UNITED NATIONS

TD

United Nations Conference on Trade and Development

Distr.
GENERAL

TD/B/50/5
7 August 2003

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Fiftieth session
Geneva, 6–17 October 2003
Item 3(b) of the provisional agenda

MAIN RECENT INITIATIVES IN FAVOUR OF LEAST DEVELOPED COUNTRIES IN THE AREA OF PREFERENTIAL MARKET ACCESS: PRELIMINARY IMPACT ASSESSMENT

Note by the UNCTAD secretariat

Executive Summary

This note has been prepared to facilitate the debate at the fiftieth regular session of the Trade and Development Board on the benefits effectively derived from least developed country status. It responds to the request, by the Board at its forty-ninth session, that the secretariat "in the context of its analysis of the benefits effectively derived from LDC status … [should] pay particular attention, on an ongoing basis, to the expected impact of the most recent initiatives in favour of LDCs in the area of preferential market access, *inter alia* the "Everything But Arms" initiative, the African Growth and Opportunity Act (AGOA) and other such initiatives".

The note briefly reviews the recent preferential market access initiatives in favour of LDCs by the main trading partners of these countries, namely the Quad countries (Canada, the European Union, Japan and the United States). It shows that the utilization of market access preferences by LDCs has been relatively low, and highlights the benefits that could be drawn from enhanced preferences on these markets, in trade flows and, ultimately, in terms of investment, employment creation and income. The note discusses some of the main obstacles that should be overcome or removed if the use or effectiveness of market access preferences is to be enhanced. These obstacles relate to the relative unpredictability of market access preferences, the rules of origin and non-tariff barriers to trade, the persistence of agricultural subsidies in developed countries, and weaknesses in the supply capacities of most LDCs. Given the temporary nature of market access preferences, maximum use should be made of them while they are still available. As these preferences erode, other means of special and differential treatment ought to be considered in the interest of LDCs.

GE.03-52070

CONTENTS

Pages

I. Introduction

1. Since 1971, the United Nations has designated as “least developed countries” (LDCs) those States that have been regarded as structurally disadvantaged in their development process, and in need of the highest degree of consideration from the international community in support of their development efforts. In response to the socio-economic weaknesses of LDCs, the United Nations gives a strong signal to the main development partners of these countries by periodically identifying them and highlighting their structural problems, thereby pointing to the need for special concessions in their favour, essentially in the areas of trade, development financing and technical assistance.

2. UNCTAD II, in 1968, had recommended the establishment of a Generalized System of Preferences (GSP) and “special measures … in favour of the least developed among developing countries, aimed at expanding their trade and improving their economic and social development”. Since the introduction of GSP schemes and approval by the General Assembly of the first list of LDCs in 1971, the need for a particularly favourable treatment of LDCs through the GSP has been reiterated by numerous international resolutions as a cornerstone of the general architecture of special and differential treatment for those countries.[1] The 1996 Singapore Ministerial Declaration enhanced the scope for such treatment within the World Trade Organization (WTO), by launching a plan of action in favour of LDCs, including provisions for positive measures such as duty-free access on an autonomous basis. Since then, a number of new initiatives have been taken by developed and developing countries that are trading partners of LDCs, with a view to offering more favourable market access conditions to these countries. These initiatives have prompted UNCTAD to examine their expected impact.[2]

3. In 2002, the Trade and Development Board, at its forty-ninth session, endorsed “the secretariat’s efforts to pursue its research and analytical work on the benefits effectively derived from the least developed country status with a view to identifying approaches to make this status a more effective tool for socio-economic transformation and convergence with other developing countries” and requested the secretariat “in the context of its analysis of the benefits effectively derived from LDC status, to pay particular attention, on an ongoing basis, to the expected impact of the most recent initiatives in favour of LDCs in the area of preferential market access, *inter alia* the ‘Everything But Arms’ initiative, the African Growth and Opportunity Act (AGOA) and other such initiatives”.

4. This note has been prepared in response to the above request, and concentrates on the special treatment of LDCs in the context of the most recent market access initiatives of Quad countries.[3] It offers an overview of the recent market access initiatives of Quad countries (section II), before discussing some of the difficulties one finds in assessing the benefits effectively derived or expected from preferential market access (section III). It then briefly examines the utilization of relevant preferences by LDCs (section IV), and the conditions for making this utilization beneficial, considering the specificities of the market access initiatives themselves, the problems associated with rules of origin and non-tariff barriers to trade, the

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[1] See UNCTAD (1985).
[2] See, in particular, UNCTAD (2001a); UNCTAD and the Commonwealth Secretariat (2001); UNCTAD (2002a).
[3] The Quad countries are Canada, the European Union, Japan and the United States.

persistence of agricultural subsidies in developed countries, and the constraints faced by LDCs in their supply capacities (section V). Concluding remarks summarize the main relevant policy challenges (section VI).

II. Overview of Quad market access preferences

5. In recent years, several developed and developing countries have reviewed their schemes of market access preferences for developing countries, and decided to improve the preferences granted to LDCs. These intentions have been notified to the WTO. By 2001, the WTO had announced that 27 countries had improved market access preferences for LDCs. These preference-giving countries included the Quad countries, which are the largest export destinations for LDCs.[4]

A. The preferential scheme of Canada

6. In September 2000, the Canadian Government widened the product coverage of its GSP scheme for the benefit of LDCs. Since January 2003, it has expanded its market access preferences for those countries even further. The new scheme improves market access for textiles and clothing, but continues to exclude sensitive products such as dairy products, eggs and poultry. With these exceptions, Canada now provides duty-free access under all tariff items for imports from LDCs. The initiative also changed the rules of origin. It introduced an innovative cumulative system that allows inputs from all beneficiary countries.

