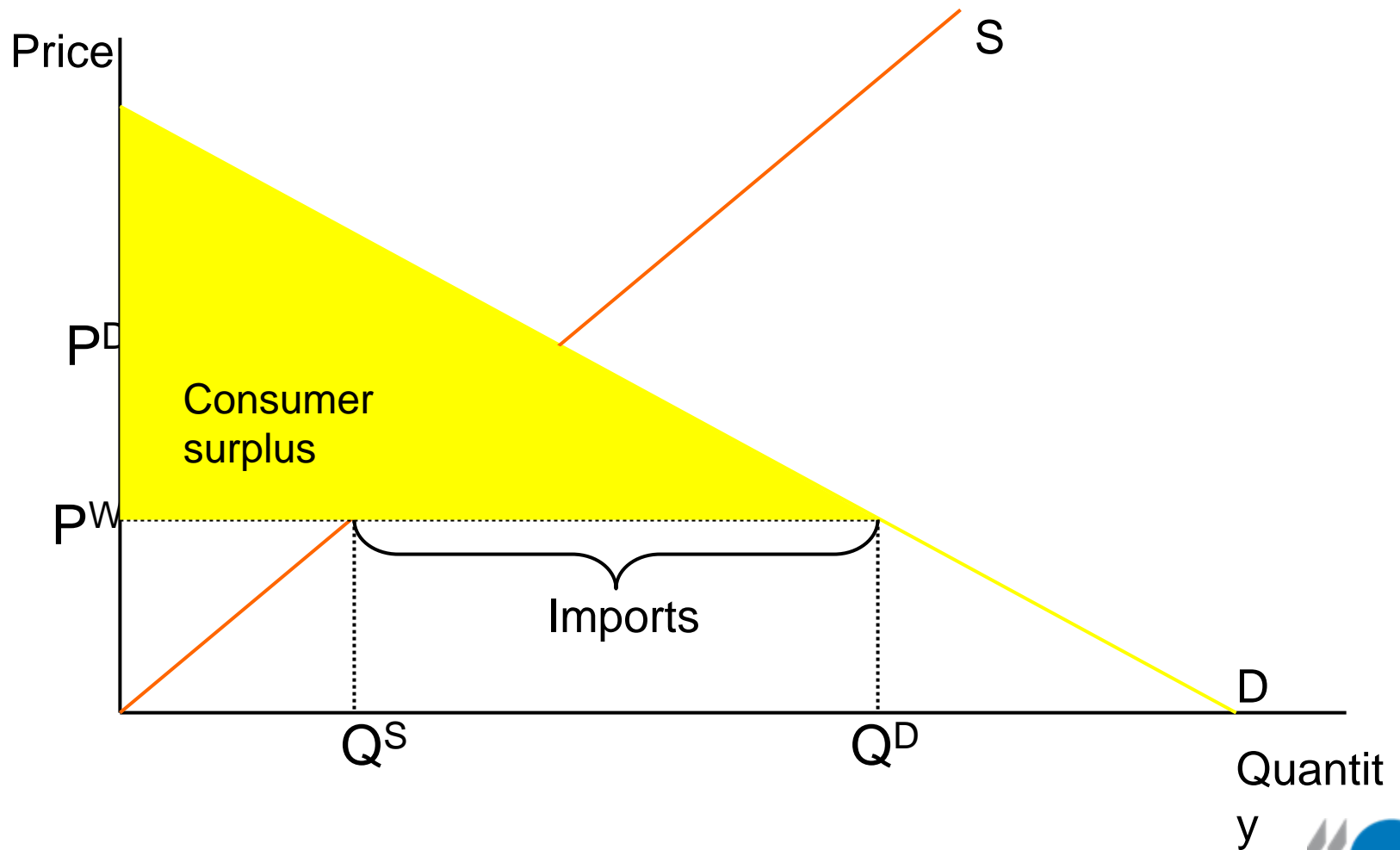
Free trade for a small country



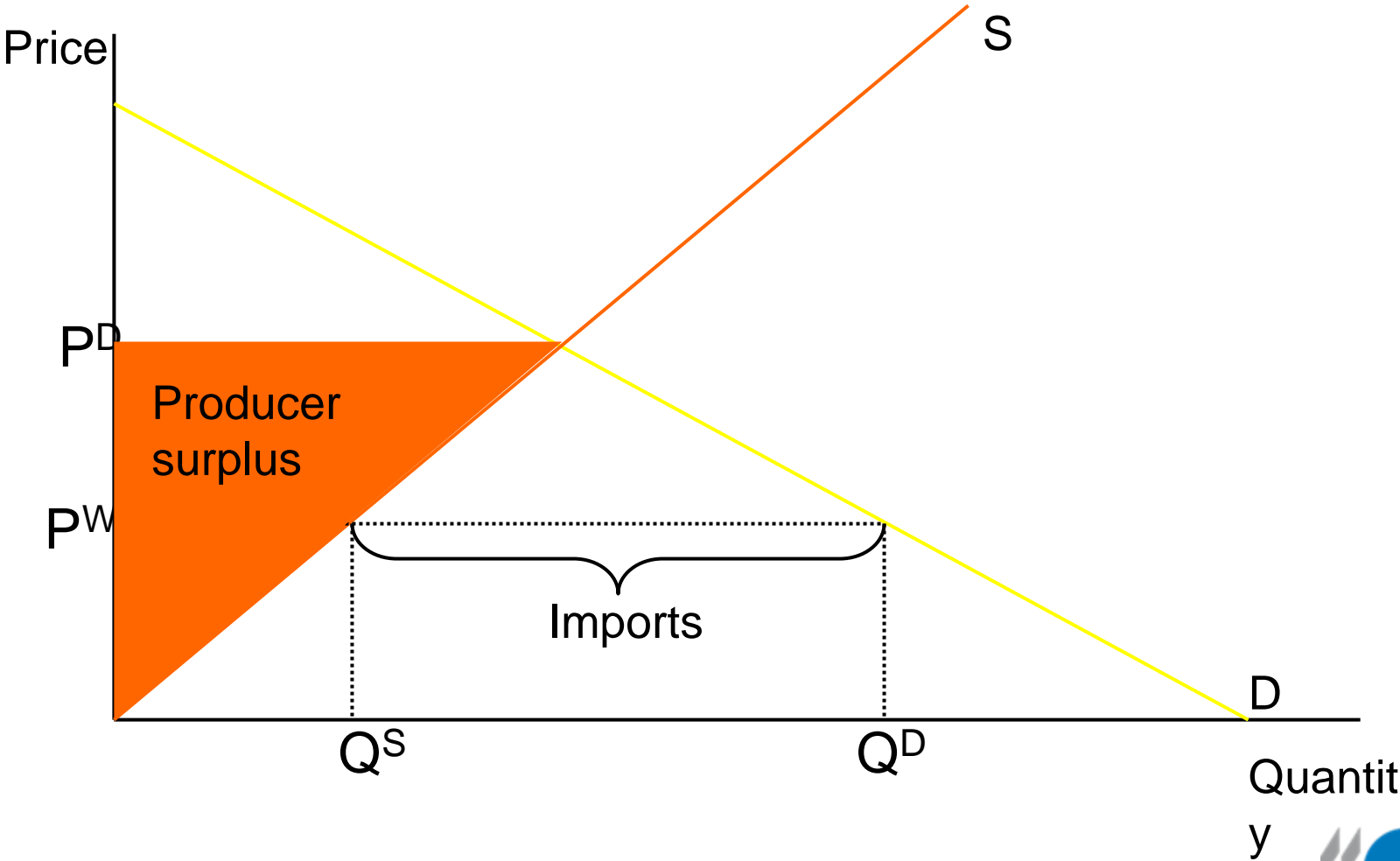
