Differential and More Favorable Treatment of Developing Countries and the International Trading System

Martin Wolf

This article argues that "differential and more favourable treatment" of developing countries in the General Agreement on Tariffs and Trade (GATT) has been a logical consequence of their own inward-looking policies and the GATT's implicit mercantilism, the latter implying that liberalization, being costly, should not be demanded of relatively poor countries. Time has, however, reduced both the appeal of the protectionist model of development and the willingness of developed countries to accord differential treatment. The upshot has been pressure on more advanced developing countries to "graduate" and a growing literature recommending fuller and more equal participation of developing countries in the GATT. The case for fuller and more equal participation is not self-evident. It needs to be assessed on its merits in terms of the prospects for improved market access abroad and more efficient policy at home. The analysis indicates that the potential benefits should not be oversold. On balance, however, the most advanced developing countries would probably gain from active and more equal participation in both GATT and the multilateral trade negotiations while the remaining developing countries would benefit from graduation by the more advanced.

(iv) Contracting parties agree that the principle of differential and more favourable treatment embodied in Part IV and other relevant provisions of the General Agreement and in the decision of contracting parties of November 28, 1979 on differential and more favourable treatment, reciprocity and fuller participation of developing countries applies to the negotiations. In the implementation of standstill and rollback, particular care should be given to avoiding disruptive effects to the trade of less-developed contracting parties.

(v) The developed countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other

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barriers to the trade of developing countries. Developed contracting parties shall therefore not seek, neither shall less-developed contracting parties be required to make, concessions inconsistent with the latters' development, financial and trade needs.

(vi) Less-developed contracting parties expect that their capacity to make contributions or negotiated concessions or take other mutually agreed action under the provisions and procedures of the General Agreement would improve with the progressive development of their economies and improvement in their trade situation and they would accordingly expect to participate more fully in the framework of rights and obligations under the General Agreement.

(vii) Special attention shall be given to the particular situation and problems of the least developed countries and to the need to encourage positive measures to facilitate expansion of their trading opportunities.

—From the Ministerial Declaration at Punta del Este, Uruguay, announcing agreement to start the “Uruguay Round” of multilateral trade negotiations within the framework of the General Agreement on Tariffs and Trade, September 1986.

The theme of this article is the relation between two sets of ideas. The first of these is the approach to trade policy that derives from the view of economic development adopted by the governments of most developing countries since the end of World War II. The underlying vision is one of market failure and of the need for active government intervention in the market, particularly with regard to transactions with other countries. The second set of ideas is that of the General Agreement on Tariffs and Trade (GATT) itself. Those ideas may be described as “disciplined mercantilism” or, better perhaps, the “mutual disarmament approach to trade liberalization.” Protection is appropriate, according to this vision of the world, in the absence of an acceptable reciprocal bargain. Such a vision makes it easier to justify giving in to protectionist pressure, while still retaining some curb upon it, than would a consistent attachment to the principle of free trade, an attachment which existed in the United Kingdom, for example, during much of the nineteenth century.

The issue to which much of the present article relates these ideas is the “differential and more favorable treatment” of developing countries within the GATT. The concept of more favorable treatment derives from the attempt to accommodate the interventionist view of the relation between trade and development within the GATT system. The article argues that this process of accommodation has created problems because the economic ideas that underlie both the interventionist approach to trade policy and the GATT are unsound.

The focus of the present discussion is this broad theme, not precise negotiating tactics and options.1 The argument is structured as follows. First, the meaning of “differential and more favourable treatment” will be explored, along with the

1. Those negotiating issues and options are carefully considered in Balassa and Michalopoulos 1985; see also Scott and others (1984).
way in which the place of developing countries in the international trading system has become a vexed issue. Second, the origin of the calls for special treatment of developing countries will be traced, focusing on the economic ideas and experience that persuaded the representatives of developing countries to advance these arguments. Third, the discussion will turn to how those claims have interacted with the principles of the international trading system itself.

The way in which economic developments have undermined the postwar view of the link between trade and development and the implications for the trade policies of developing countries is the next subject. The principal conclusion is that the developing countries have won a series of largely pyrrhic victories. The discussion concludes with a consideration of the issue of graduation and examines what the developing countries should do now and what benefits they might derive from alternative approaches to the issue of “differential and more favorable treatment” in the Uruguay Round.

I. Role of Developing Countries in the Trading System

“Differential and More Favourable” Treatment

The essence of the exceptional status desired by developing countries is quite simple: the developed countries should grant to the developing countries more favorable market access than they do to one another, while conceding to the developing countries very considerable freedom in their own trade policies. To clarify the dimensions of that special position, it is useful to start with the Framework Agreements of the Tokyo Round. In a decision of the GATT’s contracting parties of November 28, 1979, entitled “Differential and More Favourable Treatment, Reciprocity and Fuller Participation of developing Countries,” the first article in the general statement states:

Notwithstanding the provisions of article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties. [GATT 1979, pp. 5-7]

This article is then explained as having four aspects: (i) the Generalized System of Preferences (GSP); (ii) “differential and more favourable treatment” of developing countries in the context of codes on nontariff barriers negotiated within the GATT; (iii) permission for developing countries to create regional and global trading arrangements that do not conform to Article XXIV of the GATT; and (iv) particularly special treatment for least developed countries. The narrowest definition of “differential and more favorable treatment” would look only at item (ii) above, namely, treatment of developing countries within the codes on nontariff barriers. A somewhat broader definition would include all the four enumerated exceptions.