B. The preferential scheme of the European Union

7. The European Union had originally granted two sets of market access preferences to LDCs. It provided relatively far-reaching market access preferences to African, Caribbean and Pacific (ACP) countries, and lesser market access to other developing countries, including LDCs among them. Market access for ACP countries was regulated by the Lomé Conventions. It is now regulated through the Cotonou Agreement, while market access for all other developing countries is provided under the GSP. The existence of this dual market access scheme meant that ACP LDCs benefited from better market access conditions than non-ACP LDCs.

8. In 2001, the European Union, through the "Everything But Arms" (EBA) initiative, consolidated and improved market access preferences for all LDCs. The EBA grants duty-free and quota-free market access for all types of exports from LDCs, with the permanent exception of arms and ammunition, and temporary exceptions for bananas, rice and sugar. Market access restrictions for the latter goods are to be phased out between 2006 (bananas) and 2009 (rice and sugar).[5] As a result of the EBA initiative, non-ACP LDCs[6] are now enjoying greater access to the European single market than ACP non-LDCs. It must be noted,

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[4] See WTO (2001). The description of market access preferences of Quad countries is based on UNCTAD (2003, forthcoming).

[5] Cernat, Laird and Turrini (2002) point to "the significance of improved access for LDCs to the EU sugar market as the single most important source of change. This derives in the first instance from the substantial price wedge that exists between EU domestic and world prices in this sector".

[6] The non-ACP LDCs are Afghanistan, Bangladesh, Bhutan, Cambodia, the Lao People's Democratic Republic, Maldives, Myanmar (which is currently being excluded from market access preferences), Nepal and Yemen.

however, that only about half of the non-ACP LDCs have so far utilized preferential market access to the European Union, primarily because of the rules of origin[7].

C. The preferential scheme of Japan

9. The GSP scheme of Japan was recently reviewed, and extended for a new decade (until March 2014). During the 2001/2002 fiscal year, the special treatment granted to LDCs was improved by the addition of a number of tariff lines involving duty-free and quota-free treatment. Zambia, the Democratic Republic of the Congo,[8] Kiribati and Tuvalu were added to the list of beneficiaries. The Comoros and Djibouti are also eligible for this treatment under the Japanese scheme if they request it. Senegal was added to the Japanese list of LDC beneficiaries after it was added to the United Nations list of LDCs in 2001.

10. In short, all LDCs, under the Japanese scheme, are eligible for duty-free entry and exemption from ceiling restrictions for a list of relevant products. In early 2003, Japan further improved its GSP scheme for the benefit of LDCs. After many industrial goods had already benefited from far-reaching market access preferences under the previous scheme, the new scheme improves market access preferences by granting duty-free treatment for a number of additional agricultural goods and fish products (such as frozen fish fillets), as well as prawns.

D. The preferential scheme of the United States

11. In contrast to other Quad countries, which offer a single set of market access preferences to LDCs, the United States *de facto* provides two sets of market access preferences to these countries, one to non-African LDCs and the other to LDCs within sub-Saharan Africa. The former is provided through the GSP scheme, which expired in September 2001 and was re-authorized until December 2006. The set of preferences relevant to African LDCs is provided through the African Growth and Opportunity Act (AGOA), which was improved in 2002 and extended until September 2008.[9]

12. The GSP scheme of the United States excludes sensitive products such as textiles, work gloves, footwear, handbags, luggage and watches, while AGOA provides preferential market access for many sensitive goods, including electronic articles, steel articles, footwear, handbags, luggage, flat goods, work gloves, leather wearing apparel, and semi-manufactured and manufactured glass products. The enhancement of AGOA, in 2002, was mainly relevant to textiles and apparel. Knit-to-shape products were included, the technical definition for merino wool was revised, the origin of yarn under the Special Rule for designated LDCs was clarified, and “hybrid” apparel articles were made eligible for preferences.

13. Another important difference between the GSP scheme and the AGOA scheme is that while the list of products that are eligible for GSP preferences is reviewed annually, it was decided that the list of products that are eligible for AGOA treatment will not be reviewed with the same frequency. The decrease in the frequency of reviews implies increased stability

[7] See UNCTAD (2001a).

[8] With regard to refined copper imported from the Democratic Republic of the Congo and Zambia, the normal GSP tariff rate involving a 40 per cent tariff cut from most-favoured-nation levels is applied, and the ceiling will not be removed until the end of the 2005 fiscal year.

[9] All developing countries of sub-Saharan Africa, including LDCs and non-LDCs, are in principle eligible for market access preferences under the AGOA. Developing countries of all other regions, be they LDCs or non-LDCs, are in principle eligible for market access preferences under the regular GSP scheme.

and predictability in market access preferences. The differences between the two schemes imply that African LDCs enjoy more favourable access to the United States market than non-African LDCs, and that the latter face lesser market access stability than African LDCs. For these reasons, AGOA is referred to as a “super GSP” scheme.

