



# Aid for Trade

## I. Introduction

International aid to assist developing countries in their efforts to implement economic reforms is not new. However, aid has rarely been a simple transfer of resources from rich to poor countries. Often, aid comes to developing countries attached to a development "toolbox" in the form of aid conditionality. This toolbox traditionally involves neo-liberal macroeconomic and trade policy prescriptions in the form

of structural adjustment programmes that are more often a reflection of the political and economic ideology of donors than of the economic development priorities of aid-receiving countries. A report by the World Bank states that "[d]onors use aid to advance their values, their commercial interests, their cultural aspirations and their diplomatic and political objectives." <sup>1</sup>

Aid for trade is a reflection of the fact that trade liberalization in itself does not automatically

## Executive Summary

The availability of trade-related assistance is not enough to fulfil the development dimension of the Doha Work Programme. It is an important element of it, but it is not sufficient. Reaching a negotiating outcome that is truly pro-developmental in each area of the Doha Work Programme is also essential and aid cannot replace such an outcome. Nor can aid offset a bad trade package. Aid and trade assistance in favour of developing countries is rightfully recognised in the 2001 WTO Ministerial Declaration, and has to be delivered without further conditions. Likewise, trade negotiations within the context of the Doha Round have to be negotiated and agreed upon on the basis of the benefit that they will bring for poverty reduction and human development.

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lead to growth and development. In fact, most developing countries have not been able to fully benefit from trade because they either lack tradable surpluses or have deficient knowledge of market access opportunities. Even when poor countries do have products to trade and are aware of export opportunities, they may still fail to penetrate world markets because they lack the necessary exporting infrastructure (e.g. roads, ports, electricity) or are unable to meet technical standards prevailing in high value markets (sanitary measures, technical barriers, certification, etc.). Whereas the benefits of multilateral trade liberalization may not be fully materialised in developing countries, the costs of liberalization will automatically be realized.

Consequently, there is an emerging consensus that trade liberalization in the context of the current WTO Doha Round will require adequate trade-related assistance in order to enhance the trading capacity of developing countries and make sure they do benefit from new market access opportunities and at the same time avoid or mitigate undesirable, detrimental effects of trade reforms. In other words, aid is essential to balance the realization of the potential benefits and the costs of multilateral trade liberalization.<sup>2</sup>

There is no doubt that such assistance is needed and that it must be a major component of a pro-development WTO Round of negotiations. It however will not be sufficient to fulfil the developmental promises of the Doha negotiations.

In fact, enhanced trade-related technical and financial assistance could be used as the flag of a "WTO Development Round", distracting attention away from the importance of reaching a pro-developmental outcome in the various negotiating areas. Aid, however attractive, cannot replace a truly pro-development negotiating outcome and should therefore not be used as an incentive to force developing countries to accept an outcome that is incompatible with their developmental priorities. In essence, an "aid for

trade package" must not be used as a "bargaining chip", in exchange for a comprehensive "trade liberalization package".

Developing country negotiators in the WTO should be aware that the idea of a trade-off between liberalization and aid is very likely, particularly as we approach the finalization of negotiating modalities and Members start to assess the overall benefit they can draw from the Round. They should reject an outcome that does not favour their negotiating interest even when accompanied by aid.

In view of the forthcoming Sixth WTO Ministerial Conference, it is useful to shed some light over the proposed concept of aid for trade and assess the implications that accepting a trade off could have for the negotiating process and outcome.

## II. Background elements for the discussion

*"... assistance is ... a major component of a pro-development WTO Round .... It however will not be sufficient to fulfil the developmental promises of the Doha negotiations".*

### *The Aid for Trade Package*

The World Bank and the IMF, in response to requests from the G7 Finance Ministers and the G8 in Gleneagles, jointly proposed an aid for trade package.<sup>3</sup> The package is a proposal for provision of financial and technical assistance to developing countries for two related objectives. The first is to address supply-side constraints in developing countries ("maximization of the benefit") and the second is to assist them in coping with the adjustment cost of trade liberalization, which is assumed to be transitional ("minimization of the cost").

The first objective could be the result of the recognition that market access does not necessarily result in developing countries actually penetrating global markets and that developing countries can benefit from ambitious trade liberalization in industrialized markets only when they are able to bolster their production and marketing capacity. The second objective is the reflection of the long-

standing argument by proponents of free trade that opening up to trade and ensuing higher integration in global markets is a prerequisite for economic development in developing countries.

In general, aid for trade is envisaged as a toolbox to entice developing countries to take more ambitious liberalization commitments with the promise that assistance will be made available to help them cope up with the resulting adjustment cost.