There is, however, more to the special position of developing countries. As is
made clear in Article 5 of the decision of November 28, 1979, reciprocity is not expected of developing countries, an exception that had already been admitted in the GATT's Part IV (Article XXXVI [8]). More precisely, "The developed countries do not expect the developing countries . . . to make contributions which are inconsistent with their individual development, financial and trade needs." The waiving of reciprocity, though not strictly part of "differential and more favourable treatment," cannot be ignored, since the GATT is a framework for mutual concessions.

Mention should also be made of Article XVIII of the GATT, which covers infant industry protection and restrictions for balance of payments purposes, the latter being much the more important. In this case, however, it is not the position of developing countries de jure that is "differential and more favourable," as the developed countries have the largely equivalent Article XII. What is special is how the developing countries have been treated. In practice, Article XVIII, Section B, on balance of payments restrictions has provided developing countries with what amounts to a carte blanche for quantitative restrictions on imports that in some cases have lasted for years and in a few for decades.2

Accordingly, in the present discussion "differential and more favourable treatment" is taken as referring to everything mentioned in the Decision of November 28, 1979, plus the freedom of developing countries to introduce quantitative restrictions for balance of payments purposes. While this is not, perhaps, the legal definition of the term, it is the one that makes practical sense. The position of developing countries in the GATT system and the problems associated with it are the product of all aspects of their special treatment.

So far as their own policies are concerned, developing countries have not reciprocated in tariff bargaining, their tariffs are virtually unbound, they can readily impose quantitative restrictions for balance of payments purposes and they have been relatively unconstrained—at least until recently—in the use of domestic subsidies and other nontariff measures. Starting in the second half of the 1970s and continuing in the 1980s, the enthusiasm with which the United States of America has pursued so-called unfair trade practices has grown substantially, one result being a great increase in countervailing duty cases against exports from developing countries. These cases have affected not merely the use of export subsidies by developing countries, but almost equally that of domestic subsidies (though countervails of such subsidies are, at least arguably, contrary to the Code on Subsidies and Countervailing Duties agreed in the course of the Tokyo Round). (On this development and its implications for the developing countries, see the papers by Nam and by Finger and Noguès in this volume.)

This new limitation on the freedom of action of developing countries has oc-

2. According to a paper by Richard Eglin of the GATT Secretariat, seventeen countries were invoking Article XVIII (B) in 1985, many of these countries having consulted in the GATT's Balance of Payments Committee repeatedly in the previous ten years. In fact, fourteen countries consulted six or more times between 1974 and 1985. (See Eglin 1987, table 1). On the general issue of quantitative restrictions for balance of payments purposes, see also Anjaria in this volume.
curred not so much because of changes in their formal obligations under the GATT but rather because of changes in the domestic policies of the GATT’s most important single contracting party. In other words, in the area of subsidies the de facto curbs on the developing countries are now tighter than those in effect de jure. So far as the policies of developed countries are concerned, however, the principle of preferential access to the markets of developed countries was formally accepted as a permanent part of the GATT after a long rearguard action by the United States.

Difficulties with the Position of Developing Countries

It had been thought by developing countries that favorable treatment would be granted because of a consensus that they have special problems. Despite apparent agreement on the principle, the developing countries have found themselves exposed to discriminatory export restraint arrangements and other trade distorting measures in many industries in which they have shown a comparative advantage, agriculture, textiles and clothing, and steel being the most important examples. Moreover, the incidence of these restrictions has not been declining as the developing countries have secured concessions—quite the contrary (see World Bank 1986, pp. 23–24, and Nogués and others 1986). At the same time, the preferences granted to the developing countries have been so hedged about by safeguards that their value has been widely questioned (for an assessment of the GSP, see Langhammer and Sapir, forthcoming).

From the point of view of the developed countries, the “concessions” they have granted to the developing countries have carried only modest domestic political costs, largely because they have had little disruptive economic effect at home. The developed countries might feel thankful that the existence of highly protected markets in developing countries provides a convenient excuse for their protectionism against developing countries, even if it is not the reason for it.

Nevertheless, not all in developed countries are protectionist. Some incline to liberalism. Consequently, to the evident dissatisfaction of the governments of developing countries must be added the dissatisfaction of those in the developed countries who would like to see a more liberal international trading order. The question naturally arises whether it is not possible to do better.

II. Trade Policy and Theories of Development

The cornerstones of the Havana Charter of 1948 were the removal of quantitative restrictions, nondiscrimination, and reciprocal bargaining over tariffs. Representatives of the developing countries rejected these ideas, tabling some eight hundred amendments to the draft Charter, demanding, in effect, that they should be free of obligations which would limit their autonomy in trade policy.

They wished to protect infant industries with measures not otherwise permitted; they wished to be permitted to receive new tariff preferences from
other developed or developing countries; they wanted the right to benefit from
developed country tariff concessions without having to offer equivalent
tariff concessions of their own . . . About the only element of current
developing country policy . . . that did not appear at Havana was the call
for systematic tariff preferences by the developed countries . . . There were
demands that the ITO rules should permit the granting of such preferences,
but there was no demand for a legal obligation requiring developed coun-
tries to do so. [Emphasis in original; Hudec, forthcoming]

As Hudec has shown, it took a long time for the developed countries to grant
freedom of action formally, but de facto even those relatively few developing
countries that joined the GATT in its early days had that freedom from the
beginning (part I). Most of the already independent developing countries either
continued with or reinforced the protectionist policies of the 1930s and 1940s.
The principal colonial governments had also adopted protectionist policies on
behalf of their dependencies during the 1930s and World War II. Following
independence these countries generally went still further along the same path.
India, in particular, which was probably the most influential to the newly inde-
pendent countries, showed a strong and growing attachment to an inward-
oriented development strategy.