Free trade: consumers gain



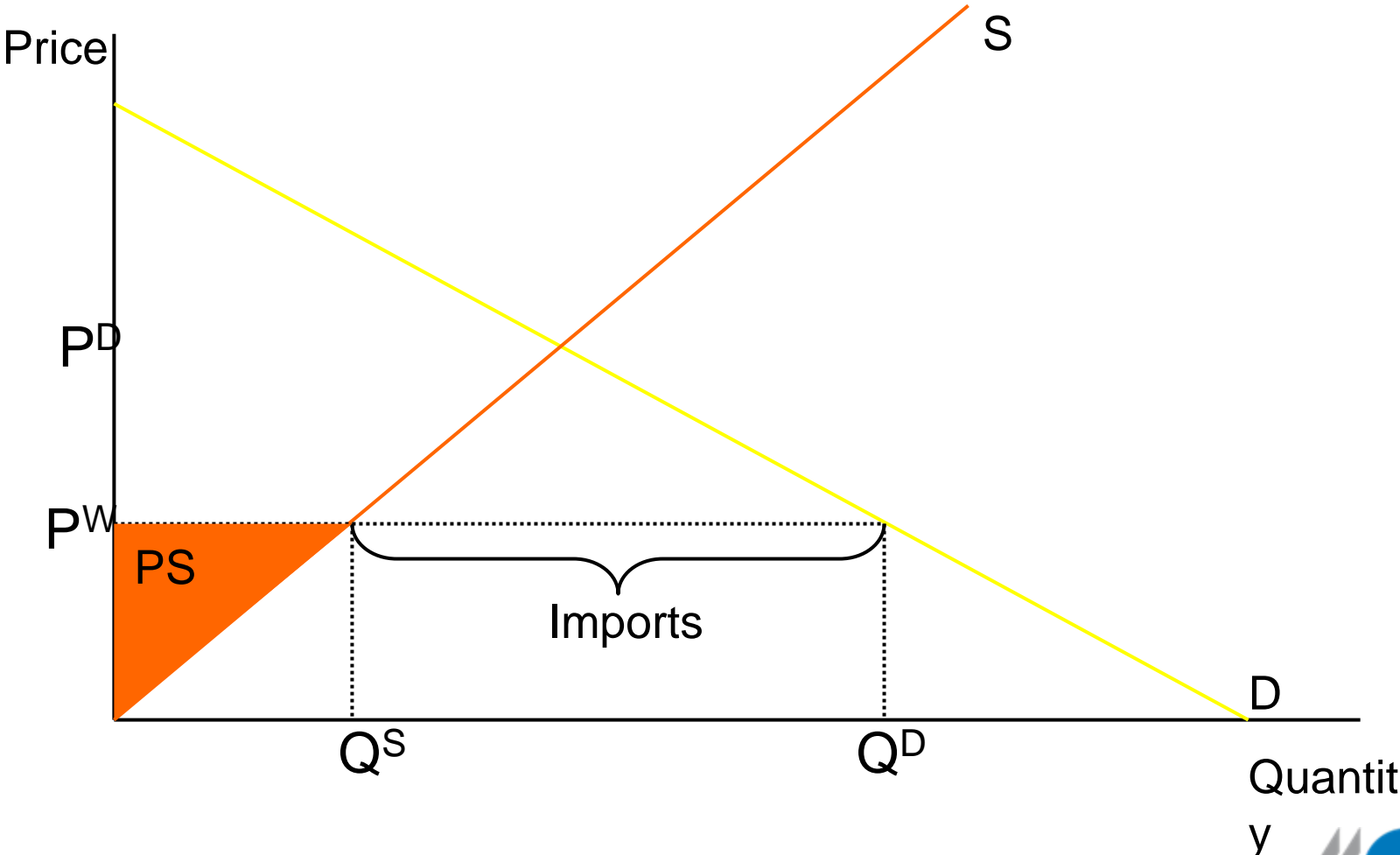
