

## Trade on Human Terms

### Vulnerability, Trade Integration and Human Development

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#### I. INTRODUCTION

Trade integration can potentially be a powerful instrument for economic growth and poverty reduction. Virtues of trade integration are well documented (see, for example, Sachs and Warner 1995; Dollar and Kraay 2002), but the claims regarding their benefits have often been oversold (see Rodriguez and Rodrik 1999; Rodrik 2002; Stiglitz 2003). Empirically, it is hard to prove that trade integration enhances broad-based economic growth or reduces poverty. However, it is equally true that no country achieved broad-based economic growth by shutting its doors to the outside world.<sup>1</sup> Given this dilemma, it is a daunting challenge for the developing countries to design and implement appropriate policies that help them reap the benefits from trade integration, without compromising with the policy space they require to achieve development objectives based on the principles of equity, empowerment, productivity, sustainability – collectively known as human development objectives. Such development objectives have been envisaged, under the Millennium Development Goals (MDGs) – the world's time-bound and quantified targets for addressing extreme poverty in its many dimensions – income poverty, hunger, disease, lack of adequate shelter, and exclusion – while promoting gender equality, education, and environmental sustainability (UNMP 2005).

Even if gains do occur from trade integration, all the players do not gain equally. Size does matter, not least because minimum efficient scale cannot be achieved in absence of critical market size. Therefore, firms located in bigger countries tend to outperform those located in smaller countries.<sup>2</sup> Moreover, while countries well-endowed with natural, human, financial and technological resources tend to be the winners; those that lack one or many of these critical resources tend to lose out. The problem is more severe in the case of vulnerable economies. While they are too small to make any impact on the international market, they get, in turn, affected by any change in the international market. The typical problem of price volatility of commodities is one example. Such problems are commonly shared by all the least developed countries (LDCs), classified as such by the United Nations (currently 50 in number) as well as small low income countries(LICs).

Standard textbook general equilibrium trade theory portrays small size as a distinct advantage, which appears under the rubric of 'importance of being unimportant'. Since small countries are 'price takers' in the global market, they can potentially trade at the outer-boundary limit of profitable international relative price ratios or terms of trade (Thomas 2004, 5). While this results in static gains from trade for the small economies, the dynamic gains, at least in theory, are enormous. Moreover, there is compelling evidence suggesting that bystanders to the trade integration process (i.e., excluded countries) are likely to suffer a great deal (see Deardorff and Stern 2004). At the same time, trade integration in the strict legal sense, i.e., by making binding commitments at multilateral, regional or bilateral levels, is likely to produce other spill over benefits such as policy lock-in and predictability of domestic economic environment, which can result in economy-wide benefits.

At the same time, it is necessary to understand that costs of trade integration are non-trivial. Besides the financial, human and material costs of implementation of the legal commitments, the adjustment costs that the domestic economy and stakeholders (including import competing sectors, farmers and workers) are likely to be subjected to are enormous. The prices being paid by the countries, which accede to the multilateral trade regime – the World Trade Organization (WTO), in comparison to its founder members – are much higher. Moreover, developing countries entering into regional trade arrangement (RTA) with developed countries are obliged to make several 'side payments' – beyond the requirement of the WTO – the so-called 'WTO-plus' conditions.

Most integration processes lead to the shrinkage in policy space of the governments, making it difficult for them to achieve their human development objectives. As Human Development Report (UNDP 1999, 35) rightly puts it, in the context of the WTO: “The rapidly increasing multilateral agreements – the new rules – are highly binding on national governments and constrain domestic policy choices, including those critical for human development.” Arguably, countries that manage to pitch their trade integration process as a part of their broader development strategy are likely to achieve better human development outcomes than others.

Despite the realization that the costs of integration are fairly high, sovereign countries – ranging from the size of Vanuatu to Vietnam in the Asia Pacific context – have been making a conscious decision to enter into trade agreements at various levels. They must have done so after serious cost benefit analyses and must have concluded that, on balance, benefits of integration outweigh the costs involved.<sup>3</sup> Besides, countries, which are in the multilateral trading system, are signing various RTAs and bilateral trade agreements (BTAs) with breakneck speed, due in part to the failure of WTO members to tear down trade barriers at the multilateral level and facilitate greater global integration.

Against this backdrop, this chapter focuses on vulnerability-prone states in Asia and the Pacific from the perspective of trade integration and human development. The range of vulnerabilities will be identified and addressed with the twin aims of improving trading prospects of these countries and their better integration into the world economy in ways that promote human development. The chapter is organized as follows:

Section II defines vulnerability and outlines the country characteristics of vulnerable economies that are so fundamentally different from other economies in terms of trade integration. Section III delves on their vulnerabilities in relation to trading prospects and human development. Section IV deals with trade integration processes and conditions attached thereto – within the multilateral, regional and bilateral frameworks. Section V deals with the possible implications of these processes – positive as well as negative – on human development. Section VI takes stock of the current initiatives designed to address their vulnerabilities and critically analyzes their successes and failures. Section VII provides some policy recommendations so as to help them leverage trade integration for human development.

## II. DEFINING VULNERABILITY IN THE CONTEXT OF TRADE INTEGRATION

Small size of the economy, high export concentration ratio and volatility of exports, high import penetration ratio, scarcity of natural resources, low level of technological development, low income, high incidence of poverty and hunger, low human development indicators, inaccessibility, prone to natural disasters, and lack of institutional preparedness to deal with these problems are all features of vulnerability. These vulnerabilities fall into four broad categories (Box 1).

For the purpose of this chapter, vulnerability is defined as low per capita income, low human assets index, and high economic vulnerability index, which are based on United Nations Economic and Social Commission (ECOSOC) criteria for defining LDCs. As per these criteria, all the LDCs of the Asia Pacific region and some of the LICs as defined by the World Bank are included in the list of vulnerable countries (see Annex 1). Though the World Bank classifies relatively bigger economies such as India, Indonesia, Pakistan, China and Vietnam as LICs, they are not included here because they do not meet the primary criteria of vulnerability.

### Box 1: Vulnerabilities faced by LDCs and small LICs

Economic vulnerability, the greater than average risk faced from exogenous shocks that adversely affect income, employment, domestic production, distribution, markets, consumption, and the stock of wealth, and their limited capacity to deal with these.

Environmental vulnerability, the greater than average threat of calamities induced by natural or human made factors. While small island states of the Pacific are often hit by droughts, floods, hurricanes, volcanoes and earthquakes, mountainous countries in Asia are prone to flashfloods, volcanoes and earthquakes.

Social vulnerability, the greater than average risk posed by both internal and external factors (whether exogenous or endogenous) that undermine social cohesion, introduce systemic social pathologies, and erode social capital. In these states these factors have a high “recurrence rate” even as we recognize the restricted capacity of these states to respond.

Institutional vulnerability, the greater than average risk posed by the limited capacity of domestic institutions, including the strongest of them all, the state, to respond to the complexity and intensity of pressures flowing from globalization.

Source: Thomas (2004) 8-9

Vulnerabilities per se may not have as much negative impact on human development as the lack of resilience within the communities, and lack of institutional preparedness at the state level. This is a problem for small island states as well as mountainous countries. However, the severity of problems seems to be greater in the mountainous countries, not least because there is an intra-country variation in the ability to adapt to changing circumstances. Lack of education, skills, resources and strong traditional practices means that mountain communities cannot adapt to fast changing economic realities ushered in by rapid trade integration process.

Trade integration that is taking place at present is the most rapid in the human history. The degree of integration of the LDCs and small LICs – measured by trade liberalization – is higher than those of the bigger economies. For example, the depth and extent of trade liberalization in the LDCs can be gauged by using the International Monetary Fund (IMF) index of trade restrictiveness, which classifies countries according to their average tariff rate and also the extent of non-tariff barriers (NTBs). From the data it is apparent that very few LDCs have restrictive trade regimes now (See Box 2).

#### Box 2: Trade openness in LDCs

In 2002, on the basis of evidence provided by IMF index of trade restrictiveness, for the 46 countries for which data are available:

- a) The average tariff rate of 42 LDCs was less than 25 percent.
- b) The average tariff rate of 36 LDCs was less than 20 percent.
- c) The average tariff rate of 26 LDCs was less than 15 percent.
- d) In 29 LDCs NTBs were absent or minor in the sense that less than 1 percent of production and trade is subject to NTBs.
- e) Twenty-eight LDCs had no or minor NTBs coupled with average tariff rates of below 25 percent.

The extent and depth of trade liberalization reflect the wide and long involvement of most LDCs with structural adjustment programmes. As a result, most LDCs now have more open trade regimes than other developing countries and as open trade regimes as high income countries. The whole process has been undertaken very rapidly in quite a number of LDCs.

Classifying LDCs according to their degree of openness into ‘open’, ‘moderately open’ and ‘restrictive’ and their impact on long term poverty reduction United Nations Conference on Trade and Development (UNCTAD 2004a) finds that those LDCs, which were moderately open, did much better than either of the other two categories. This explains the reason for approaching both speed and depth of trade liberalization cautiously. For example, African LDCs have undertaken deeper and faster trade liberalization than Asian LDCs. But it is the latter that have generally had a better performance in terms of poverty reduction, and they have also been more successful in developing more market-dynamic manufacturers’ exports.

Source: UNCTAD (2004a, viii)

Further, as per another measure to ascertain the level of trade liberalization, i.e., ratio of trade (imports plus exports) to gross domestic product (GDP), the LDCs and small LICs rank significantly higher than other developing countries or even developed countries (see Annex 1). For example, trade/GDP ratios of

Mongolia (102 percent), Papua New Guinea (94 percent) and Yemen (68 percent) are significantly higher than those of developing countries like Pakistan (38 percent), India (27 percent) and developed countries like Japan (19 percent) and the United States (US) (25 percent).

Trade integration can take place through various modes of liberalization – unilateral, bilateral, regional and multilateral. One of the major indicators of trade liberalization is reduction in border protection, in particular tariff barriers. According to World Bank (2004a, xvi), historically unilateral liberalization, which is usually linked to a broader programme of domestic reform, has accounted for most of the reductions in border protection. In fact, of the 21 percentage point cuts in average weighted tariffs of all developing countries between 1983 and 2003, unilateral or autonomous liberalization accounted for 66 percent tariff cuts, whereas multilateral commitments in the Uruguay Round (UR) of trade negotiations accounted for 25 percent. During the corresponding period proliferation of RTAs accounted for about 10 percent reduction.

Conventional wisdom holds that increased trade – particularly expansion of export – helps vulnerable economies generate much needed resources for financing their development efforts and alleviating poverty. However, what is required is not simply a process of export expansion, but also the promotion of developmental linkages between growing export activities and the rest of the economy. Achieving better human development outcomes by meeting specific goals and targets envisaged by the MDGs is the major challenge the LDCs and small LICs face in the context of trade integration. Three concerns are particularly noteworthy.

First, given the current structure of trade and trading regimes, trade integration alone does not help ensure sustained economic growth. Therefore, it is not possible for them to generate resources for investing in social sectors or infrastructure, which could help ensure better human development outcomes.

Second, trade integration has often generated ‘enveloped-growth’ pattern with certain sections of the economy gaining reasonably well, but the vast majority continuing to be marginalized. This phenomenon could invite conflict and social unrest in the already conflict prone countries, thus creating further constraints for the state machinery to achieve human development objectives. Despite significant export take-offs in a large number of LDCs since the late 1980s, they are simply not having a strong and sustained virtuous poverty-reduction effect (UNCTAD 2004a, v). This can be again ascribed to lack of linkage between export growth and large part of the economy, which is basically subsistence-based agrarian economy.

Third, open trade policies in LDCs and small LICs seem to have resulted in higher amount of imports – thus creating serious adjustment problems for the import competing sectors and a drain on scarce foreign exchange resources. Though import (of inputs and capital equipment) is equally necessary for achieving higher exports, the pace of export growth has not been that satisfactory – due to unfavourable market access conditions and domestic supply-side constraints. This has led to serious balance of payment (BoP) problems. The generous official development assistance (ODA), which they used to receive during the 1970s and early 1980s, has sharply declined since mid-80s. This could have provided much needed cushion against the deteriorating BoP. Most developing countries have been able to make up for this deficiency through inward foreign direct investment (FDI). However, the LDCs and LICs have failed to attract FDI. Some of them have fallen back upon workers’ remittances and income from tourism, but they cannot be considered permanent solutions due to the sheer volatility of such receipts.

Export diversification in the LDCs and small LICs is easier said than done, given the various supply-side constraints (to be discussed later) that dampen competitiveness of business enterprises. However, on the supply of niche products in which exposure to international competition is limited by virtue of the relatively unique nature of the product, they offer significant prospects (Box 3).

### Box.3: Niche products: An opportunity for small economies

Some landlocked or small countries do have chances of achieving higher export growth through alternative development options that better match their disadvantages and are commonly referred to as pertaining to the niche market approach to export production.

Of special interest are the trading opportunities in niche markets for nature-based (green) products such as organic fruits or vegetables; and woolen floor coverings/shawls using only natural fibers and vegetable dyes. These products mainly cater to the taste of ever-growing segment of 'green consumers' in the developed countries. Niche products could also cash on the unique cultural heritage of these countries – such as Kava, a traditional drink in several Pacific nations (e.g., Fiji, Samoa, Tonga, Vanuatu), which has the potential to be developed as an exportable item, both as a drink and as a medicinal plant. Yet some others, called endemic biological resources, are not only unique but also location specific.

Similarly, in the sphere of services, environment-based services, which depend on natural features such as unspoiled nature or environmental beauty, are considered market worthy. Environmental tourism in Nepal and Bhutan and "Bungalow tourism" in Vanuatu are the living examples of such services. Also in the tourism sector, more locally specific forms of specialization (such as yacht chartering in archipelagic waters or sports fishing) could be successful and at the same time protect the country from the full force of global competition, as experienced by the Maldives in the field of water sports.

