UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

FLEXIBILITIES FOR DEVELOPING COUNTRIES IN AGRICULTURE:

MARKET ACCESS FORMULA

UNCTAD series on assuring development gains from the international trading system and trade negotiations

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PREFACE

As the focal point of the United Nations for the integrated treatment of trade and development and interrelated issues, and in accordance with the São Paulo Consensus adopted at the eleventh session of UNCTAD, the UNCTAD secretariat supports member States in assuring development gains from international trade, the trading system and trade negotiations, with a view to their beneficial and fuller integration into the world economy and to the achievement of the United Nations Millennium Development Goals. Through intergovernmental deliberations and consensus-building, policy research and analysis, and technical cooperation and capacity-building support, UNCTAD's work on trade negotiations and commercial diplomacy aims at enhancing the human, institutional and regulatory capacities of developing countries to analyse, formulate and implement appropriate trade policies and strategies in multilateral, interregional and regional trade negotiations.

This paper is part of a new series entitled "Assuring Development Gains from the International Trading System and Trade Negotiations". It builds on the previous series entitled "Selected Issues in International Trade Negotiations". Experts are invited to express their own views, which do not necessarily reflect those of the UNCTAD secretariat. The target readership is Government officials involved in trade negotiations, policymakers dealing with trade and trade-related matters, and other stakeholders involved in trade negotiations and policymaking, including non-governmental organizations, private sector representatives and the research community.

The objective of the series is to improve understanding and appreciation of key and emerging trade policy and negotiating issues facing developing countries in international trade, the trading system and trade negotiations. The series seeks to do so by providing a balanced, objective and sound analysis of the technical issues involved, drawing implications for development and poverty-reduction objectives, and exploring and assessing policy options and approaches to international trade negotiations in goods, services and trade-related issues. It seeks to contribute to the international policy debate on innovative ideas to realize a development dimension for the international trading system with a view to the achievement of the Millennium Development Goals.

The series is produced by a team led by Mina Mashayekhi, Head, Trade Negotiations and Commercial Diplomacy Branch, Division of International Trade in Goods and Services, and Commodities.

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ABSTRACT

Apart from the tariff-reduction formula and domestic support, exceptions from the formula cuts and other flexibilities were the major sticking points in the World Trade Organization (WTO) negotiations on agriculture. This note provides an overview of flexibilities for developing countries, with a focus on the formula. Countries have different interests and different tariff structures, which makes it difficult to design a formula and special and differential treatment provisions that could be accepted by all members. The harmonizing tiered formula complicates the specification of the degree of special and differential treatment based on certain criteria such as the two thirds principle. Countries that bound their tariffs at ceiling levels, and small and vulnerable economies (SVEs), need additional flexibilities if they are not to make deeper tariff cuts than other members and experience a higher adjustment burden. The proposed formula in the draft modalities text from December 2008 provides for additional flexibilities for a group of SVEs and recently acceded members. For many developing countries not in these groups, the formula may lead to higher than two thirds average cuts compared with developed countries if the proposed maximum average cut is not agreed.

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1. Introduction

Multilateral talks at the World Trade Organization (WTO) continue at a slow pace in 2009 after very hectic negotiations in July and December of 2008. Progress has been made on many issues, but not enough to conclude the modalities for agriculture and non-agricultural market access (NAMA) by the end of 2008 as was proposed by a G-20 meeting in November 2008. No new deadlines have been set, although it has been argued that the threat of protectionism as a possible consequence of the economic crisis increases the importance of a successful conclusion of the Doha Round.

A draft modalities text issued by the Chair of the negotiation committee in July 2007, and its subsequent revisions, the latest dated December 2008, was welcomed by all sides as the basis for further negotiations. The first draft contained ranges for the tariff-reduction formula and domestic support cuts, but not all details – especially on exceptions – were spelled out. Later revisions contained more concrete numbers for cuts and other details. Director-General Pascal Lamy wants to keep the momentum going and urges further acceleration of the negotiations, but the NAMA negotiations and the balance between agriculture and NAMA puts up additional hurdles, as these are controversial issues.[1]

Although not all members are satisfied with all provisions in the draft modalities text, many important and previously controversial elements seem to be settled and are currently not being negotiated. The reduction of overall trade-distorting domestic support in the United States is proposed to be 70 per cent, high tariffs in the European Union not selected as special products would be cut, as in all developed countries, by 70 per cent, export subsidies would be eliminated, and progress has been made on exceptions from formula cuts through Sensitive and Special Products. Since these were very controversial issues, if there is an agreement any time soon, it is not likely to look very different from what is currently on the table, so an analysis of developing-country flexibilities is timely. Issues that remain controversial are mainly the special agricultural safeguard mechanism for developing countries, reduction of cotton subsidies, treatment of long-standing preferences, and a few other technical issues such as expansion of tariff rate quotas.[2]

Apart from the special agricultural safeguard mechanism for developing countries, the developing-country tariff-reduction formula including exceptions from line-by-line reductions is the most important element regarding developing countries' defensive interests. Flexibilities for developing countries with respect to the formula reduction are accepted due to their different level of development, and were already agreed in the 2001 Doha Ministerial Declaration and confirmed in the 2004 July Framework and the 2005 Hong Kong Ministerial Declaration. However, these agreements do not determine the degree of special and differential treatment given to developing countries, which therefore leaves wide scope for the current negotiations. The flexibilities impact greatly on the overall level of ambition. Since WTO members, including the group of developing countries, have diverging interests on the level of ambition, it is essential to find a balance that is acceptable to both sides.

This note provides an overview of flexibilities for developing countries, with a focus on the tariff-reduction formula.[3] It is shown that if an overall average cut in developing countries of around two thirds of those undertaken by developed countries is found to deliver on the needs and interests of developing countries regarding the formula reduction, then the draft modalities text formula from December 2008 is about right if the maximum overall average cut is 36 per cent for developing economies that are not small and vulnerable economies (SVEs). Average cuts of about two thirds for the latter group of countries are higher than 36 per cent if the proposed formula is applied and lower cuts for exceptions (Special and Sensitive Products) are not taken into account. Four countries would make cuts above 40 per cent, which is clearly higher than two thirds of the developed country cuts. Some recently acceded members would be exempt from further commitments, and other recently acceded members have additional flexibilities.