Self-fulfilling Prophecy of Foreign Exchange Scarcity

The thinking underlying this inward-oriented development strategy was that
import substituting industrialization would be required both to accelerate eco-
nomic development and to save scarce foreign exchange. There were, in other
words, both microeconomic and macroeconomic arguments for protection.

On the microeconomic level, rapid industrial growth was assumed to be the
defining characteristic and sine qua non of economic development. There was a
hope that protection would accelerate the development of infant industries by
internalizing the externalities presumed to be involved in industrialization. On
the macroeconomic level, it was widely believed, both by the governments of the
developing countries and by many distinguished academic commentators, not
only that commodity exports faced stagnant demand and falling relative prices,
but also that developing countries had little chance of competing successfully in
world markets for exports of manufactures.3 Given such export pessimism,
foreign exchange was presumed to be in permanently scarce supply. Import
substitution plus aid were then the only feasible ways of avoiding the foreign
exchange famine with which the developing countries were believed to be threat-
ened. In short, whether the argument began with “linkages,” “externalities,” or
“self-reliance,” the desirability of protection was the conclusion.

3. These ideas are discussed in Little (1982, chap. 4) and Riedel (forthcoming). Some of the classic
references include Nurkse (1953), Prebisch (1964), and Myrdal (1968). Prebisch’s book was the intellec-
tual starting point for the first United Nations Conference on Trade and Development, but it built on
already influential ideas that Prebisch had promoted in previous years. Similarly, Myrdal’s work synthe-
sized previous analyses of the obstacles to economic development.
Protectionist pressure in developing countries has been further increased by the tendency to expand budget deficits in the name of development finance. Aid donors can be criticized for encouraging development strategies that included the deliberate planning of resource gaps to be filled by aid. The outcome has been pressure on the balance of payments, and inflation. Currencies have tended to become overvalued and import controls have had to be introduced, increasing protection in a haphazard, even chaotic, manner.

A tragic element in this all-too-common history is that the idea of a foreign exchange shortage is generally self-fulfilling. Import restrictions usually start with supposedly nonessential consumer goods, but as they are tightened, the supply of imported basic intermediates and capital goods is also curtailed. As the level of protection increases so does the implicit taxation of exports, and export performance tends to deteriorate (see Clements and Sjaastad 1985). In most developing countries the result has been slower growth of output and, in some cases, a decline. Since the current account reflects the difference between national output and expenditures, declining output (absolute or in relation to trend) often offsets the effects of any policies to constrain expenditures and the balance of payments position worsens. It can become impossible to combine the desired rate of growth with a manageable balance of payments, however high the level of protection.

Few countries have managed successfully to reverse their direction once far down this protectionist road due mainly to the role of interest groups. On the whole, the protectionist trade policies of developing countries were not created by industrial interests, for those interests, like the industries themselves, did not exist. On the contrary, it was the protection that created the interests, but they have come to represent a powerful obstacle to liberalization. In the absence of international commitments (other than intermittent pressure from international lending agencies like the International Monetary Fund and the World Bank), those government elements wanting to liberalize have usually found themselves opposed both by other parts of government and by affected producer groups.

Preferences as Panacea

By the mid-1950s it was becoming obvious that trade liberalization among the developed countries was associated with an explosive growth of trade. At this stage, there were no miraculous examples of export growth of manufactures from developing countries, even Hong Kong's performance being barely noticeable, while the developing countries were losing market share in the exports of many primary commodities.

The international order did not appear to be satisfying the needs of developing countries. In 1957 in response to these concerns the GATT commissioned a report

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4. Little (1982 p. 53), remarks that "it was often the need to justify aid that produced plans"; see also Johnson (1967, p. 4). These plans were often, perhaps usually, overambitious, so that the one part of the economy over which government has some control, public expenditure, was the most likely to expand in line with these overambitious expectations, creating serious public finance problems.
entitled *Trends in International Trade*, which was drafted by a distinguished group of economists chaired by Gottfried Haberler. The report revealed the failure of the exports of developing countries to grow as rapidly as those of the developed countries and argued that an important reason was the obstacles in developed countries to imports of products in which the developing countries had a comparative advantage. General trade liberalization by the developed countries on products of interest to the developing countries was recommended. The report led to the Program of Action advanced by developing countries in 1963, but no general liberalization of obstacles to exports from developing countries was achieved, the principal (and disappointing) outcome being the GATT's Part IV on "Trade and Development."

The first United Nations Conference on Trade and Development (UNCTAD) took place in 1964. Its intellectual father was Raúl Prebisch (see Hudec, forthcoming, part I). Prebisch's analysis revealed that import substitution had proved to be insufficient on its own; there had to be more exports as well. But, as Harry Johnson noted:

The most important points of [Prebisch's] indictment [of import substitution industrialization] relevant to development through exports are the effects of import substitution in raising the cost of production above world market costs and the effects on competition and efficiency of protected production for a small market. Prebisch blames this situation on the unwillingness of the developed countries to open their markets to industrial producers in less developed countries, instead of on the maintenance of overvalued exchange rates by protectionist import-substitution policies. The solution he recommends is preferential entry, whose high costs would be borne by the consumers of the developed countries, instead of a combination of exchange rate adjustment and import liberalisation by the less developed countries. [1967, pp. 73-74]

Johnson also described Prebisch's recommendation as "the internationalisation of protectionism, or the inversion of protection in developed countries in favour of the less developed countries" (1967, p. 28).