III. Assessing benefits from market access preferences

14. The existence of market access preferences for LDCs raises the question of the link between the special treatment offered to those countries and the benefits they have effectively derived, or will derive, from this treatment. Market access preferences are not always conducive to effective benefits for recipient countries, particularly when the latter are severely disadvantaged countries facing serious supply constraints. Market access preferences may induce little effective benefits if they do not involve sufficient product coverage or sufficient preferential depth (in the context of preference erosion), or if they have not been effectively utilized, or because their effective utilization has not generated a durable socio-economic impact. One generally considers that market access preferences generate effective benefits when structural (durable and sustainable) socio-economic progress has taken place as a result of the treatment granted. Such progress usually implies that investment in the relevant economic sectors has been encouraged, and has translated into job and income creation while strengthening innovative and productive capacities.

15. Meaningful assessment of the effective benefits derived from market access preferences essentially implies country-specific examination, in each LDC, of the causal link between the preferences and their impact on investment and trade flows, and on the related socio-economic performance (job creation, foreign exchange earnings, income, etc.). The UNCTAD secretariat is pursuing this exercise in the context of its ongoing analysis of effective benefits from LDC status. This note is not based on the outcome of that exercise, the results of which are not expected to be available until 2004, when sufficient data have been collected at country level in the wake of recent initiatives. Nevertheless, preliminary quantitative observations on the extent of product coverage and effective utilization of the market access preferences granted through these initiatives can already be made. While this preliminary assessment constitutes a modest approach to the complex question of the effective or potential socio-economic benefits expected from trade preferences, policy considerations of relevance to the aim of enhancing the beneficial impact of preferences will be examined in section V.

16. LDCs faced relatively high tariff barriers, in comparison with other developing countries, prior to the recent market access initiatives. In 1999, for example, tariff peaks on Quad markets affected 11.4 per cent of total imports from LDCs, but only 5.2 per cent of total imports from other GSP beneficiary countries. None of the Quad market countries has by now dismantled duties and quotas on all products from LDCs[10]. However, the latter often have a competitive advantage in the production of goods, and in some cases, have managed to move up the value-added chain. Further removal of trade restrictions could generate benefits for LDCs with competitive manufacturing capacities, especially in the area of textiles and apparel. Although most of these LDCs are in Asia, there are notable exceptions on the African continent, specifically in Lesotho and Madagascar, which are currently among countries benefiting most from AGOA.

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[10] Canada maintains restrictions on dairy products, eggs and poultry; the European Union on bananas, rice and sugar; Japan on selected agricultural goods; and the United States on textiles and apparel.

17. The examples of Lesotho and Madagascar show that market access preferences not only can enhance trade competitiveness within existing productive capacities, but also may trigger new investment responses. Both countries have benefited from substantial investment in the textile sector, originally as a result of special arrangements in favour of LDCs (allowing the use of imported fabrics to make finished garments), and more recently in the context of AGOA. This has had a significant impact on employment, with the creation of some 25,000 jobs in Lesotho, and about 5,100 in Madagascar. According to UNCTAD's Investment Policy Review of Lesotho (2003), foreign direct investment flows into export-oriented manufacturing accounted for a very large share (approximately 90 per cent) of total recent investment in that country. As a result, Lesotho is now a major exporter of textile products and apparel to the United States, and the largest supplier of apparel in sub-Saharan Africa.

18. For LDCs to be able to derive consistent benefits from trade preferences, the supply capacities of these countries should be not only enhanced or strengthened, but also kept stable over time. The reality of supply capacities among LDCs is often dominated by instability factors, either as a result of external shocks beyond domestic control (natural disasters, economic shocks) or because of domestically generated disturbances that have a negative impact on productive capacities. Recent calculations of the Economic Vulnerability Index used in the triennial review of the list of LDCs by the Committee for Development Policy have revealed that LDCs, over the 1979-2001 period, had 9.5 per cent more instability in their agricultural production, and 49 per cent more instability in their exports of goods and services, than other developing countries.[11] The latter estimate reflects the considerable impact of external shocks (cyclones, drought, commodity prices fluctuations, shortfalls in the international demand for goods or services, etc.) on the foreign exchange earnings of LDCs and, therefore, on their general socio-economic performance. This underscores the importance of analyzing the beneficial impact of market access preferences in the light of the physical and economic factors beyond domestic control that affect, and are specific to, every individual LDC. As section V will point out, while little can be done against adverse external factors as they affect LDC exports, a range of international and domestic action remains possible –and highly desirable— in a number of policy-related areas where contributions can be made in order to bring effective benefits from trade preferences to fruition.

IV. Utilization of market access preferences

19. In theory, market access preferences provide LDC exporters with a competitive advantage. In practice, LDCs are often unable to realize this advantage. This has been illustrated by the low degree of utilization of market access schemes in favour of those countries. The table annexed to this note summarizes the utilization of Quad market access preferences by LDCs over the 1994-2001 period, through three main indicators: the product coverage ratio[12], the utilization ratio[13], and the utility ratio[14]. The table shows an increase in

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[11] It was also found that African LDCs, over the same period, recorded 25 per cent more instability than all other LDCs in their agricultural production.

[12] The *product coverage ratio* is defined as the ratio of imports covered by preferential trade arrangements to total dutiable imports from beneficiary countries. The higher the product coverage ratio, the more generous preferences appear to be, depending on the structure of dutiable imports from beneficiary countries. Coverage does not automatically mean that preferences are granted at the time of customs clearance.

