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MAKING TRADE PREFERENCES WORK FOR SOUTH ASIAN LDCs

BRIEFING PAPER

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INTRODUCTION

Developing countries, including least developed countries (LDCs), have been granted preferential market access in major industrialised countries for the past three decades. However, the latter enjoy the discretion to apply preferences to some LDCs but not to others. In this respect, many regional trade agreements exempt South Asian LDCs from enjoying similar facilities as their LDC counterparts in other regions of the world. In most cases, preferences are applicable if LDCs fulfill rules of origin requirements whilst various tariff and non-tariff barriers also undermine the utility of trade preferences. The result is that South Asian LDCs have been unable to optimally utilise existing preferences in major developed country markets. This paper scrutinises the benefits of such preferences in the wake of challenges that continue to hamper sustainable trading prospects and export growth of South Asian LDCs.

Preferential market access facilities, which allow developing countries to enjoy reduced or unrestricted tariff and non-tariff barriers (NTBs) in developed country markets on a non-reciprocal basis, were constituted in the early 1970s (Box 1). Recently, these programmes have come under close scrutiny as some studies have questioned their effectiveness, while others have found significant positive impacts of preferential schemes.[1] Notwithstanding this academic debate, there is a broad consensus on the need for trade preferences for LDCs. In fact, a growing concern associated with the trade prospect of LDCs has been how to make the preferences more effective. In this paper, this issue is being explored in greater detail with regard to the South Asian LDCs.

SOUTH ASIAN LDCs

Of the 50 countries classified as LDCs by the United Nations, Bangladesh, Bhutan, Maldives and Nepal are geographically located in the South Asian region. These countries differ remarkably in terms of their size, export structure, and dependence on international trade (Box 2). Bangladesh is the largest economy, but its per capita gross domestic product (GDP) is just one-sixth of Maldives and is half of that of Bhutan. Nepal has the lowest per capita income in the region. Merchandise exports of Bangladesh and Nepal are dominated by manufactured items, largely because of textile and clothing products, while Bhutan and Maldives mostly export mostly primary goods. Dependence on exports from commercial services (primarily tourism) is high for Maldives with its total trade (exports plus imports of goods and services) registering 182 percent of GDP – much higher than any other South Asian LDC.

Although exports of South Asian LDCs have registered a growth rate of around 10 percent, during the past two decades, their absolute export volumes remain small. Bangladesh, which is the 50th largest economy in the world (in terms of GDP) and ninth biggest country in terms of population, has an absolute export volume four times smaller than that of Chile, which is the 42nd largest economy with a population one-tenths of Bangladesh. Similarly, Mauritius's exports are more than double of Nepal although the former has a population 10 times smaller than Nepal. These comparative figures cannot emphasise the need for expanding trade of South Asian LDCs.

The 'Quad' (compromising Canada, the European Union, Japan, and the United States) are the major export markets of South Asian LDCs, accounting for respectively; 75 percent, 70 percent, and 46 percent exports of Bangladesh, Maldives and Nepal. For Bhutan and Nepal, India is the main market, where 88 percent of

SAWTEE
SOUTH ASIA WATCH ON TRADE, ECONOMICS & ENVIRONMENT

P.O. Box: 19366,
254 Lamtangeen Marg,
Baluwatar, Kathmandu, Nepal
Tel: 977-1-4415824/4444438
Fax: 977-1-4444570
E-mail:sawtee@sawtee.org
Web: www.sawtee.org

BOX 1

TRADE PREFERENCES

The provision of providing unilateral trade preferences to developing countries emerged under an UNCTAD initiative and is known as the Generalised System of Preferences (GSP). The basic objective was to provide developing countries with lower tariff rates than those normally enjoyed under the Most Favoured Nation (MFN) status as a special measure to promote the recipient countries' export earnings. The two basic principles of the GSP initiative were: (1) all developing countries would be beneficiaries without discrimination and (2) recipients would not have to reciprocate. The European Union (EU) and Japan introduced their GSP programmes in 1971, followed by Canada in 1974, and the United States (US) in 1976. Since such preferences were against the spirit of the GATT MFN principle, GSP schemes were first instituted with a ten-year waiver, which was replaced by the GATT "Enabling Clause" in 1979, making GSP a salient feature of the multilateral trading system. Despite the principle of non-discrimination, preferences offered to developing countries differ, with LDCs given more favourable preferences than others.