Why did preferences become the principal positive demand of developing countries at UNCTAD (apart, that is, from commodity agreements)? The answer is not self-evident, for, as Johnson noted, the logic underlying Prebisch's recommendation is unclear. Perhaps the failure of the Action Program convinced developing countries that nondiscriminatory liberalization by the developed countries was politically infeasible. What is evident, however, is that the central case for preferences actually presented at UNCTAD derived from the infant-industry argu-

5. Other members of the Panel of Experts were Roberto de Oliveira Campos, director of the Brazilian National Bank; James Meade, professor at Cambridge University; and Jan Tinbergen, professor at the Netherlands Institute for Advanced Economic Studies, Rotterdam.

6. On the attempt to deal with the problems of developing countries, see Dam (1970, chap. 14) and Johnson (1967, especially chap. 1).
ment for protection (Johnson 1967, p. 181). Use of the infant industry argument to justify preferences implies that exports of manufactures from developing countries were deemed to be uncompetitive without a degree of special assistance. Nondiscriminatory liberalization by the developed countries could not provide infant industry assistance to the exports of manufactures from developing countries since those exports would then be subject to equal competition from all other suppliers.

Much of the pessimism about the capacity of the new industries of developing countries to compete on equal terms derived naturally from one of the most important consequences of inward-oriented trade regimes, namely, that highly protected import-competing industry looks highly uncompetitive, because the domestic prices of protected products are inevitably above (sometimes well above) those of imports. It must have appeared self-evident that such products could be exported only if they enjoyed a preferential advantage over products coming from competitors. Equal treatment of unequals then appeared to be not merely unfair in the abstract, but unworkable. Under that principle, the performance of developing countries, which virtually everybody agreed to be unsatisfactory, was unlikely to improve. In consequence, it was argued that developing countries needed positive discrimination in their favor if their infant exports of manufactures were to be encouraged.

By the early 1960s there was in place an apparatus of mutually reinforcing self-justification. Many developing countries pursued inward-oriented policies, the consequences of which were poor export performance and increasing scarcity of foreign exchange. The poor export performance could be blamed, with considerable plausibility, on the protectionism of developed countries, the reaction being insistence on improved market access. Furthermore, it was argued, infant industry assistance required preferential access, and so long as preferences were granted only grudgingly and protection of the most vulnerable industries of developed countries continued in force, it was always possible to blame external circumstances rather than internal policy for the continuing failure.

III. GATT Mercantilism and Developing Countries

There was a very good reason for the developing countries to think in the way they did: the developed countries appeared to as well. The GATT is based on the same protectionist ideas. The French nineteenth-century pamphleteer, Frédéric Bastiat, has put the point as follows:

But, they say, free trade must be reciprocal. If we lowered the barriers we have erected against the admission of Spanish goods, and if the Spaniards do not lower the barriers they have erected against the admission of ours, we should be victimised. Let us therefore make commercial treaties on the basis of exact reciprocity, let us make concessions in return for concessions, let us make the sacrifice of buying in order to obtain the advantage of selling.
People who reason in this way, I regret to say, are, whether they realise it or not, protectionists in principle; they are merely a little more inconsistent than the pure protectionists, just as the latter are more inconsistent than the advocates of total and absolute exclusion of all foreign products. [Bastiat 1964, pp. 67-68]

The principal idea in GATT negotiations is that the liberalization of imports is the price of improved access for exports. While some negotiators might say, when outside the negotiation, that liberalization is in the interests of the liberalizing country, such ideas are quickly dropped when the practical reality of trade negotiations arrives. Then the fear of going naked into the conference chamber ensures that there will be a plentiful supply of protection at home with which to bargain. All too often one hears the arguments that unilateral liberalization is like unilateral disarmament and that protection must be kept as a bargaining chip for the negotiations.

The fact that the GATT is presented as a mutual disarmament treaty for mercantilists has great importance for relations between the developed and the developing countries. It has made it effectively impossible for developed countries to insist on equal participation by the developing countries. What is more, it has made such unequal participation attractive to many in the developed countries.

The unequal role of developing countries in the GATT, indeed the very insistence that equal treatment of unequals is unfair, was a natural corollary of the ideas of the GATT itself. It took time and much rearguard action by the United States, in particular, before the inherent logic of the situation became reality, but by the end of the Kennedy Round the outcome was already quite predictable.

These ideas are still very much alive, as can be seen from the ministerial declaration at Punta del Este. The declaration insists that reciprocity shall not be required of developing countries and, in general, that they should not make "concessions inconsistent with [their] development, financial and trade needs." The declaration goes on to remark that "the capacity to make contributions or negotiated concessions . . . would improve with the progressive development of their economies and improvement in their trade situation." Liberalization is presented as a policy that only the relatively rich and successful can adopt.

What alternative to this way of incorporating the developing countries into the GATT could there have been? The alternative consistent with the nondiscrimination and liberalization principles of the GATT would have involved an absolute
commitment by the developed countries to nondiscriminatory treatment of developing countries, that is, to the most-favored-nation (MFN) rule, and a willingness on their part to negotiate a reduction in protection of particularly sensitive industries of importance to developing countries, such as agriculture, textiles, or clothing. These were the most important immediate export interests of the developing countries during the late 1950s and 1960s, when most of the exceptions regarding the place of developing countries in the trading system were agreed.