[13] The *utilization ratio* is defined as the ratio of imports actually receiving preferential treatment to imports covered by preferential arrangements, based on the customs declaration made by the importer at the time of importation. Higher or lower utilization ratios are mainly the result of the stringency and/or complexity of rules of origin and ancillary requirements. In some cases, exporters may have failed to submit the necessary

the utilization of Quad market access preferences by LDCs. The utilization ratio, which was 48.2 per cent in 1994, had risen (though not steadily) to 68.5 per cent by 2001. This increase was mainly explained by a sudden rise in the utilization ratio relevant to the United States market, from 74.0 per cent in 1994 to 95.8 per cent in 2001.

20. In **Canada**, 70.2 per cent of covered imports from LDCs were actually receiving preferences in 2001. This utilization ratio improved over the years, from 46 per cent in 1996. Canadian imports from LDCs that effectively received preferential treatment accounted for 8.5 per cent of total dutiable imports from LDCs in 2001.

21. In the **European Union**, as pointed out earlier, the GSP scheme grants LDC exporters a wide preferential coverage. However, an examination of the utilization of these preferences by LDCs provides a different perspective. Imports from LDCs actually receiving tariff preferences ($1.8 billion in 2001) account for less than 50 per cent of total dutiable imports from LDCs (46.7 per cent utility ratio). Thus, although the potential preferential coverage of LDC exports to the European Union has been close to 100 per cent, more than half of total LDC exports to the European single market were actually facing MFN duties rather than enjoying preferential treatment in 2001.

22. Low utilization of the GSP scheme of the European Union by LDCs has been a constant feature of LDC-EU trade in recent years. The utilization ratio was 41.8 per cent in 1994, and rose to 47.5 per cent in 1996, before falling to 26.7 per cent in 1997, largely as a result of the low utilization of GSP preferences for important products such as textiles (21 per cent utilization ratio) and food preparations (12 per cent). Low utilization levels were also recorded in 1998 and 1999 (26.2 per cent and 33.7 per cent, respectively). Despite an increase to 46.9 per cent in 2001, preferences under the scheme of the European Union are still far from being fully utilized.

23. **Japan** is the only Quad market that experienced a decrease in the utilization ratio in the long run, from 94.9 per cent in 1994 to 82.1 per cent in 2001, with an exceptionally low ratio (38.4 per cent) in 2000. The significant improvement in the utilization ratio in 2001 (in comparison with 2000) resulted from a substantial increase in product coverage in 2000. LDC exports effectively taking advantage of preferences on the Japanese market accounted for 57.4 per cent of total dutiable imports in 2001. This relatively high utility ratio may still increase as a result of the changes introduced in market access preferences in 2003.

24. Utilization ratios appear to vary considerably among products. In particular, high ratios (almost 100 per cent) have been recorded for fish products, hides and skins, and footwear products. Conversely, lower than average ratios have been recorded for metals and textile products. The low utilization of preferences for textile and clothing products has been explained by difficulties in complying with origin requirements under the scheme. The LDC that has benefited most from the Japanese scheme is Myanmar (prawns).

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documentation (such as a certificate of origin or bill of lading) for receiving preferential treatment, owing to a lack of knowledge or incorrect information.

[14] The *utility ratio* (which could alternatively be called the *beneficiary ratio*) is the ratio of imports actually receiving preference to all dutiable imports, covered or not. A low level of the utility ratio means that a large part of dutiable imports (covered or not) face the MFN rate.

25. In 2001, the **United States** had the highest utilization ratio among Quad countries (95.8 per cent). The ratio increased significantly after 1997, a year in which it was as low as 29.1 per cent. This progress was largely driven by an increase in mineral imports, particularly oil imports. Without oil imports, the utilization ratio would have dropped to 47 per cent in 2001.

26. The product coverage ratio was only 44.1 per cent in 2001. This relatively low coverage has been reflecting the highly concentrated structure of LDC-US trade, in which petroleum and textile products account for about 90 per cent of total imports from LDCs, with textiles and apparel alone representing nearly 50 per cent of imports from LDCs (49.5 per cent in 2001). With a product coverage ratio for textiles and apparel near to zero (0.5 per cent), the overall coverage ratio (44.1 per cent) is considerably lower than it would have been if textile products were among preferential imports from LDCs. This indicates that there is scope for improving market access preferences by expanding product coverage on the United States market, essentially in the textile and clothing area, which is excluded from GSP preferences for LDCs.[15]

V. Enhancing benefits from market access preferences

27. Despite improvements, since 1998, in the aggregate utilization of market access preferences on Quad markets, effective utilization by LDCs has remained well below its potential. The inability of LDCs to make better use of the market access concessions granted to them is explained by a variety of factors. Some of these relate to the specificities of domestic economies, others to exogenous influences. The *Least Developed Countries Report 2002* noted that “the reasons for low and uneven levels of utilization of trade preferences include: the lack of security of market access, rules of origin, and lack of technical knowledge, human resources and institutional capacity”. Five important sets of factors influencing the ability of LDCs to make use of market access preferences are: (a) the specificities of the schemes themselves; (b) the rules of origin associated with the eligibility for preferences; (c) the difficulties stemming from non-tariff barriers; (d) the impact of policies, such as some of the agricultural policies of developed countries, that directly affect production and exports of interest to LDCs; and (e) the supply capacities of these countries. This section will focus on those factors with a view to highlighting possibilities for enhancing benefits from preferential market access initiatives.