Adapted from UNCTAD (1999), 109-17

### III. VULNERABILITIES RELATING TO TRADING PROSPECTS

The LDCs and small LICs, as a group, face serious vulnerability relating to trading prospects, a factor responsible for their poor trade performance, and dismal success in achieving sustained and broad-based economic growth and poverty alleviation, with serious implications for human development. This section attempts to discuss them in detail, with the help of some examples, where possible.

#### 3.1 Geographical constraints

Geographical constraints could be a major impediment to trading prospects of two types of LDCs and small LICs. While LDCs with access to sea, like Bangladesh, Cambodia and small LICs located close to international market centers are likely to perform better, landlocked LDCs and small LICs located far from the international market centers tend to perform poorly. Many landlocked countries have to face constraints on their transit trade that reduce their competitiveness. By way of example, UNCTAD figures show that the international transport costs for imports of African landlocked countries account for an average of 20.7 percent of the value of the imports, as compared to the world average of 5.1 percent and the average for African countries of 12.7 percent (UNCTAD 2004b, 1). Besides, they lack of control over the development of transport management and policy, which are shaped by the transit country with its own economic and social interests.

Mountain terrains add further to the vulnerability of some Asian LDCs, for example, Afghanistan, Bhutan, Nepal and Myanmar. First, it is highly cost-intensive exercise to construct road to facilitate cheaper means of transport – surface transport. Therefore, most mountainous regions are only linked by air transport, adding hugely to the cost of doing business. Second, due to scattered locations of houses, it is not cost effective to provide utilities – electricity and telephone connection. This also adds to the cost of doing business, preventing their integration into the national economy, let alone the international market.

This is, however, not to suggest that small economies, which are located in costal areas, are in particularly advantageous position. Those, which are located far from the major ports, city centers or markets, face severe cost disadvantages, even if they use their own ports. Further, they may sometimes depend on ports in neighbouring countries if their volumes do not justify enough ship calls (UNCTAD 2004a, 1). According to

Winters and Martins (2004) micro states' cost disadvantage measured by the percent deviation of the costs from those in the median country are, on an average, 221.6 percent in sea freight, 98.5 percent in telephone costs, 93.1 percent in electricity costs, and 115.7 percent in personal air travel (Cf Thomas, 2004).

### 3.2 Exposure to international shocks

The LDCs and small LICs are fairly open to international trade. Since their market size as well as production is very small, they can neither export nor import in huge quantities. Therefore, they cannot influence international prices; they are largely 'price takers' in the international trade. Any demand shock or supply shock in the international market affects their volume of trade and may even alter their competitiveness, if the situation of international shock persists for a relatively longer period of time. This increases the risk of them being trapped in international trade determined 'poverty trap' (Thomas 2004, 7).

While trade openness has forced them to specialize in certain products with comparative advantages – whether real or artificial – (e.g., commodities such as coffee, or manufactured products such as readymade garments), they have a very limited range of exports (discussed in the next sub-section). Any excess supply of these products from other markets makes them the net losers, as their relatively low profit margin is wiped out by the reduction in price due to excess supply in the international market. Their limited absorption capacity to withstand such international shocks makes them more vulnerable.

### 3.3 High export-concentration ratio

The LDCs have not been able to diversify their domestic production structures with regard to manufactured goods as well as primary commodities, which renders them particularly vulnerable to international market volatility. Of the 4,162 products exported by the LDCs to 30 major trading partners in 2000, 127 accounted for 90 percent of their total export trade. On an average, the top three commodities exported by each LDC usually account for over 70 percent of its total exports (WTO 2000). The export concentration ratios (defined as the share of the principal export product in the total export value) have remained high and largely unchanged since 1980 for all LDCs. Several countries greatly depend on particular primary commodity exports. What makes the situation even worse is that while exports of a single product may constitute a large share of their export basket, they count for relatively little in terms of the international supply, so that they are unable to influence world prices in a way that is beneficial to them (Chandrasekhar and Ghosh 2000).

An analysis conducted by UNCTAD and the Commonwealth Secretariat calculates export concentration indices and the number of exported products for selected LDCs. According to this study, despite sustained efforts to diversify their export base, the number of products exported by LDCs is very small (especially for Pacific LDCs such as Kiribati and Vanuatu) while for others it is well below the 1998 non-LDC world average. Also, for certain LDCs, the export concentration index is close to one and much higher than the average of non-LDC countries.<sup>4</sup>

### 3.4 Limited competitive ability and supply side constraints

The major elements of the structural weaknesses that underlie poor productive capacities and competitiveness in the LDCs and small LICs are supply side constraints. The lack of linkages within and between productive services and infrastructural sectors, insufficiently developed human resources, shortcomings in production technologies, deficiencies in physical infrastructure, and inability to generate resources to address these problems are their major supply side constraints (UNCTAD 1999). Further, other infrastructural bottlenecks include transport and communication problems, cumbersome bureaucratic procedures, lack of data on exportable items, and lack of awareness among the business communities about the rules and procedures (Adhikari 2002). The problem is further compounded by limited access to finance, which can be ascribed to the virtual absence of capital market in some LDCs and high interest rates on credit charged by financial institutions reflecting high risk (Adhikari 2005a).

Trade promotion and facilitation services such as access to business information (particularly on rules and procedure of the export markets), use of information technology, development of new products, advice on

standards, packaging, quality control, marketing and distributional channels, and functioning of trade promotion organizations are virtually non-existent in LDCs and small LICs. LDCs in particular also lack the capacity and resources to modernize and reform customs and other government agencies participating in trade transactions and simplifying export and import procedures (See Bhattacharya and Rahman 1999, 7).

### 3.5 Implementation problems

Implementation problems faced by the LDCs and small LICs can be broadly divided into two parts. The first relates to the structure of the agreements signed by these countries. As will be discussed later, the LDCs and LICs have been subjected to several WTO-plus commitments, i.e., commitments that go beyond the existing WTO rules – both at the time of accession to the WTO and while signing the bilateral or regional trade agreements. Since these conditions are often unreasonable, the LDCs and LICs find their implementation extremely onerous. The second relates to the capacity constraints of these countries. Such constraints include: a) lack of administrative capacity to understand the implication of the commitments and identify the policy flexibilities contained in trade agreements; b) lack of adequately trained human resources; and c) financial constraints to implement the agreements and create requisite institutions.

Agreement specific implementation problems have many facets. While agreements relating to tariff reduction can be implemented by the stroke of a minister's or a legislature's pen, agreements relating to customs valuation, intellectual property rights (IPRs) and standards require huge investment to bring them in full compliance with trade rules. Their implementation could have long term financial implications for the country – for example, investment in the purchase and installation of equipment and procedures, training of staff, etc. (see Finger and Schuler, 1999).

### 3.6 Capacity constraints

The major stakeholders of trade integration, namely government, private sector and civil society organizations (CSOs) have different limitations. Government is not only limited in its capacity to make the trade agreements work for trade expansion, its limited negotiating capacity means that trade officials will, despite good intentions, continue to compromise with national interests and human development priorities while signing trade agreements. Besides, there is limited a participation of the representatives of these countries in most of the multilateral negotiating processes because most of the Asia Pacific LDCs and LICs do not have a mission in Geneva. Those that have their missions in Geneva also have limited staff members devoted to participation in WTO negotiations.

Due to lack of understanding of the trade agreements and their potentials in the private sector, they are unable to exploit the available opportunities. Orientation on competition and competitiveness is at best limited. One of the major problems of the private sector is the lack of constant search for upgrading technology to bolster total factor productivity (TFP) through investment in research and development (R&D). While lack of awareness could be a reason for apathy, lack of financial resources acts as a major impediment to undertake such activities, which require huge investments.

Due to lack of resources and capacity for specialized research, a majority of CSOs are also unable to conduct informed advocacy at the policy level. They tend to design their campaign strategies, more often than not, based on their perception of how trade agreements work, which is not necessarily in sync with actual reality.

### 3.7 Exclusion from knowledge based economy

Knowledge based economy is the most promising sector in the global economy with potential to grow even faster in days to come. These include sector such as pharmaceutical, biotechnology and information and communication technologies (ICTs). Since these are technology intensive sectors, the LDCs and small LICs, which are largely technology-deficit countries, have not been able to harness their potential.

Most inventions resulting from R&D are protected by IPRs – a system of rewarding and recognizing the contribution of the inventor – by conferring monopoly rights for a certain period. For many rich countries,

IPR-intensive goods and services constitute a rising share of the income they derive from their presence in foreign markets (Fink and Maskus 2005, 2). However, for the LDCs and LICs protection of IPR is completely an alien concept. Though the development implications of strong IPR protection is a contentious issue and any attempt to harmonize it across the world under one-size-fits-all framework is bound to invite criticism,<sup>5</sup> the LDCs and small LICs should develop intellectual property protection capacity – without compromising with the flexibilities provided by Trade Related Aspects of Intellectual Property Rights (TRIPS) Agreement of the WTO. This is likely to spur investment in both primary and adaptive R&D and help them move up the technology ladder.

In today's society, ICTs play an important role in achieving one's competitive advantages. In the era of globalization, ICT revolution does not only offer genuine potential, but also presents the risk that a significant portion of the world will lose out (ILO, 2001). Applied to commercial needs, information technology can enhance foreign export marketing, improve the access of exporters and importers to foreign market information, establish and sustain linkages between buyers and suppliers, and facilitate access to training and technical assistance (OECD 2001, 50). Similarly, the role of ICT in trade facilitation – data processing and document clearing at the customs – cannot be overemphasized. However, the LDCs and small LICs are not only constrained by limited access to ICTs, they face a threat of losing out exacerbating their vulnerability due to the yawning disparity between their ability to make use of this technology on one hand and those of the developed and large developing countries on the other. This phenomenon known as 'digital divide' is apparent from Table 1.

Table 1: Digital exclusion among LDCs and small LICs of Asia and the Pacific (2003)

World and Countries	Telephone lines and cellular subscribers per 100 population	Personal computers in use per 100 population	Internet users per 100 population	DAI
Developed countries (2002)	102	36.4	34.3	0.77
World (2002)	36.5	9.9	10.1	0.48
Bangladesh	1.5	0.7	0.18	0.18
Bhutan	4.5	1.3	2.0	0.13
Cambodia	3.7	0.22	0.24	0.17
Mongolia	18.6	7.7	5.8	0.35
Myanmar	0.87	0.56	0.05	0.17
Nepal	1.7	-	-	0.19
Tonga	14.6	2.0	2.9	-
Vanuatu	6.9	-	3.6	0.24

Source: ITU website [www.itu.int](http://www.itu.int); and World Bank (2005)

As shown in the table 1, countries like Bangladesh, Myanmar and Nepal have less than 2 percent of the people connected to telephone lines (both landline and cellular put together), which are many times lower than global average. Likewise, internet user percentage of Myanmar and Bangladesh is less than 1 per hundred users. With such a rate of digital divide, it is impossible for these countries to reduce the gap in the face of ever increasing world average.

#### IV. VULNERABILITIES RELATING TO TRADE INTEGRATION

Trade integration, rightly or wrongly, has become a major priority of the LDCs and small LICs. As noted above, it can take place through various means. Since unilateral trade liberalization, which has resulted in most reduction in border barriers as noted above, has already taken place to the maximum possible extent, and such conditionalities are no more on the prescription list of the Bretton Woods institutions, they are not likely to become an important mode for trade liberalization. Moreover, since countries have realized the



virtues of reciprocal liberalization, they are more likely to follow other tracks – multilateral, regional and bilateral.

#### 4.1 Multilateral track

The WTO, with its 148 members and 24 countries in the process of accession, provides the multilateral forum for the liberalization of trade. Prior to the WTO coming into being (1 January 1995) multilateral trade relations used to be governed by the General Agreement on Tariffs and Trade (GATT), which was established in 1947. Countries, which could not become the founder member of the WTO when it was signed on 15 April 1994 at Marrakesh, have to enter the organization through accession. The rules relating to accession are loosely crafted in the form of Article XII of the Marrakesh Agreement Establishing the World Trade Organization. Since these rules are vague, incumbent member countries have exploited them to impose onerous conditions on the acceding countries. Unlike GATT, the WTO rules deeply intrude into national – beyond the border – policy measures, which are critical from the point of view of achieving human development objectives.

Despite these anomalies, several LDCs and LICs from Asia and the Pacific have either acceded to the WTO or are in the process of accession (See Annex 1). Motives for WTO accession include: a) binding commitments and policy lock in; b) predictability of market access; c) shelter against unilateral pressures from powerful countries; d) access to powerful dispute settlement mechanism; and e) role in shaping the future of world trade (See Adhikari 2004). However, in order to ensure that these motives are achieved in a way that contributes to achieving human development objectives, countries are not only required to have a clear-cut post-accession strategy, but also the necessary determination and capacity to implement the commitments.

Since WTO membership means joining an institution, where members have framed certain rules for its effective functioning, it is necessary for all the members to abide by them. The major difference is that the acceding countries are subjected to several unreasonable WTO-minus conditions (conditions that are imposed on the acceding countries thus preventing them from making use of certain rights contained in the WTO Agreements) and WTO-plus conditions (conditions that are imposed on the acceding countries, which are either not the requirement of the WTO or have not been undertaken by the existing members of the WTO – thereby creating new obligations). At times, it even appears that the WTO provision on accession was deliberately kept vague so that the existing members can interpret them to suit their requirements.

During accession negotiations, the objective of the existing members is to extract maximum concessions from any new applicant. This is evident by the flurry of unreasonable conditions all the acceding countries have been subjected to (See Annex 2). This is done for three reasons. First, it will help the existing members set a precedent for extracting higher concessions from other applicants in the queue. Second, it provides them benefits without them having to reciprocate. Third, they try to use accession terms achieved as an instrument in the multilateral trade negotiations (like the current Doha negotiations).

While the intensity of the onerous demands being placed on acceding countries are discussed elsewhere (See, Adhikari 2004; Butkeviciene et. al 2001; UNCTAD 2004a), some of them are worth highlighting here, with the help of new information and analysis. They are broadly divided into two categories – policy space and systemic issues.