Strict adherence by the developed countries to MFN combined with liberalization of the most vulnerable industries was not a plausible alternative. The talk of "market disruption" by low-wage producers that led to the Short Term Arrangement Regarding International Trade in Cotton Textiles in 1961 (followed by the Long Term Arrangement in 1962), made it clear that the MFN rule would not be applied to such "sensitive" products (see Dam 1970, chap. 17). Similarly, the birth of the Common Agricultural Policy in the early 1960s, itself following the agricultural waiver granted to the United States in 1955, made it evident that liberalization of agriculture was not to be expected.

The importance of these developments in agriculture can be judged from the fact that both the terms of reference of the report of the panel of experts, Trends in International Trade, and the report itself focused almost entirely on primary commodities. The generally negative reaction of the developed countries to the Action Program confirmed their unwillingness to offer much liberalization to developing countries. In addition, the developing countries had, in any case, very little with which to bargain in the standard reciprocal framework. Accordingly, the alternative route of full and equal membership, to the extent that it was considered at all (which is unclear), would have been rightly judged to be quite unpromising by the developing countries.

For the developed countries, acquiescence in the demands for special treatment was less politically costly than the alternative of significant nondiscriminatory liberalization on products of interest to developing countries. Those advantages bear elucidation.

In the GATT framework the only effective way to bring liberalization is through reciprocal bargaining. In the nonreciprocal relationship between the developed and developing countries, therefore, there was little likelihood of any politically effective demand that the developed countries liberalize imports of the more sensitive products.

By conceding the right to protect to the developing countries, the developed countries assured themselves of what turned out to be a persuasive excuse for not granting liberal access to the exports of the developing countries. They could, indeed, complain about the injustice of the protectionism of more advanced developing countries.

By concentrating positive assistance to developing countries in preferences, developed countries were able to minimize the potential inconvenience to themselves, for preferences are not bound under GATT. Not being the result of reciprocal bargaining, they are regarded as ex gratia favors. Accordingly, developed
countries have constructed a protectionist system of preferences, removing them whenever the result might be uncomfortable for competing domestic interests.\(^8\)
The special position of developing countries has followed naturally from the economic ideas of both developed and developing countries, at least as they appear in the GATT. The combination has been both a compellingly logical and politically cheap way for the developed countries to accommodate the developing countries within the GATT system.

IV. Economic Developments

It is particularly ironic that a system of ideas was to be enshrined in the international trading order—in Part IV of the GATT, in the waiver for the GSP, and in the general grant of differential and more favorable treatment—just when economic development itself was to demonstrate the fallacies underlying it. Unlike the developed countries, in whose trade policies the reciprocal bargaining of the GATT has tended to bring about conformity, the developing countries have adopted a variety of trade policies and that very variety has given rise to one of the rare, relatively controlled, experiments in economic life.

Hong Kong was the first free trader, largely by necessity, followed by Singapore, Taiwan, and the Republic of Korea.\(^9\) These economies experienced what appeared to be almost miraculously rapid growth, both of exports of manufactures and of their economies. The supposedly crippling obstacles to export-oriented manufacturing turned out to be illusory.

None of these successes had much, if anything, to do with the special position of developing countries in the GATT. They had much more to do with the GATT's central achievement, the liberalization of the trade policies of the major developed countries. Preferences did not exist at first, and when they did they were of marginal significance, and either the governments of the more successful developing country exporters did not use the freedom to protect domestic markets or offset the adverse effects by means of export promotion. The result was that unilateral liberalism worked, at least in an environment in which the major developed countries continued, on the whole, to adhere to the generally liberal policies agreed in the framework of the GATT.

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8. The idea of preferences was much more acceptable to the European Economic Community than to the United States, for few member countries have been concerned about nondiscrimination, and a system of preferential trade with former colonies and Mediterranean countries was already being developed. There may also have been recognition of the value of preferences as an easy alternative to more liberal market access. The "Brasseur plan" for selective preferences, proposed by the Belgian representative to the GATT in 1963, seems to have been an important step on the way to generalized preferences. (See, on this, Dam 1970, p. 248 and, on the general attitude of the Europeans, Johnson 1967, p. 180.) In practice, the European Economic Community seems to have been concerned to avoid excessive erosion of the value of preferences accorded to associated states.

9. Southern Europe, Greece, Portugal, Spain, and Israel all liberalized to a considerable extent in the 1950s or 1960s, and all enjoyed relatively favorable performance. These are important cases, but their example was probably somewhat less influential than that of the four East Asian economies.
The significance of these developments began to become evident to economists in the late 1960s. By the 1970s a number of major research projects had recorded and explained what was happening. While a relatively small number of developing countries took the greatest advantage of the opportunity, many began to put more emphasis on exports and some were influenced to try some degree of unilateral liberalization. As a result of these developments and basic changes in the pattern of comparative advantage, developing countries experienced major changes in export structure during the 1960s and 1970s, the most important aspect being the rapid growth and increasing importance of exports of manufactures.

These developments have implications for the appropriateness of the institutional and conceptual legacy of the 1950s and 1960s. (1) The implicit assumption that developing countries would, in general, have little to gain from reciprocal bargaining has become less compelling, given the height of their own trade barriers and the diversity of their exports of manufactures. (2) The belief, expressed again in the ministerial declaration at Punta del Este, that liberalization can be afforded only by the more advanced is not merely wrong in theory but has been shown to be wrong in practice. (3) Relatedly, the view that developing countries can compete with developed countries only if they enjoy special favors has been demonstrated to be mistaken. (4) The major issue in the external environment for a large proportion of developing countries has clearly become security of access for exports that have the potential to displace production in developed countries and are therefore likely to create what the governments of developed countries would perceive as injury. In short, there is no obvious reason why the problems of developing countries should be regarded any differently from those of smaller developed countries.

