CENTER FOR GLOBAL DEVELOPMENT
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Trade Policy and Global Poverty

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Preface

Would freer trade free more of the world's poor from the misery their poverty represents? Though few would argue anymore that globalization has only winners and no losers, this book answers the question with a resounding yes. Though successive rounds of postwar multilateral trade negotiations have reduced the costs of protection and increased trade and its benefits, there is much more still to be gained, especially for the developing countries. And much of those gains for developing countries could come from further reductions in protection in the richest countries.

The recent Uruguay Round of negotiations, completed in 1994, continued the pattern of progress toward sharp reductions in protection in industrial countries for most manufactures but only meager advances in liberalizing high protection in sectors with politically important domestic constituencies, especially agriculture and textiles and apparel. Yet these are the sectors in which the developing countries have a comparative advantage. The Uruguay Round left tariffs largely unchanged in these sectors, although it converted agricultural quotas to tariffs and promised the removal of textile and apparel quotas by 2005. The effective postponement of liberalization meant that developing countries gained much less from the round than they might have. Stiff resistance in Europe to cutting its large farm subsidies and an increase in these subsidies within the United States have recently deepened this impression. So has the increasing attention paid to the rules developing countries agreed to on intellectual property rights, which became closely associated in the public mind with the high costs of medicines to fight the AIDS pandemic in the poorest countries.

The current Doha Round was therefore designated the "Development Round" to show international commitment to a stronger realization of potential benefits for developing countries from the new round. The implication is that the Doha Round is designed to go beyond the traditional commercial deal-making whereby countries place import liberalization offers on the table solely to obtain reciprocal offers from trading partners. To live up to its title, the round will have to make special efforts to ensure the opening of new opportunities for developing countries.

William R. Cline, a joint senior fellow at the Center for Global Development and the Institute for International Economics, has written extensively on both trade and development issues. This study seeks to provide a comprehensive analysis of the potential for trade liberalization to spur growth and reduce poverty in developing countries. It provides specific analysis of how much impact liberalization by industrial countries, along with liberalization by the developing countries themselves, can have on global poverty.

Cline finds that the global poverty stakes in trade policy are large. Global free trade would convey long-term economic benefits of about $200 billion annually to the developing countries. Half or more of these gains would be attributable to the removal of industrial-country protection against developing-country exports. By removing their trade barriers, the industrial countries could thereby convey economic benefits to developing countries worth about twice the amount of their annual development assistance. Helping developing countries grow through trade, moreover, would be accompanied by economic benefits for the industrial countries themselves in the form of lower consumer costs for imports and other increased economic efficiencies from opening trade.

The study further estimates that free trade could reduce the number of people in global poverty (earning less than $2 per day) by about 500 million over 15 years. This would cut the world poverty level by an additional 25 percent. Agricultural liberalization alone contributes about half of these gains. Cline thus judges that the developing countries were right to risk collapse of the Doha Round at the Cancún ministerial meeting in September 2003 by insisting on much deeper liberalization of agriculture than the industrial countries were then willing to offer.

The study calls for a two-track strategy. The first track is deep multilateral liberalization involving phased but complete elimination of protection by industrial countries and deep reduction of protection by at least the middle-income developing countries, albeit on a more gradual schedule. The second track is immediate free entry for imports from "high risk" low-income countries (heavily indebted poor countries, least developed countries, and sub-Saharan Africa), coupled with a 10-year tax holiday for direct investment in these countries. The "poverty intensity" of imports from these countries is far higher than the average for imports from other developing countries, and the head start from immediate free entry would provide an important boost to the pace of global poverty reduction.

Political leadership is required to realize the poverty-reduction potential of global free trade. As this book goes to press there are some signs that this leadership is emerging and can begin to overcome the powerful resistance from such interests as the recipients of agricultural subsidies. If this new momentum can build, the Doha Round may yet prove worthy of being recorded as the Development Round.

* * *

The Center for Global Development is a nonprofit, nonpartisan institution dedicated to reducing global poverty and inequality through policy-oriented research and active engagement on development issues with the policy community and the public. A principal focus of the Center's work is policies of the United States and other industrialized countries that affect development prospects in poor countries and policies of the international institutions such as the World Bank and the IMF that are central to the world's development architecture.

The Center's Board of Directors bears overall responsibility for the Center and includes distinguished leaders of nongovernmental organizations, former officials, business executives, and some of the world's leading scholars of development. The Center receives advice on its research and policy programs from the Board and from an Advisory Committee that comprises respected development specialists and advocates. The Center's president works with the Board, the Advisory Committee, and the Center's senior staff in setting the research and program priorities, and approves all formal publications. The Center is supported by an initial significant financial contribution from Edward W. Scott Jr. and by funding from philanthropic and other organizations.