##### 4.1.1 Policy space

Tariffs and Other Duties or Charges (ODCs): Most developing countries have not bound all their tariff lines and they continue to enjoy the policy flexibility to raise the level of tariff (even astronomically) if circumstances so dictate. However, all the acceding countries have been asked to bind tariff on almost all tariff lines. This is despite the fact that unlike in the case of agricultural products, total binding of tariff for industrial products is not a legal requirement. Such a requirement imposed on acceding countries is in stark contrast with binding coverage of the incumbents: Tanzania and Cameroon (0.1 percent); Mozambique (0.5 percent); Togo (0.9 percent) and Ghana (1.2 percent) (See WTO 2005, 303-6). Even a developed country like Australia has bound only 96.5 percent of its tariff lines; and Canada and Japan have bound only 99.7 and 99.5 percent of their

industrial tariff lines respectively (See WTO 2005). Moreover, despite the legal basis contained in Article II:1 (b) seen in conjunction with the Understanding on the Interpretation of Article II:1 (b) of the GATT 1994 to bind ODCs at the existing level but not to raise them any further, all the acceding countries have been asked to either bind them at zero or phase them out over a short period of time. Only two acceding countries which have so far been allowed to maintain ODCs with agreed timeline to phase them out are Bulgaria (WTO 2001a) and Nepal (WTO 2003a); all other have been compelled to bind them at zero from their date of accession. This is despite the fact that many WTO members still maintaining ODCs have never been challenged by their trading partners (Adhikari 2003).

**Special and differential treatment:** While application of these provisions is automatic for the existing members, the acceding countries have been asked to 'negotiate' them, on a 'case-by-case' basis. Majority of acceding countries have been denied these rights at the time of their accession.

**Elimination and/or bindings of export duties:** There is no provision in the GATT/WTO obliging members to bind, reduce or eliminate export duties. Virtually, all WTO members have avoided binding export duties in their schedules of concessions. However, some acceding countries have been compelled to eliminate export duties or bind them at a certain level.

**Services liberalization:** The idea of positive list approach introduced in the services negotiations during the UR was to allow countries to liberalize the sectors and modes of services in which they not only feel comfortable to liberalize, but also see benefits in opening up. However, acceding countries have been asked to make extensive commitments in various services sectors, much beyond what incumbent members have done. For example, out of the 12 services (including 'others services' meaning those sectors which are not included in any of the 11 normal categories) sectors and 155 sub-sectors. One could measure the gravity of the problem by contrasting commitment of Moldova (acceding country) with Tanzania (an incumbent member). While the former opened up 148 sub-sectors the later opened up only one.

**Intellectual property protection:** Article 27.3 (b) of TRIPS requires WTO members to provide protection to plant varieties either through patent, an 'effective' sui generis (of its own kind) system or any combination thereof (Adhikari and Adhikari 2003). While developing countries have chosen to put in place an effective sui generis system for the protection of new plant varieties, which suits their social, economic and environmental needs, developed countries argue that the International Union for the Protection of New Varieties of Plants (UPOV) model is the only effective sui generis system.<sup>6</sup> The developed countries are trying to impose this requirement on each acceding country.<sup>7</sup> Countries like China, Kyrgyzstan, Cambodia and other eastern European countries have been cajoled into signing onto UPOV as a part of their accession deal. Nepal was a major exception in the sense that it was able to fend off pressures from developed countries to become a member of UPOV, due to the collective efforts of the government and CSOs.<sup>8</sup> Moreover, the requirement of data protection, which is not mandated by TRIPS, is also being imposed on acceding countries, Cambodia being a living example (see Box 7).

**Participation in plurilateral agreements:** The rights and obligations emanating from the two plurilateral agreements, contained in Annex 4 of the WTO Agreement, apply only to the signatories to these agreements. However, as a part of their general approach to acceding countries, some members have been insisting that the acceding countries agree to accept, or at least enter into negotiations, to accede to these agreements. Accordingly, some of the acceding countries, such as Kyrgyzstan and Vanuatu, have been made to agree to such demand (Ognivtsev et al 2001,132).

**Participation in sectoral initiatives:** These are tariff reduction initiatives launched by some WTO members during and after the UR. These include: the "zero to zero" initiatives, the Chemical Harmonisation Initiative (CHI), and the Information Technology Agreement (ITA). For WTO members, participation in these initiatives is optional and coverage of products for commitments is flexible. However, all the acceding countries have been asked to participate in one or more of such initiatives, and all the developing countries but one

(Ecuador) which have acceded to the WTO, have made commitment to participate in one or more of such initiatives, with at least 10 of them making commitment to participate in all the three initiatives mentioned above (See also Annex 2).

#### 4.1.2 Systemic issues

**Non-market economy status:** Although there is no explicit requirement in the WTO agreements that a member have a market economy, a requirement that acceding countries have, fundamentally, such an economy is being pushed de facto by existing members as part of their leverage in the accession process (Michalopoulos 2002, 67). While China, Kyrgyzstan and Mongolia have been subjected to this condition, Vietnam faces an imminent danger of being treated in the same manner. This designation places acceding countries at a considerable disadvantage because it is used to apply different, less transparent and potentially discriminatory practices in the determination of anti-dumping duty<sup>9</sup> and other trade measures.

**Privatization of state owned enterprises (SOEs):** Questions about the privatization process of each acceding member country is invariably raised during the process of accession, though no rule within the WTO mandates countries to embark on the path of privatization to seek accession to the WTO. What the WTO does is to regulate the monopolies – that too with the objective of promoting fair competition. However, not all the SOEs are monopolies, and hence engaged in anti-competitive conducts. Despite this, a number of acceded countries, especially the economies in transition (including Cambodia and Mongolia), have been asked to periodically report to the WTO about the status of their privatization programmes.

**Investment regime:** The Agreement on Trade Related Investment Measures (TRIMs) deals with trade-related investment measures and prohibits five specific measures that are inconsistent with the GATT – one of them being so called ‘export balancing requirement’, which requires firms to meet certain export targets in order to be able to import their inputs. However, in accession negotiations, some WTO members have requested commitments to eliminate or refrain from introducing export performance requirements even if they are not linked to import volume or value. Moreover, requests for liberalization of the investment regime and application of national treatment to foreign investments across the board have been made in the accession negotiations (Butkeviciene et al 2001, 160).

**Non-application of certain provisions:** Article XIII:3 of the WTO Agreement allows members not to apply the WTO agreements to an acceding country upon notification before the approval of the accession terms. The US has invoked this Article for the accession of Georgia (disinvoked in 2001, after accession), Kyrgyzstan (disinvoked in 2000, after accession), Moldova, Armenia and Mongolia (disinvoked in 1999, after accession) according to the ‘Jackson-Vanik Amendment’ provision of Section 402 of the 1974 US Trade Act. Originally, this provision was introduced to enable the US government to deny unconditional MFN treatment to the Soviet Union and to all ‘non-market economies’ that deny or restrict the right of their citizens to emigrate (Butkeviciene et al 2001, 171). Article XIII – unlike its predecessor, i.e., Article XXXV of the GATT 1947 – allows WTO members to invoke this provision even after the acceding country has entered into tariff negotiations. Thus, acceding countries are exposed to the threat that invocation of Article XIII may be used as a bargaining chip to extract more commitments (Wang 1994).

#### 4.2 Regional and bilateral track

As noted above, an increasing trend towards lowering down market access barriers by entering into reciprocal or preferential agreements between a group of countries through RTAs is being observed, particularly during the 1990s and first half of the ongoing decade. The number of these agreements have more than quadrupled rising to around 230 by late 2004.<sup>10</sup> Trade between RTA partners now makes up nearly 40 percent of total global trade (World Bank 2004, 27). Since it is possible to have an RTA only among two members (e.g., India-Sri Lanka and Australia-New Zealand), BTAs are also considered a sub-set of RTA. While first generation of agreements mainly focused on dismantling trade barriers, the new agreements contain provisions for much deeper integration of the economies and also deal with ‘behind the border’ measures.

Similarly, while the first generation RTAs were normally among the members within the same geographical region, second generation RTAs are even cross-continental (e.g., Japan-Mexico and US-Morocco).

#### 4.2.1 Ongoing debate

Economists are sharply divided on whether RTAs are building blocs or stumbling blocs to multilateral trade liberalization.<sup>11</sup> Those who consider RTAs as building blocs to multilateral trade liberalization (See Summers 1991; Bergsten 1997; Baldwin 1997) argue that the benefits of trade creation outweigh the losses caused by RTAs; due to the ease in negotiations they not only promote faster trade liberalization, but also help developing countries lock-in reform much faster. It is certainly much easier for the like-minded small group of countries to agree to a particular trade liberalization agenda than at the WTO with 148 members having different of interests and priorities. As per them, RTAs often pioneer new liberalization ideas that can subsequently be generalized in the multilateral system; and they could often have important demonstration effect. Regional initiatives can accustom government officials 'through learning by doing' and thus increase the probability that they will subsequently move on to similar multilateral actions. As per the proponents of RTA, the political payoffs (peace dividends) of RTAs are as important as economic payoffs, but the former cannot be quantified.<sup>12</sup>

Those who label RTAs as stumbling blocs (see Bhagwati, 1999; Panagariya 1999) maintain that RTAs are inherently discriminatory, countries which are outside the system tend to lose, and there is a serious 'trade diversion' effect due to the requirement to import from within the member countries, which may not necessarily be the lowest cost suppliers, or the most efficient. Therefore, as the argument goes, RTAs are welfare reducing. They also argue that there are other systemic issues: due to their high visibility RTAs can energize and unify protectionist lobbies, turning them into effective obstacles to multilateral trade liberalization and that there is a diversion of scarce negotiating capital to negotiate RTAs. The latter problem is particularly severe for the LDCs and small LICs, with very limited human and intellectual resources to devote to trade agreements. Growing number of RTAs and overlapping rules of origin (ROO), tariff schedules and periods of implementation – referred to as 'spaghetti bowl' by Bhagawati – complicate the process of administration of the agreements. As noted by one commentator: "The picture is becoming increasingly complex as RTAs proliferate, change their goals, produce overlapping blocs, and take on a so-called 'hub and spoke' pattern."<sup>13</sup>

A balanced approach propounded by Bergsten (1997) is that of 'open regionalism' – which provides best of the both worlds: the benefits of regional liberalization without jeopardizing the continued vitality of the multilateral system. Under 'open regionalism' countries within the group reduce MFN tariff at more or less the same speed with which they reduce intra-regional tariffs and other barriers to entering into the agreement for the outsiders are not very high. A major analytical contribution to this theory is made by 'domino' theory of regional trade integration, developed by Baldwin (1997), which shall be discussed later. However, open regionalism has also been criticized by Panagariya (1999) and Srinivasan (1997), the later calling it an 'oxymoron'.

Contemporary viewpoints tend to suggest that regionalism and multilateralism can complement each other and that one should not feel threatened by the existence of the other. A comprehensive study done by World Bank (2000a) on the debate on regional integration, titled Trade Blocs concludes that regionalism is generally a building bloc to multilateral trade liberalization. It goes on to explain how benefits of trade creation resulting from an RTA outweigh the costs of trade diversion.<sup>14</sup> This conclusion is also supported by Ethier (1998), who argues that regionalism – by internalising an important externality – plays a key role in expanding and preserving the liberal trading order. Similarly, Baldwin (1997, 888) calls regionalism "half of the trade liberalisation 'wheel' that has been rolling towards global free trade since 1958."

#### 4.2.2 Future of RTAs

Nearly all countries belong to at least one RTA. There are only 12 countries that are not recorded as being party to an RTA, and many of these are small islands and principalities.<sup>15</sup> On average, each country belongs to

six RTAs, though there is a considerable variation across regions and levels of development (World Bank 2004, 29). Given the spate of RTAs and BTAs, it appears that this mode of trade liberalization is going to be very significant in days to come, due to the following reasons:

First, the failure of the fifth Ministerial Conference of the WTO held at Cancun led some countries, notably the US to accelerate the process of signing BTAs. This was stated in the statement made by the former USTR – Robert Zoellick immediately after the failure of the Cancun Ministerial (ICTSD 2003, 2). The fact that USTR has concluded most BTAs in the post-Cancun era reinforces this statement. Proliferation of RTAs/BTAs may serve as a threat to force unwilling parties to negotiate in earnest at the multilateral level, as was done with the EU during the UR (See Kelegama and Adhikari, 2002).

Second, due to the domino effect of regional integration (see Baldwin 1997) and the problem of bystanders suffering hugely from exclusion from the RTA rather than from the exclusion from the multilateral trading system (see Deardorff and Stern 2004), countries are likely to increasingly become parties to some RTAs or the other. Of the several theories of regional integration domino effect seems to be the most powerful one. This explains in part the reason for the expansion of the EU from original six countries to 15 and now to 25. The possibility of facing exclusion due to US-Mexico trade, when the trade talks were going on between the US and Mexico, Canada requested the parties to trilateralize talks which led to the birth of North American Free Trade Area (NAFTA) (Baldwin 1997). There are several examples from the Asia Pacific region as well, which shall be discussed later.

Third, there is a competition among the economic superpowers for gaining incremental market access in developing countries. While the EU was the first one in the race and has already signed several agreements with Eastern European, Mediterranean, African and Asian countries, the US is a close second in the race. Though the US started its drive towards regional economic integration much later, it is expanding free trade agreements with leaps and bound – with countries in Asia, Africa and Latin America. The US has also been making efforts to enhance market access through BTAs with countries as diverse as Singapore, Jordan, Chile, Australia and Morocco. Moreover, through Asia Pacific Economic Cooperation (APEC), the US is aiming at maintaining its clout in Asia.