V. DEMAND OF DEVELOPED COUNTRIES FOR GRADUATION

The alteration in the prevailing view of the link between trade and economic development has led a number of scholars to question the basis on which the developing countries had been incorporated into the GATT. At the same time, with the success of a number of developing countries, especially their success in world markets, attitudes among the governments of developed countries appear to have changed. These new ideas and attitudes provide the framework

10. It is impossible to provide a complete bibliography. The more important publications were Little, Scitovsky, and Scott (1970); Balassa, (1971); Donges (1976); Bhagwati (1978); and Krueger (1978). There is a particularly lucid recent discussion of the evidence on the issue of export promoting trade strategy in Bhagwati (forthcoming).

11. The implications of this development for economic relations between developed and developing countries is the principal theme of Riedel (forthcoming). In the author’s judgment, the “engine of growth” vision which lay behind much of the theorizing on trade and development in the 1950s has been entirely overtaken by events.
within which developing countries will have to take decisions, whether individually or collectively, about their role in the Uruguay Round.

Within the GATT's intellectual framework the demand of developed countries for graduation by the more successful of the developing countries is inevitable. As countries show themselves to be competitive and economically successful, developed countries conclude that they do not warrant preferential access and are no longer entitled to exemption from the obligations of membership. Such countries are seen as free riders on the willingness of others to bear the onerous burden of liberal trade policies (and these are politically, if not economically, burdensome). It is this notion that underlies clause (vi) of the Uruguay declaration, itself not a new one, which states that "less-developed contracting parties expect that their capacity to make contributions or negotiated concessions or take other mutually agreed actions... would improve with the progressive development of their economies and improvement in their trade situation."

The demand for graduation is not radical, since it retains the basic dividing line between developed and developing countries, but it indicates that a number of countries should move from below to above the line. Emphasis on graduation reinforces the belief that the right to protect is a benefit to be given up only by the more successful, and then only in return for a suitable consideration (see Hindley 1986).

Four questions arise regarding the demand for graduation. (1) Would any changes in the GATT and its codes be required for there to be graduation? (2) To what extent is agreement actually required to make the demand effective or can graduation be imposed unilaterally? (3) Do developed countries want the developing countries to graduate or is the demand rather an excuse for protection against them? (4) Can the developing countries use the demand for graduation for their own benefit? These questions are considered in turn.

Prima facie graduation can take place without any change in GATT rules. There can be a purely ad hoc accommodation. Graduation would require controversial changes only if it were to be made automatic, for this would require a definition of the term "developing country." There has never been agreement on such a definition, and it is not easy to believe that there could be agreement now.

Part of the demand for graduation can be (and is now being) imposed by developed countries, since they can make unilateral changes in eligibility for GSP treatment, if they wish. Developed countries can also try to be stricter in reviewing the developing country import restrictions that are justified by the need to manage the balance of payments. Nevertheless, within the framework of the GATT, which stipulates nondiscrimination, they can do little about the trade regimes of developing countries without their agreement. A substantial part of what developed countries appear to want is in the hands of developing countries so there is apparently room for negotiation.

Developed countries state firmly that graduation is necessary if developed countries are to maintain low barriers to exports from advanced developing countries, let alone to liberalize further. It is asserted that it is difficult to justify
low barriers to imports from successful developing countries that not only receive GSP treatment but also have both high tariffs and highly restrictive non-tariff barriers against imports. It is unclear, however, whether the demand for graduation is made by those inclined to keep trade barriers low or by those who hope that graduation will be refused, so justifying further protection. Even completely liberal economies like Hong Kong suffer from discriminatory protection against their exports. Accordingly, it is a matter of judgment whether the developed countries are offering anything in return for graduation or are merely proposing to graduate countries into a limbo of adverse discrimination.

So far as the last question is concerned—whether there is an opportunity here for developing countries—the only way of finding out is to bargain. There is no overwhelming prima facie case for taking the protestations of developed countries seriously. At the same time, the developed countries may be prepared to improve their policies or at least make a serious effort to hold the line against increased protection in return for fuller and more equal participation by the advanced developing countries. With that thought in mind, the discussion turns to the options and opportunities now facing developing countries.

VI. DIFFERENTIAL AND MORE FAVORABLE TREATMENT IN A NEW ROUND

Some observers conclude from experience with the demand for differential and more favorable treatment, that a far better alternative would be full and equal participation, especially for the newly industrializing countries. The right of developing countries to protect themselves freely is, they would argue, no more than the right to shoot themselves in the foot. The preferences that they have obtained are so surrounded by safeguards as to be of no more than modest value, and they are very unlikely to improve. Would it not be worthwhile to try the alternative tack of equal participation, now that experience has shown both that the economic problems of developing countries are really not so very different from those of the smaller developed countries and that the attempt to codify a special position has yielded but modest fruit?

The argument is popular among scholars and has been made by, among many others, the present author (1984). But, while from this perspective the ideas that underlie the demand for differential and more favorable treatment are wrong, so also are those underlying the GATT. It is not self-evident that the developing countries would benefit from changing (what these writers perceive to be) fallacies in midstream. I consider below the two benefits one might obtain out of fuller and more equal participation: improved market access abroad and more liberal and efficient policies at home. But first it is necessary to consider what fuller and more equal participation might mean and for whom.