### *The Rationale*

The rationale advanced by the World Bank and the IMF is that developing and least developed countries have not been able to take full advantage of the benefits of multilateral trade liberalization because of limitations that impinge on their trading capacity (usually referred to as “supply-side constraints”) and their own trade policy framework, such as - for instance - the maintenance of high unbound tariffs that, they say, create “disincentives to enter international markets”. Hence, the World Bank and the IMF say that the benefit of multilateral trade liberalization could be realized in developing countries if such limitations are mitigated through increased financial and technical assistance.

Proponents of an aid for trade package build their proposal on the premise that trade liberalization necessarily leads to economic growth and development and that it would suit all countries provided aid for trade is available to assist them. In fact, aid for trade is seen as an instrument to help countries reach further levels of trade liberalization.

### *The Elements of the proposed package*

An aid for trade package, as proposed by the IMF and World Bank, could have five elements: technical assistance, capacity building, institutional reform, investment in trade-related infrastructure and assistance to mitigate specific adjustment cost.

The first four elements of the package target improving the supply capacity of developing

countries including through investments in infrastructure (e.g. roads, ports, telecommunications, irrigation, electricity), institutions (e.g. implementation of specific reforms, such as tax reforms, better understanding of rules, customs administration), private sector capacity (e.g. export promotion, assistance to meet technical standards in export markets, and knowledge about new market opportunities) and human capital (e.g. education and training).

The last element aims at mitigating the adjustment cost associated with trade liberalization in developing countries (e.g. loss of government revenue because of a reduction in import duties, increased import competition, erosion of preferences, etc.).

Trade liberalization commitments that developing countries make in multilateral trade negotiations should be commensurate with their level of economic development and compatible with their developmental priorities. This is fully recognized, for instance, in the Preamble to the WTO Agreement, in various Special and Differential Treatment (S&D) provisions contained in WTO Agreements, and in the Doha Declaration. It is further confirmed by WTO jurisprudence, such as, for example, the appellate body ruling in *EC-Conditions for the Granting of Tariff Preferences to Developing Countries*.<sup>4</sup> Of particular importance are the principles of progressivity and flexibility in trade liberalization.

Many developing countries are concerned that drastic trade liberalization, particularly substantial reductions in tariff, could entail, for instance, loss of tariff revenue hence fiscal difficulties, losses of output and jobs, close-down of businesses (deindustrialization) and balance of payment problems. Preference-receiving developing and least developed countries are also concerned that they will face serious difficulties as a result of MFN liberalization and the ensuing erosion of the preferential margins of market access that they enjoy in preference-giving countries. Similarly, Net Food-Importing Developing Countries (NFIDCs) are highly concerned that the phasing out of agricultural export subsidies and substantial reductions in domestic support, as part of an ambitious Doha Package, would raise world food prices thereby threaten-

ing food security and causing balance of payment difficulties.

All these concerns are thought to be obstacles to an ambitious Doha Round of trade liberalization. Aid for trade is thus seen as a catalyst for the conclusion of a more ambitious Round.

### **III. Aid will be a fundamental element of a pro-development Doha outcome but it cannot suffice**

Considering that the linkages between trade liberalization and growth on the one hand, and trade growth and poverty reduction on the other hand are not automatic or guaranteed; the discussion about aid for trade is not about whether or not aid is needed. Past experience and theoretical evidence show that aid, particularly aimed at addressing supply-side constraints, is a real need to guarantee the realization of the potential benefit of the multilateral trading system for all developing countries. Therefore, discussions on aid for trade can be split into two broad issues. The first is whether or not the aid that is currently being delivered or planned is effective and sufficient to fulfil the objectives that were set for that assistance. The second concern the operationalization of that aid, how it is administered, and the attachment of conditions to it.

The first issue concerns the content of the current programmes of technical assistance, capacity building and financial aid that are delivered through multilateral agencies (including but not restricted to the WTO) and individual donors. There is a clear need to change and improve aid: make better use of existing resources, increase the amounts currently allocated and make their future availability more predictable, make aid more meaningful and better targeted to individual circumstances, broaden the concept of aid for trade to encompass more than only a narrow definition of trade facilitation and implementation of legal commitments, etc. However, the scope of this paper is not to re-

view the possible contents of a meaningful aid for trade package.

The second concerns the linkage, or better still, the subordination of aid (however framed or whatever its contents) to a comprehensive agenda of trade liberalization. It concerns the utilisation of aid as an incentive for the acceptance of greater liberalization by developing countries. It concerns the acceptance of a trade liberalization package, instead of a development package, in exchange for promises of aid. It is this subordination that is of immediate concern and has serious implications for developing countries.