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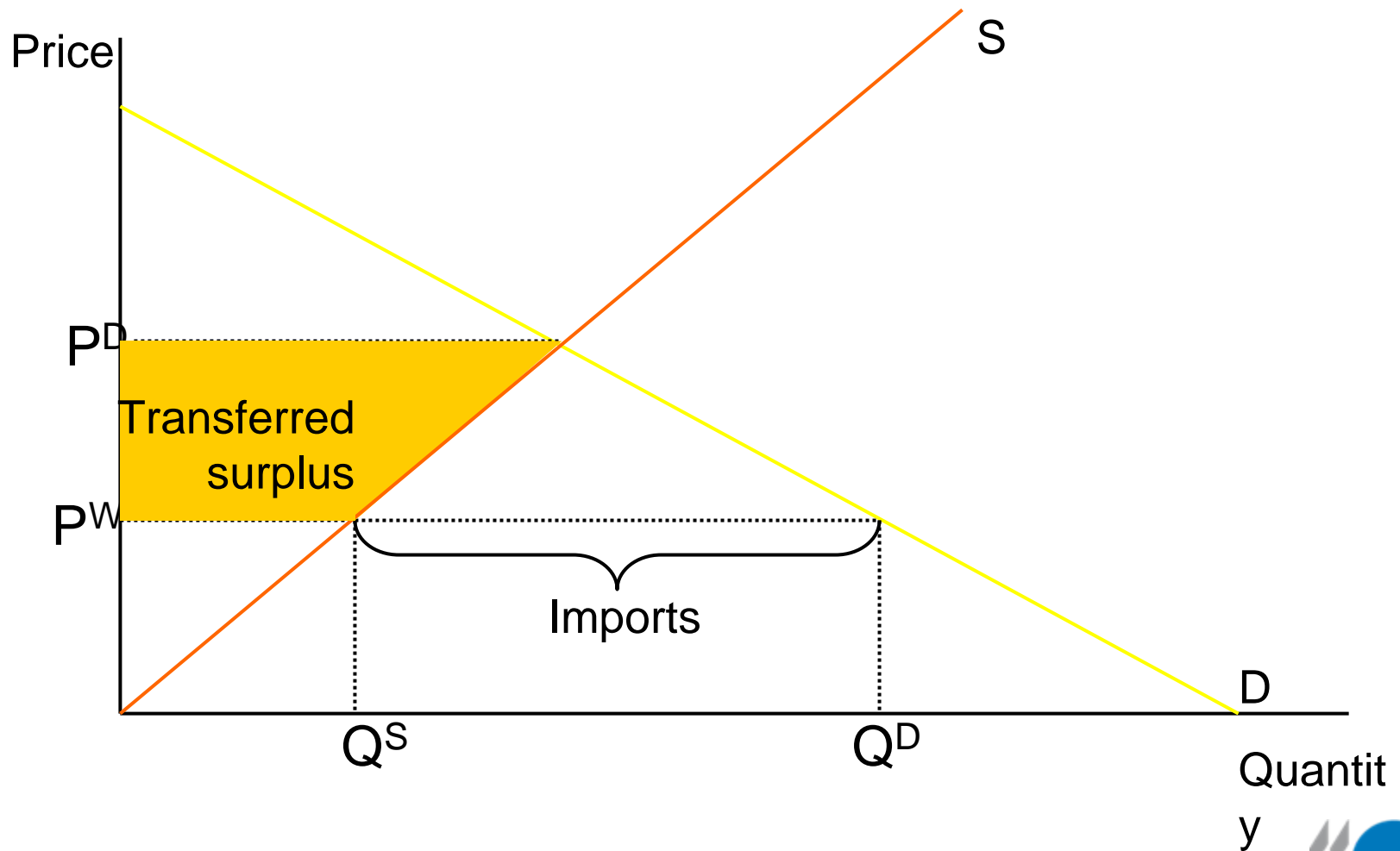
Free trade: producers loose