**Defining Fuller and More Equal Participation**

Three elements can be envisaged in fuller and more equal participation. First, developing countries might participate, either individually or in groups, both in
tariff bargaining on a reciprocal basis and in bargaining on nontariff barriers (if there were to be direct reciprocal bargaining of these barriers). In the case of tariffs, any bargaining is likely to start with a generalized tariff-cutting formula, over which the developing countries are likely to have little influence. The participation of developing countries would, therefore, have to be mainly in the negotiation of exceptions. Developing countries would presumably attempt to negotiate away the peaks of their own tariffs for the relatively high protection in developed countries of industries of interest to developing countries, like textiles and clothing, that have been made exceptions to past tariff-cutting formulae. In the case of nontariff barriers, however, there is not yet any plan for a direct negotiation. In the past the GATT process has dealt with nontariff barriers either through bans or codes.

Second, developing countries might agree to apply GATT articles and codes more stringently on, for example, quantitative restrictions for balance of payments purposes, subsidies, and emergency protection. They would try, in other words, to abide by such discipline as is left in these various GATT articles and codes and would negotiate new codes, for example, on services and safeguards, with the expectation that they would apply equally to themselves.

Third, some developing countries might accept the withdrawal of GSP privileges in return for nondiscriminatory and liberal protection in areas of particular interest to themselves.

Changes in all these aspects could be made de jure, to apply to all developing countries, but in practice this is unlikely to happen. Many developing country contracting parties will certainly resist so radical a formal change in their place in the GATT. It is therefore best to envisage the options discussed below as applying to those developing countries that are particularly interested in improving their position through bargaining, many of whom are under strong pressure to graduate.

Improving Market Access

The first and most obvious question to be asked by developing countries considering fuller participation is what it would bring from their trading partners. Even if the main objective were improved policy at home, it would be difficult to sell these changes in policy if they had little impact abroad.

Unfortunately, while the understanding of the economic position of developing countries and their competitiveness in exports of manufactures, in particular, has greatly improved in the past quarter century or so, the capacity and willingness of developed countries to liberalize in relation to these exports has not. The chances that the developed countries would liberalize significantly in the interests of developing countries without reciprocity are negligible. But the chances that they would do so with reciprocity are probably little better.

Consider the situation of the principal developed countries. The United States is afflicted by strong protectionist pressures associated with a very large current account imbalance. Given the fact that the presidential veto of the highly protec-
tionist Jenkins bill on textiles was nearly overridden, the main objective for the Uruguay Round, so far as American policy is concerned, is probably to avoid increases in protection. The European Economic Community has high unemployment and needs to absorb countries of southern Europe that are direct competitors of many developing countries. The Community is also preoccupied with the liberalization of the internal market. Furthermore, the larger the number of cooks—now twelve—the more difficult it will be to prepare a meal containing anything other than a minimalist position on trade liberalization. In addition, the EEC may be adversely affected by the adjustment of the American balance of payments. Whether covertly protectionist or not, Japan's willingness to import, regardless of formal liberalization, is widely doubted. It may be noted that Japan has started to negotiate voluntary export restraint arrangements with some of its suppliers, particularly Korea and China in textiles.

It has to be doubted whether there is anything that developing countries can offer in standard bargaining that would induce these countries to liberalize significantly, even though taken together the developing countries accounted for 20 percent of world imports in 1985, more than the United States (GATT 1986, table A12). In general their markets are too small or uncertain, individually, while coordination of the offers and demands of many developing countries together would be difficult, because their interests are so diverse.

Willingness to enter into reciprocal bargaining with the developed countries may therefore have not much more than an atmospheric effect, though it might produce the important benefit of slowing the deterioration in the policies of developed countries. There may also be benefits for one another from liberalization of the markets of developing countries.

There could well be some important indirect effects of liberalization by developing countries on market access in developed countries, especially if that liberalization were combined with adherence to codes on subsidies and more limited use of quantitative restrictions for balance of payments purposes. High protection against imports is often offset by generous incentives for exports and, even where there are no such incentives, goods protected by quantitative restrictions on imports are often exported at prices below those in domestic markets. For both reasons exports from protected economies are extremely vulnerable to countervailing or antidumping duties imposed by developed country importers, especially the United States. It is noteworthy that exports from Hong Kong are so far unaffected, while harassment by fair trade law has become a major concern of exporters from Korea. For this reason there may be a valuable indirect effect on market access from reductions in import barriers at home (see Finger and Nogués, this volume).

What return might be derived from a willingness of newly industrializing countries to acquiesce in graduation from preferences? The answer, unfortunately, is "probably none." Preferences are, and are likely to remain, a useful diversionary tactic for the developed countries, but it is unlikely that abandoning this claim would encourage much liberalization by developed countries in sensi-
tive areas. At the same time, developing countries should recognize that if aid is to be a part of trade, the obvious countries to get it are those that appear to need assistance to compete in world markets, among whom Brazil and Korea cannot be numbered. What would be desirable would be for developing countries to exchange a precise and relatively narrow definition of the appropriate beneficiaries (along with rules for graduation) for a commitment by developed countries to make preferences available to beneficiaries without restriction. Such changes might bring no benefit to the more advanced newly industrializing countries, but would presumably ensure that the one positive benefit the developing countries have obtained would in fact be of use to those most in need of assistance.

Improving Domestic Policy

While not often made explicit, a principal reason for participation in GATT negotiations is not just to obtain improved access abroad but to make it politically easier to liberalize at home. Large countries cannot only secure greater market access abroad but can also use it effectively to secure liberalization at home. For them, reciprocity is twice blessed. Small countries, however, can hardly argue convincingly that liberalization at home is the price of improved market access abroad because their influence on policies abroad is transparently negligible. Rightly, Hong Kong and Singapore did not retain barriers to imports in the hope that they could be bargained away for more favorable access. The GATT does not care for the very small.