Bhutan's and 50 percent of Nepal's exports are destined. Like their counterparts in other regions, South Asian LDCs have been receiving trade preferences in developed country markets under different GSP schemes. However, because of several reasons, export response to the preferences has been weak. In the following, constraints facing the South Asian LDCs in utilising trade preferences are first identified and then suggestions are provided about making them more effective.

WIDE VARIABILITY IN TRADE PREFERENCES OFFERED BY DONORS

Trade preferences offered by industrialised countries have been far from homogenous and differ in terms of product coverage, depth of preference, eligibility, and rules of origin (ROO). Each donor country has its own list of 'sensitive' products and preferences offered on them can be substantially different from other products within a donor country as well as from the existing preferences in other markets in similar products. The importance of sensitive products for the recipient countries has not been given much attention in offering the preferences and donors can discriminate among the beneficiaries. For example, in the case of textiles and clothing (T&C) products, which are of export interest particularly to Bangladesh, Maldives and Nepal; the EU has been providing duty-free and quota-free access to LDC exports (subject to the fulfillment of its ROO requirements), but such preferential access has never been granted to South Asian LDCs by the US. Japan's GSP scheme traditionally kept these products in the negative list until 2001, when preferences for some selected T&C exports of LDCs were introduced. Likewise, duty-free and quota-free access for LDCs (in all products) in Australia and Canada were offered as recently as 2003. The unevenness in preferential treatment and lack of comprehensiveness have undermined effective supply responses.

EXCESSIVELY HIGH TARIFF BARRIERS ON SOUTH ASIAN LDCS

High tariffs are also a major obstacle to LDC exports (Box 3). According to one estimate, 54 percent of all LDC exports (in terms of value) to Canada in 1998 were subject to import tariffs, followed by 51 percent in Japan and 48 percent in the US. The EU was a major exception as only about 3 percent of all LDC exports had been subject to tariff restrictions in 1998. Things have certainly changed for most LDCs recently. After the "Everything but Arms" (EBA) initiative in 2001, virtually all LDC exports have been granted unrestricted access into the EU. Australia, Canada and Japan have introduced more significant preferential trade regimes; and under various preferential schemes, the US has offers zero-tariff access to some LDCs and developing countries.[2]

High tariffs continue to be a major problem for South Asian LDCs, as the US has excluded them from its most attractive preferential schemes (Box 4). As a consequence, South Asian LDCs T&C exports in the US are subject to an average tariff peak of 16 percent with many individual items facing rates as high as 35-40 percent. Amongst other exports from South Asian LDCs to the US, tobacco faces an import duty as high as 63 percent, while for leather

BOX 2 Countries	Population (million)	GDP (million US$)	Per capita GDP (US$)	Merchandise exports (million US$)	Services exports (million US$)	Manufactures in goods exports (%)	Trade of goods and services (as % of GDP)	HDI rank (2004)
Bangladesh	140.5	56,800	404	6,959	1,486	93.8	35.3	138
Bhutan	0.87	710	816	113	26	38.0	52.1	134
Maldives	0.30	750	2,500	173	514	40.0	182.4	84
Nepal	25.25	6,700	266	715	359	70.2	47.8	140

Note: With the exception of the last column all data reported have been taken from the country specific information sheet prepared by the World Bank Group. Trade of goods and services includes both exports and imports. HDI rank is based on the relative ranking of 177 countries in terms of their human development indicators, as prepared by UNDP.