Fourth, which is related to the third one, RTAs in Asia is seen as a defensive response to the regionalism trend elsewhere. The expansion and deeper integration of the EU and the establishment of continental economic blocks in the Americas including the proposed Free Trade Area of the Americas (FTAA) raise the concern about the polarization of the world economy. Asian exporting countries worry that they are becoming increasingly vulnerable to the discriminatory practices of RTAs that could impede their entry into these markets. The 1997-98 Asian crisis clearly demonstrated the high degree of economic and financial interdependence and interconnectivity among East Asian economies and created the Association of South East Asian Nations (ASEAN) +3 process of regional financial cooperation (Abidin, 2004).

Fifth, since parties to RTAs and BTAs make deeper liberalization commitments, which are not possible at the WTO, developed countries, in particular the US are finding it attractive to sign BTAs. In such a scenario, the US will enjoy the twin luxury of not only being able to pick and choose its partners and not make commitments to open its market for all the WTO members; but also impose its institutional preferences on other countries, as demanded by domestic interest groups. The way alliance-building and other dynamics work in the WTO, it would be unthinkable for the US to impose the investment, labour, environmental and competition related standards of its choice in the WTO. However, through BTAs the USA has not only succeeded in imposing these rules to its BTA partners, but has also obliged them to sign onto TRIPS-plus IPR standards and GATS-plus market opening commitments on services (see Annex 3).

However, a dangerous trend is visible in the way developed countries, particularly the US, are choosing their developing country partners. While developing countries are driven by their 'economic agenda', developed countries are increasingly seeking FTAs as part of their global 'political agendas'. US FTAs are ever

increasingly being used for political objectives, to reward countries which acquiesce to US policy objectives.<sup>16</sup> Some of these FTAs are also being used to create defection among the developing country groups, which oppose US negotiating strategies at the WTO (VanGrasstek 2004).

#### 4.2.3 RTAs in Asia-Pacific Region

The Asia-Pacific region is a relatively latecomer in the regionalism scene. Most of the countries in the region chose to liberalize either unilaterally or through multilaterally – on an MFN basis. The earliest preferential arrangement in Asia was the Bangkok Agreement – established under the auspices of United Nations Economic and Social Commission for Asia and Pacific (UN-ESCAP) – signed in 1975, between Bangladesh, India, Sri Lanka, Korea, Laos, the Philippines and Thailand, but it only covers tariff elimination and its efficacy is limited. China signed up to the Bangkok Agreement in 2000 (Abidin 2004). Two LDCs from South Asia, namely Bhutan and Nepal are in the process of becoming parties to this Agreement.

ASEAN countries (Brunei, Cambodia, Laos, Indonesia, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam) formed the ASEAN free trade area (AFTA) in 1992. AFTA has almost completed the liberalization of trade in goods and its attention is on the integration process in services, investment and other trade-related areas. The AFTA liberalization obligations among member countries vary according to the level of development of each country (Abidin, 2004).

Seven member countries of South Asian Association for Regional Cooperation (SAARC), namely Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan and Sri Lanka entered into preferential trading arrangement – South Asian Preferential Trade Agreement (SAPTA) – which came into effect from 1995, but it could not achieve desired success (Kelegama and Adhikari 2002). They have now decided to enter into a Free Trade Agreement – South Asian Free Trade Area (SAFTA) – slated to start from 1 January 2006, with the target to achieve full liberalization of trade in goods by 2016. There is limited focus of the agreement on NTBs, services and investment liberalization.

Three South Asian countries and two South East Asian countries came together to form an Economic Cooperation arrangement, named Bangladesh, India, Myanmar, Sri Lanka and Thailand – Economic Cooperation (BIMSTEC).<sup>17</sup> Two new members, namely Bhutan and Nepal have also joined this initiative, following which a free trade agreement (BIMSTEC FTA) has been signed in February 2004, with the target of achieving full liberalization by 2017. This envisages deeper level of liberalization compared to SAFTA because it covers not only tariff barriers, but also NTBs. Moreover, it also covers services and investment issues.

In the Pacific region, the major FTA is the Australia-New Zealand Closer Economic Cooperation Agreement (CER), which was established in 1996 and is probably the most successful economic integration in the region (Abidin 2004). Pacific Island Forum (the Forum) was established in 1971 to provide the Pacific Island countries, Australia and New Zealand with a forum to express their joint political views and to cooperate in areas of political and economic concern (ESCAP 2004). It is also a part of Pacific Islands Countries Trade Agreement (PICTA), an accord signed in August 2001, to lower tariffs and NTBs among the Pacific island states under the umbrella of the Forum. The Agreement does not deal with services and investment, unlike other recently formed RTAs, but it does contain a provision on government procurement.<sup>18</sup> The Forum has also concluded agreement on Pacific Agreement on Closer Economic Relations (PACER) on the same day as PICTA was signed. This Agreement will go into force among the 16 member states of the Pacific Forum as soon as seven countries have ratified it. Besides the 14 Forum Island Countries (FICs), it also includes Australia and New Zealand, which are excluded from the PICTA (Adhikari 2004a)

The first trans-continental regional economic cooperation in the Asia-Pacific is APEC modeled on the concept of 'open regionalism' (discussed above). Signed by 21 members drawn from the littoral of Pacific Ocean, APEC is the only inter-governmental grouping in the world operating on the basis of non-binding commitments, open dialogue and equal respect for the views of all participants. Unlike the WTO or other

multilateral trade bodies, APEC has no treaty obligations required of its participants. Decisions made within APEC are reached by consensus and commitments are undertaken on a voluntary basis. 'Bogor Goals' adopted by the leaders of APEC member countries, envisage free and open trade and investment in the Asia-Pacific by 2010 for industrialized economies and 2020 for developing economies.<sup>19</sup>

Asian countries have become equally active in signing BTAs. South Asian countries – particularly India is the leader in this initiative, by signing bilateral FTA with Nepal and Bhutan to begin with. Later India signed FTA with Sri Lanka, which is now advancing towards Comprehensive Economic Partnership Agreement (CEPA). A typical hub-and-spoke pattern is emerging in South Asia, with India being the hub and other relatively smaller economies in the region being the spokes. This is in part a reflection of still somewhat tense relations between India and Pakistan, the later of which is in an advance stage of signing a bilateral FTA with Sri Lanka and is in the process of negotiating one with Nepal. This phenomenon is unique in South Asia, where despite the existence of an FTA at the regional level, two relatively better off countries are signing FTAs with their smaller neighbours. Not that smaller countries remain mute spectators. Commerce Ministers of Bangladesh and Nepal held talks in October 2004 to push for a preferential trade agreement, to begin with (Dahal, 2005 – Trade Insight)

Among the South East Asian countries, Singapore took the lead by signing a bilateral FTA with New Zealand in 2000. It has since entered into five other BTAs – with Japan, European Free Trade Area (EFTA), Australia, Jordan and the US. It is in the process of negotiating BTAs with Bahrain, India and others. Following Singapore, Japan is negotiating BTAs with Malaysia, Thailand, the Philippines and Korea. Apart from bilateral FTAs, ASEAN as a group is making significant strides in expanding its partnership with other countries and groups. The ASEAN leaders' summit in 1999 endorsed the ASEAN + 3 regional grouping, comprising ASEAN, China, Japan and Korea. Meanwhile, ASEAN is negotiating individual FTAs with them. As a 'domino' effect of this, the US has proposed an ASEAN-US initiative (AUI). ASEAN will soon start trade talks with the EU. Finally, in line with India's look-East policy which matches with ASEAN's desire to expand its orbit, talks on India-ASEAN FTA is likely to start from this year.

#### 4.2.4 Intents and implications

According to World Bank (2000a), South-South RTAs are likely to result more in trade diversion than trade creation. This is premised on the sound theoretical basis, because large and more efficient ones in general are likely to reap most benefits of trade liberalization. The result for smaller countries could be just the opposite: industrial closure, loss of income, income divergence, and increased poverty. This can be explained with the help of a real life example. Take two East African countries Kenya (more competitive) and Uganda (less competitive) to elaborate the point. Kenya not only exports more because of access to the Ugandan market, but also because of the preferences afforded by an FTA, whereas Uganda not only loses by the flooding of imports from Kenya, which swamps its domestic manufacturers, but also because it cannot compete in the Kenyan market (even at a zero duty) because of greater comparative disadvantage.

Further, due to resources, superior technology and proximity to larger markets, migration of light industries to Kenya is inevitable. These factors lead to income divergence, unlike in the case of rich (or less poor) countries, where income convergence is inevitable (e.g., Spain and Portugal after joining the EU), primarily because of vast differences in comparative advantage in the initial stage (i.e., lower wages). Therefore, poorer countries, which are at comparative disadvantage, are less likely to cooperate. In fact, the collapse of the East African Community (EAC) in 1977 is ascribed to the failure of poorer countries like Uganda and Tanzania to reap the benefits of trade liberalisation, while the entire benefits accrued to the relatively higher income country – Kenya (World Bank 2000a, 52).

However, the theory as well as example of a failed EAC can be contested with the help of the examples of Southern Common Market (MERCOSUR) and Indo-Sri Lanka Bilateral Free Trade Agreement (ILBFTA). In the first case, an economic powerhouse like Brazil alone has not taken away the benefits; other members have also obtained reasonably good shares of benefits. In the second case, despite the differences in economic size

and similar level of comparative advantages, both the countries are reaping significant benefits. Despite fears expressed by many pessimists, the Agreement led to reducing Sri Lanka's trade deficit with India from 11:1 in 1999 to 5:1 in 2002. Trade has been growing rapidly between these two countries, such that India is the 5<sup>th</sup> largest export destination for Sri Lanka (as opposed to 20<sup>th</sup> rank before the Agreement) and India has become the largest source of import to Sri Lanka, accounting for 14 percent of overall imports. As a logical second step, India and Sri Lanka are now negotiating for deeper economic integration (Kelegama 2003). What the Sri Lankan experience shows is that if the regulatory framework in an RTA is correctly designed to accommodate the disparity between the countries (through S&DT), then a small country could, in fact, gain from an RTA. In this case, the time frame of tariff phase out, ROO, and negative list were designed to accommodate the smallness of Sri Lanka's export and production capacity (Kelegama and Adhikari 2005, 122).

The issue of S&DT seems to have been kept in mind at the time of negotiating all three major agreements within Asia – ASEAN, BIMSTEC and SAFTA. ASEAN and BIMSTEC provide higher transition periods for certain countries (new entrants or LDCs as the case may be) to implement tariff reduction. SAFTA goes much beyond that (see Box 4). However, it is yet to be seen how they are going to be actually operationalized.

#### Box 4: S&DT provisions within SAFTA

Apart from recognizing the need to provide S&DT to the LDCs in the preamble, the SAFTA Treaty contains the following specific S&DT provisions:

**Trade liberalization programme:** For the first round of tariff cuts, to be achieved in two years, developing countries are required to reduce their tariffs to 20 percent, while LDCs are required to reduce them only to 30 percent. For the second round of tariff reduction, which will bring down the tariffs to 0-5 percent, India and Pakistan are given five years' time, Sri Lanka six years and LDCs have been given eight years.

**Sensitive list:** LDCs have been provided with flexibility to seek derogation in respect of the products of their export interest while developing sensitive list.

**Safeguards measures:** Safeguards measures cannot be taken against LDCs products as long as its share of imports of the product concerned in the importing Contracting State does not exceed 5 percent, and collective share of all the LDCs put together does not exceed 15 percent. This appears to be a straightforward point.

**Technical assistance:** Technical assistance and cooperation arrangements designed to assist LDCs in expanding their trade with other Contracting States and in taking advantage of the potential benefits are also envisaged.

**Revenue compensation:** Members agree to establish an appropriate mechanism to compensate the LDCs for their loss of customs revenue.

#### V. HUMAN DEVELOPMENT IMPLICATIONS OF TRADE INTEGRATION

As such there is no organic link between trade integration and human development. As remarked by Rodrik (2001) "Trade liberalization is not a reliable mechanism for generating self-sustaining growth – let alone human development." Conventional wisdom holds that trade is linked to human development through economic growth, which could contribute to human development if that resulted in increased income and higher government revenue which could positively influence human development via increased investment in social and productive sectors (UNDP 2003a). While broadly based economic growth is necessary for human development, it is not sufficient. Human development also requires enlarging people's choices and opportunities – especially poor people's (UNDP 2003a, 21). Translating trade and growth into human development is a tall order, but with appropriate policies and institutional arrangements, some dent can be made (Box 5).



### Box 5: Translating trade and growth into human development

Even though there is a strong link between trade and growth, there is no automatic link with human development. Egypt and Pakistan achieved annual export growth of more than 5 percent and per capita income growth of more than 3 percent in 1985–97, yet both still have far to go in human development. At the other extreme, countries can open their economies, but generate neither growth nor human development. Russia generated trade and attracted private capital flows by opening in the 1990s, yet economic stagnation and human deprivation are serious.

By contrast, the Republic of Korea managed trade and growth to improve its human development. The main elements of the Republic of Korea's success are: a) A pro-growth strategy, with a commitment to poverty reduction; b) Bold economic reforms, with sound macroeconomic policies and a focus on price reforms; c) Institutions oriented to the market, with a restructuring of banking and financial institutions; d) An emphasis on rural areas and agriculture, with widespread land reform; e) Extensive public provision of social services; and f) Redistributive income policies, creating more labour-intensive employment and instituting measures for social protection.

Similar policies in Botswana, Chile, Malaysia and Thailand have also translated good performance in trade into economic growth—and into the well-being of their people. Contrasting the examples of Poland and Russia, a major lesson is that capturing global opportunities in trade requires a comprehensive package such as building up institutions, putting in place democratic and participatory processes and ensuring transparency and accountability. These were present in Poland's transition towards market based economy, but not in Russia; and the results are evidently clear.