2. Flexibilities for developing countries

Members had already made much progress by agreeing on provisions that had seemed unlikely only a few years earlier. Furthermore, the proposed numbers in the run-up to the Hong Kong Ministerial in December 2005, such as average tariff reductions, indicated that views were not that far apart. Nonetheless, the negotiations in July 2006 and 2007/08 showed how difficult it is for WTO members to narrow down the remaining gaps, and how far apart they are once details such as exemptions from line-by-line reductions and safeguard measures are taken into account. The details are important, and the flexibilities could make almost all the difference (see also Vanzetti and Peters, 2007; and Ben Hammouda et al., 2007).

In addition to the existing flexibilities for developing countries that are part of the Uruguay Round Agreement on Agriculture,[4] essentially six areas of flexibility for developing countries have been agreed.[5]

Flexibilities for developing countries:[6]

1. Flexibilities in the tariff-reduction formula: proportionality achieved by requiring lesser tariff-reduction commitments from developing countries.
2. Sensitive products (SeP): Developed and developing countries can designate an appropriate number of products as "sensitive". "Substantial improvement in market access" for these products will be achieved through a combination of tariff cuts and most favoured nation (MFN)-based tariff quota expansion. Developing countries would enjoy special and differential treatment (SDT), such as no tariff quota expansion, in exchange for a lower number of SePs and a lower deviation from the formula cuts.
3. Special products (SP): Developing countries can designate 12 per cent of tariff lines as special products, guided by indicators based on food security, livelihood security and rural development. Tariffs would not have to be reduced for up to 5 per cent of tariff lines, and the average cut of tariffs for all 12 per cent of SPs would have to be 11 per cent.
4. Special agricultural safeguard mechanism for developing countries (SSM): A mechanism that temporarily allows for additional duties to protect farmers against import surges or very low import prices.
5. Special provisions for least developed countries: Least developed countries (LDCs) would be exempt from tariff reductions and would receive favourable market access to developed countries and developing countries that so decide.
6. Flexibilities on domestic support and export subsidies: Inclusion of developing country–friendly measures in the green box (annex II, Agreement on Agriculture (AoA)); no *de minimis* level cuts have to be undertaken by developing countries that do not have Aggregate Measurement of Support (AMS) entitlements; existing provisions, such as article 6.2 of the AoA ("development box support", which allows for input subsidies for resource-poor farmers in developing countries) and article 9.4 of the AoA (which allows for subsidizing internal transport and freight charges and marketing costs in developing countries) will remain (article 9.4 possibly for a limited time period).

These flexibilities reflect the limited capacity of developing countries to bear the burden of multilateral trade liberalization (which is in addition to enjoying the benefits) and the fact that since agreements are taken by consensus in WTO, it is necessary that developing countries agree to the whole package. Developing countries have made it clear that without meaningful flexibilities, they would not say yes to a new agreement on agriculture. The different treatment of developing countries was a principle of the General Agreement on Tariffs and Trade and later of WTO that contributed to WTO's success in becoming an almost universal organization.

There are two major aspects with regard to flexibilities: (a) political aspects; and (b) economic/social aspects. For countries with an emphasis on defensive interests, such as the majority of the G-33 group of developing countries,[7] a lack of sufficient flexibilities can have an immediate economic/social impact if tariffs on sensitive products have to be reduced substantially. Uncompetitive producers may find it difficult to improve their productivity sufficiently to be able to compete with cheaper imports, which may threaten their livelihood security if they cannot find other employment opportunities. It has also been argued that it may worsen the food security situation. It may also be politically necessary to have sufficient flexibility in order to receive the support necessary at home for signing an agreement. However, for countries with a focus on offensive interests – such as Cairns Group members, which includes developing countries – higher flexibilities could mean less improvement in market access; limiting flexibilities may, therefore, also be a political necessity for agricultural exporters.

As regards political concerns, the focus is currently on special products and the special agricultural safeguard mechanism for developing countries. These two provisions are highly controversial, because they can impact greatly on the overall level of ambition. However, the flexibility regarding the formula plays an equally important role, since the formula will be applied to the vast majority of the tariff lines.

Tariff structures

The structures of bound tariff schemes of WTO members are quite different. As a result of the Uruguay Round Agreement on Agriculture, countries either bound their tariffs at the level of their applied rates during the base period (or at the tariff equivalent in the case of non-tariff barriers), or in the case of many developing countries, at ceiling levels. The Uruguay Round Agreement on Agriculture tariff-reduction formula allowed for flexibility to reduce some tariff lines by a small percentage (of only 10 or 15 per cent, in developing and developed countries respectively) whenever the average cut of 24 and 36 per cent was met (see also box 1). This led to a further dispersion of tariff rates, since higher tariffs were often reduced by a smaller percentage than tariffs that were already low. The typical tariff structure of developed countries is, therefore, to have many tariff lines bound at rather low levels, and to have some very high tariffs on sensitive products. Figure 1 shows the tariff structure of the European Union (EU). It shows that the EU bounds many tariff lines at zero or at low levels, but that it has some very high tariffs on certain products. MFN applied tariffs are mostly equal to bound rates. The pattern is exactly the same in the United States and in Japan, although with somewhat different scales, since the United States has – on average – lower tariffs, whereas Japan has – on average – higher tariffs than the EU. Norway and Switzerland have a higher proportion of medium and high tariffs.

Figure 1. EU tariff structure for agricultural products, bound rates

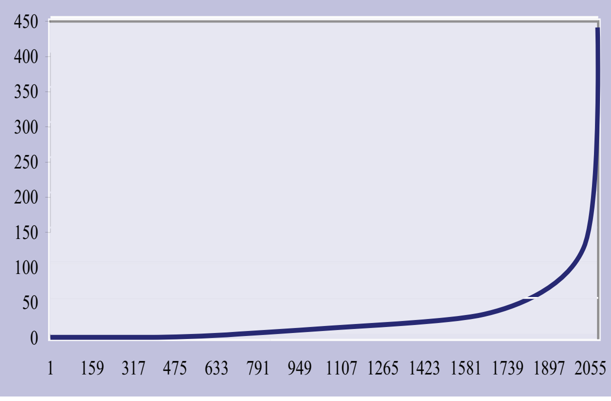


Table 1: Average agricultural tariffs in developed and developing countries

		Bound	Applied
Agriculture	Developed countries	38	34
	Developing countries	61	25

In general, developing countries have higher bound rates and lower applied rates for agricultural products. Table 1 shows the simple average tariffs in developed and developing countries.