A. Unpredictability of market access preferences

28. The utilization of market access preferences is negatively affected by uncertainties: (a) about the coverage of products in the relevant schemes; (b) about the length and durability of market access; and (c) with regard to non-trade-related criteria, which are a common feature of some of the market access initiatives. Uncertainties regarding product coverage and non-trade-related criteria are generally exacerbated by built-in reviews.

29. Investors in preference-receiving countries may be hesitant to step up their investment in these countries if preference-giving countries do not make clear commitments with respect to the period for which the market access schemes will remain effective, and/or the products covered by the preferences. While all Quad countries have made general commitments on the

[15] LDC exporters of these products still face, on average, a trade-weighted tariff of 15.5 per cent. The LDC that is most affected by the exclusion of textiles and clothing from the GSP of the United States is Bangladesh. Other countries that are partially affected are Nepal and Yemen.

countries and products that are covered by relevant initiatives, they also maintain the option of reviewing the lists of countries and products that can benefit from the initiatives, or introducing ad hoc safeguards. The list of products is generally reviewed on the basis of the economic sensitivity of relevant goods, and the list of eligible countries is determined in accordance with non-trade-related concerns.

30. The product coverage now granted to LDCs by the European Union as a result of the EBA initiative, though not binding, is established for an unlimited period of time.

31. In order to increase the stability and predictability of AGOA, the United States decided not to conduct annual reviews of the goods that are eligible under the Act, while it continues to conduct annual reviews of the eligible goods under its GSP scheme. In principle, AGOA targets 48 countries of sub-Saharan Africa (including 34 LDCs). However, after the country review for 2003 eligibility, only 38 countries (including 25 LDCs) were found eligible for tariff preferences.[16]

32. Whatever the merits of individual market access initiatives may be, firm and unrestricted commitments by preference-giving countries are considered essential for enabling LDCs to make use of the preferences and derive effective benefits through expansion of exports. This consideration points to the suggestion that market access preferences, which have been determined on a unilateral basis, could be brought under multilateral rules in the context of a reform of special and differential treatment in the WTO[17].

B. Rules of origin

33. Rules of origin are rightly regarded as a predominant cause of the under-utilization of trade preferences. As preferences are granted unilaterally and non-contractually, preference-giving countries have consistently expressed the view that they ought to be free to decide on the rules of origin, although they have indicated their willingness to hear the views of beneficiary countries. Preference-giving countries tend to feel that the process of harmonization of rules of origin can be limited to a number of practical aspects, such as certification, control, verification, sanctions and mutual cooperation. Even on these aspects, however, progress has been limited, as basic requirements and the rationale for rules of origin remained almost unchanged for nearly 30 years.

34. Among requirements often cited as causing implementation difficulties among preference-receiving countries is the obligation to devise and operate an accounting system that is conceptually and operationally different from national legal requirements, and often beyond the capacity and resources of local enterprises[18].

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[16] The United States, under non-trade-related criteria, can regularly change the coverage of AGOA with respect to countries. Angola, Burkina Faso, Burundi, Equatorial Guinea, Liberia, Togo (LDCs) and Zimbabwe (non-LDC) were found not eligible under the country review for 2003.
[17] This suggestion has been developed and elaborated on by UNCTAD as a possible WTO-consistent instrument (UNCTAD, 2001a).
[18] In the textile industry, the concomitance of a peak in imports of fabrics and the low rate of utilization of preferences indicate that manufacturers in the relevant country have forgone tariff preferences because they cannot comply with rules of origin. This has been observed in Bangladesh and Cambodia, which have consistently imported fabrics rather than yarn. Their manufacturing industries are greatly dependent on the sourcing of fabrics from external suppliers, a factor of competitiveness that is generally more important than the use of market access preferences.

35. Doubts have also been cast on whether calculations of the domestic content of exportable goods are accurate and valid. In this connection, it has been noted that the cost of labour and materials may often fluctuate, leading to different levels of domestic content, and consequently, to eligibility or non-eligibility for preferential treatment, although the extent of transformation carried out in the preference-receiving country remains unchanged. By contrast, it has been argued that the "import content" is more easily defined, as determining its exact value leaves less room for doubtful or incorrect interpretation. Although there remains a possibility that the finished product will earn or lose its entitlement for preferential treatment as the value of imported materials fluctuates, this possibility is more limited than under the "domestic content" methodology, considering the variability of local costs.

36. There is a tendency, among exporters, to advocate the idea of a maximum imported input allowance as opposed to a minimum local-value-added requirement. There are two reasons for this preference: (a) calculation of the value of imported inputs is easier, as it can be supported by suppliers' invoices (on this aspect, the GSP scheme of the European Union provides clear rules); and (b) calculation of the value added is complex, since it implies appropriate differentiation of costs (overestimating certain costs will entail underestimating the local value added), and evaluation of unit costs based on units of production. Accordingly, the principle of minimum local value added requires accounting, as discretion may be used in assessing unit costs.

C. Product standards

37. Overcoming non-tariff barriers to trade and complying with product standards —be they technical barriers to trade or sanitary or phytosanitary measures— is a formidable challenge for many LDCs, and often a greater market access problem than tariff barriers. The inability to adhere to strict health or environment-related measures (e.g. eco-labelling, packaging requirements, pesticides residue levels) not only may cause a loss of shares in the targeted markets but also, may damage prospects for penetrating other markets. Benefits from market access preferences may therefore, for LDCs, be seriously impaired by non-tariff barriers to trade.