Source: UNDP (1999), 85-86

It is indeed a daunting task to try and establish a firm correlation between trade integration and human development because the impact of the former on the latter could go into either direction. Before moving further, it is also necessary to highlight a major caveat. Since most of the RTAs in Asia and the Pacific Region are still evolving, there is a lack of empirical evidence to understand their implications on human development. It is even more challenging to assess the implications of WTO accession on human development. Such implications could be better gauged if data and information were available on the socio-economic, and political impact of WTO membership on countries which have acceded as early as 1997 (Mongolia) and 1996 (Bulgaria and Ecuador). It is useful to have information, for example, on the impact of WTO accession on FDI, technology transfer, government revenue, aggregate government spending on social sector et al. Though these data and information are available in crude form and can be analyzed to reach to tentative conclusions, their robustness could be established only if the impact of other variables could be separated. Such an exercise requires a regression analysis, which is beyond the scope of this Chapter.

The existing literature on the impact of WTO accession is not only scarce, but also highly specialized and not necessarily relevant from human development perspective. For example, Evenett and Gage (2005) only focus on the impact on trade flows of four countries after WTO membership and fails to establish any clear cut linkage between WTO membership and increased trade flow – mainly exports; Rose (2004) challenges the argument that GATT/WTO membership could actually increase trade; and Subramanian and Wei (2003) conclude that the WTO promotes trade, strongly but unevenly. Due to these limitations, most of the analyses made in this section deal with prospective impacts, based on available literature.

#### 5.1 Institutions and governance

Trade integration could be used as a means to create, design and strengthen supportive institutions at the domestic level. To the extent trade integration contributes to trade policy reform, it can be hoped that supportive institutions will be created. Trade integration, in general, creates both winners and losers. Those who can organize themselves (such as private sector) exert pressures on the government and lobby for compensation or 'side payments'. However, those who cannot organize themselves (such as farmers, workers and tax payers) will neither be able to press for compensation nor for any 'side payments'. While farmers protected by high tariff barriers may lose their livelihood security, workers in import competing industries might lose their jobs and tax payers may have to bear the additional burden of direct taxes imposed on them by the government to augment their revenue because of reduction in customs duty due to trade liberalization.

In such a situation, sensible and responsive governments create social safety nets in the form of providing unemployment allowances, retraining facilities, assistance to business entities in introducing necessary structural adjustments etc., and by creating additional employment opportunities. Indeed, there is a striking correlation between economies' exposure to foreign trade and size of its welfare state. It is in the most open countries such as Sweden, Denmark and the Netherlands, that spending on income transfers has expanded the most (Rodrik 1997). It is not surprising that these countries are amongst the best achievers on human development front. Similarly, a middle income developing country Ecuador has enacted a new Social Security Law in 2001, after its accession to the WTO and after signing several regional trade agreements. This law, among others, makes a provision of unemployment allowance for those in private and public sector losing jobs.<sup>20</sup> Likewise, in 2001 Mongolia, a small LIC, obtained loan from ADB to strengthen its social security programme, post WTO accession. The programme will, among others, help the unemployed and underemployed to find jobs.<sup>21</sup>

On the contrary, blame-shifting and non-responsive governments do exactly the opposite. They simply wash their hands off by putting the blame on foreign forces, or even worse the WTO. If the second category of the governments could be convinced of the need to create an institution of social safety net, this would serve a useful purpose for the entire country. In the future, should the country feel like further reducing its trade barriers, it will be able to garner a broader political support for the same. The reverse can be equally true – if domestic political support for trade erodes, return to old-style protectionism becomes a serious possibility (Rodrik 1997, 54).

Other institutions such as those relating to protection of property rights, enforcement of contracts, equality of opportunity, transparency, protection of consumers from fraud and deception, setting up standards for import, sale and export of goods and services, and promoting competition and competitiveness of domestic enterprises are also needed to take advantage of trade integration. All of these contribute to better human development outcomes.

In general, economic integration has also been shown to have an important impact on reducing corruption, increasing government responsiveness, and improving the quality of economic policies (ADB, 2001). It is also argued that trade integration and binding rules help country improve its governance system since discretionary powers breed corruption and rent-seeking behaviour. By making a binding commitment through trade agreements and locking-in reforms, the hands of the politicians and civil servants could be tied. It would be difficult, if not impossible, for them to change the rules and regulations merely to appease the vested interests. Moreover, exposing domestic firms to foreign competition means that they would themselves want to enhance their competitiveness. When they realize that corruption is a tax on their efficiency and a major barrier for them to take advantage of market access opportunities, they themselves will become a major constituency advocating for good governance. This has a higher payoff than trade liberalization per se as far as improving human development situation is concerned. Good governance, once institutionalized, does not only smoothen trade flows across nations, it can create a culture, which will help ensure, among others, that social safety nets function properly and people's fundamental rights to food, nutrition, health, sanitation, education, employment securities are both protected and promoted. Such a culture is likely to contribute to positive human development outcomes.

## 5.2 Policy space

While efficiency – the buzzword on economic literature – is something trade agreements aim at achieving through the removal of economic distortions, the equity consideration, which is more important for human development, should also be taken into account during the process of trade policy making as well as signing various trade agreements. As it is, a basic tension exists between setting trade rules and providing member countries space to design policies suited to their economic situations. The current trade regime takes a one-size-fits-all approach – one that invariably reflects the needs and demands of powerful industrial countries (UNDP 2003a).

This approach would work if all the parties of trade agreement had similar needs from the system. But wide disparities make it difficult for some members to comply, for example, with many WTO agreements (UNDP 2003a, 63). In fact, policy space is good not only for development; it is also good for trade. When developing countries can grow their economies, they can also expand their trade volumes (Rodrik 2004). Poor countries need space to follow development policies that rich countries no longer require. When countries use the trade system to impose their institutional preferences on others, it erodes the system's legitimacy and efficacy. Trade becomes contentious when it unleashes forces that undermine the norms implicit in domestic practices (Rodrik 1997, 5). Trade rules, at best, should seek peaceful co-existence among national practices, not harmonization (UNDP 2003a, 67).

Various trade rules restrict the policy space of the governments to achieve their human development objectives. The issue of policy space becomes even more important in the context of WTO accession and signing BTAs with developed countries. For example, in the context of WTO accession, what is provided by the WTO agreements in the form of policy space (such as S&DT provisions) is taken away at the time of accession. However, certain agreement provides much more policy space to WTO members. For example, the General Agreement on Trade in Services (GATS) Agreement, by allowing the members to make selective liberalization commitment and maintain certain conditions on both market access and national treatment, respects the rights of members to pursue their human development objectives. As mentioned above, policy space is mostly taken away at the time of WTO accession, if the acceding countries are not extremely cautious about this reality or they are unable to negotiate reasonable terms of accession. In this case, the approach taken by Nepal is quite instructive (Box 6).

#### Box 6: Nepal's cautious approach to liberalisation of services sector

The Schedule of specific commitments submitted by Nepal at the time of accession (WTO, 2003a) reveals that it has liberalised 11 services sectors and 70 sub-sectors, which, on the face of it, is very high for an LDC. However, a thorough study of the limitations entered in horizontal commitments as well as market access and national treatment columns tells us a different story. Nepal entered into extensive negotiations with the developed member countries during the process of services negotiations. However, the objective of Nepal was, right from the beginning, to liberalise only those services sectors in which: a) Nepalese private sector may never get involved given the huge sunk cost and high gestation period (e.g., pipeline transportation); b) Nepalese private sector is already competitive and is confident that it would be able to outperform the foreign service suppliers, even if the sector concerned is liberalised (e.g., banking services); and c) sectors where employment potential for the locals are high (e.g., computer and related services).

A few other major cautious approaches taken by Nepal include : a) capping foreign investment in most sectors at 51 percent; while in some others at 66-67 percent and only in two sectors at 80 percent; b) the requirement that a majority of the board members of basic telecom providers should be Nepalese nationals; and in the case of financial institutions, composition of the board should be proportionate to the shareholding pattern; c) foreign banks, with minimum 'B' rating by credit rating agency can only establish branch in Nepal for wholesale banking (not retail banking); d) incentives and subsidies be available only to enterprises wholly owned by Nepalese nationals; e) not allowing foreigners to purchase or own land in Nepal; and f) movement of natural persons be limited to intra-corporate transferee at the executive, manager or specialist levels with a proviso that number of such transferee shall not exceed 15 percent of the number of local employees in the firm.

Source: Adhikari (2004a)

### 5.3 FDI and technology transfer

To the extent trade agreements enhance the predictability of the business environment, they are likely to stimulate the inflow of FDI. The relationship of human development with FDI is as unclear as with trade integration. Yet, FDI, managed properly, could stimulate growth, facilitate technology transfer, raise total factor productivity and incomes for the locals, and result in additional government revenue. Only quality investment – which is channeled into desired sectors and which has a strong linkage with the local economy –

is likely to achieve the above mentioned objectives. If these objectives are achieved, they could significantly contribute to positive human development outcomes.

However, determining the extent to which FDI levels are influenced by trade integration in reality is a difficult task as there are so many factors, which determine investment decisions. They include traditional factor such as market size, administrative bottlenecks, entry restriction and risk factors as well as non-traditional factors such as cost factors, complementary factors of production and openness to trade (Nunnenkamp 2000). A simple analysis of data on FDI inflow, post-WTO accession, for example, reveals that there is no clear cut relationship between trade openness (which can be used as a proxy for trade integration) and increased inflow of FDI (See Adhikari 2004). This finding is consistent with Nunnenkamp (2002, 35), who found non-traditional determinants including openness to trade, though mostly revealing the expected correlation with FDI, having typically not become more important with proceeding globalization. The only area in which openness to trade could contribute to FDI inflow is on manufacturing sector (Taylor 2000).

Some even argue that strong IPR regime – which trade agreement aids in achieving – could stimulate the flow of FDI. However, evidence is inclusive about the responsiveness of FDI to intellectual property regimes. Although surveys of foreign investors typically indicate concerns for IPRs, this is often of secondary priority (Mansfield 1995). Maskus (2000) concludes that countries (especially low income countries) should focus on their overall investment climate to attract more and high technology investment, rather than to fine-tune their IPRs. Other studies have found that weak [IPR] laws and weak enforcement deter investment in middle income countries, but the results for low income countries are inconclusive (World Bank 2004, 110).

Another related issue is technology transfer, not least because the acceding LDCs and LICs lag behind technology frontier and confront the issue of how best to bridge the technology gap so as to acquire knowledge and expand knowledge base. Technology transfer is becoming more difficult in certain sectors. For example, tighter IPRs raise the price of technology transfer, and risk blocking developing countries out of the dynamic knowledge sector in areas such as computer software and generic drugs (UNDP 1999, 66).

The process of technology diffusion, regardless of the channel by which it occurs, is neither automatic nor costless, as most traditional neoclassical models assume (Saggi 2002, 351-2). There are two channels through which technology transfer occurs, namely direct channel such as trade in technology, joint venture, licenses and FDI and indirect channel such as international trade in goods and services, movement of labour and imitation (Saggi 2002, 352). Open trade policies are critical for developing countries in attracting technology. But openness is not sufficient – there needs to be absorptive capacity and ability to adapt foreign technology, both of which are related to human capital endowments and investment in R&D intensive industries. To the extent trade integration induces open trade policies, there is bound to be some degree of technology transfer to the local enterprises/personnel of the integrating countries. Technology transfer and diffusion can contribute to improved state of human development via productivity growth it ensues.

While countries like South Korea made extensive use of national policy tools such as screening and choosing investors that were more willing to transfer technology (UNDP-ATI 2003, 7), multilateral processes could be even more critical in achieving this objective. TRIPS contains provisions relating to international technology transfer. Article 7 notes that IPRs should contribute to the promotion of technological innovation and the transfer and dissemination of technology. Article 8.2 recognises that countries may wish to adopt policies to prevent the abuse of IPRs by right holders or the use of practices that “adversely affect the international transfer of technology.” Finally, Article 66.2 of the Agreement requires the developed countries to provide incentives to their enterprises and institutions to transfer technology to the LDCs. However, given the fate of its implementation aspect, there is no reason to be optimistic about this provision. This has probably led some commentator to argue that multilateral efforts to identify actions that governments should pursue to encourage international technology transfer are largely of a best-endeavour nature (Hoekman, et al 2004).

### 5.3 Public health

The three health related MDGs (reducing child mortality, improving maternal health and combating diseases) are influenced by regimes of IPR and the potential of trade in services, which influence availability and pricing of health services and drugs (Rajivan, 2004, 8). Access of poor people to affordable medicines could be threatened by the strong IPR regimes. It has been well established that intellectual property protection results in increased prices of protected products, including medicines.<sup>22</sup> Prior to the TRIPS Agreement of the WTO, non-availability of product patent in pharmaceutical sector allowed for the development of domestic industries using different methods to produce mainly generic drugs, similar to but far cheaper than the original brand names. The difference is highlighted by contrasting drug prices in Pakistan, where there were patents, to India, where there were none. Despite similar economic status and pharmaceutical industry, it was found prices of select pharmaceutical products in Pakistan were between 3 and 14 times higher than that of India (UNDP 1999, 69). After all, TRIPS was drawn up with remarkably little analysis of its expected economic impacts. The costs of implementation – revising laws, training officers, testing and enforcing patents – are high, yet the benefits are unclear (UNDP 1999, 75).

By restricting the ability of the companies in the South to produce affordable, generic version of drugs, once the transition period for the providing 'product' patent expires, TRIPS is all set to create a public health crisis in Asia and the Pacific where more than seven million people suffer from HIV/AIDS and almost half a million people die every year as a result (ADB/UNAIDS 2004). This impact is more pronounced in the case of Cambodia, which has recently acceded to the WTO. Unfortunately, it is the one that was forced to give up the policy flexibility contained in the WTO, at the time of accession.

#### Box 7: TRIPS and Looming Public Health Crisis in Cambodia

It is estimated that 2.8 percent of the adult population in Cambodia is infected with HIV/AIDS, among the highest in Asia; that many tens of thousands have already died as a result; and that possibly two hundred thousand people including children will develop HIV/AIDS within the next 5-10 years (Ouyahia-McAdams, 2002). In such a situation, the ability of the country to achieve its human development objective in general and Goal 6 target 7 of Millennium Declaration in particular is severely restricted by its inability to administer anti-retroviral (ARV) therapy to its people infected with HIV. Currently, only 700 patients have access to generic ARV drugs distributed by humanitarian agencies and NGOs (Macan-Marker, 2003).