BOX 3

TARIFF PEAKS ON LDC EXPORTS

Despite generally low average tariffs, many products lines in the Quad countries attract duties more than 15 percent (known as tariff peaks). Such tariff peaks are mainly concentrated on agricultural (sugar, fish, cereals, etc.) and labour-intensive manufacturing (apparel and footwear) goods. Since exports from LDCs are concentrated on these items, tariff peaks have had a disproportional effect on them. In a study, Hoekman et al. (2002) show that, during 1996-99, more than US$ 5.5 billion of LDC exports (i.e., 25 percent of their total exports) were potentially affected by tariff peaks in Canada, while the comparable figure for the US market was US$ 3 billion. Tariff peaks in Japan and the EU were affecting some US$ 500 million and US$ 800 million of LDC exports to the world, respectively. Using a partial equilibrium model, Hoekman et al. found that the elimination of tariff peaks would result in an extra US$ 2.5 billion of LDC exports. However, tariff peaks have been reduced with the introduction of generous preference regimes in individual Quad countries.

and leather goods and fish products, tariffs are higher than 15 percent. Amongst the Quad countries (apart from the US), LDC exports face tariff peaks in Japan on a number of commodities which include T&C, sugar, raw hides and skin, and footwear. Some of these products are of particular export interest to South Asian LDCs.

DISCRIMINATORY TRADING BLOCS AND TRADE PREFERENCES

The operation of various trading blocs and trade preferences affect South Asian LDCs. On the one hand, more than 70 countries enjoy generous trade preferences in the US market but comparable facilities are not available for South Asian LDCs. On the other hand, although LDCs have access to an attractive EU preference regime, the extension of similar preferences to a large number of countries under the Cotonou Agreement and to the group of East-European countries acceding to the EU, have resulted in the loss of preferential margin to LDCs. Furthermore, many relatively advanced developing countries, which are potential export markets of LDCs, are involved in various regional blocs thereby discriminating against those LDCs which are not members of the relevant regional arrangements.

Discriminatory trade preferences not only weaken international competitiveness but also lead to export price shocks for excluded countries, resulting in deteriorating terms of trade and loss of welfare (Winters, 1997; Winters and Chang, 2000). It is indeed worrying that while a large number of countries have been accessing duty-free and quota-free access to some important markets, South Asian LDCs do not have such

BOX 4

EXCESSIVE TARIFFS ON BANGLADESH AND NEPAL IN THE US

Although a large number of countries enjoy unrestricted access to the US market, T&C exports of South Asian LDCs are subject to high MFN import duty (and had been subject to MFA quotas until the end of 2004). Figure 1 provides the distribution of US tariffs on the combined T&C exports of Bangladesh and Nepal, where it is found that in 36 percent of all US Harmonised Tariff Schedule (HTS) lines related to T&C with some exports from the two countries, ad valorem import duties in the range 5-9.9 percent are specified. While another 10 percent of HTS lines face 10-15 percent, tariff rates higher than 15 percent comprise a staggering 43 percent product lines. On 13 percent of HTS, tariffs charged are more than 25 percent! Of the US$ 2.2 billion of combined T&C exports from Bangladesh and Nepal in 2004, 46 percent (i.e., about US$ 1 billion) were subject to ad-valorem duties between 15.1 percent and 20 percent (Figure 2). Tariff slabs above 25 percent were applicable to another 13 percent (i.e. US$ 0.29 billion) of exports. Altogether, 60 percent of the combined export volume was subject to tariff rates higher than 15 percent.

Figure 1

Distribution of US tariffs on T&C exports of Bangladesh and Nepal by HTS-8

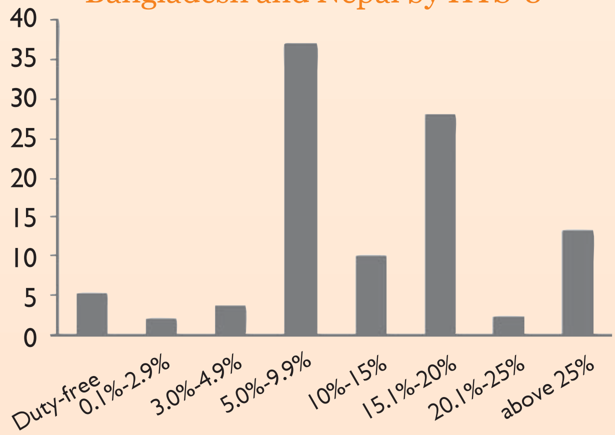
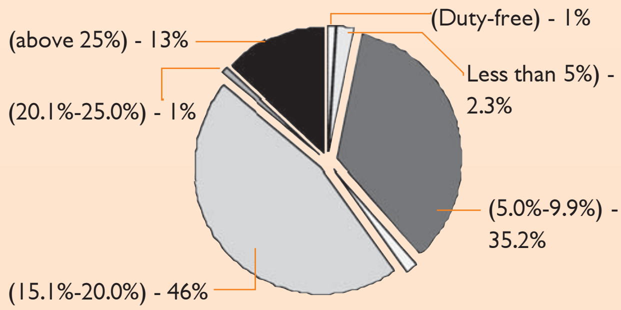