38. Most LDCs face serious capacity constraints in complying with stringent technical standards such as sanitary or phytosanitary measures and environmental requirements. These constraints generally include a lack of infrastructure, such as internationally accredited and recognized laboratories with advanced testing equipment, a poor legislative capacity, limited skills and training capacities, and a lack of engagement in international standard-setting processes, because of the smallness of local scientific communities and government resources. This adds to the unpredictability of market access preferences and tends to dampen the attractiveness of LDCs from the viewpoint of potential foreign direct investors. Capacity-building measures to strengthen the ability of preference-receiving countries to meet product standards are generally deemed critical for enhancing the effective benefits associated with trade preferences.[19]

[19] A senior official of the European Commission alluded to the complementary roles of trade preferences and support policies by recalling, in a letter to the *Financial Times* on 14 March 2003, that the European Union provides LDCs "with the necessary trade-related assistance so that they can make use of improved market access. It is only the combination of both that will help LDCs reap the full benefits".

39. Exports of fish and other seafood –which are among the most important exports of LDCs — are particularly sensitive to sanitary and phytosanitary measures. The import restrictions and bans that were imposed by the European Union, in 1997-1999, on fisheries products from Mozambique, the United Republic of Tanzania and Uganda on grounds of risk of poisoning from the presence of pesticides are illustrative of how LDCs' exports can be affected by problems relevant to product standards. The socio-economic effects of such measures can be serious, as shown by the case of Uganda, where losses caused by the ban on fish imports were estimated at nearly $37 million.[20]

40. Another example of the significant losses that can result from import restrictions based on product standards is that relevant to the shrimp industry in Bangladesh. Shrimps are one of Bangladesh's most important primary commodity exports, and the industry is a major employer in that country. A study by the Consumer Unity and Trust Society (CUTS) indicated that 1.2 million people are directly employed in the shrimp industry. When the European Union banned shrimp imports from Bangladesh between August and December 1997, the country's shrimp exports to the European single market dropped from $65 million to zero, while exports of the same product to other major markets increased enough to offset the losses incurred on the European market.[21]

41. The case of Bangladesh is important not only because it highlights the loss in foreign exchange earnings that can result from an import ban, but also because it points to the lack of coherence in international trade policies. Since importing countries have different levels of standards, they could consider a downward harmonization of standards (harmonization toward less stringent standards), provided that legitimate concerns about safety are not compromised, in order to lessen the adjustment burden that LDC exporters will have to bear.

42. Imposition of product standards can lead to decreases in export earnings, losses of employment and income, and eventually, increases in poverty. It is therefore desirable that setting of product standards be based on a careful and transparent assessment of relevant capacities in exporting countries. To ensure that they will not have devastating effects on LDC exports, changes in standards should imply the provision of technical assistance to enable LDCs to comply with revisited standards. Such technical assistance could be provided, for example, through the Integrated Framework for Trade-related Technical Assistance to LDCs.

D. Subsidies in developed countries

43. Market access preferences can stimulate LDCs' agricultural production and exports if other policies of developed countries do not act in the opposite direction. According to a World Bank study, several of the large subsidies that developed countries provide to their domestic agricultural sector negatively affect agricultural production and exports from LDCs[22], because these subsidies artificially increase the competitiveness of producers in the developed countries, thereby making it very difficult for LDC exporters to compete on the world market. The concomitance of market access preferences and agricultural subsidies in developed countries reveals a lack of policy coherence that can make a set of development policies ineffective. To increase the effectiveness of preferential market access initiatives and

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[20] See Mussa, Vossenaar and Waniala (2002). For other case studies, see for example Otsuki, Wilson and Sewadeh (2000).
[21] cf. CUTS Centre for International Trade, Economics and Environment (2002).
[22] See Hoekman, Ng and Olarreaga (2002).

other international support measures in favour of LDCs, it is important that developed countries demonstrate coherence in their different policies relevant to aid, trade, technical assistance and direct support to agricultural and industrial development.

E. Supply capacities of LDCs

44. LDCs generally suffer from weaknesses in their supply capacities, either within existing economic sectors, or in their efforts toward economic diversification. These weaknesses often hinder competitive advantages. Preferential market access aims at offsetting this disadvantage by creating a competitive margin (through a lower tariff) vis-à-vis competing countries that enjoy either a lower preferential margin (other developing countries), or no preferential margin at all (most-favoured-nation treatment).

45. To enable LDCs to effectively benefit from the market access preferences they have been granted, it is desirable that financial and technical assistance be also extended to them. This generally implies that more aid be allocated to productive sector development, without hampering ongoing efforts in favour of the social sector. As a majority of the population of LDCs lives on, or below, the internationally recognized limit of extreme poverty,[23] development aid to these countries ought to be targeted toward developing productive sectors as much as it is aimed at developing human capacities.

46. In the 1990s, however, net disbursements of official development assistance by OECD/DAC countries to LDCs declined in real per capita terms. Moreover, the share of development aid to LDCs from the same donors that was allocated to productive sectors also diminished.[24] It is therefore important that continuation be seen in the increase that recently took place in the level of aid to LDCs.