As a WTO-plus requirement, Cambodia was compelled to provide early (prior to the expiry of transition period) protection to undisclosed test or other data for pharmaceutical products for five years. This is going to have a devastating effect on its public health policy. This requirement will prevent test data from being used by the regulatory authority to assess a bio-equivalent generic, and thereby slowing down the production or import of generic versions of new patented medicines after patent expiry. The generic producing or importing company would have to repeat the trials – expensive and slow – or wait for five years (Charveriat and Kirkbride, 2003).

This requirement will make, among others, ARV medicines even more scarce than at present resulting in price increase. With the increased price not only in Cambodia but also in India – which is the major supplier of ARV drugs to Cambodia – because of its recent TRIPS-compliant legislation, percentage of people being administered ARV therapy is likely to decline further. This is likely to create serious public health crisis in Cambodia.

Source: Adhikari (2004a)

While the Doha Declaration on TRIPS and Public Health is considered a laudable effort on the part of the WTO members to increase both affordability and accessibility of medicines for poor people suffering from HIV/AIDS Malaria and other diseases in most developing countries and LDCs, access is still restricted for countries without sufficient manufacturing capacity. The Decision of 30 August 2003 (WT/L/540) titled Implementation of paragraph 6 of the Doha Declaration on the TRIPS Agreement and Public Health is likely to restrict the positive outcomes. With the current rate of access to medicine, which is bound to deteriorate once product patent is provided on pharmaceuticals, it is impossible for most LDCs and small LICs of the Asia-Pacific

region to meet the Goal 6 of the Millennium Declaration to have halted by 2015 and begun to reverse the spread of HIV/AIDS.

On the other hand, the liberalization of health services under GATS could open up the possibilities for people to enjoy higher quality of health services – but such opening may not necessarily make the health service affordable and accessible to everyone. Rapid commercialization of health services without due regard to equity and accessibility, combined with the pressures to reduce public spending on health, can be particularly harmful to human development. For example, cost recovery programmes including introduction of user fees and price increases for health services led to a decline of up to 50 percent in the use of medical services in countries such as Ghana, Kenya and Nigeria (UNDP, 2003a).

#### 5.4 Empowerment, representation and participation

Empowerment is an all-encompassing notion that addresses the people's capability to shape the processes and events that affect their lives, not just on the economic front, but also the socio-political-cultural (UNDP-ATI 2003, 2). Therefore, it is critical that people, communities and groups – broadly defined as stakeholders – have a voice in trade policy making. Unfortunately, mechanism for consultation on trade policy among government and other stakeholders is weak or non-existent in most LDCs and small LICs of the Asia Pacific region, due mainly to three problems. First, capacity of the stakeholders to understand the implications of trade rules and voice their concerns is limited. Second, governments in most of these countries have a tendency to claim 'monopoly over wisdom' and are infamous for shunning the stakeholders in the policy making processes. Finally, a few non-governmental organizations (NGOs) having knowledge and skills to empower the grassroots actors through capacity building lack resources. As noted above, they also lack resources to engage in high quality research and make informed intervention at the policy level.

The role of NGOs is even more critical in influencing and shaping the trade policy making/negotiations processes because they can act as a counterbalancing force against the organized and powerful vested interest lobbies. They could represent the voices of the poor, marginalized and vulnerable communities. They could advocate in favour of a number of social issues, which are neither the priorities of the private sector nor the government. As remarked in UNDP (1999, 35): "[T]hey have been effective advocates for human development, maintaining pressure on national governments, international agencies and corporations to live up to commitments and to protect human rights and environmental standards."

In most LDCs and small LICs, where such mechanism exists, they are at best ad hoc and based on the personal preference of the concerned trade negotiators. Since such practices have already been institutionalized in most developed countries and it is generally said that trade liberalization and openness lead to greater convergence of ideas, there is a possibility, albeit limited, of trade policy making process becoming broad-based. Widespread participation in national dialogues involving multiple stakeholders – including parliamentarians, CSOs, community groups and private sector leading to equitable ownership of such discussions can significantly contribute to long-term human development (UNDP, 2003a).

#### 5.5 Environmental concerns

The linkage between trade and environment has been a contentious issue in most of the trade agreements, not least because the developing countries do not feel that trade sanction is the best means to achieve environmental objectives. Developed countries are exerting pressures to include environmental issues within the WTO on the premise that an environmental agreement within the WTO will help reduce environmental pollution and regulate 'race to the bottom' which confer disproportionate advantage to the 'pollution heavens'. However, empirical evidence does not support this hypothesis. As per a recent empirical study by Busse (2004, 22), which examined the hypothesis on the basis of evidence drawn from 119 countries in five polluting industries, there is no clear evidence that national government choose sub-optimal policies that result in insufficient environmental regulations. Only exception found was in the case of iron and steel products. Therefore, the study concludes that the case for environmental standards within the WTO

framework is relatively weak. Same applies to environmental standards in bilateral trade agreements like NAFTA and US-Singapore BTA.

At the same time, Article XX (b) and (g) of the GATT allow imposing restriction on international trade, without violating the core principles of the WTO, provided they are judged harmful to the interest of plant, animal and human health or to the goal of conservation of exhaustive natural resources. Since trade provides significant impetus to transfer of environmentally sound technologies, and results in some form of learning by doing, environmental sustainability will become a matter of concern for the national level policy makers – thus aiding the achievement of MDGs (goal 7). Liberalization of trade in environmental goods and environmentally sound technologies, which is also mandated by Doha Declaration, could potentially result in positive outcomes.

However, the stringent IPR standards – not only those included in the TRIPS Agreement, but also those included in US BTA (which even higher than TRIPS mandated standards) seem to show utter disrespect and insensitivity towards the objectives of promoting environmental sustainability. Provision on patenting of life form is in sharp contrast with the prior informed consent and access and benefit sharing provisions of the Convention on Biological Diversity (CBD).<sup>23</sup> It is also likely to help developed countries provide legal cover to and institutionalize the process of 'bio-piracy' and theft of traditional knowledge of the indigenous communities.

## 5.6 Livelihood

### 5.6.1 Education

Against the backdrop of MDGs (goal 2) of achieving universal primary education by 2015, Nobel Laureate Joseph Stiglitz highlights the long term positive outcome associated with education: "There are policies that in the long run may enhance growth and reduce poverty, such as enhancing education opportunities for disadvantaged groups, which allows countries to tap into vast reservoirs of underused talent" (UNDP 2003b, 80). However, most LDCs and small LICs of Asia and the Pacific continue to post modest gain in educational attainment. Therefore, it is necessary for them to use trade agreements as a tool to facilitate improvement in outreach as well as quality of education. One way of doing it is to liberalize the education sector under the GATS. However, acceding countries seem to have feared that liberalization of primary and secondary education could result in 'foreign' value system being imposed on their students. Therefore, most acceding countries have only made a commitment to open up tertiary education. Moreover, like in the case of environmental services, the equity, inclusiveness quality issues are of paramount significance – from a human development perspective. Liberalization of tertiary education and inflow of FDI could help release resources to primary education sector, thus aiding the goal 2 of achieving universal primary education, envisaged by MDGs.

### 5.6.2 Employment

Under goal 8 of Millennium Declaration, developing a global partnership for development, target 16 emphasizes development and implementation of strategies for decent and productive work for youth. In the context of trade integration, conventional economic theory posits that trade liberalization will increase productivity and wages, especially for tradable goods, thus expanding jobs and opportunities for poor people. In the 1980s and 1990s great progress in reducing global poverty and advancing human development was propelled by many countries seizing global opportunities (UNDP 1999, 32). It is also true that the pressures of global competition have led countries and employers to adopt more flexible labour policies, and work arrangements with no long-term commitment between employer and employee are on the rise (UNDP 1999, 37).

Further, evidence from most countries tends to confirm the widely held belief that it is high-skilled people who are going to benefit from trade liberalisation. In the face of WTO accession and signing of RTAs leading to increased competition, workers in import competing industries may face job loses and wage cuts. Though it is generally assumed that increased activity in export industries absorb most of the displaced workers, in

reality these transitions are far from easy (MHHDC 2004: 59). In general, for the poorest countries, opening up trade will expand the production of goods intensive in the use of low-skilled labour, but the demand for the least-skilled labor may not be boosted by trade and may be adversely affected by technological change spread by globalization (World Bank, 2000b). Likewise, heightened protection in the North in the sectors of export interest to the LDCs and small LICs is already fuelling the problem of unemployment in the latter.

Unlike other agreements of the WTO, GATS provides a window of opportunity for these countries, not least because liberalisation of FDI under GATS could help create new jobs. Acceding countries can create employment opportunities, to the extent countries have put the conditions to employ locals. It is also imperative for the LDCs and LICs, which have recently acceded to the WTO, to join the alliance of developing countries to push for the liberalisation of mode 4 of service delivery (movement of natural persons). For example, if temporary movement of labor up to 3 percent of the total labor force in rich countries were permitted, developing countries would stand to gain as much as US\$160 billion in additional income (Walmsley and Winters 2003). However, if the current negotiations on services are any guide, it is not difficult to predict that developed countries are not going to liberalize this mode of service delivery.

Based on the above analysis it is clear that the net implication of trade integration for employment, particularly for those in the low skilled category, in LDCs and small LICs of the Asia Pacific region is negative. However, if, and only if, rich countries remove their trade barriers on goods and services of export interest to the LDCs and small LICs, it tends to move towards positive direction.

#### 5.6.3 Poverty and food security

The MDG 1 (goal of eradicating extreme poverty and hunger) is linked to opportunities for livelihoods among the relatively deprived sections of the population. There exists some possibility to enhance livelihood opportunities through trade integration. Reduction in barriers to trade can impact rural livelihoods through increased opportunities in agriculture, fishing, and through movement of persons across national borders (Rajivan 2004, 8). However, the link does not always move into positive direction. Reduction in trade barriers, without adequate cost benefit analysis, could result in flooding of cheap imports from outside, which could pose serious threat to the livelihood of the farmers, as happened in Nepal due to Indo-Nepal BTA (see Pandey 2004)

The relationship between trade integration and poverty is further complicated by the fact that even a growing export does not guarantee poverty reduction, as measured by increase in private consumption per capita UNCTAD (2004a) identified three types of trade-poverty relationship, particularly in the context of LDCs: a) A virtuous trade effect, where average PCP is raising along with export growth; b) An immiserizing trade effect, where average PCP is falling with export growth; and c) An ambiguous trade effect, where there is no clear trend in average PCP along with export growth. It is the second and third types of nexus, the policy makers should worry about, because as per UNCTAD's finding only three LDCs – Bangladesh, Guinea and Uganda – observed the first type of effect both during 1990-95 and 1995-2000.

Similarly, food security continues to remain a pivotal issue in most LDCs and small LICs. However, trade integration seems to have contributed to more food insecurity, not least because of the strong IPR regime. For example, Article 27.3 (b) of TRIPS requires protection of plant variety. This requirement could restrict the rights of farmers of the South to save, replant, exchange and sell seeds if the developing countries are forced to accept UPOV model. These requirements, designed to protect the interest of the biotechnology and seed industry of the North, are likely to restrict the livelihood options of the poor, marginalized and vulnerable farmers and indigenous communities of the South. Similarly, due to genetic erosion, monoculture farming practices and dependence on multi-national plant breeders and agrochemical giants for inputs, which is hastened by strong IPR protection – food security situation can worsen in most of the LDCs and LICs.

Another related issue is that of food trade. While imports of cheap or even subsidised products, in theory, are beneficial for alleviating widespread hunger, evidence of most countries shows that the difference is, more



often than not, taken away by the intermediaries. The supposed relief does not reach the poor consumers. Moreover, as noted above, cheap import destroys the livelihood of the farmers – who do not find it worthwhile to continue farming profession. Developed countries, which could otherwise have considered it as a natural adjustment process, because of the employment opportunities available elsewhere, feel the need to protect the farmers. They continue to dole out subsidies to their farmers in order to retain them in the farming sector. The LDCs and small LICs, which can neither subsidize their farmers nor provide alternate employment opportunities, face a critical problem – less farmers mean less output, more hunger and perpetuation of dependence on imported food.

The above discussions make it amply clear that unless the WTO agreements and BTAs are re-negotiated with a view to creating a window to help LDCs and small LICs achieve human development objectives, it is not possible for the vulnerable economies to meet goal 1 of Millennium Declaration. While various internal factors are equally responsible for hindering the achievement of this goal, trade agreements, in their present forms coupled with the onerous WTO-plus requirements included in the WTO accession package as well as BTAs will only fuel the fire.

## VI. ADDRESSING VULNERABILITIES: CURRENT INITIATIVES

Recognition of problems of vulnerability inherent in the LDCs and small LICs, coupled with the realization of the need to integrate themselves into the global economy have led development partners to make some genuine (some not so genuine) efforts. However, most such endeavours, despite being genuine, have failed to achieve their objectives. The following section deals with four such initiatives, mainly at the multilateral level.

### 6.1 Special and differential treatment

While S&DT is a necessary condition to help developing countries achieve their development objectives, this is in no way a sufficient condition (See generally Ismail 2005, 11-21). Accordingly, analysts are divided on whether or not S&DT is the right policy tool to facilitate the integration of developing countries and LDCs into the multilateral trading system. According to Srinivasan (1999), the continued insistence of developing countries on S&DT and their reluctance to take part in the GATT negotiations as equal partners was the main reason for their marginalization from the global economy. However, developing countries, as a group, insisted on S&DT, asserting that applying the same rules to unequal trading countries could be disastrous, because they do not have the capacity to implement several commitments and that they would prefer modulated commitments, based on their trade, development and financial needs. A well-designed, effective, enforceable and time-bound S&DT is necessary for the successful integration of the developing countries and LDCs into the multilateral trading system (Adhikari 2005a). The different WTO agreements contain about 124 separate articles or paragraphs containing around 160 provisions for S&DT (UNCTAD 2004a, 241). They can be broadly divided into binding and non-binding (or enforceable and non-enforceable) (see Box 8).