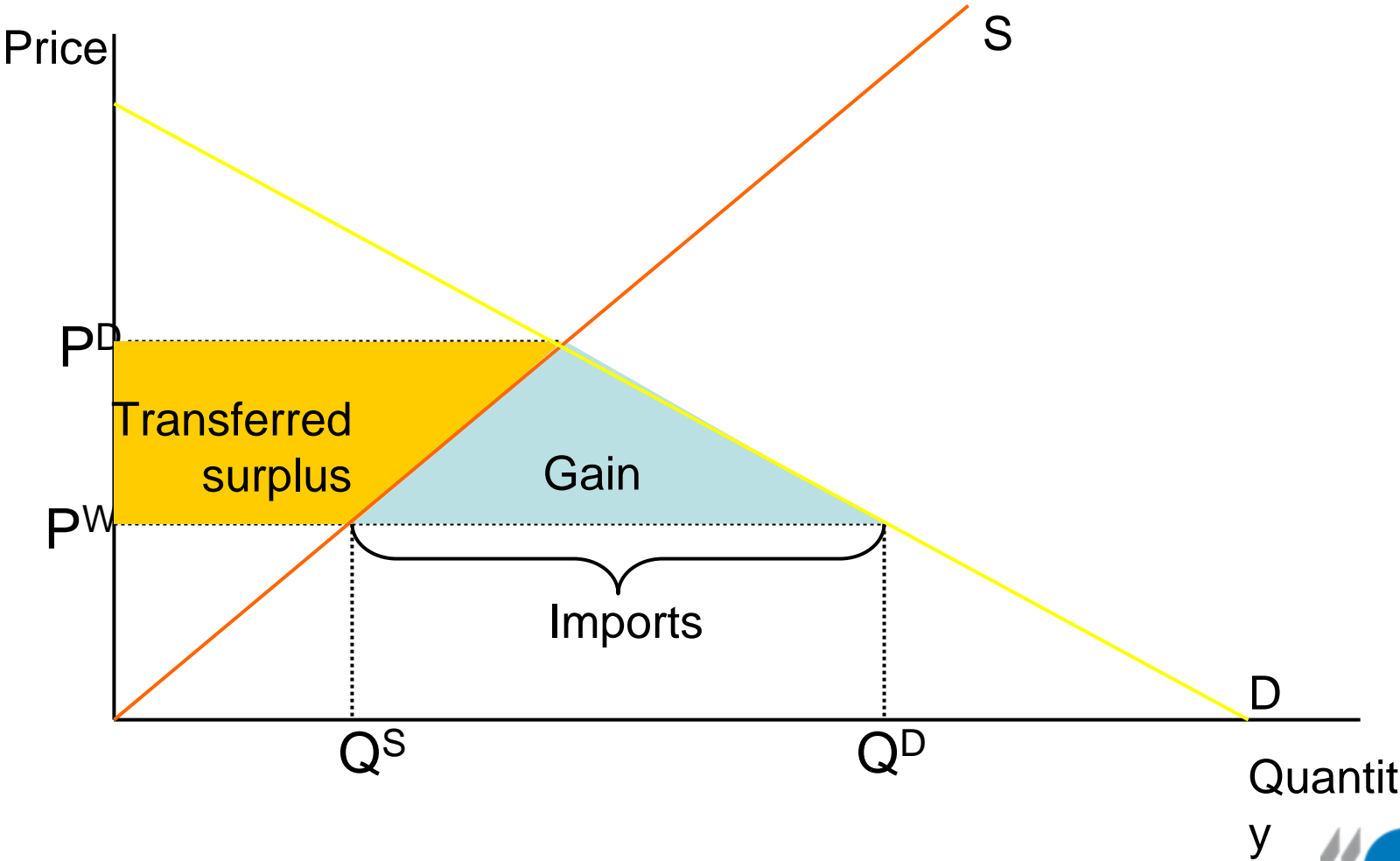
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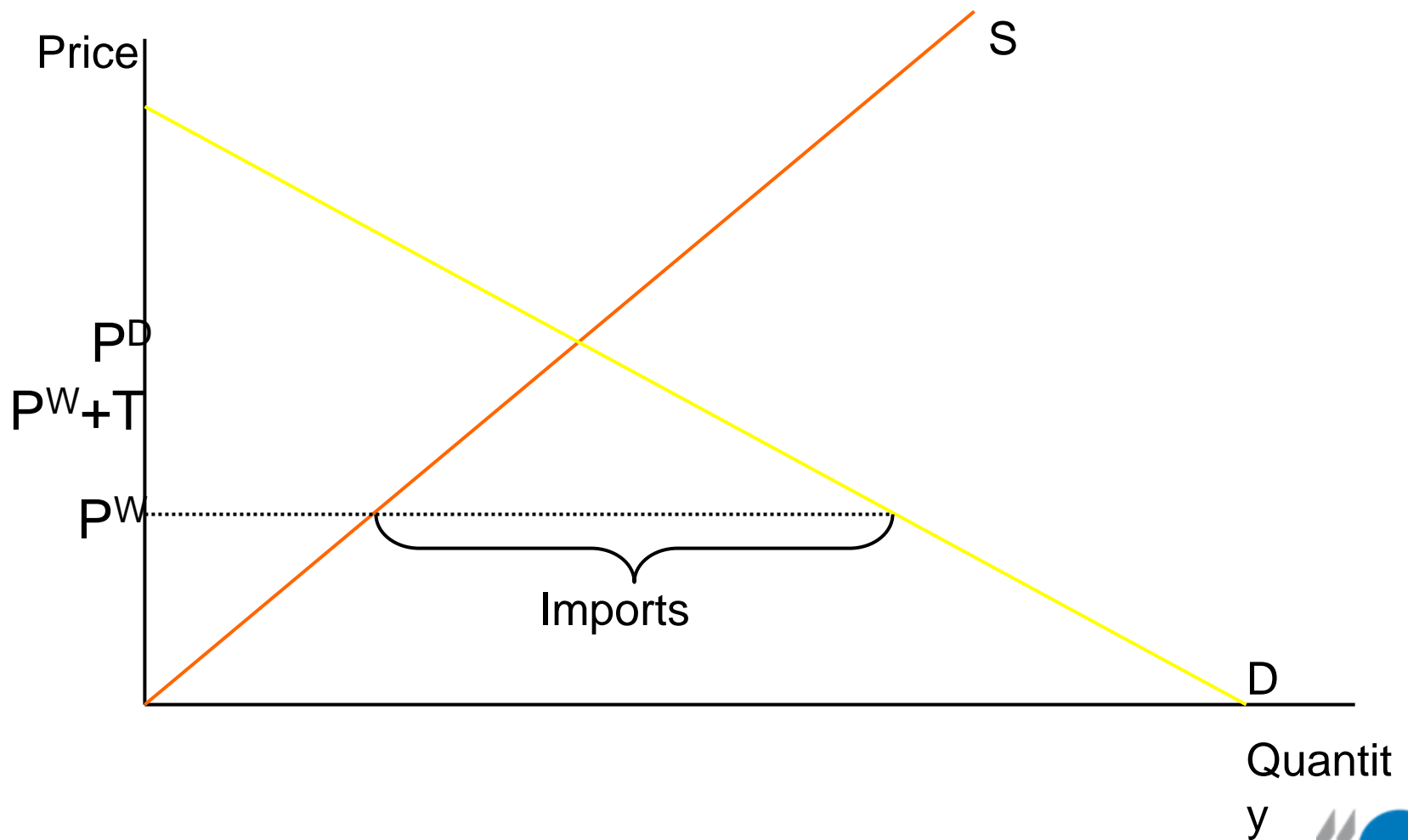
Free trade: economy as a whole gains