Figure 2

US tariffs over the volume of exports of Bangladesh and Nepal



Source: Author's estimate using the data as available from the Office of Textiles and Apparel (OTEXA) of the US.

BOX 6

ECONOMIC GEOGRAPHY AND INTERNATIONAL COMPETITIVENESS

Geographical location is now considered to be an important determinant of international trade and capital flows. Ad valorem transport costs of 20 percent on both final output and intermediate goods can reduce the domestic value added by 60 percent when intermediate goods account for 50 percent of costs. To show the importance of geographical location, Redding and Venables (2004) undertook some hypothetical experiments, based on an econometric estimate of a structural model of economic geography, to find that if, for example, Zimbabwe and Paraguay were moved from their current respective positions to the Central Europe, their per capita income would have increased respectively by 80 percent and 58 percent. Estimates are not available for South Asian LDCs, but costs associated with disadvantageous geographical location are likely to be high. The implication is that only because of favourable geographical location, some countries will experience much higher gains from trade, and foreign firms might be reluctant to move or relocate their production to those countries that are far from their main export markets even when wages in those countries are low.

access to all markets. According to one recent estimate, discriminatory tariff preferences given to Mexico in the US under North American Free Trade Area triggered an annual welfare loss of US$ 250 million for Bangladesh (Razzaque, 2005). If LDCs are to be considered as the poorest and most vulnerable countries of the world, it is in their interest that these countries should be provided with completely free access to every market in every product.

RULES OF ORIGIN

Accessing trade preferences is conditional on complying with the ROO requirements laid down by donor countries. These requirements are constituted to protect the importing country from imports originating in a non-eligible third country but being channeled through the preference-receiving countries. ROO requirements also attempt at helping develop backward linkage activities in LDCs. However, there exist complicated rules, which are difficult to comply with. In this regard, the EU's ROO for T&C exports is a vivid example. The ROO for EU-GSP scheme stipulate a value addition criterion for non-textile goods and processing criteria for textile apparel products. Until the late 1990s, the ROO required that, in the case of woven garments, an LDC would have to be involved in three stages of value addition, i.e., first, yarns would have to be produced domestically (first stage), which then would be used in producing fabric (second stage), and finally the local fabrics should be used in making the garments. For knit ready-made garments (RMG), the ROO requirement was of two stages: yarns would be produced domestically to be used in knitting. These preconditions, therefore, implied that for benefiting from the EU-GSP, an LDC would have to have a strong backward linkage and domestic industrial base, which appeared to be too unrealistic given the situation of LDCs.

In the past, both Bangladesh and Nepal had serious difficulties in fulfilling the ROO laid down by the EU. Despite enjoying a rapid growth of T&C exports, Bangladesh continued to depend critically on imported fabrics for its apparel industry and hence for an overwhelming part of woven garment exports failed to fulfill the three-stage value addition. Following a request from Bangladesh and as a part of global initiative, the EU-ROO was revised in 1998 to allow two-stage value addition for both woven and knit products. Even with this derogation, the ROO remain stringent, as Bangladesh's capacity of producing fabrics has not increased rapidly.