#### Box 8: S&DT provisions in the WTO

Binding provisions, which can be unilaterally implemented without having to wait for actions from others. There are two sub categories of provisions under this heading.

- a) Permitting developing countries to assume lesser obligations (such as 10 percent de minimis domestic (amber box) support as opposed to five percent for developed countries in AoA or lower reduction commitment in the case of tariff (24 percent as opposed to 36 percent) and subsidies reduction (13.3 percent as opposed to 20 percent).
- b) Providing transitional time period, which are higher for the developing countries, compared to developed countries. For example, Article 66.1 of TRIPS provides transitional period of five years for developing countries to implement the commitment, while such time limit for developed countries is only one year. In both the cases, provisions for the LDCs are more generous.

Binding provisions, which require action from others, particularly developed countries such as obligations to address important needs. For example, Article 66.2 of TRIPS requires developed country members to provide incentives to enterprises and institutions in their territories for the purpose of promoting and encouraging technology transfer to LDCs.

Non-binding provisions, which are also known as best-effort clauses: There are three sub-categories of provisions under this heading.

a) Requiring WTO members to safeguard the interest of developing countries. An example is Article 10.1 of Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures that requires members to take into account the special needs of the developing countries and LDC Members in the preparation and application of SPS measures.

b) Requiring developed countries to provide technical assistance to the developing countries and the LDCs to help them implement the commitments under the WTO. For example, Article 11.2 of Agreement on Technical Barriers to Trade (TBT) requires members to provide technical assistance to developing countries and the LDCs on mutually agreed terms and conditions for the establishment of national standardizing bodies.

c) Requiring developed countries to enhance trade opportunities of the developing countries and LDCs. For example, the need to provide market access Article XXXVII.1 of the GATT requires the developed members to accord high priority to the reduction and elimination of barriers to products currently or potentially of particular export interest to developing member countries.

An important aspect of S&DT provision as argued in UNDP (2003a, 4) is worth highlighting here. Many developing countries argue that the single undertaking's human development impact would be maximized if it ensured that all countries' interests were reflected in trade regime's rules and agreements. Thus a major challenge for the international trade regime is to incorporate human development objectives as positive obligations in its rules and agreements. Many developing country governments and trade policy specialists argue that S&DT can help achieve this goal.

## 6.2 Preferential market access initiatives

Preferential market access has its historical root in the addition of Article XXXVI – XXXVIII of the GATT 1947, which was added in 1965 – under Part IV of the GATT. This can also be considered a sub-set of a broader S&DT rubric. The objectives of inclusion of these Articles in the GATT were to provide opportunity for the developing countries to take advantage of the multilateral trading system by ensuring rapid expansion of their export earnings with a view to helping them raise the standard of living in these countries.

During the 1970s, several advanced economies introduced preferential market access schemes for developing countries, in the form of Generalized System of Preferences (GSP). Since these tariff preferences contradicted the general MFN principle, as embodied in GATT's Article I, GSP schemes required a waiver from the main GATT rules. The GSP schemes were firstly introduced into the GATT framework in 1971, through a 10 year waiver. This waiver was superseded in 1979 by the Enabling Clause, making GSP a perennial feature in the multilateral trading system. The number of GSP schemes increased in the 1980s as many other developed countries introduced bilateral schemes. Under the GSP, developed countries (donor countries) applied, on a voluntary and unilateral basis, preferential tariff rates to imports from developing countries (beneficiaries) (UNCTAD and Commonwealth Secretariat 2001, 8).

A second preferential market access scheme which is of interest to Asia-Pacific LDCs and small LICs is preferential market access provided by the EU under Lome Convention (now Cotonou Agreement). These preferences provided by the European countries to their former colonies, including the Pacific countries, are far deeper compared to normal GSP scheme. Moreover, since 2001, the EU has introduced Everything but Arms (EBA) initiative, as per which all the products originating in LDCs, other than arms and munitions receive duty and quota free access to the EU market. Three exceptions are: banana, rice and sugar – which will be phased in by 2006 (for banana) and 2009 (for rice and sugar).

Similarly, other Quad countries too have refined their GSP schemes. The new GSP scheme offered by Canada in January 2003, is more liberal than EBA, because it provides market access on textile and clothing products, the only exceptions being dairy products, eggs and poultry. Moreover, the initiative has also changed the ROO, introducing an innovative cumulative system that allows inputs from all the beneficiary countries (UNCTAD 2004a, 246). Japan too has recently reviewed its GSP scheme and extended it for a new decade (until 2014). In early 2003, Japan further improved its GSP scheme for the benefits of LDCs with duty free entry of not only industrial products, but also a few agricultural products, such as prawn and frozen fish fillets (UNCTAD 2004a, 246). Apart from the regular GSP scheme of the US, it provides deeper preferences to select African countries through the African Growth and Opportunity Act (AGOA) and to Caribbean countries through what is known as Caribbean Basin Initiative (CBI). Countries in Asia and the Pacific receive less favourable treatment within the US GSP scheme. Similarly, 24 other countries (developed and developing ones) have either offered some form of preferential market access to the LDCs or are in the process of doing so (see UNCTAD 2004a, 247-8).

Despite these preferential offers, their take up (or utilization) rates have been disappointing (see Brenton 2003). For example, LDCs exports figures to the Quad countries (as of 2002) reveal that they are 0.2 percent of the total import in Canada; 0.6 in the EU; 0.4 percent in Japan and 0.8 percent in the US. These figures have remained unchanged since 1992, and in the case of Japan it showed a decline of 0.1 percent over the decade. There are several factors responsible for lower utilization. As per Inama (2002), these reasons are: a) lack of security of access, due to the unilateral and optional nature of preferences, which can be eliminated at the discretion of the providers; b) insufficient product coverage, due to exclusion of certain "sensitive" sectors from the preference scheme by the providers; c) ROO that are excessively stringent in light of the industrial capacity of the LDCs; and d) lack of understanding or awareness of the preferences available and the conditions attached thereto, leading to the application of MFN rates rather than preferential ones. Brenton (2003) argues that the prime suspects for the lower utilization of trade preference are the ROO, at the least it is time they were brought in for questioning.

NTBs are increasingly becoming an important form of trade barriers, even for the preference receiving countries. For the exports of agriculture, livestock, horticulture and floriculture items the fast changing SPS standards in the major markets (the EU and the US) are posing serious problems. They include: a) inappropriateness of such standards to the local circumstances; b) skewed distribution of gains from trade; and c) disproportionately onerous on burden small exporters (see Stevens and Kennan 2004, 4).

However, preferential market access remains a vexed issue, mainly because of the arguments that it is inherently discriminatory and benefits to preference receiving countries come at the cost of other developing countries (see Anderson, 2004; UNMP 2005). Moreover, the value of preference to the LDCs and small LICs, as discussed above, has been extremely limited. The current debate is driven by two divergent views that could be labelled 'preference skeptics' and 'GSP reformers'. "Preference skeptics" (e.g., Bhagwati, 2002; Whalley, 1990) emphasize that trade preferences have been granted for more than three decades to developing countries, including LDCs, and that so far there is little evidence that these countries have benefited considerably as a result of such schemes (Puri 2005, 21).

However, GSP reformers believe that GSP schemes have played and will continue to play a positive role in the export and development performance of developing countries (see Rose 2004; Romalis 2003). Rose (2004) goes one step further to claim that GSP extended from the North to developing countries approximately doubles trade. Moreover, preferences enabled the "Asian success story" countries to gain market penetration, sustain themselves in markets over time and build the necessary competitiveness (Puri 2005, 21).

At the same time, a new school of thought is emerging, as per which developed countries should liberalize their markets on an MFN basis, and provide technical assistance to the LDCs and small LICs, who have

suffered preference erosion. The latter should not only use the resources for their adjustment programme, but also for strengthening their supply capacity and competitiveness. This approach, though sound from theoretical perspective, is likely to encounter several implementation problems, as vividly demonstrated by best endeavour nature of technical assistance commitments contained in various WTO agreements and the wide divergence between rhetoric and reality of technical assistance (See Sachs 2005), to which we turn now.

### 6.3 Trade related technical assistance

The objective of trade related technical assistance is to ensure that LDCs and LICs are better integrated into the multilateral trading system. Two types of trade related assistance are of particular importance: a) those that help the recipient countries implement the commitments made at the WTO and to address their supply-side constraints and enhance their competitiveness and (hardware part); and b) those that help enhance the understanding of various stakeholders on trade policy issues and negotiating capacity of trade officials (software part).

Most multilateral and bilateral donors/institutions, including the WTO, have focused only on the minor part of the trade related capacity building programme. Main attention is on: a) providing training to the trade officials on the WTO issues; and b) conducting 'studies'. A discussion on Integrated Framework for Trade Related Technical Assistance (IF) reveals the yawning gap between promises and practices.

In response to the complexity of LDCs' trade-related problems, IF was inaugurated in October 1997 at the WTO High Level Meeting on "Integrated Initiatives for Least Developed Countries' Trade Development". The IF was launched by six multilateral institutions – IMF, UNDP, the World Bank, International Trade Centre (ITC), UNCTAD and the WTO, which, with their distinct competence, could complement each other to deliver greater development dividends to the LDCs in the multilateral trading system. The IF has two objectives: (a) to 'mainstream' (integrate) trade into the national development plans such as the Poverty Reduction Strategy Papers (PRSPs) of the LDCs; and (b) to assist in the coordinated delivery of trade-related technical assistance in response to needs identified by the LDCs.

The IF has received support from both trade and development communities. At the Doha Ministerial, WTO Ministers endorsed the IF as a viable model for LDCs' trade development (paragraph 43 of the Doha Ministerial Declaration). On 15 July 2003, the Heads of the six IF agencies and their representatives issued a joint communiqué underscoring the commitment of agencies to the IF model. The support for the IF is also reflected in the form of increased contributions to the IF Trust Fund, which amounted to US\$ 19.3 million as of 3 July 2003. Built on principles of country ownership and partnership, it is financed from a Trust Fund comprising two main 'windows' - a window to finance the Diagnostic Trade Integration Study (DTIS) and a second window created in 2003 to finance high-priority projects from the action matrices that serve as a basis for delivery of trade-related technical assistance (Puri 2005, 39).

Despite the board support on paper, its effectiveness in helping LDCs overcome their integration challenges are limited at best (Adhikari and Dahal 2004). The major problems are: a) lack of inter-agency coordination; b) lack of adequate funding; and c) the failure to address disconnect between a number of WTO agreements and development priorities of low income countries (Hoekman and Kostecki 2001, 399). So far the IF has not realized its potential. While DTIS have had little impact on the allocation of donor funds and critical trade infrastructure remains unfunded, the budget per country of US\$ 1 million under Window II is insufficient and its use too unfocused to make such a difference (Puri 2005, 39).

### 6.4 Recent developments

Development has been one of the major planks of the DDA. This was the first time that WTO members not only recognized the need to provide special measures to prevent marginalization of the LDCs and small economies from the multilateral trading system, but also made several commitments to help reverse the trend. Three issues are particularly noteworthy.

First, there was a commitment to ensure speedy accession of the LDCs into the WTO. It was decided that “accelerating the accession of LDCs” (Paragraph 9) was the priority for WTO membership. Moreover, in paragraph 42 of the DMD, Ministers agreed “to work to facilitate and accelerate negotiations with acceding LDCs” (WTO 2001b). Furthermore, General Council (GC) too decided on 10 December 2002 to streamline and facilitate the process of LDCs’ accession (WTO 2003b).

Second, the DMD showed its commitment to this issue by dedicating full six Paragraphs (Para 38 to Para 43) to the issue of technical assistance and capacity building. Moreover, the Declaration on Implementation Related Issues and Concerns makes mention of this issue at several places. A closer look at these provisions reveals that an unprecedented level of political commitment was expressed to the agenda of trade related capacity building.

Third, on Paragraph 35, Ministers agreed to a work programme, under the auspices of the GC, to examine issues relating to the trade of small economies. The objective of this work is to frame responses to the trade-related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system, and not to create a sub-category of WTO members.

However, little attempts have been made, if at all, to convert this level of political commitment into reality. This is evident not only from the fact that a number of deadlines agreed during the Doha Ministerial were missed, but there were little discussions on these issues during the run up to the Cancun Ministerial Conference of the WTO and during the Ministerial itself. After the failure of the Cancun Ministerial, which threatened to derail the multilateral trade negotiations at the WTO, members finally managed to hammer out a deal on 1 August 2004 (known as July Framework) to revive the stalled talks.

The Framework, which was essentially prepared by select influential developing countries and developed countries, with limited participation of LDCs and LICs, fails to address most of the concerns relating to latter’s integration into the multilateral trading system. Among the issues agreed for negotiations by the Framework, trade facilitation text is the only text which contains strongly worded technical assistance language. This text provides the leeway to the developing countries as a whole not to implement their part of the commitments in the absence of technical assistance.

On the area of agriculture, S&D provisions are mostly related to higher transition period and lower level of reduction coefficients. S&DT language, as in the past, are non-binding best endeavour nature.<sup>24</sup> Moreover, though the LDCs are not required to participate in any reduction commitment, the non-binding language relating to duty free quota free access<sup>25</sup> have further weakened their bargaining position in their efforts to obtain such facilities from the developed countries. The NAMA text is similar to that of agriculture. As per Annex C of JP titled Recommendations of the Special Session of the Council for Trade in Services “Members shall strive to ensure a high quality of offers, particularly in sectors and modes of supply of export interest to developing countries, with special attention to be given to least-developed countries” (WTO 2004). This language does not mean anything to the developing countries as there is a vast difference between “shall strive to ensure” (existing text) which is not mandatory and “shall ensure” which would have been mandatory, provided this text was there. Members, as per the text, “note the interest of developing countries as well as other members on in Mode 4”. However, noting the interest and actually making a commitment to liberalize this mode of supply are two entirely different issues.