### **IV. Realization of benefit and Mitigation of cost: what counts is a pro-development negotiating outcome**

Aid for trade is said to be an instrument to simultaneously boost the benefit and reduce the cost of trade liberalization. However, the maximization of benefit is only possible in a scenario that contains at least some beneficial elements for developing countries. Similarly, the establishment of mechanisms to minimize possible difficulties would not be necessary at all if there were no difficulties to cope with. In other words, emphasis on a negotiating outcome that truly responds to the interests of developing countries is itself the best step towards ensuring gains for developing countries.

For example, drastic agricultural tariff liberalization in developing countries could result in a surge in imports of agricultural products, often heavily subsidised by developed countries, forcing local producers into bankruptcy and threatening local food security. Therefore, unmanaged, drastic tariff liberalization combined with a failure to effectively curb agricultural subsidies in developed countries would undoubtedly enhance the hardship of developing countries and lead to a situation where no aid package as impressive as it may seem can adequately address that hardship.

Managed and progressive tariff liberalization of agricultural products in developing countries,



respectful of their capacity to absorb reforms, together with the effective elimination of agricultural subsidies in developed countries and an improvement of market access conditions for products of export interest to developing countries is the outcome that members should strive for.

In sum, the existence of an aid for trade package, however attractive, cannot replace the benefit of a negotiating outcome that reflects the developmental needs and priorities of developing countries.

### **V. How could the Aid and liberalization Trade-off Creep in the WTO?**

The need for aid for trade has emerged in several negotiating groups of the WTO. It emerges, in the Agricultural negotiations as, for instance, the need to establish a fund to assist NFIDCs to cope with higher prices of agricultural imports resulting from the phase-out of agricultural export subsidies. It also appears in non-agricultural market access (NAMA) negotiations as the need to assist tariff-dependent developing countries undertake tax reforms in order to compensate for the loss of government revenue. It emerges explicitly in trade facilitation, where negotiating assistance and aid for the implementation of commitments being currently negotiated are full pillars of the negotiations. Finally, it also emerges at a more general level in the Committee on Trade and Development, for instance, during discussions about the full integration of LDCs into the multilateral trading system.

The question in these negotiating groups could ultimately be: do developing countries agree to compromise on their initial development demands and accept more binding commitments in the WTO in exchange for the promise of increased aid? Can they undertake larger liberalization and binding commitments than they would otherwise be able to do without the offer of increased aid?

### **VI. Implications of the trade-off between negotiating outcome and aid**

The acceptance of a trade-off between trade liberalization and aid for trade would have many implications for the fulfilment of the developmental promises of the Doha Work Programme.

#### *Binding commitments vs. Promises only*

The aid for trade package is not a blank check. It is aimed at achieving ambitious trade liberalization under the Doha Round negotiations by encouraging developing countries to undertake market liberalization in NAMA, services, and agriculture in exchange for promises of assistance to cope with the resulting adjustment cost. In essence, the proposed aid for trade package encourages developing countries to make binding commitments under the WTO in exchange for non-binding promises. While an infringement of commitments made in the WTO would result in sanctions under the Dispute Settlement mechanism, the disrespect of promises for aid would have no implications for donors.

For developing countries, the danger of undertaking binding commitments for unduly ambitious trade liberalization in exchange for an aid for trade package escalates when considering that promises made in the past by bilateral and multilateral donors under bilateral and multilateral trade agreements were seldom respected. In fact, there is already a clear deficit in the aid that is currently available. Several promises had also been made during the Uruguay Round.

Moreover, given the narrow trade-related mandate of the WTO, aid is likely to be pledged in and channeled through other international organizations. This would significantly reduce the negotiating leverage of developing countries, who would accept to compromise in the

WTO leaving their demands to be dealt with outside the strict boundaries of the WTO.

### *Development priorities vs. a 'Straight jacket'*

Being conditional upon ambitious trade liberalization, the aid for trade package is rooted in the premise that ambitious trade liberalization supports long-term development in all developing countries, regardless of their differences, provided that they are assisted to cope with the transitional cost of adjustment and to enhance their trading capacity. In essence, the proposed package sees development as a linear function that simply follows trade liberalization. It does not consider the development priorities of developing countries and how ambitious trade liberalization commitments in developing countries could destabilize these priorities. More importantly, the package ignores the importance of "policy space" for development and accepts a one-size-fits-all model of development.

As a matter of fact, developing countries are different in their economic structure and have different development priorities. Consequently, the potential benefit and cost of trade liberalization varies widely among different developing countries thereby requiring different policy instruments for adjustment. Hence, presenting aid for trade as a "straight jacket" that fits all developing countries and equally ameliorate the cost of trade liberalization that they would encounter should they take ambitious trade liberalization commitments is grossly detached from reality.

### *Inadequate funds: Who gets what?*

Assuming that additional commitments are made in WTO in exchange for increase aid, there will also be a problem of allocation of limited resources among developing countries. Unfortunately, there has not been enough political commitment from donors to make sufficient funds available for effective development aid,

leading to the current deficit in all areas of development assistance. In fact, a major question surrounding the aid for trade debate is how that aid would relate to existing resources and schemes, including the impact that it would have on the availability of resources for non trade-related development assistance.