After the expiry of the Multi Fibre Arrangement (MFA) regime in global T&C trade on 31 December 2004, the restrictive ROO is likely to adversely affect South Asian LDCs. In the absence of quantitative restrictions, while the large countries such as China and India are able to expand their exports rapidly, the ROO act as a binding restriction on the supply capacity of LDCs. During the first six months of the post-MFA regime (i.e. January-June 2005) Bangladesh's RMG export to the EU, most of which is not eligible for zero-tariff access because of ROO, declined by 6 percent compared to the same period of the previous year.[3]

NON-TARIFF BARRIERS

Apart from ROO, a slew of NTBs inhibit the utilisation of existing trade preferences by South Asian LDCs. According to an estimate by UNCTAD, 40 percent of LDC exports to developed country markets are affected by such NTBs such as technical barriers to trade, sanitary and phytosanitary measures (SPSM), customs rules and procedures, anti-dumping duties, countervailing duties and other compliance requirements with regard to labour and environment standards. A significant proportion of South Asian LDC exports have to comply with the health and quality standards of the western developed countries. These standards differ between destinations and suppliers normally lack adequate capacities to comply with all the requirements.

Consider fish and fish products (including shrimps), which are vital exports of Bangladesh and Maldives. For these exports, the EU quality control rules and regulations require compliance with about 300 points check list, as specified in the HACCP (Hazard Analysis Critical Control Point) manual in minute detail. In the past, sanctions on Bangladesh's shrimp exports were imposed both in Europe and North America because of non-compliance with standards. Although EU preferences now extend over all LDC agricultural products, the application of SPSM will undermine export prospects of South Asian LDCs.

Complying with labour standards has been a critical challenge facing garment exporters in Bangladesh and Nepal. In the early 1990s, both these countries were threatened with import bans as there were allegations of child labour being used in the industry. This resulted in elimination of under-age workers from the export industry despite the fact that children worked both in export and non-export sectors and their elimination from one sector could actually contribute to deteriorating working conditions in the other. Labour standards and work environment continue to pose serious threats for apparel exporters from South Asian LDCs. While the need for improving the working conditions cannot be overstated, evaluating the performance against unusually high standards would be unrealistic to the situation of LDCs and could actually erode their competitive advantage.

Anti-dumping duties have also been used by the US against Bangladesh. Settling an anti-dumping case at the WTO can be quite lengthy and expensive. Weak technical expertise also acts as a constraining factor for LDCs in pursuing such cases. Furthermore, the imposition of anti-dumping duty by the US could at least be partly attributable to the inability of Bangladesh in preparing documents (i.e., lack of trade-related capacities) as required by US laws (Bhattacharya and Rahman, 2000).

ECONOMIC GEOGRAPHY AND WEAK PHYSICAL INFRASTRUCTURE

Geographical location, coupled with weak physical infrastructures, undermine the ability of South Asian LDCs to optimally utilise trade preferences. Unfavourable geographical locations increase costs of both export and import trade relative to countries with more favourable geographical characteristics. A 10 percentage point increase in transport costs is found to reduce trade volumes by around 20 percent (Limao and Venables, 2001). Consequently, transport costs alone can erode a country's export competitiveness (Box 6). Europe and North America are two major markets of South Asian LDCs, but there are other developing countries geographically closer to these markets. This natural disadvantage may make exporting more difficult and the existing relative preferential margins may not be enough to attract foreign investment in the export oriented sectors. In addition, weak and inefficient physical infrastructures, including ports and road networks in South Asian LDCs, aggravate the situation.

Two South Asian LDCs, Bhutan and Nepal, are landlocked with serious consequences for their trading prospects. It has been found that median landlocked country's shipping costs are more than 50 percent higher than those of the median coastal country (Limao and Venables,

BOX 5

UTILISATION OF PREFERENCES BY SOUTH ASIAN LDCS

The actual use value of preferential schemes depends on : (1) the proportion of a country's exports that are covered (the potential cover rate), and (2) the ratio between exports that actually receive preferential treatment and those that are in principle covered (utilisation rate). Table 2 summarises the utlisation of preferences by South Asian LDCs in the individual Quad markets, the most striking aspect of which is the abysmally low potential cover rate in the US, as the overwhelming majority of South Asian LDC exports are not covered in that market. The cover rate is very high in the EU, but the utilisation rate is low. This is most likely to be attributable to the countries' inability to satisfy ROO requirements. If this is so, ROO are much more restrictive than what would be needed to prevent import from a non-eligible third country (Brenton, 2003). Therefore, the key point that emerges from Table 2 is that either preferences given to South Asian LDCs have limited product coverage or preferences are conditional on complying with very restrictive origin rules. Note that the cover rate for Canada has actually increased in recent times after it introduced duty-free and quota-free access to all LDC products.