On the issue of small economies, JP provides a non-binding formulation, stating that the trade related issues identified for the fuller integration of small, vulnerable economies into the multilateral trading system, should also be addressed, without creating a sub-category of members, as part of a work programme, as mandated in paragraph 35 of the DMD. Though it is not difficult to visualize the overall sentiments among the majority of WTO membership, which does not want to create a separate category of membership, the lack of commitment to address their problems is clearly visible from the use of very weak language.

WTO members failed to prepare 'first approximation' for the Hong Kong Ministerial to be held in December within the agreed deadline of July 2005, despite the repeated rhetoric that "development issues should be at the heart of the Doha negotiations". The outgoing Director General of the WTO characterized state of talks as "disappointing but not disastrous." Therefore, considerable efforts will be required to bridge the gap between fairly entrenched positions of the developed and developing countries in the run up to Hong Kong Ministerial Conference.

## VII. THE WAY FORWARD: HELPING VULNERABLE STATES LEVERAGE TRADE FOR HUMAN DEVELOPMENT

Based on the analyses made above, we can draw six main conclusions. First, trade integration alone is not sufficient to ensure economic growth or poverty alleviation. However, no country achieved broad-based economic growth in a sustained manner by shutting its door to the outside world. Trade's relation with human development is even more ambiguous. However, managed properly, trade integration can provide stimulus for economic growth as well as poverty alleviation. If such results do occur, increased opportunities and resources could be utilized for meeting the human development objectives.

Second, vulnerable economies face several hardships, some of which are inherent in their geographical location and natural factors, while others are related to the structure of their economies, which cannot be radically altered without meaningful efforts for diversification. It has been proven – both theoretically as well as empirically – that vulnerable economies have little choice than to integrate themselves into the regional and global trading system. Moreover, since most of them have already made unilateral liberalization commitments, they are already integrated into the global economy, at least in practice if not in strict legal sense. The new integration initiatives are mainly about locking-in trade and other policy reforms, i.e., integration in the legal sense, and making a commitment not to reverse them.

Third, costs of integration in legal sense seem to be very high, though the rules of the WTO themselves are not terribly useful for the vulnerable economies to meet their human development objectives. Added to this, these countries are being imposed extremely onerous requirements that go beyond the WTO norms, at the time of their accession to the WTO. Their participation in the regional integration efforts has not been very a costly affair, but they have not benefited enormously from such efforts either. Due to their 'unattractiveness' developed countries have not shown much interest to sign BTAs with these vulnerable economies. However, given the 'side payments' made by the countries which have signed BTA with developed countries, vulnerable economies are better advised not to waste their scarce negotiating capital on signing such self-defeating trade agreements.

Fourth, trade agreements, which provide incremental market access opportunities, help the vulnerable economies address one side of the issue, i.e., the demand side. Since most these economies face severe supply-side constraints and their competitiveness is limited, these issues should be tackled as a priority. Such an effort could greatly help vulnerable economies enhance their trading prospects.

Five, efforts made so far at the multilateral level to help the LDCs and LICs to better integrate them into the multilateral trading system – either through preference or through special treatment – have not produced desired results, because of their questionable intent and faulty design. Given the fact that on balance trade integration helps the vulnerable economies, efforts of the international community should be geared towards ensuring better integration, by minimizing the associated costs.

Finally, trade integration is like a two-edged sword, as far as its contribution (or lack of it) to leverage human development is concerned. However, managed properly, trade integration could positively contribute to human development. In order to ensure that, the ability of the nation states to maintain the policy space required for achieving human development objectives is necessary, even when trade integration becomes a continuous process, as it is likely to be.

It is an imperative for the vulnerable economies to leverage trade integration to achieve human development objectives for two main reasons. First, they have the potential to take advantage of trade integration, given the structure of their economies. Second, since vulnerable economies already have very low human development indicators, they should anchor their trade integration as well as domestic reform agenda on human development. At the same time it is necessary for the policy makers as well as other stakeholders to understand that their efforts at the national level should be supplemented by the efforts at the international level. Therefore, the recommendations are made at the following two levels:

### 7.1 National agenda

a) **Mainstreaming and feed forward processes:** A two-way mainstreaming and feed-forward mechanism should be put in place. Mainstreaming trade into the overall development architecture, such as PRSP, so as to ensure national ownership and facilitate better coordination among different agencies is a primary requirement. It is also necessary to integrate human development concerns in the trade policy making process, as well as at the time of preparing negotiating positions and implementing the commitments made under various trade agreements. Inter-ministerial or inter-departmental coordination mechanism should be strengthened to create better impact. Similarly, private sector and CSOs – particularly those actively working on human development issues – should be constantly updated on the development in the field of trade integration and their inputs should be sought at every stage.

b) **Strengthening supply-side and competitiveness:** This is the most difficult part of domestic reform agenda, not least because it covers a number of areas. Investing in infrastructure development – including road, telecommunications, warehouses, and port facilities – which are resource intensive is the major challenge. These activities cannot be conducted without external assistance, but the role of domestic resource mobilization cannot be understated. Further, building capacity of the stakeholders, harnessing the potential of knowledge based economy, and improving governance could help enhance the supply capacity of the domestic enterprises.

c) **Compensatory and safeguard mechanisms:** A functional mechanism should be devised to compensate those sections of the society that lose out in the short run from trade integration. Such compensation normally takes the form of retraining facilities, unemployment benefits and adjustment credits, but there could be other innovative ways. A mechanism should be devised to safeguard the areas of vital human development interest – such as food security, livelihood, public health, employment – which could come under threat due to trade integration. Regulatory mechanism should be put in place or existing institutions should be strengthened, for example, to ensure foster competition, prevent fraud and deception, and capital flight.

d) **Diversification of export and market:** In order to prevent deterioration in terms of trade triggered by international volatility of commodities exports, the LDCs and LICs should not only diversify into more valued added, dynamic manufacturing sectors, but also into services sectors. Efforts for export diversification should move in tandem with efforts geared towards identifying the niche products and services. Similarly, new destinations for exports should be identified in order to reduce vulnerability.

### 7.2 International/regional agenda

a) **Building credible alliances:** One or a small group of countries, having limited share in international or regional trade will not be able to influence the outcomes of negotiations, if they acted in isolation. Therefore, it is necessary to build credible principle based as well as issue based alliances during the multilateral as well as regional trade negotiations – and negotiate as a bloc. For example, vulnerability issue is common to both the LDCs and LICs, and they could create better impact if they negotiated as a bloc.

b) **Favourable terms of WTO accession and trade agreements:** Since quite a number of the LDCs and LICs of the Asia Pacific region are still in the process of accession to the WTO, they advocate the WTO members to adopt a clear-cut guideline for acceding countries. These should include timeframe for each stage of

negotiations, maximum (not minimum) level of market access commitments and a requirement to genuinely take into account their trade, development and financial needs as well as institutional capacity. Further, they should tie implementation of their commitment with the availability of technical assistance. Similarly, WTO-plus conditions contained in various RTAs and BTAs must be stopped.

c) Targeted technical assistance: Technical assistance for the implementation of WTO commitments, and strengthening supply capacity as well as competitiveness of the domestic players (industry, farmers and service providers) would go a long way in the genuine integration of the LDCs and small LICs of Asia and the Pacific. This will also free the governments' resources for investing in social sectors, which is crucial for achieving their human development objectives.

d) Meaningful market access: While preferential market access remains important from the LDCs and small LICs, what they should advocate for is a binding commitment – mainly from the developed countries – to provide them duty free quota free market access, allowing for flexible ROO. They should also insist that standards should be based on sound science and be sensitive to the ground realities in the exporting countries.

e) Strengthening S&DT provisions: Recognizing the vulnerability of the LDCs and small LICs, the S&DT provisions should be made operational, effective and enforceable. For this they should not only be included in the WTO architecture, but a mechanism should also be devised for each commitment to monitor their implementation. In the context of multilateral regime, where ineffectiveness of S&DT has been a major problem, various Committees in the WTO should be entrusted with the responsibility to prepare reports on implementation status of the commitments (Purohit 2004).

f) Mainstreaming human development concerns: Given the belief that future trade negotiations should be corrective, once within the regional or multilateral trading arrangement, it is the duty of the member countries to raise the debate and make submissions from a human development perspective. The focus should be on achieving improved human development outcomes, not merely on market access. Since trade is a means to an end – not an end in itself, the issues of trade rules having to allow for diversity in national institutions and standards should be brought out clearly during the negotiations.



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## Notes

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- <sup>1</sup> Trade and poverty linkage in LDCs is asymmetrical. Although LDCs with declining exports are almost certain to have a rising incidence of poverty, increasing exports does not necessarily lead to poverty reduction (UNCTAD 2004a, iv).
- <sup>2</sup> Trade integration, in theory, would mean even firms located in the smaller countries can consider the entire universe as their market. However, in practice such a market does not exist because of several trade barriers.
- <sup>3</sup> However, the possibility of these exercises being conducted by few elite groups of people – including bureaucrats, industrialists having export interests, and donor organization without any meaningful participation of the possible losers cannot ruled out.
- <sup>4</sup> Export concentration index is numbered between 0 and 1, where 0 represents the lowest concentration and 1 represents the highest. While the non-LDC world average is 0.2 for the 1990s, Kiribati had a concentration index of 0.73 in 1995. See Commonwealth Secretariat and UNCTAD (2001)
- <sup>5</sup> See, for example, CIPR (2002) and Fink and Maskus (2005)
- <sup>6</sup> The U.S., for example, proposed that the UPOV be designated the only acceptable 'effective sui generis system.' See IATP (2003: 10)
- <sup>7</sup> For a detailed discussion on this issue see Kanniah, R. (2003)
- <sup>8</sup> For a detailed account of how Nepal was able to fend off such a pressure, see Adhikari and Adhikari (2003)
- <sup>9</sup> This is particularly striking because on an average the anti-dumping duties on dumped imports from non-market economy tend to be more than 12 times higher than normal anti-dumping duties. Messerlin (2004, 42) reveals that in the anti-dumping investigations initiated by the US (between 1995 and 1998), which resulted in positive determination average dumping margin with price comparison as the basis for estimated normal value of exports was only 3.2 percent, whereas following non-market economies principle as the basis for arriving at estimated normal value of exports resulted in dumping margin of 40 percent on an average.
- <sup>10</sup> The recent accession of 10 new members to the European Union reduced the total number of RTAs in force from 285 to 229. See World Bank (2004): 27
- <sup>11</sup> See Kelegama and Adhikari (2002) for detailed analysis of the positions of the proponents, opponents as well as neutral observers – both individuals and institutions.
- <sup>12</sup> Several countries having serious political rivalries have set aside their differences and come together to work under a single umbrella of regional integration arrangement. While France and Germany fought several wars in the past, Argentina and Brazil as well as Indonesia and Malaysia had border disputes. But they have now set aside their differences and are moving towards greater economic integration. One could also hope that South Asian Free Trade Area (SAFTA), would be instrumental in toning down political rivalry between India and Pakistan, which have fought two wars over border dispute and taken nuclear overtones. See Kelegama and Adhikari (2005).
- <sup>13</sup> A country which is the epicenter of industrial/trading activities; is the common denominator for majority of the RTAs; and has bilateral or regional trade agreements with all (or most) other countries is the hub and other countries

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which may not have any agreements within themselves but have a bilateral or RTA relation with the hub are called 'spokes.' Of late, the US and EU have emerged as major hubs, while other countries have remained spokes.

<sup>14</sup> Large scale foreign direct investment from Japan played a key role in stimulating intra-ASEAN trade via the investment-trade nexus. Further details are given in Kelegama, S. (1996).

<sup>15</sup> They are: American Samoa, Bermuda, Channel Islands, Guam, Isle of Man, Monaco, Mongolia, N. Mariana Islands, Palau, Puerto Rico, Timor-Leste, and the Virgin Islands. See World Bank (2004, 53)

<sup>16</sup> One set of US BTAs are intended to promote U.S. goals in the Middle East. Some agreements are with Middle Eastern countries themselves, such as those with Jordan, Morocco and Bahrain - and others are with countries that have joined the "Coalition of the Willing" in Iraq. These include all seven Latin American countries in the coalition (three of which sent troops), as well as Australia and Thailand. See VanGrasstek, Craig (2004).

<sup>17</sup> Now renamed Bay of Bengal Initiative on Mutli-Sectoral Technical and Economic Cooperation, with the same acronym.

<sup>18</sup> As per Article 15.2 (d) PICTA, the signatories are determined to conclude arrangements for detailed rules on government procurement. Inclusion of this WTO-plus condition, within a relatively under-developed RTA, could provide an avenue for the WTO members, which are parties to this GPA, to impose the requirement to sign GPA as a condition for WTO accession.

<sup>19</sup> See [www.apec.org](http://www.apec.org)

<sup>20</sup> <http://www.ssa.gov/policy/docs/progdesc/ssptw/2002-2003/americas/ecuador.pdf>

<sup>21</sup> <http://www.adb.org/printer-friendly.asp?fn=%2FDocuments%2FNews%2F2001%2Fnr2001092.asp>

<sup>22</sup> For example, in Brazil, the price of AIDS drugs fell by 82% over five years as a result of generic competition, while the price of drugs that had no generic competitor remained stable, falling only 9% over the same period. See Ford (2001).

<sup>23</sup> A Convention signed during the Rio Earth Summit in June 2002 with the objective of ensuring conservation and sustainable use of genetic resources and facilitating benefit sharing mechanism and currently ratified by 187 governments

<sup>24</sup> For example, the S&DT text on Export Competition mentions: "S&D will be granted to developing countries, and disciplines on export support will be developed with consideration of the impacts on least-developed and net food-importing developing countries."

<sup>25</sup> The actual language is as follows: "Developed Members, and developing country Members in a position to do so, should provide duty-free and quota-free market access for products originating from least-developed countries." See paragraph 45 of Annex A, WTO (2004).