Meaningful and effective trade-related assistance would necessarily have to comprise heavy investments in infrastructure, human capital and institutional building under full ownership of the recipient countries. Even assuming that the necessary political will for that is available, it is unlikely that there will be enough funds to cover projects in all countries that need assistance. In such cases, how would limited funds be allocated among developing countries? Should it be allocated on the basis of countries' capacity to cope with the cost of trade liberalization and the gravity of the supply-side constraints?

Undoubtedly, the allocation of funds under the aid for trade package could be a "Pandora Box" that could potentially fragment developing country coalitions and weaken their positions in the WTO negotiations. The consequences of a 'race for aid' could have systemic implications for South-South cooperation well beyond WTO and international trade.

### *Time mismatch: Potential benefit vs. Cost of liberalization*

Trade has a potential benefit to developing countries which could be realized only when trade liberalization is undertaken gradually and progressively matching their level of economic development and development priorities. As the experience of many countries shows, rapid trade liberalization that neither matches developing countries' level of economic development nor supports their development priorities leads to non-realization of the potential benefit of trade but to the realization of its cost. Moreover, while the cost of trade liberalization is felt immediately, the realization of its benefit, if ever, could take many years. Hence, taking a binding commitment for ambitious trade liberalization as conditional to

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accessing funds under the aid for trade package is tantamount to taking a binding obligation to incur guaranteed cost in exchange for uncertain benefit from trade and uncertain and non-biding promise from donors.

### *Aid is a right in its own*

Developing country negotiators need not be apologetic or defensive about needing aid to better benefit from trade. All of today's developed countries have needed heavy investments to boost their production and trading capacity before engaging in international trade, so donors should not feel that aid is charity.

In fact, trade-related assistance is an integral part of the Doha Work Programme. It is mentioned more than twenty times in the Doha Declaration (paragraphs 2, 16, 21, 24, 26, 27, 33, 38, 39, 40, 42 and 43) and should therefore be negotiated and implemented in its own right, independently from the advancement of a pre-established agenda of trade liberalization.

Similarly, development is said to be at the core of current negotiations, permeating all the negotiating areas. Hence, negotiations in each of the areas of the Work Programme must lead to an outcome that truly incorporates developmental priorities; aid cannot replace such an outcome.

### *Surprise Effect*

The aid for trade package has only recently crept into the WTO and has not been thoroughly discussed. Hence, many aspects of it including the amount of the aid, the fund allocation mecha-

nism, the duration and administration of the package remain unknown. Nonetheless, the aid for trade package is likely to be used by developed countries in Hong Kong as a "bargaining chip" to buy market access from developing countries and to weaken their commonality. An aid for trade package could possibly be used to argue that the developmental promise of the Doha Round has been fulfilled, diverting negotiators' attention away from the various negotiating areas.

## VII. Conclusion

Developing countries must not accept a negotiating outcome that does not suit their developmental interests and need not review their developmental demands in exchange for aid. The 2001 Doha Ministerial Declaration is very explicit in making technical assistance and capacity building a right of developing countries. A whole section of the Declaration is devoted to the issue and it is also fully incorporated in specific negotiating mandates. Aid for trade is thus a right, without further conditions.

Trade-related aid should be untied, comprehensive, demand-driven, sufficient and incremental to existing programmes, predictable and available in the long term. An aid for trade package must not have any link with a pre-established negotiating outcome, especially one that is not compatible with the developmental needs of poor countries. If the condition to receive aid is the acceptance of an outcome where developing countries stand to lose, such a package should be rejected.

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## End Notes

1. World Bank (2000), *Can Africa Claim the 21st Century*. Washington D.C.
2. This premise is precisely the reason why an increase of aid by industrialized countries is seen as central to achieving the UN Millennium Development Goals. In addition, the centrality of aid for fuelling economic development in developing countries was emphasized in different international instruments such as the Monterey Consensus and the Sao Paulo declaration. Most recently, the Blair African Commission Report called for several-folds increase in aid to give the continent a "big push" for a steady and sustainable development.
3. "Doha Development Agenda and Aid for Trade", prepared by the Staffs of the IMF and the World Bank, 9 September 2005 (DC2005-0016).
4. WT/DS246/AB/R at page 65.



## SOUTH CENTRE

Chemin du Champ d'Arnier17  
PO Box 228, 1211 Geneva 19  
Switzerland

Telephone: (4122) 791 8050  
Fax: (4122) 798 8531  
E-mail: [south@southcentre.org](mailto:south@southcentre.org)

Contact us in the web:

<http://www.southcentre.org>

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