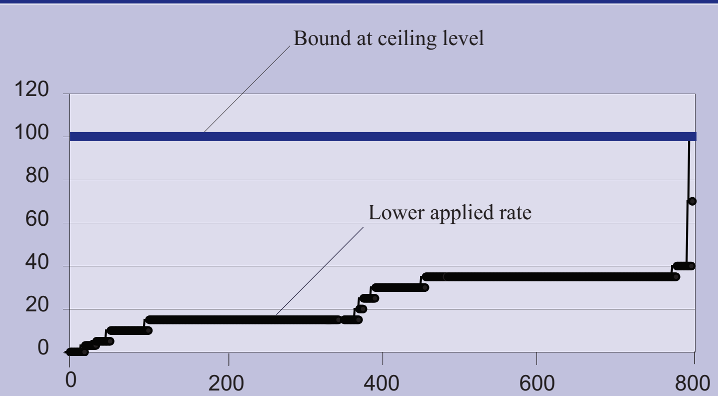
Many developing countries, especially in Africa, opted for ceiling bindings during the Uruguay Round. They have, for example, a bound rate of 100 or 120 per cent across the board. Figure 2 shows the tariff structure of Kenya. Some developing countries, among them many Latin American countries, have rather low bound rates. Suriname and Ecuador, for example, have average bound tariffs of 20 per cent and 26 per cent respectively. Recently acceded members are those that have acceded to WTO since 1995. They have an average bound tariff of 20 per cent (UNCTAD, 2007a), which compares to 38 per cent and 61 per cent for existing developed and developing WTO members respectively (table 1)

Formula flexibility

This wide range of different tariff structures makes it difficult to find a tariff-reduction formula that achieves the objectives and is considered as fair or acceptable by all parties. The objectives are:

1. To establish a fair and market-oriented trading system (AoA, recalled in the Doha Ministerial Declaration);
2. Substantial improvements in market access (Doha Ministerial Declaration);
3. Special and differential treatment for developing countries shall be an integral part (Doha Ministerial Declaration);
4. Tariff reduction will be made through a tiered formula[8] that takes into account their different tariff structures (July Package);
5. Progressivity in tariff reduction through deeper cuts in higher tariffs (July Package).

Figure 2. Tariff structure of Kenya



Box 1. Agreed provisions on the tariff-reduction formula

Doha mandate on agriculture

«Substantial improvements in market access; [...]. We agree that special and differential treatment for developing countries shall be an integral part of all elements of the negotiations [...], so as to be operationally effective and to enable developing countries to effectively take account of their development needs, including food security and rural development» (para. 13 of the Doha Declaration, 2001).

Agreements in July 2004 and the Hong Kong Ministerial Declaration

The Framework Agreement and the Hong Kong Ministerial Declaration provide for one tiered formula, with four tiers and deeper cuts in higher tariffs. Proportionality in tariff-reduction commitments, which means lesser commitments from developing countries, is agreed.

Deeper cuts in higher tariffs have a harmonizing effect, that is to say, tariffs become closer to each other. However, flexibilities to deviate from the formula through SPs and SePs may reduce the harmonizing effect, since it is likely that tariff lines with higher rates would be selected for the exceptions. Harmonization is not explicitly agreed, nor is it specified whether it would be within countries or also between countries.

Another major question in the negotiations is the degree of special and differential treatment in the tariff-reduction formula. Many proposals imply a basic concept of ⅔, which means that developing countries make two thirds of the cuts that developed countries undertake. This was, for example, the case in the Uruguay Round, when developed countries reduced their tariffs on average by 36 per cent and developing countries by 24 per cent (24 = 36 x ⅔). Ambassador Falconer wrote in one of the reference papers that he issued as Chair of the negotiations session: "There was a certain centre of gravity for two-thirds cuts for developing countries. […] As Chair, I find it hard to get away from the sense that the basic concept of ⅔ has a certain resonance as broadly "about right" when it comes to the concept that there should be "lesser" cuts for developing than developed." He acknowledges that this principle is resisted by certain members – in both directions – i.e. some support a greater degree of special and differential treatment than two thirds, and others support a lesser degree.

One unspecified issue regarding this concept is whether it means that developing countries undertake two thirds of the cuts for a given tariff (e.g. on a tariff of 50 per cent), or that cuts in each tier are two thirds lower, or that their overall average cuts are two thirds of those that developed countries undertake. A tiered formula with higher cuts in higher tariffs may lead to higher average cuts in those countries that start with higher initial bound tariffs, even if cuts in each tier respect the ⅔ concept. One country may find all or almost all its tariffs in the highest tier, with correspondingly high overall cuts, whereas other countries may have most of its tariffs in the lower tiers. Nigeria, with a ceiling level of 150 per cent, is an extreme example, since it would find all its tariff lines in almost all proposals in the highest tier, and under some proposals it would make higher average cuts than developed countries. Thus, there is harmonization across countries as well as within countries. This would, however, eliminate, to a certain extent, the special and differential treatment that was given to some countries during the Uruguay Round. Since developing countries tend to have higher bound rates than developed countries, this effect may well result in some developing countries making higher average cuts than some developed countries. The cut in the average tariff may be higher or lower (see box 1).

Box 2. «Cut in the average» versus «average cut»

Assume country A has two tariff lines that have to be reduced due to a multilateral agreement. The tariff for product 1 is 100 per cent and the tariff for product 2 is 10 per cent. The Uruguay Round formula was to reduce each tariff line by at least 15 per cent to make average cuts of 36 per cent. The tiered formula determines de percentage cuts in each tier and cuts are higher for higher tariffs.

	Uruguay Round			Tiered formula	
Initial tariff	Percentage cut	New tariff	Initial tariff	Percentage cut	New tariff
10	57	4.3	10	15	8.5
100	15	85	100	57	43
Average: 55	36	44.65	Average: 55	36	25.75

Although both formulas lead to average cuts of 36 per cent, the cut of the average tariff (from 55 per cent) is 19 per cent only in the case of the Uruguay Round formula (to 44.65 per cent) and 53 per cent in the case of the tiered formula (to 25.75 per cent). Thus, the former formula leads to higher average cuts than cuts in the average, whereas the tiered formula leads to lower average cuts than cuts in the average.