TABLE 2

Countries	Canada		EU		Japan		US		Total	
	Potential cover rate	Utilisation rate	Potential cover rate	Utilisation rate	Potential cover rate	Utilisation rate	Potential cover rate	Utilisation rate	Potential cover rate	Utilisation rate
Bangladesh	10.3	74.2	100	50.8	64.5	76.6	1.9	69	57.3	51.6
Bhutan	100	0	81.8	15.5	100	100	7.1	56.7	18	39.5
Maldives	6.9	99.2	99.9	26.2	8.5	79.5	0	0	73.8	28.1
Nepal	45.4	77.4	100	71.3	99.7	80.1	4.7	90.7	44.9	74.1
All LDCs	59.3	60.6	58.8	45.6	39.8	30.7	36.4	66.6	46.9	46.8

Source: Table 7 from the report "Market Access Issues Related to Products of Export Interest Originating from Least Developed Countries", Sub-Committed on Least Developed Countries Negotiating Group on Market Access, WTO, September 29, 2003.

BOX 7

HUMAN CAPITAL AND INTERNATIONAL TRADE

The Heckscher-Ohlin trade theory posits that the composition of a country's export is influenced by its factor endowments. Therefore, a country will tend to produce and export the commodities that use its abundant factors of production more intensively. Considering three factors of production, viz., human capital, land and labour in the Hecksher-Ohlin framework, Mayer and Wood (2000 and 2001) have tried to explain the export composition of African and South Asian Countries. They find that compared to other regions, the skill to land ratio is lower for Africa, making the countries in the continent dependent on primary commodities. On the other hand, South Asia has a relatively low supply of human capital. Although the share of manufactures in total exports is high for some South Asian countries, low-skilled labour intensive products dominate their export baskets. In sharp contrast, manufacturing exports of East Asia, which has a rich endowment of human capital, are skill-intensive. The implication of this finding is that the compositional change of South Asian LDCs' manufacturing production (hence exports) from low to high value-added items is unlikely to change substantially unless the general level of education (i.e. skill formation) rises. Mayer and Wood suggest that this fact should be considered while assessing the long-term export prospects of poor countries.

2001). This cost can increase further if goods are transported through a neighbour ing country, which also suffers from weak road networks and port infrastructure. Bhutan and Nepal are thus adversely affected, partly because of their neighbours' weak and inefficient infrastructure. Another South Asian LDC, Maldives, is associated with characteristic features of many other small states including excessive exposure to international shocks, remoteness and isolation, and proneness to natural disasters – all of which have debilitating effects on trade prospects (Atkins et al. 2001).