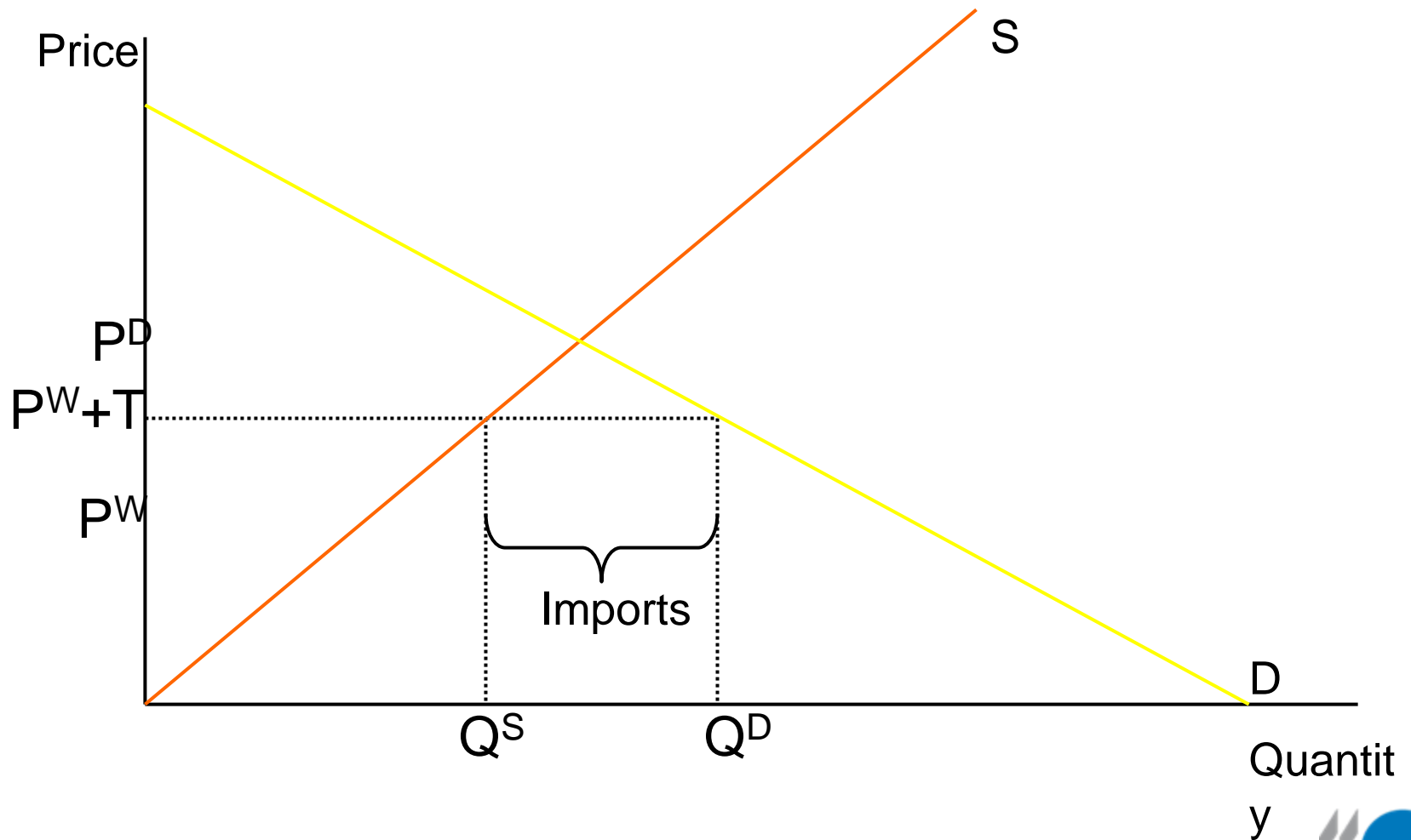
Free trade: economy as a whole gains



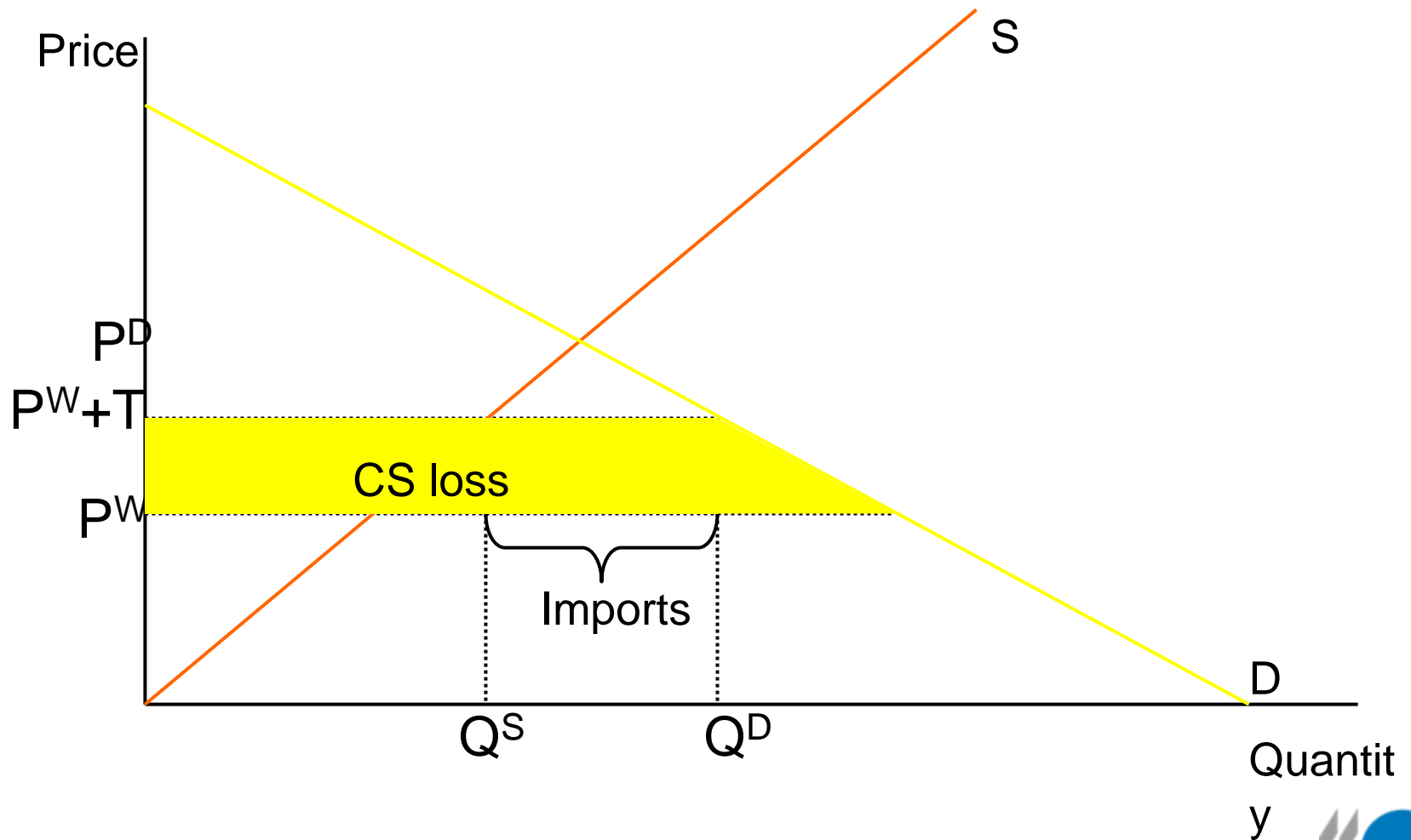