3. Proposals on a tariff-reduction formula

Most formal written offers are still from October 2005, when negotiations were active in the run-up to the Hong Kong ministerial meeting. The EU rejected the G-20 proposal of a 54 per cent reduction for developed countries at Hong Kong, but agreed to the G-20 proposal on the developing-country tariff-reduction formula and the tariff caps.[9] Reportedly, the EU offered in the beginning of 2007 to cut its tariffs on average by 54 per cent – although it is not clear how this average would be achieved. This has been the October 2005 proposal for developed-country cuts by the G-20 group of developing countries. The United States had requested a cut of around 67 per cent and more ambitious tariff caps for both developed and developing countries. For developing countries, the United States requested "slightly lesser cuts" than [the ambitious] developed-country cuts. Thus, the EU and the G-20 seem to be closer together on the tariff-reduction formula than they both are with the United States.[10]

However, differences between the EU and G-20 persist on the number of tariff lines that could be designated as sensitive products (see table 2) and on many other issues.

Table 2. Summary of proposals on market access (from most to least ambitious proposal)

		US	G-20	EU	ACP	G-10
Highest threshold	DDs DCs	> 60% > 60%	> 75% > 130%	> 90% > 130%	> 80% > 150%	> 70% > 100%
Highest cut	DDs DCs	90% Slightly less	75% 40%	60% 40%	42% 30%	45% -
Overall average	DDs DCs		54% 36%		36% 24%	
Formula	DDs DCs	Progressivity in each band	Linear	Linear with flexibility	Linear with flexibility	Linear or flexibility
Sensitive products	DDs DCs	1% full compensation	1%	8%	Preference products	10%–15%
Tariff cap		Yes	Yes	Yes, sensitive products?	No	No

Note: Second number for developing countries.

The G-10 group of countries rejects tariff caps, asks for a relatively high number of sensitive products, and proposed – like the African, Caribbean and Pacific (ACP) Group of States – relatively low cuts for the band with the highest tariffs. The G-10 countries have many tariffs that would fall into the high bands, and ACP countries are concerned about preference erosion.

As indicated by the Chair of the agricultural negotiation group, Ambassador Falconer, in the first half of 2006 (WTO, 2006a), it seems that any possible compromise would by somewhere "around the G-20" proposal of average cuts of 54 per cent for developed countries and 36 per cent for developing countries. The United States seems to be the major proponent of more ambitious liberalization in developing countries.

Box 3. Proposals for tariff-reduction formulas

G-20 proposal (12 October 2005)

	Developed Countries		Developing countries	
	Bound tariffs (X) within the band	Will be reduced by linear cut	Bound tariffs (X) within the band	Will be reduced by linear cut
1	20 ≤ X < 0	45%	30 ≤ X < 0	25%
2	20 ≤ X < 50	55%	80 ≤ X < 30	30%
3	20 ≤ X < 75	65%	130 ≤ X < 80	35%
4	> 75	75%	> 130	40%
Capping	at 100%		at 150%	

Note: The G-20 proposal is, in addition, that developed countries shall make at least average cuts of 54 per cent, and developing countries at most 36 per cent.

European Union proposal (28 October 2005)

	Developed Countries		Developing Countries	
	Bound tariffs (X) within the band	Will be reduced by linear cut	Bound tariffs (X) within the band	Will be reduced by linear cut
1	30 ≤ X < 0	35% (20%-45%)	30 ≤ X < 0	25% (10%-40%)
2	60 ≤ X < 30	45%	80 ≤ X < 30	30%
3	90 ≤ X < 60	50%	130 ≤ X < 80	35%
4	> 90	60%	> 130	40%
Capping	at 100%		at 150%	

United States Proposal (13 October 2005)

	Developed Countries		Developing countries	
	Bound tariffs (X) within the band	Will be reduced by linear cut	Bound tariffs (X) within the band	Will be reduced by linear cut
1	20 ≤ X < 0	55%-65%	30 ≤ X < 0	40%
2	20 ≤ X < 40	65%-75%	80 ≤ X < 30	47%
3	40 ≤ X < 60	75%-85%	130 ≤ X < 80	53%
4	> 60	85%-90%	> 130	58%
Capping	at 75%		at 150%	

* The United States Proposal does not have concrete numbers for developing-country cuts and the developing-country cap. The proposal is a "slightly lesser reduction" than developed countries. The assumption here is 2/3cuts of the developed-country medium cut in the corresponding tier.

Draft modalities text (6 December 2008)

	Developed Countries		Developing Countries	
	Bound tariffs (X) within the band	Will be reduced by linear cut	Bound tariffs (X) within the band	Will be reduced by linear cut
1	20 ≤ X < 0	50%	30 ≤ X < 0	33%
2	20 ≤ X < 50	57%	80 ≤ X < 30	38%
3	50 ≤ X < 75	64%	130 ≤ X < 80	43%
4	> 75	70%	> 130	47%
Capping	at 100% except sensitive products		at 150% except sensitive products	

Note: In addition, developing countries make at most 36 per cent average cuts, and developed countries at least 54 per cent.

* Only those developing countries that are not covered by footnote 11 (WTO, 2008), which are mainly the small vulnerable economies (SVEs) and not recently acceded members (RAMs).

Box 4. Modalities text provisions for small and vulnerable economies (SVEs)

65. Those small, vulnerable economies, including those among them which are ceiling-binding and homogenously low-binding countries, which choose to [apply the tiered formula plus the Special Product entitlement] shall be entitled to moderate the cuts specified [for developing countries] by a further 10 ad valorem percentage points in each band.

130. [...] Alternatively, they may choose not to apply the tiered formula but simply meet an overall average cut of 24 per cent through having in effect opted to designate as many tariff lines as they choose as Special Products. The tariff lines so chosen need not be subject to any minimum tariff cut and need not be quided by indicators.

In his draft modalities text (WTO, 2008), the Chair suggests a more flexible treatment for small and vulnerable developing economies, and suggests extending the treatment to include the Republic of Congo, Côte d'Ivoire and Nigeria, thereby covering members of the SVE group and all ACP members.