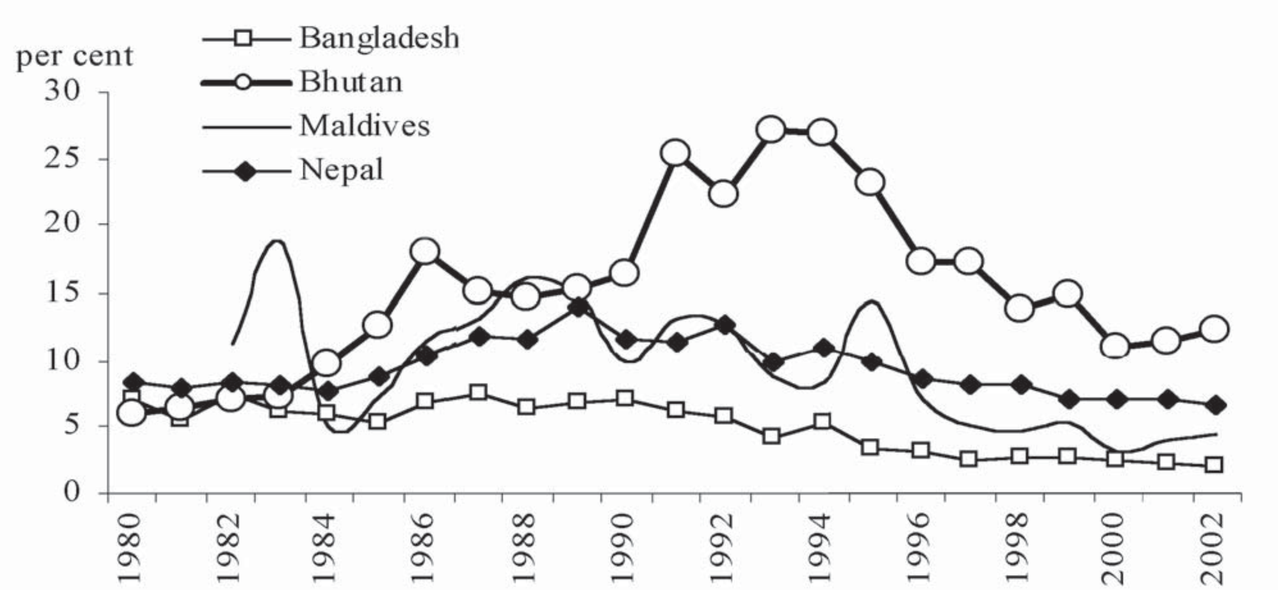
LIBERALISATION OF SERVICES

Although the goods sector has been marked by various unilateral preferences, nothing much has been offered to LDCs in the services sector. Negotiations in the services sectors where LDCs have a clear comparative advantage have not yet made any progress. The liberalisation of the temporary movement of natural persons can generate large returns to many LDCs, including Bangladesh and Nepal.[4] Despite the potential benefits of increased mobility of workers, movement of temporary workers supplying services currently accounts for only about 2 percent of the total value of services trade. A meaningful and effective trade preference regime now requires ensuring market access in areas of interest to LDCs.

FIGURE 3

ODA FLOWS TO SOUTH ASIAN LDCS

All the South Asian LDCs have witnessed a sharp decline in the significance of ODA in their national economies. Most strikingly, the share of ODA in Bhutan's GDP has fallen from more than 25 percent in the early 1990s to about 12 percent by 2002. One important fact is that even on absolute terms, the ODA flow has been stagnant to each of these four countries.



WAY FORWARD FOR MAKING PREFERENCES EFFECTIVE

Despite the urgency for providing meaningful market access to LDCs, South Asian LDCs continue to face high and discriminatory tariff barriers, which are completely against the spirit of the ongoing Doha Development Round under the WTO regime. Granting unrestricted access to every product in every market would thus constitute one direct route to make trade preferences effective. Preferential access of LDCs to the markets of developing countries is very limited. Many developing countries are now growing markets and preferences granted to these markets can be effective in stimulating export response from South Asian LDCs. Special and differential treatment for LDCs both in the markets of developed and developing countries, has so far been non-binding in nature, but to ensure their credibility and predictability, they need to be bound in the WTO.

ROO, particularly those of the EU, have become a barrier to trade. As shown in Box 5, the low preference utilisation rates of EU preferences by South Asian LDCs are an indication of the ROO being a binding constraint for these countries (Table 2). Trade preferences will be effective if origin rules are simplified and relaxed, taking into consideration supplying capacities of South Asian LDCs. Special care and restraints should be exercised and the realities of LDCs should be considered in using NTBs against them.

The preferential margins to LDCs are being eroded because of the ongoing multilateral trade negotiations as well as the autonomous liberalisation in the developed countries. Therefore, some kind of compensatory measures will be needed to mitigate the loss of preferences and to sustain LDC producers' relative competitiveness.

Liberalisation of the services sector related to temporary movement of natural persons is of particular interest to South Asian LDCs and this is an area where they can make use of any preferences given.