47. Paragraph 43 of the Doha Ministerial Declaration of member States of the World Trade Organization recognizes the need to answer the particular supply constraints faced by LDCs, in response to their long-standing concern. Accordingly, it is important that Diagnostic Trade Integration Studies under the Integrated Framework expand their focus by paying increased attention to policy issues relating to the development of productive economic sectors, in particular, sectors with recognized export-related potential.

VI. Conclusion

48. Market access preferences without obstacles to the export of agricultural and basic manufactured products can have a beneficial impact on trade, investment, job creation and poverty reduction in many LDCs, in particular those with a competitive export capacity. For LDCs with weaker supply capacities, such an impact will take longer to materialize. However, the relatively low degree of utilization of market access preferences shows that there is scope for improvement in the impact of preferential schemes, and therefore, for encouraging competitive progress even in the weakest LDC economies. At present, several factors militate against a more effective utilization of market access preferences by LDCs.

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[23] Extreme poverty is defined by a poverty line of $1 per person per day in 1985 currency (at purchasing-power parity). The *Least Developed Countries Report 2002* showed that a majority of the population of LDCs lives in extreme poverty. This has severe implications for the ability of LDCs to promote economic growth and development in an autonomous manner (UNCTAD, 2002b).

[24] OECD/DAC countries are member States of the Organisation for Economic Co-operation and Development (OECD) that are also members of its Development Assistance Committee (DAC).

These include, besides structural impediments in the supply capacities of these countries, the relative unpredictability of the preferences themselves, the persistence of overly stringent rules of origin, cumbersome administrative procedures for receiving preferential treatment at the time of customs clearance, and non-tariff barriers to trade in preference-giving markets. These obstacles should be overcome or removed if the utilization and effectiveness of preferential schemes are to be enhanced.

49. Most LDCs are now granted improved preferential market access to Quad countries. However, further progress can be aimed at in order to minimize the negative impact of preference erosion, which underscores the temporary nature of market access concessions. There are three principal sources of erosion: (a) MFN tariff reductions in the World Trade Organization; (b) the extension of market access preferences to new countries by preference-giving countries; and (c) bilateral or regional free-trade arrangements between preference-giving countries and third countries. Erosion of preferences implies that other countries, and among them, countries with more competitive supply capacities and export potential, enjoy increased market access to the preference-giving countries, and regain competitiveness vis-à-vis countries that had been enjoying preferential margins. LDCs, with generally weaker productive capacities than other developing countries, bear a heavy burden as a result of this phenomenon.

50. While preference erosion cannot be prevented, its negative consequences could be partially remedied through efforts to establish or deepen preferential margins for products that still face relatively high tariffs. However, this option remains narrow for most LDCs, as the latter already benefit from duty-free and quota-free market access for most products. It is therefore important that other compensatory forms of special treatment be deployed to overcome the problems that market access preferences were designed to answer. The overall policy challenge is to enhance existing preferential schemes while supporting and encouraging structural improvements in the productive capacities of LDCs. Realizing this dual objective implies, on the part of preference-giving countries, a constructive partnership with LDCs. To that end, policy coherence in answering the structural problems of the economies of these countries is highly desirable.

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Annex table

The use of market access preferences granted by Quad countries to LDCs

Country	Year	Total imports	Dutiable imports	Imports eligible for GSP treatment	Imports receiving GSP treatment	Product coverage ratio	Utilization ratio	Utility ratio
(1)	(2)	(3)	(4)	(5)	(6)	(5)/(4)	(6)/(5)	(6)/(4)
		million $				%		
Quad	1994	5,347.0	3,917.3	2,071.0	999.0	52.9	48.2	25.5
	1995	6,087.8	4,706.1	2,564.3	1,361.2	54.5	53.1	28.9
	1996	9,956.3	7,451.1	2,985.0	1,517.9	40.1	50.9	20.4
	1997	10,634.1	8,163.4	5,923.1	1,788.2	72.6	30.2	21.9
	1998	9,795.7	7,915.1	5,564.2	2,704.5	70.3	48.6	34.2
	1999	10,486.5	8,950.4	5,869.3	3,487.5	65.6	59.4	39.0
	2000	13,359.2	11,715.5	7,836.0	4,990.2	66.9	63.7	42.6
	2001	12,838.2	11,167.1	7,185.5	4,919.9	64.3	68.5	44.1
Canada	1994	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	1995	175.9	41.3	6.4	4.1	15.5	64.1	9.9
	1996	336.9	34.5	6.3	2.9	18.3	46.0	8.4
	1997	205.3	47.3	8.6	4.7	18.2	54.7	9.9
	1998	256.0	92.1	9.8	5.8	10.6	59.2	6.3
	1999	154.6	60.7	8.2	4.9	13.5	59.8	8.1
	2000	180.1	75.9	9.9	7.2	13.0	72.7	9.5
	2001	243.2	94.6	11.4	8.0	12.1	70.2	8.5
European Union	1994	2,471.2	1,823.4	1,791.7	748.1	98.3	41.8	41.0
	1995	2,814.6	2,277.8	2,246.3	1,077.6	98.6	48.0	47.3
	1996	3,219.0	2,580.3	2,520.1	1,196.8	97.7	47.5	46.4
	1997	3,614.8	2,926.3	2,888.8	770.8	98.7	26.7	26.3
	1998	3,519.4	2,932.1	2,908.0	761.8	99.2	26.2	26.0
	1999	3,562.2	3,100.9	3,075.2	1,035.0	99.2	33.7	33.4
	2000	4,247.1	3,671.7	3,633.6	1,499.5	99.0	41.3	40.8
	2001	4,372.4	3,958.1	3,935.7	1,847.4	99.4	46.9	46.7
Japan	1994	1,120.5	695.5	211.2	200.5	30.4	94.9	28.8
	1995	1,309.8	912.7	241.9	230.1	26.5	95.1	25.2
	1996	1,504.3	939.8	388.9	269.9	41.4	69.4	28.7
	1997	1,204.9	757.3	306.3	222.1	40.4	72.5	29.3
	1998	1,045.4	643.8	364.0	189.9	56.5	52.2	29.5
	1999	989.0	679.6	366.2	231.9	53.9	63.3	34.1
	2000	1,236.5	881.3	615.3	236.0	69.8	38.4	26.8
	2001	1,001.3	398.1	278.3	228.4	69.9	82.1	57.4
United States	1994	1,755.3	1,398.4	68.1	50.4	4.9	74.0	3.6
	1995	1,787.5	1,474.3	69.7	49.4	4.7	70.9	3.4
	1996	4,896.1	3,896.5	69.7	48.3	1.8	69.3	1.2
	1997	5,609.1	4,432.5	2,719.4	790.6	61.4	29.1	17.8
	1998	4,974.9	4,247.1	2,282.4	1,747.0	53.7	76.5	41.1
	1999	5,780.7	5,109.2	2,419.7	2,215.7	47.4	91.6	43.4
	2000	7,695.5	7,086.6	3,577.2	3,247.5	50.5	90.8	45.8
	2001	7,221.3	6,716.3	2,960.1	2,836.1	44.1	95.8	42.2