Import tariff: imports reduce



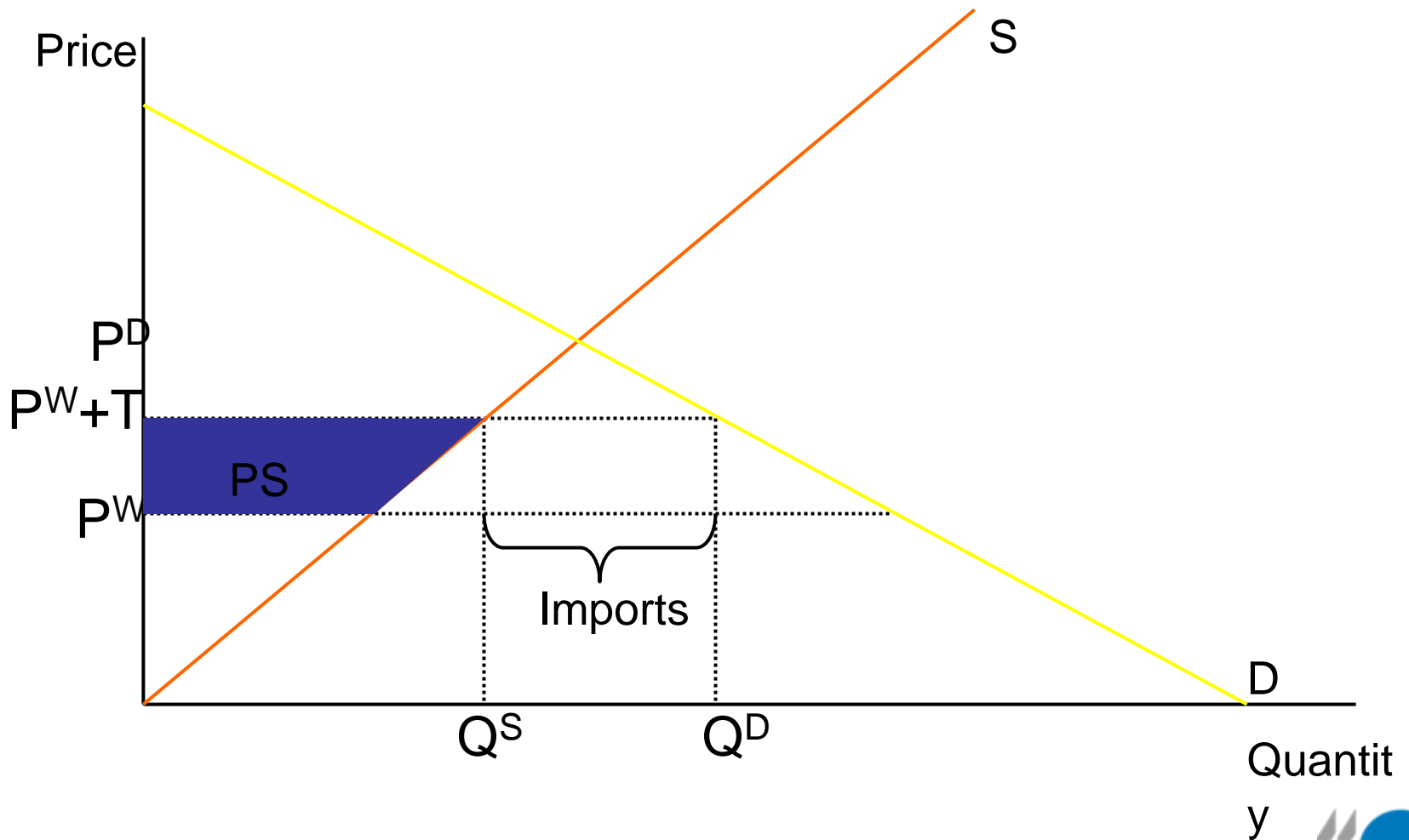