Small vulnerable economies have the option to apply the formula line by line, with reduced reductions in each band, and to make use of sensitive and special products or to ensure an average cut of 24 per cent without additional conditions. For some SVEs, the selection would be clearly the average cut option, since it provides for lower average cuts and for more flexibilities regarding the selection of tariffs with deeper and those with lower cuts. On the other hand, for some countries there will be a trade-off between lower average cuts (under the formula option) and more flexibility (under the average cut option). Each SVE has to decide during the scheduling phase which option to select.

Recently acceded members (RAMs) that acceded to WTO after 1995 benefit from additional flexibilities due to the fact that these countries have taken strong commitments as a result of their accession process. Some RAMs have lower reduction commitments and a longer implementation period and others are exempt from tariff reductions.[11]

The various formulas and special and differential treatment provisions are applied to WTO member tariff schedules taking SPs and SePs into account.[12] Provisions for tropical products and products benefiting from long-standing preferences are not taken into account, since the details have not yet been determined.

Box 5. Draft modalities text provisions for recently acceded members

66. RAMs shall be entitled to moderate the cuts they would otherwise have been required to make under the tiered formula for developing-country members [...] by up to 8 ad valorem percentage points. All RAMs shall be entitled to exempt their final bound tariffs at or below 10 per cent from reductions in bound tariffs.

67. [...] very recently acceded members and small low-income RAMs with economies in transition shall not be required to undertake reductions in final bound tariffs.

4. Simulation results

Developed and developing countries

Table 3 shows the results when the four proposals are applied to the actual bound tariffs of selected countries without taking exceptions and maximum or minimum average cuts into account (this is for demonstration purposes; for details, see below). One important first result is that the overall average cut of the developing-country tariffs is not ⅔ of the overall average cuts of developed countries, even if (as was assumed in all four proposals) (a) in each tier the ⅔ principle holds; and (b) in addition, the developing-country thresholds are higher. This is because of the higher initial tariffs of developing countries. India makes, for example, the same average cut like the United States in the EU proposal, and more than ⅔ of the cuts in the G-20, United States and draft modalities proposal. Nigeria makes an even higher average cut than all the selected developed countries in the EU proposal.[13] An additional provision such as that in the G-20 and draft modalities text formula demanding that average cuts in developed countries be at least 54 per cent and in developing countries at most 36 per cent would prevent these results. The Chair suggests in the draft modalities text (DMT) a maximum cut of 36 per cent for developing countries. The threshold of 36 per cent would become binding for almost 70 per cent of developing countries. An earlier-proposed second possible threshold of 40 per cent (draft modalities text from July 2007) would become binding only for few non-SVE developing countries with relatively high bound rates.

Average cuts for developed countries are higher under the DMT formula than under the G-20 formula. The reason is that percentage reductions are higher for lower tariffs but smaller for higher tariffs in the DMT formula. Since developed countries have a high share of tariffs in lower tiers, the average cuts seem more ambitious under the DMT formula, although higher tariffs are reduced less than under the G-20 formula.

Table 3. Average cuts of selected WTO members

	G-20 proposal	European Union proposal	United States proposal*	Draft modalities
European Union	52	39	67	55
United States	47	36	63	52
Japan	53	38	67	55
Brazil	29	29	47	37
India	36	36	57	43
Indonesia	30	30	48	38
Kenya	35	35	58	32
Nigeria	40	40	58	36
Turkey	31	31	51	38
Venezuela (Bolivarian Republic of)	30	30	50	38

Source: UNCTAD calculations.

Note: Sensitive products and special products not taken into account for this table; proposed average cuts in G-20 formula and DMT formula not applied, for demonstration reasons; tariffs bound at zero not taken into account in calculating the average cut.

* See assumptions made in box 2 for developing-country cuts in the United States proposal.

Developing countries

A comparison among the developing countries shows a wide range of average tariff cuts. Tables A1 and A2 in the annex show the application of the G-20 and the DMT formula for all developing countries, with and without the inclusion of SPs and SePs. For demonstration purposes, maximum average cuts such as 36 per cent for developing countries are not taken into account. Under the G-20 formula, the average cuts range from 25 per cent (Albania, Armenia, Congo, Côte d'Ivoire, Georgia, Kyrgyzstan, Republic of Moldova) to 40 per cent (Nigeria), and under the DMT formula from 23 per cent (same countries for minimum) to 43 per cent (India). Average cuts for SVEs are in general lower under the DMT formula than under the G-20 formula, whereas it is the other way around in the case of non-SVE developing countries.

Many of the ACP countries bounded their tariffs at ceiling levels during the Uruguay Round. The average of the average cut under the G-20 formula is 33 per cent. For the non-LDC non-ACP developing countries, the average of the average cut is 28 per cent, and thus smaller than in the ACP group of countries. The same pattern, albeit to a lesser extent, is also true when comparing SVE and non-SVE developing countries under the G-20 formula. Under the DMT formula, average cuts for SVEs, with 29 per cent on average, are considerably lower than those for non-SVE developing countries (37 per cent). This is the case even if the SVEs apply the formula with lower cuts in each band and do not make use of the second option of average cuts of 24 per cent (box 4). Thus, the G-20 formula is slightly more ambitious for ACPs or SVEs than for those developing countries that are not in either of those groups, whereas the DMT formula is more ambitious for non-ACP or non-SVE developing countries.

An earlier proposal for a special provision for countries with ceiling bindings was that these countries (a) shall be subject to the overall average reduction only; (b) shall have the right to distribute their tariff lines across the lower tiers of the formula; and (c) shall not be required to undertake the cuts in the highest tier (WTO, 2006).

The right to bind tariffs at ceiling levels has been given to developing countries as a special and differential treatment provision in the Uruguay Round. The countries that opted for these argue that they paid a price for it, too, such as not having access to the existing special agricultural safeguard mechanism. If this special and differential treatment provision does not lead to higher average cuts in the current round of negotiations, these countries would need additional flexibility in order to benefit from the ⅔ principle for average cuts, or in order to not make higher contributions than other developing countries. The above-mentioned proposal (a) to (c) could deliver on these needs, although there have been complaints that some provisions such as (b) may be too flexible.