Source: based on UNCTAD (2003, forthcoming)
Notes: (a) Values for Quad countries for 1995 exclude Canada; (b) figures are based on member State notifications; (c) figures for Japan are based on fiscal years; (d) figures for the European Union for 1994-1995 exclude Austria, Finland and Sweden.

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TD/B/50/5/Corr.1
1 October 2003

ENGLISH ONLY

TRADE AND DEVELOPMENT BOARD
Fiftieth session
Geneva, 6–17 October 2003
Item 3(b) of the provisional agenda

MAIN RECENT INITIATIVES IN FAVOUR OF LEAST DEVELOPED COUNTRIES IN THE AREA OF PREFERENTIAL MARKET ACCESS: PRELIMINARY IMPACT ASSESSMENT

Note by the UNCTAD secretariat

Corrigendum

Paragraphs 23 and 24 and the annex table (section relevant to Japan) of the note should read as follows:

23. In **Japan**, the sudden decrease in the utilization ratio to 57.4 per cent in 2001 from 76.4 per cent in 2000 was mainly explained by a sharp (+29 per cent) increase in the total value of imports eligible for GSP treatment in 2001 (as a result of significant improvements in product coverage), while total imports effectively receiving preferential treatment did not change significantly in 2001 compared with 2000 or earlier years. The product coverage and utilization ratios are both likely to increase as a result of the changes introduced in market access preferences in 2003.

24. Utilization ratios appear to vary considerably among products. In particular, high ratios (almost 100 per cent) have been recorded for fish products, hides and skins, and footwear products. Conversely, lower than average ratios have been recorded for metals and textile products. The low utilization of preferences for textile and clothing products has been explained by difficulties in complying with origin requirements under the scheme. The LDC that has benefited most from the Japanese scheme is Cambodia.

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Country	Year	Total imports	Dutiable imports	Imports eligible for GSP treatment	Imports receiving GSP treatment	Product coverage ratio	Utilization ratio	Utility ratio
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	1995	175.9	41.3	6.4	4.1	15.5	64.1	9.9
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	1999	154.6	60.7	8.2	4.9	13.5	59.8	8.1
	2000	180.1	75.9	9.9	7.2	13.0	72.7	9.5
	2001	243.2	94.6	11.4	8.0	12.1	70.2	8.5
European Union	1994	2,471.2	1,823.4	1,791.7	748.1	98.3	41.8	41.0
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	1997	1,204.9	757.3	306.3	222.1	40.4	72.5	29.3
	1998	1,045.4	643.8	260.9	189.9	56.5	72.8	29.5
	1999	989.0	679.6	286.4	231.9	53.9	81.0	34.1
	2000	1,236.5	881.3	308.7	236.0	69.8	76.4	26.8
	2001	1,001.3	754.9	398.1	228.4	69.9	57.4	30.3
United States	1994	1,755.3	1,398.4	68.1	50.4	4.9	74.0	3.6
	1995	1,787.5	1,474.3	69.7	49.4	4.7	70.9	3.4
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	2000	7,695.5	7,086.6	3,577.2	3,247.5	50.5	90.8	45.8
	2001	7,221.3	6,716.3	2,960.1	2,836.1	44.1	95.8	42.2

Source: based on UNCTAD (2003, forthcoming)

Notes: (a) Values for Quad countries for 1995 exclude Canada; (b) figures are based on member State notifications; (c) figures for Japan, based on fiscal years, are UNCTAD estimates based on Japanese notifications; (d) figures for the European Union for 1994-1995 exclude Austria, Finland and Sweden.