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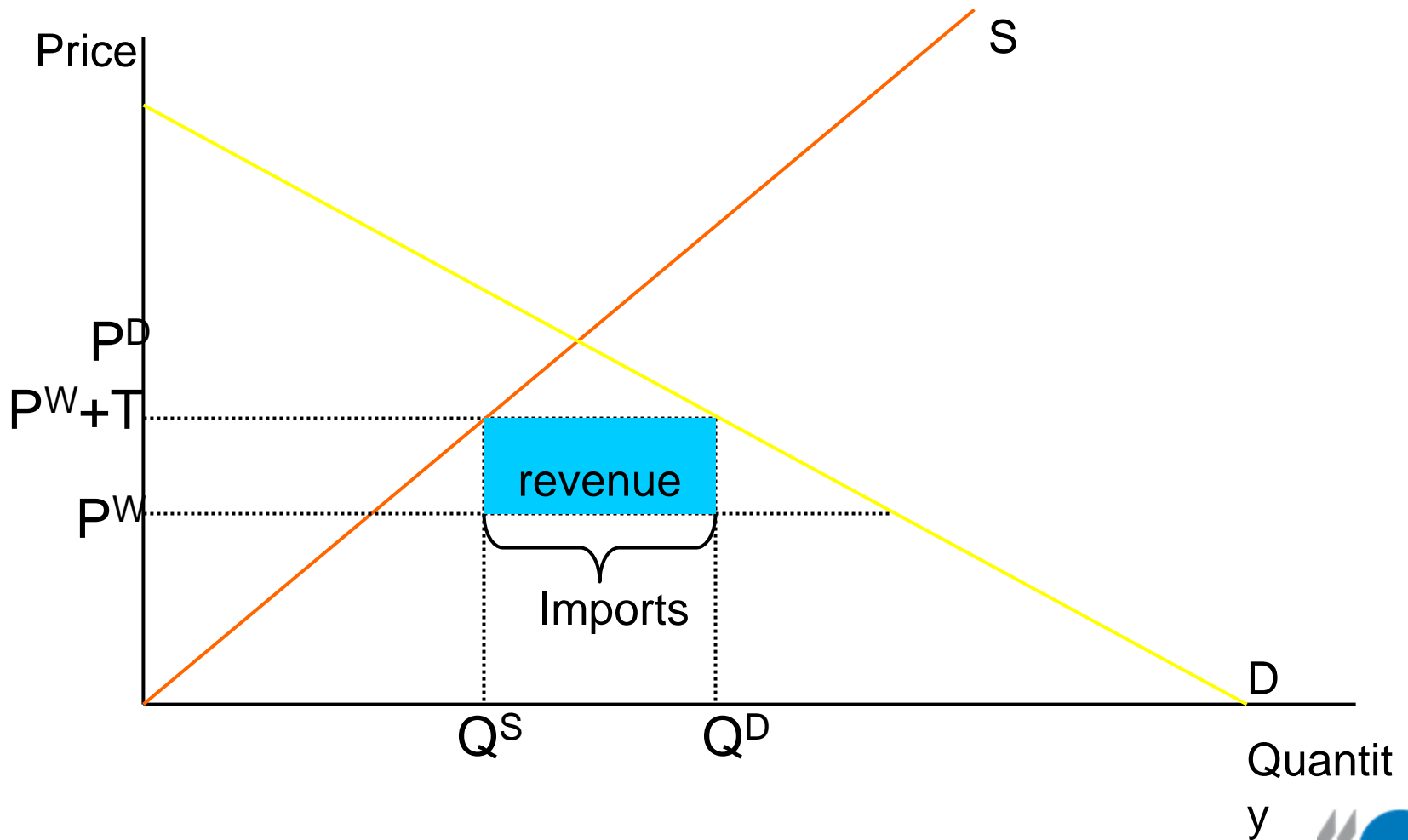
Import tariff: consumers loose