The proposal in the DMT also seems to provide a good solution to this issue. In the first half of 2007, the SVE group submitted a proposal which is partly reflected by the Chair in the DMT, as has already been stated in box 4. The DMT provisions ensure that SVEs make lower cuts than under the ⅔ principle, and on average, lower cuts than other developing countries. The specific provisions for SVEs lead, de facto, to a separation of developing countries into two groups, with lower commitments from SVE countries and higher commitments from non-SVE countries.

This additional flexibility for countries with ceiling levels or SVEs is strongly linked to the question of whether or not tariffs should be harmonized across countries, in addition to harmonization within the tariff schedule of a country. There is no mandate to harmonize tariffs across countries, but it is nevertheless an objective of some member states in the negotiations. Harmonization within countries would reduce distortions and address tariff peaks and tariff escalation. Thus, there are good reasons for the latter, and the agreed tiered formula delivers on this aspect. There remains, however, the shortcoming that the formula is not continuous. A tariff line A that is initially higher than tariff B may end up being smaller than B after application of the tiered formula.[14]

For many non-SVE developing countries, the DMT formula leads to higher than ⅔ overall average cuts compared with the major developed countries as shown in the tables 3 and A2. Almost 70 per cent make cuts higher than 36 per cent, which would roughly be two thirds of the developed-country average cut (36% = 54% x ⅔). Therefore, for these countries, the maximum average cut of 36 per cent is essential if the ⅔ principle is supposed to hold regarding the average cuts. However, exceptions reduce the average cuts by about 2 or 3 percentage points (table A1, columns 2 and 5). For the calculation of the maximum average cut of 36 per cent (30 per cent in the case of the Bolivarian Republic of Venezuela), lower reductions for SePs are taken into account, but not the lower cuts for SPs.

Since RAMs would benefit from additional flexibilities, and due to the fact that they already have comparably low bound rates (and thus their lines fall into low tiers), their percentage reduction is lower. However, their final new bound rates would still be considerably lower than those of "old" members.

Special products and sensitive products

Discussion of SPs and SePs is not the focus of this paper. Therefore, they are not taken into account when comparing the different formulas, since proposals differ not only with respect to the formula but also with respect to provisions regarding SPs and SePs. However, since these exemptions impact on the effectiveness of the tariff-reduction formula, they are discussed here briefly. Taking into account SPs and/or SePs when applying the formula does reduce the average tariff cuts. Vanzetti and Peters (2007a) show that for the European Union, the United States, Japan, Canada, Switzerland and Norway, the initial average tariff of 48.5 per cent is reduced to 15.6 per cent under the DMT formula without any SePs, but only to 24.0 per cent with 5 per cent SePs, and to 27.1 per cent with 10 per cent SePs (table 4). They selected the highest tariffs as SePs and reduced the tariffs for those lines only by one third of the formula cuts. The impact of SePs on developing-country tariffs is much smaller. The difference between the new tariff without SePs (39.1 per cent) and with 10 per cent SePs (41.0 per cent) is less than 2 percentage points. However, the selection rule is different, since for developing countries those tariff lines with the lowest percentage difference between bound and applied rates were selected, and it was assumed that SPs were already excluded in developing countries (wheat, maize and rice).

Table 4. Initial and final tariffs at various levels of exemption for sensitive products

	Initial	SeP 0%	SeP 1%	SeP 3%	SeP 5%	SeP 7%	SeP 10%
	%	%	%	%	%	%	%
WTO developed	48.5	15.6	20.2	22.3	24.0	25.4	27.1
WTO developing	59.7	39.1	39.3	39.7	40.2	40.5	41.0
WTO developing applied	17.2	15.0	15.1	15.3	15.4	15.5	15.6

Source: Vanzetti and Peters (2007). DMT formula.

The direct impact of SPs on the average cuts for developing countries is shown in the tables in annex 1 for the DMT formula. The average reduction is about 2 to 3 percentage points lower if developing countries can exclude up to 5 per cent of their tariff lines from any reductions, apply lower than the formula cuts for another 7 per cent of tariff lines (given that the average cut for SPs is 11 per cent (see footnote 13)), and apply ⅔ of formula cuts for SePs. In the Dominican Republic, for example, the average reduction without SPs and SePs is 27.5 per cent, and 25.2 per cent if the tariff lines with the highest tariff revenue impact or the lowest percentage difference between bound and applied rates receive lower cuts. The right to reduce their tariffs on average by 24 per cent that is foreseen for SVEs simplifies current negotiations. For some SVEs it might be more favourable and for others less favourable than applying the formula and having the right to designate SPs and SePs. Some SVEs, such as Côte d'Ivoire, face a trade-off between a higher average cut of 24 per cent with the average-cut option than with the formula (21.6 per cent) and a higher level of flexibility under the average-cut option than under the formula.

Applied tariffs

Although WTO negotiations are a legal process concerned with the negotiation of reduction in bound rates, many negotiators look at the implication on applied rates to ascertain the likely direct economic effects of possible negotiated outcomes. This has been justified by the fact that the mandate is to substantially improve market access. On the other hand, looking at applied rates penalizes unilateral liberalization. For developing countries, a deep reduction of bound rates that may or may not cut into their applied rates reduces their policy space, in addition to the above-mentioned social and economic implications. On the other hand, agricultural exporters expecting to benefit from increasing South–South trade will only see those gains if there are real tariff cuts in other developing countries.

The impact on applied rates varies greatly from country to country, from zero per cent (meaning that applied rates are not affected even if bound rates are reduced) to the level of cuts of the bound rates (implying that all or almost all applied rates are reduced). The most favoured nation (MFN) applied tariff rate in developed countries is, for most agricultural products, equal to the bound rate. Thus, cuts in applied rates are comparable to those in bound rates. However, developed countries have many regional trade agreements and provide non-reciprocal preferences with lower-than-MFN applied rates. In addition, since imports are concentrated on a few tariff lines, the possibility to designate certain tariff lines as SePs can significantly limit the reduction of the *trade-weighted* average applied rate.

Many developing countries have a high binding overhang, because they have either bound their tariffs at ceiling levels or unilaterally reduced their applied rates in recent years. Other developing countries, including most RAMs, have many applied rates close to their bound rates, and therefore applied rates of a high share of their tariff lines would be affected.