The Institute for International Economics is a private, nonprofit institution for the study and discussion of international economic policy. Its purpose is to analyze important issues in that area and to develop and communicate practical new approaches for dealing with them. The Institute is completely nonpartisan.

The Institute is funded largely by philanthropic foundations. Major institutional grants are now being received from the William M. Keck, Jr. Foundation and the Starr Foundation. A number of other foundations and private corporations contribute to the highly diversified financial resources of the Institute. About 18 percent of the Institute's resources in its latest fiscal year were provided by contributors outside the United States, including about 8 percent from Japan.

The Board of Directors bears overall responsibility for the Institute and gives general guidance and approval to its research program, including the identification of topics that are likely to become important over the medium run (one to three years), and which should be addressed by the Institute. The director, working closely with the staff and outside Advisory Committee, is responsible for the development of particular projects and makes the final decision to publish an individual study.

The Center and the Institute hope that their studies and other activities will contribute to building a stronger foundation for international economic policy around the world. We invite readers of these publications to let us know how they think we can best accomplish this objective.

NANCY BIRDSALL
President
Center for Global Development
May 2004

C. FRED BERGSTEN
Director
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May 2004

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Summary

Global poverty remains at a remarkably high level. Half of the world's population lives in poverty today if one uses the definition of $2 per day (at purchasing power parity, which takes into account the lower local cost of living in poor countries). One-fourth of the world's population has an income of $1 per day or less. The proportion in poverty has gradually declined during the past decade, but the absolute number has remained about the same after taking into account population growth.

Global concessional assistance from rich to poor countries amounts to about $50 billion a year, which works out to about $17 a year per poor person globally. This assistance can make a critical difference, especially when focused on the poorest countries and linked to sound governance and economic policies. Even with potential increases, however, aid alone can make only modest inroads in reducing global poverty.

There is a second policy instrument that can make a powerful contribution to the fight against global poverty: trade policy. The opportunity to boost economic growth through increased exports to more open markets may be the most valuable benefit that policies in rich countries can give to the poor in developing countries. Moreover, opening markets would give gains to the industrial countries themselves in the form of lower prices for consumers.

The estimates of this study suggest that global free trade would confer income gains of at least about $90 billion annually in developing countries for traditional "static" effects, and total long-term gains including dynamic effects would be about $200 billion annually (chapter 5).[1] This

1. This is at 1997 prices and economic scale.

study, moreover, estimates that at least half of these gains would arise from removing protection against developing-country products in industrial-country markets, especially in agricultural goods and textiles and apparel. On this basis, it can be estimated that the elimination of industrial-country protection would provide long-term gains to developing countries of about $100 billion annually, or about twice as much as annual concessional assistance.

Chapter 1 sets the stage for this study by reviewing the evidence on trends in global poverty and delineating the principal relationships of trade policy to economic growth and poverty reduction. A poverty mapping locates about half of the world's poor in China and India alone, and places another one-seventh in just four countries with more than 100 million poor people each—Indonesia, Pakistan, Nigeria, and Bangladesh. About one-fourth of the world's poor are located in what may be called "at-risk" countries already identified in special international groupings: the least developed countries (LDCs), heavily indebted poor countries (HIPCs), and sub-Saharan Africa (SSA).

Chapter 1 proposes the concept of the "poverty intensity of trade" as useful for gauging the potential impact of trade policy in industrial countries on the global poor. This measure would be 100 percent for imports coming from a country with an entirely poor population, and zero for imports from a country with no poor people (at the $2 level). It turns out that industrial-country imports from all developing countries have an average poverty intensity of 33 percent on a headcount basis and only 7 percent on an income-share basis (figure S.1). In contrast, imports are much more poverty intensive from the at-risk countries (LDCs, HIPCs, and SSA), at a range of 60 to 70 percent on a headcount basis and 40 to 50 percent on an income-share basis.

Considering the poverty intensity of trade leads quickly to thinking about a two-track strategy for international trade policy. In the first track, there would be phased reduction or elimination of protection on a multilateral basis by all countries. In a parallel second track, there would be immediate free market access for imports from the at-risk countries, where the potential impact on the poor would be the greatest. Both tracks would be pursued in the current Doha Round of multilateral negotiations within the World Trade Organization (WTO). Ideally, middle-income countries would participate in the liberalization offered on both tracks. Because the base of imports from the at-risk countries is small (ranging from 4 percent of imports from developing countries for Japan and 6 percent for the United States to 8 percent for the European Union), any special adjustment problems in industrial-country markets from the deepening of existing special-access arrangements to immediate complete free access would be minimal, as would any likely trade diversion away from other developing countries.

The background analysis in chapter 1 considers various controversies about global poverty. One is whether the World Bank, the key source for