South Asian LDCs suffer from a poor state of physical and social infrastructures (human capital), considered to be indispensable for expanding productive capacities and particularly for exporting manufactured goods that have witnessed a rapid growth in world trade (Box 7). Physical infrastructure and human capital development require long-term investment, which will critically depend on the inflow of official development assistance (ODA). The significance of ODA in the national economy of all South Asian LDCs, however, has witnessed a major decline in the 1990s (Figure 3). Hence, increased financial aid and technical assistance are needed for trade-related capacity building in terms of human capital and infrastructure development and for compliance and standards related capacity. Support systems for such development activities need to be institutionalised and should be integrated within the multilateral trade liberalisation regime under the World Trade Organisation. Natural disadvantages associated with the geographical location of South Asian

BOX 8

"TRADE MARSHALL PLAN FOR LDCS"

Despite increasing global integration, LDCs have failed to derive benefits from the process of trade liberalisation and globalisation. Against this background and drawing upon the historical experience with the Marshall Plan for the reconstruction of war-devastated Europe, in recent times, a comprehensive trade support mechanism for LDCs – "Trade Marshall Plan" – has been proposed (Puri, 2005). Market access in both goods and services and aid for trade-related capacity building are the salient features of the proposed trade preference regime. The core action plans proposed are:

1. Bound duty-free and quota-free treatment (DFQFT) by developed countries to all export items from LDCs
2. Simplified origin rules and administrative procedures
3. Improved market access (including DFQFT) in relatively advanced developing countries
4. Disciplined NTBs against LDCs and helping them build standards-related capacity
5. Supporting supply-side capacity and offering commercially meaningful market access in the services sector
6. Additional finance for compliance and adjustment costs and trade capacity development
7. Creation of 'aid for trade' fund

It is estimated that welfare gains for LDCs from DFQFT could be upto US$ 8 billion and gains from targeted service package could be another US$ 10-20 billion. The 'aid for trade' fund is expected to accumulate US$ 15 billion in 2-3 years.

LDCs deserve special attention while providing resource support for infrastructural development and trade-related capacity enhancement (Box 8).

Last but not least, it is important to consider the domestic factors hindering the supply-side of South Asian LDC exports. In any country, firms' performance and international competitiveness will be influenced by the domestic business and investment climate. An enabling economic environment comprises of sound macroeconomic and structural policies, good infrastructure, fair policy of competition, sound legal and regulatory framework and efficiently functioning institutions. Many of these pre-requisites are lacking in the context of South Asian LDCs. Corruption, political instability and administrative red tape creates a business unfriendly environment in these countries, deterring new investment in productive activities both from local and foreign investors.

Therefore, only concerted efforts both at the domestic front and cooperation extended by other developed and developing countries can enable South Asian LDCs to make effective use of trade preferences.

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ENDNOTES

1 For example, from their empirical exercise, Özden and Reinhardt (2004) conclude that non-reciprocal preference programmes have failed to stimulate export response of beneficiary countries in the US market. In contrast, Romalis' (2003) results show significant growth effect of trade preferences, benefiting the poor countries. Romalis also finds that the growth rate of countries that received the largest tariff reductions accelerated relative to the growth rate of countries that benefited less.

2 The US preferential schemes are: the African Growth and Opportunity Act (AGOA), the Andean Trade Preference (ATP) and the Caribbean Basin Trade Partnership Act (CBTPA). Apart from these, under the North American Free Trade Area (NAFTA), a developing country, Mexico, has been offered duty-free market access by the US.

3 However, because of very robust growth of knitwear products, on the whole, the T&C sector could register a modest growth of 8 percent. Bangladesh has been able to develop substantial backward linkage activities in the knitwear sector as result of which the country can benefit from the EU GSP scheme.

4 It has been estimated that liberalisation of just 3 percent of labour market in the Organisation for Economic Cooperation and Development (OECD) countries would lead to economic gains to the tune of US$ 150 billion to the developing countries and LDCs (Winters *et al.*, 2003).

Launched in December 1994 at Nagarkot, Nepal by a consortium of South Asian non-governmental organisations (NGOs), South Asia Watch on Trade, Economics & Environment (SAWTEE) is a regional network that operates through its secretariat in Kathmandu and 11 member institutions from five South Asian countries, namely Bangladesh, India, Nepal, Pakistan and Sri Lanka. Registered in Kathmandu in 1999, the overall objective of SAWTEE is to build the capacity of concerned stakeholders in South Asia in the context of liberalisation and globalisation.

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