5. Conclusion

A major result of the analysis is that even if the ⅔ principle of special and differential treatment holds for each tier, and even if developing countries have more favourable thresholds, it may not turn out that the overall average cuts of developing countries are ⅔ of the cuts of developed countries. Thus, the question arises of the level at which this principle – if agreed – should be applied. In the Uruguay Round, it was at the overall average level. The high number of countries for which the minimum cut of 54 per cent or the maximum cut of 36 per cent for the overall average cut becomes binding seems to implicitly repeat this for developed and non-SVE developing countries. Related to this is the fact that the tiered formula is harmonizing tariffs within and across countries. If the latter is an objective, developing countries with higher initial tariffs, such as many ACP countries, have to make higher average cuts, as is the case in three of the above-mentioned proposals and most other proposals.

An exception is the draft modalities text formula, where an extended SVE group that includes all ACP countries would benefit from additional flexibilities. This would lead to lower percentage cuts in the small and vulnerable economies than in the remaining developing countries. On average, and without taking into account exceptions such as SPs and SePs, as well as maximum average cuts, the DMT formula leads to cuts of around 54 per cent in developed countries, 37.3 per cent in non-SVE non-RAM developing countries, and 28.5 per cent in the extended SVE group of countries. RAMs have lower average cuts due to the additional flexibility and the fact that they have already low tariffs which fall into low tiers. In addition, SVEs have the option to apply an average cut of 24 per cent without any conditions on line-by-line reductions. Therefore, the ⅔ principle is overachieved in the case of SVEs, but barely achieved for the average of non-SVEs' average cuts in the absence of a maximum average cut of 36 per cent. Thus, if this principle is used to determine the degree of special and differential treatment, the proposed formula with the maximum average cut of 36 per cent is about right.

The exceptions SPs and SePs have a non-negligible impact on the average cuts in all groups, and the exceptions can reduce or even convert the harmonizing effect of the tiered formula.

Whether the ⅔ principle "enable[s] developing countries to effectively take account of their development needs, including food security and rural development" (Doha Declaration) is another discussion, which is not the focus of this contribution.

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ENDNOTES

[1] Mr. Davies, Deputy Trade Minister of South Africa, said that there were at least a dozen unresolved issues in both agriculture and market-opening for industrial goods. WTD 3.3.09.

[2] For more details on the Doha round negotiations, see UNCTAD's Trade and Development Board documents from 2009 and 2008.

[3] On flexibilities regarding exemptions and quota expansion, see, for example, Anderson, Martin and van der Mensbrugghe (2006); Jean, Laborde and Martin (2006); and Vanzetti and Peters (2007).

[4] It is important to note here that although, legally, developing countries enjoy more flexibilities in the rules, as has been stated, it has been argued that *de facto* current rules and ways of implementation are imbalanced against developing countries. For example, Aggregate Measurement of Support (AMS) entitlements were based on payments during the Uruguay Round base period. Many developing countries could either not afford subsidies or had different policies at that time, with the consequence of having zero entitlements today. In fact, 97 per cent of amber box allowances accrue to countries of the Organization for Economic Cooperation and Development. Another example, on implementation, is that developed countries charge for non-agricultural products on average higher tariffs on imports from developing countries than from developed countries, which is due to the different composition of exports and the fact that developed countries tend to have higher tariffs on labour-intensive manufactures.

[5] There are some additional special and differential treatment provisions foreseen.

[6] For an overview of the current state of play in the negotiations on agriculture, see also UNCTAD (2007) and UNCTAD (2008).

[7] The G-33 is a group of developing countries led by Indonesia. The members of that group are the major proponents of the special products and the special safeguard mechanism for developing countries.

[8] Tiered formula: Bound tariffs are divided into different groups based on their initial values and subjecting each group to a different level cut. Higher tariffs are cut more than lower tariffs. For example, tariffs between 0 and 20 per cent are reduced by 30 per cent; tariffs between 20 and 50 per cent are reduced by 40 per cent and so on. See also box 2 below.

[9] The thresholds for the developing-country tiered formula and the cuts for each of the four tiers are identical. Furthermore, the proposed caps are identical. However, there is no statement by the EU on the additional feature of the G-20 proposal that developed countries should undertake cuts of at least 54 per cent and developing countries should undertake cuts of at most 36 per cent on average. There is no clear statement on tariff caps for sensitive products by the EU.

[10] Asked about the EU trade chief's remarks (before the slightly improved 54 per cent offer), United States Trade Representative Schwab said in the beginning of 2007, "I don't think we know where a landing zone is."

[11] Albania, Armenia, Georgia, Kyrgyzstan, Mongolia, the Republic of Moldova, Saudi Arabia, the former Yugoslav Republic of Macedonia, Tonga, Ukraine and Viet Nam are very recently acceded members or low-income RAMs with economies in transition.

[12] The approach used here for selecting SPs and SePs is to rank each country's tariffs according to the potential loss in tariff revenue and select the highest for exemption. Once selected, the treatment of sensitive products is as follows. One third of the formula cuts would apply to these tariffs in developed countries (with tariff rate quota (TRQ) expansion), and two thirds of the formula cuts in developing countries (without TRQ expansion). For special products, cereals, accounting for 2.3 per cent of agricultural tariff lines, were selected as exempt from any tariff reduction. An additional 9.7 per cent of tariff lines have been chosen as special products, taking the total to 12 per cent. To achieve an overall average cut of 11 per cent for special products, the 9.7 per cent non-cereals are reduced by 13.6 per cent.

[13] Even at the risk of confusing readers: The cut of the average tariff (see box 2), however, approximately meets the ⅔ principle: the average tariff in the EU, Japan and the United States, under the EU formula, for example, is reduced by 54 per cent, 69 per cent and 59 per cent respectively. The average tariff in India, for example, is reduced by 38 per cent, and that of Nigeria by 40 per cent. The reason for this result is that developed countries tend to have more dispersed tariffs, and thus the cut of the average is relatively higher than the average cut.

[14] For example, if A=82 and B=80; the new rates under the DMT formula are A_{new}= 47 and B_{new}= 50.