One recalls the warning example of Australia, whose tariffs on manufactures remain high and largely unbound in part because it has waited for reciprocal liberalization of barriers to its agricultural exports. There is the very real danger for small countries that the emphasis on reciprocity will not only misinform their public on the true gains from liberalization but also will fail to bring the expected benefits. For them, in other words, reciprocity may be twice cursed.

Reciprocity works best from the point of view of domestic liberalization when the other side is prepared to play the game. But for reasons already discussed, it is questionable whether the developed countries are so prepared. Nevertheless, perhaps a few large developing countries could make something of reciprocal bargaining with developed countries, individually, or, alternatively, through coordination of offers. It would be misleading, however, to oversell these possibilities. In some large countries where strong nationalistic sentiment exists, the fact that liberalization is a result of a bargain with developed countries may actually make it less politically acceptable. In these circumstances, it is likely that liberalization will be attacked as having been conceded under the duress of inimical foreign powers. In such circumstances, reciprocal bargaining would appear to have little, if anything, in its favor.12

At the same time, international agreements, especially commitments to other

12. The point is owed to Cable.
governments, have sometimes helped small countries to liberalize. Experience suggests that governments help one another by making their commitments to liberalize more credible. The pressure of international organizations is often too intermittent, while purely internal commitments to liberalize, on the whole, lack credibility. The cases of the agreements of Greece, Israel, Portugal, and Spain with the EEC all suggest the importance of international commitments in shielding the process of trade liberalization from day-to-day political pressures. With a credible international agreement, trade policy becomes a fixed point, to be changed only at great cost, not a weather vane to be moved with the slightest protectionist wind. An open question is whether an enfeebled GATT can serve the purpose of providing such a credible commitment.

At least the larger and more significant trading countries, if convinced of the value of liberalization for themselves, might be able to construct an international agreement in the Uruguay Round that supports their liberalization efforts at home. It would be difficult to judge what might be obtained abroad against what would be politically persuasive at home. Countries must, however, avoid the danger of convincing interests at home that liberalization is only acceptable if reciprocated and then finding that nobody wants to reciprocate. It would be worse than futile to postpone liberalization in the hope of a liberalization abroad that then never comes.

Large and Small, Richer and Poorer Developing Countries

Such limited possibilities as exist of fruitful and active engagement in the GATT process appear to be restricted to the larger and more advanced developing countries, perhaps fifteen or so countries in all. This list would include the newly industrializing countries and such giants as China and India. What of the rest? There is little they can achieve directly, though they could achieve something indirectly. Graduation of others is in the interests of those not being asked to graduate, since it would both exclude the most competitive present beneficiaries from the GSP and open up some of the world’s most dynamic markets to imports. It is puzzling, therefore, that most developing countries have not welcomed the idea with enthusiasm. Beyond this, the smaller and poorer countries are likely to be affected most significantly by whatever is agreed in the area of agricultural trade, some benefiting from liberalization and others presumably being harmed. Their capacity to influence the outcome in that crucial area, however, must be very small.

VII. Equal or Differential Treatment?

At least some developing countries have a choice, and it is not an easy one to make. Differential and more favorable treatment has little economic logic under-

13. This is one of the conclusions the author has drawn from participation on the external panel of the World Bank comparative studies research project on timing and sequencing of a trade liberalization policy (see Wolf 1986).
lying it and is also unlikely in practice to bring the developing countries major improvements in market access abroad. Unfortunately, the same may well prove true of fuller participation in the GATT itself. Even a willingness to abandon preferences is unlikely to gain much return from the developed countries in their present mood.

The most important reason for participating in international negotiations on trade is that in certain circumstances they can help to discipline domestic political processes. Developing countries have found themselves at least as vulnerable to protectionist lobbying as the developed, so that the relative freedom from external constraints on their policies has borne bitter fruit in the chaotic and costly trade regimes of so many countries.

With imagination and cunning a government that wants to liberalize and recognizes the significance of the domestic pressures against it may be able to use the forthcoming GATT negotiations for its own ends. In so doing it must aim for improvements in access to markets abroad that are feasible objectives for the negotiation and are also judged to be worthwhile gains by their citizens at home. The search for such bargains is the most obvious task of the governments of at least the more advanced developing countries.

At the same time, a situation worse than failure to obtain improved market access is threatened. There is a chance that, succumbing to the GATT’s own mercantilism, governments of major developed countries will react to a refusal of the more successful developing countries to participate more fully and equally in the GATT process by increasing their level of protection. There is certainly considerable resentment expressed in many developed countries against “free riders”—not all of which are developing countries. The developing countries that are most dependent on the open international trading system may well consider their own interest in securing the vitality of the principles that underlie it.

Nevertheless, the real challenge is now to the developed countries, who have lived very comfortably with the outsider status of the developing countries. The developed countries are likely in practice to find an effort by successful developing countries to achieve a truly equal status very unwelcome, preferring their present grounds for complaint to any remedy.

If any developing countries decide to challenge this position, they must retain the by-now widespread understanding in developing countries that liberalization is not just a favor to others. If they can promote ordered, liberal relations among countries, without succumbing entirely to the mercantilist ideology in which those values are packaged, they may be able both to contribute to and gain from the next act in the drama of the GATT. It is, on balance, worth supping with the mercantilist devil; but one should sup with a long spoon.
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