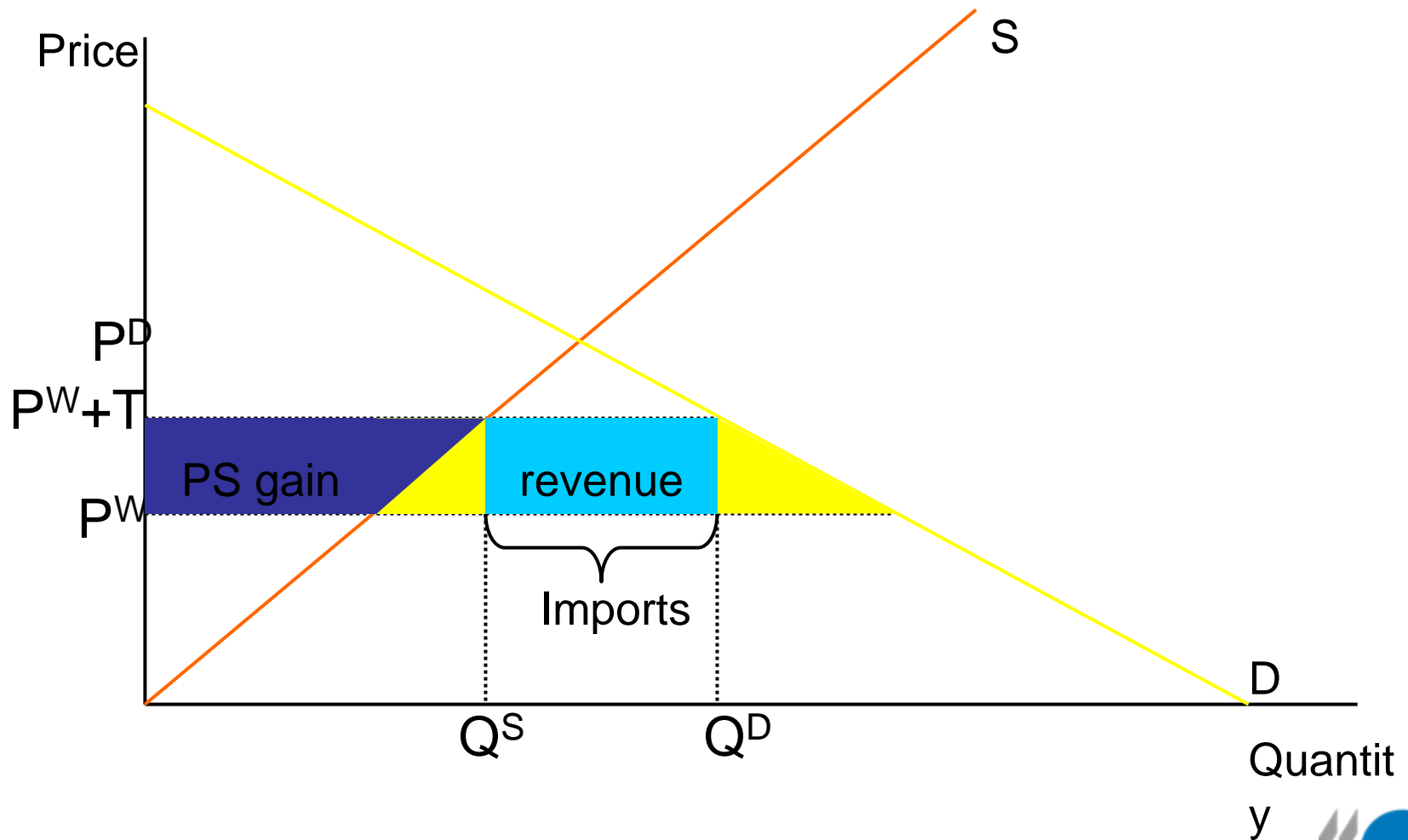
Import tariff: producers gain



Import tariff: government gets revenue



Import tariff: economy has a deadweight loss



Model-based evaluations of DDA round

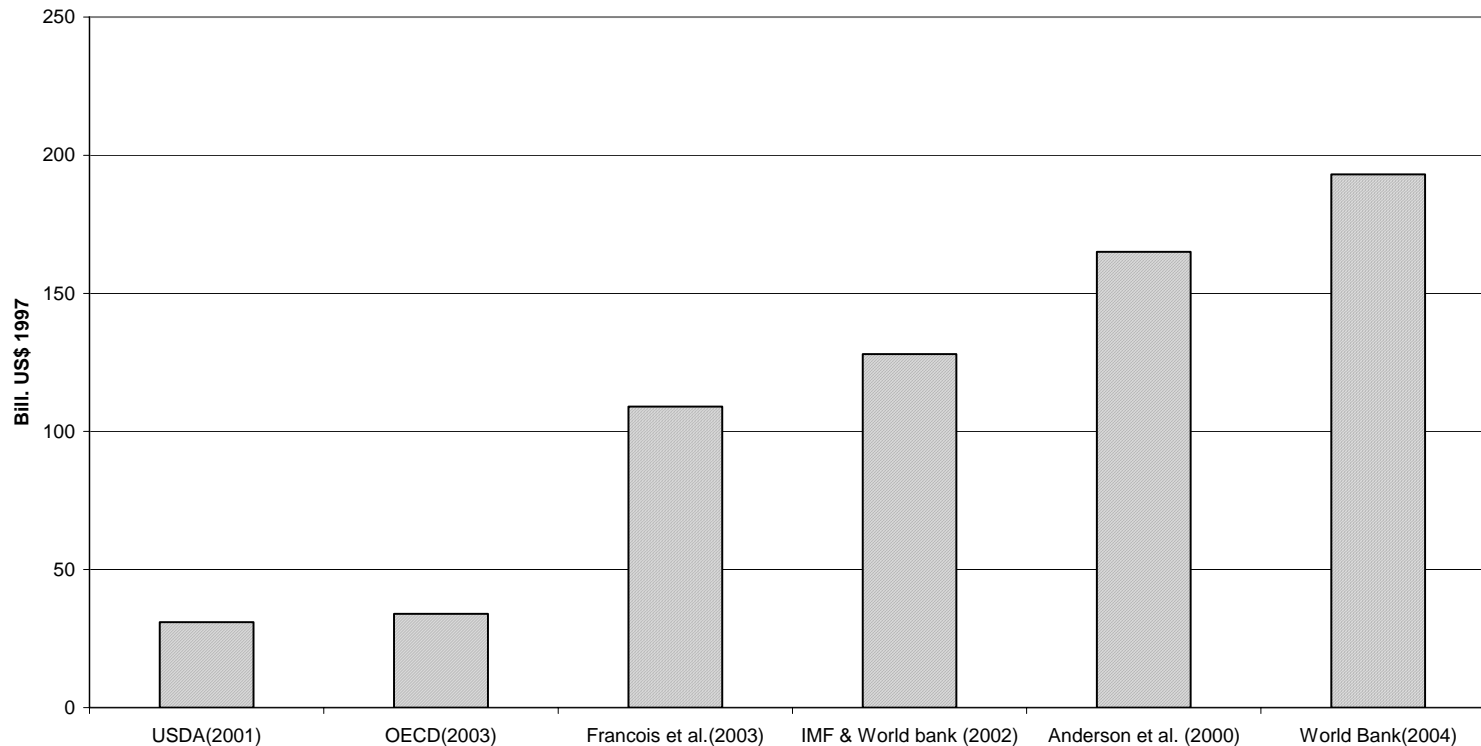
- Economy-wide view
- All activities: trade-off between sectors and resource shifts
- Circular flow of income and expenditures
- Consistency (accounting, theory)
- Ingredients:
 - Theory, Data, (computer), policy
- CGE: Computable General Equilibrium

Measurement of welfare effects

- Income effects from CGE analysis mostly reported (and cited)
- The income measure is usually *Equivalent Variation (EV)*
- This is the bottom-line measure: how well are we doing?
- It represents the change in income that would be equivalent to the proposed policy change:
 - How much money should be given to the household(s) in order to achieve the same welfare as without the policy change?
- EV is a measure of *potential gains*:
 - if $EV > 0$ we know that potentially the gainers can compensate the losers
 - EV does not inform about distribution

A sample of welfare effects from full ag libn.

Welfare gains from full agricultural liberalisation



Although all studies use the same GTAP v5 database, the results differ

Modelling assumptions and scenario design explain this

Design of simulation experiments

- Details of Doha package still to be negotiated
- Therefore ex-ante studies typically use a broad experimental design
- For example 50%, 100% cuts in applied policies
- Few studies attempt to capture bound/applied, non-binding AMS ceilings and trade preferences
- Examples of the latter:
 - LEI studies for UNECA (2004), and for Indonesia (2004/05). Preferences and binding overhang taken into account in CEPII (2004) and in recent World Bank work (2005)

Design of simulation experiments II

- Standard CGE yields static welfare gain
- Non-standard features boost the estimated gains
 - Dynamic projections (WB)
 - Endogenous productivity (TFP increases with trade and openness), WB, USDA/ERS, ABARE
 - Increasing returns to scale and imperfect competition (Francois et al)
 - Inclusion of services and Singapore issues (Francois et al)