ANNEXES

Table A1

Average reduction of bound rates in SVEs (including «footnote 3 countries» from draft modalities text)

Full Name	G-20 formula without SeP, SP	DMT formula without SeP, SP	DMT formula with SeP and SP			Option average cut 24%	
			Initial bound	New bound	Average cut bound	New bound	Average cut bound
Albania	25.0	0.0	9.5	9.5	0.0	9.5	0.0
Antigua and Barbuda	35.1	32.1	105.0	73.5	29.8	79.9	24.0
Armenia	25.0	0.0	14.7	14.7	0.0	14.7	0.0
Barbados	35.9	32.8	110.8	77.7	30.2	85.1	24.0
Belize	35.0	32.0	101.1	71.1	29.7	76.9	24.0
Bolivia (Plurinational State of)	30.0	28.0	40.0	29.7	25.7	30.4	24.0
Botswana	29.2	27.1	38.2	27.3	20.0	25.1	24.0
Brunei Darussalam	-		40.4	32.3	22.0	31.7	24.0
Cameroon	30.0	28.0	80.0	59.4	25.7	60.8	24.0
China, Macao SAR	-	0.0	0.0	0.0	0.0	0.0	0.0
Congo	25.0	23.3	30.0	23.5	21.6	22.8	24.0
Cuba	29.8	27.8	37.3	27.7	24.5	27.9	24.0
Côte d'Ivoire	25.0	23.3	14.9	11.7	21.6	11.0	24.0
Dominica	36.2	33.2	112.2	77.8	30.5	85.6	24.0
Dominican Republic	29.5	27.5	39.5	29.5	25.2	30.1	24.0
Ecuador	25.8	24.0	25.6	19.8	22.3	19.2	24.0
El Salvador	28.9	26.9	42.2	31.3	24.8	32.0	24.0
Fiji	30.2	28.2	51.6	39.8	25.7	42.0	24.0
Gabon	30.0	28.0	59.7	44.4	25.7	45.4	24.0
Georgia	25.0	0.0	13.4	13.4	0.0	13.4	0.0
Ghana	34.8	31.9	97.2	68.0	29.8	73.8	24.0
Grenada	35.0	32.0	101.0	70.5	29.3	75.9	24.0
Guatemala	30.5	28.4	51.0	36.8	26.2	38.2	24.0
Guyana	35.0	32.0	99.6	70.0	29.7	75.7	24.0
Honduras	28.9	27.0	31.9	23.7	25.1	24.1	24.0
Jamaica	34.9	31.9	96.9	68.2	29.1	73.3	24.0
Jordan	25.6	23.8	23.7	17.8	21.9	19.0	24.0
Kenya	35.0	32.0	100.0	70.2	29.8	76.0	24.0
Kyrgyzstan	25.0	0.0	12.8	12.8	0.0	12.8	0.0
Mauritius	34.9	31.9	119.7	84.0	29.7	91.0	24.0
Mongolia	25.1	0.0	18.9	18.9	0.0	18.9	0.0
Namibia	29.6	27.5	40.6	28.9	20.2	26.8	24.0
Nicaragua	30.1	28.1	43.4	32.2	25.7	33.1	24.0
Nigeria	40.0	36.7	150.0	100.1	33.3	114.0	24.0
Panama	-		27.7	21.6	22.3	21.3	24.0
Papua New Guinea	29.1	27.1	48.1	35.9	24.9	37.9	24.0
Paraguay	29.5	27.5	33.2	24.6	25.5	25.0	24.0
Republic of Moldova	25.0	0.0	13.3	13.3	0.0	13.3	0.0
Saint Kitts and Nevis	35.3	32.3	108.6	75.8	29.9	82.7	24.0
Saint Lucia	35.4	32.4	114.6	80.1	30.1	87.2	24.0
Saint Vincent and the Grenadines	35.4	32.4	114.6	79.8	30.1	87.2	24.0
Sri Lanka	30.0	28.0	50.1	37.2	25.7	38.1	24.0
Suriname			19.9	15.6	21.4	79.7	-301.6
Swaziland	29.6	27.5	40.6	28.9	20.2	26.8	24.0
The former Yugoslav Republic of Macedonia	26.1	0.0	13.4	13.4	0.0	13.4	0.0
Trinidad and Tobago	34.4	31.5	89.9	62.8	28.2	67.1	24.0
Uruguay	29.3	27.4	33.9	25.3	25.5	25.7	24.0
Zimbabwe	39.0	35.8	139.6	92.4	32.4	104.6	24.0

Source: UNCTAD calculations, based on WTO CTS database.

* For RAMs that belong to footnote 3, cuts reduced by 10 percentage points and not 10+5 percentage points (uncertainty due to the overlap of provision in paras. 52 and 127).

Table A2

Average reduction of bound rates in developing countries

Country	G-20 formula without SP	DM formula without SP	DM formula with SP
Argentina	29.3	37.4	34.1
Bahrain	30.3	38.2	34.4
Brazil	29.4	37.4	33.4
Chile	25.5	33.8	30.8
China*	25.3	15.9	13.9
China, Hong Kong SAR	0.0	0.0	0.0
China, Taiwan Province of	-	-	11.2
Colombia	32.9	40.4	36.8
Costa Rica	29.5	37.5	34.0
Croatia*	25.6	18.3	15.7
Egypt	27.5	35.6	32.3
India	35.8	42.9	39.1
Indonesia	30.3	38.2	34.4
Malaysia	28.1	36.1	28.7
Mexico	29.4	37.4	33.9
Morocco	31.1	38.9	35.2
Oman*	26.3	23.1	21.3
Pakistan	34.4	41.5	38.3
Peru	25.1	33.4	30.4
Philippines	28.5	36.6	33.3
Qatar	25.9	34.1	30.6
Republic of Korea	28.0	36.0	31.5
Saudi Arabia*	25.3	0.0	0.0
Singapore	25.6	33.8	29.7
South Africa	29.6	37.5	33.1
Thailand	27.7	35.7	32.3
Tonga	-	-	0.0
Tunisia	35.5	42.7	38.8
Turkey	30.0	37.8	34.0
United Arab Emirates	-	-	30.9
Venezuela (Bolivarian Republic of)	30.2	38.0	28.1
Viet Nam*	26.0	0.0	0.0

Source: UNCTAD calculations, based on WTO CTS database.

* For RAMs, provisions in paragraphs 66 and 67 (see box 5) taken into account.