



UNCTAD
Commercial Diplomacy Programme

**RESEARCH AND TRAINING TOOLS
ON TARIFF PEAKS
AND OTHER RESIDUAL
TRADE PROTECTION**

**Geneva
April 2001**

**Division on International Trade in Goods
and Services, and Commodities.
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INTRODUCTION

This training and research "kit" aims at providing some basic guidelines and methodological instruments to analyse the origins, the nature and the impact of the specific measures of trade protection that continue to be maintained despite the trade liberalisation undertaken after the Uruguay Round, i.e. the "residual" high trade protection through measures such as the tariff peaks, tariff escalation, and some non-tariff measures that refers to specific traded items.

The residual trade protection encompasses an important range of measures with a broad impact on the market access of many goods and services. It constitutes a topic by itself with its own features like other aspects of the international and national trade policies. Like them, it relies on its own "political economy" stemming from the economic interests that explain, for instance, the existence of a tariff peak and the behaviour of policy-makers, negotiators and businessmen on determined traded items.

This "kit" does not pretend to provide solutions for the elimination of the residual trade protection, nor to provide an exhaustive inventory of measures that can be considered as a residual trade protection, because it would be impossible to establish a definitive definition of what is "residual", and even what is "trade protection". As shown through different examples and comments, objective as well as subjective considerations intervene in the formulation and the implementation of this kind of trade measures.

This "kit" rather aims at helping the understanding and the analysis, so that researchers and trainers are stimulated to introduce this topic in their activities on trade policies, political economy and trade negotiations. The instruments being presented here may also prove useful to parliamentarians, as well as the media.

Some elements of this "kit" go beyond the specificity of the residual trade protection and may be useful when approaching other political economy aspects of trade policies from a wider perspective. Last but not least, trade negotiators are also targeted users of these analytical instruments.

The research and training tools contained in this "kit" are organised in six sections: the first section provides some of the main examples of measures that may be considered as a residual trade protection in any country –developed or developing-. The second and third sections explore the methodological tools and some criteria that may be proven useful to identify the interests and the actors involved. The fourth section is devoted specifically to trainers that wish to organise a simulation of a trade negotiation based on a residual trade protection measure. Finally, two research papers are provided as examples of the kind of analytical work that should be done from the political economy perspective to enhance the understanding of the residual trade protection.

A. EXAMPLES OF RESIDUAL TRADE PROTECTION MEASURES

In the general context of trade liberalisation, residual trade protection refers to the measures targeting a specific item and representing an exception compared to the general level of trade protection applied to other items of the same sector, or to the general level of openness applied to the whole domestic market. In other terms, we are referring here to the measures that are not representative of the overall trade policy of a country.

In this context, the term “residual” indicates that these measures are the remaining protection after a general trade liberalisation has been adopted. However, even if they are an exception limited to specific items, the impact of these measures can be very large for the exporters of the corresponding items.

As explained in the next section, political economy reasons rather than pure economic criteria explain the exceptions represented by those measures.

The more frequent examples refer to tariff measures (particularly tariff peaks and tariff escalation). But other trade instruments such as the rules of origin, some standards, or measures applied to the trade in services can also be above the general level of protection applied by a country and therefore have an impact similar to a tariff peak.

An inventory of residual trade protection measures would include the following examples:

- *Tariffs on one or more specific items that represents a “peak” compared to the average tariff level of the country.*

Tariff peaks are particularly frequent in the agricultural sector in both developed as well as developing countries and economies in transition. Dairy products, such as milk or cheese, have *ad valorem* rates of above 200%. Sugar and rice frequently appear in the national tariffs with an extremely high protection. Other recurrent examples refer to milk powder (skim and whole), butter, meat (beef and pig), wheat, barley.

A recent OECD analysis of market access for agricultural trade notes that there is “*a relatively large dispersion in the protection provided to the various commodities*”, with the largest protection to the dairy products. “*The average tariff for whey powder at 226% is almost double the average of the next highest tariff. Three dairy products –butter, whole milk powder and whey powder, have average tariff rates exceeding 100%. Other products receiving above average protection –with average tariff that exceed the average of all products – are wheat (73%) and coarse grains (64%).*”¹

Higher than average tariffs for industrial products can also be found in various countries’ schedules for products such as footwear (more than 300%), and textiles and vehicles (between 100% and 299%).²

¹ OECD, *An Analysis of Market Access Issues in OECD Agricultural Trade*. Directorate for Food, Agriculture and Fisheries, Committee for Agriculture. AGR/CA/APM/CFS/MD(2001)2, 21-Dec.2000, p.8.

² See Annex 1, UNCTAD/WTO, “ The Post-Uruguay Round Tariff Environment for Developing Countries Exports. Tariff Peaks and Tariff Escalation”, Geneva, UN, TD/B/COM.1/14/Rev.1, January 2000.

➤ ***Tariff peaks in the context of quota tariffs and non-tariff measures.***

Particularly for agricultural products, as well as textiles and apparel, tariff peaks should not only be considered in isolation, but also in the context of the implementation of the tariff rate quotas (TRQs) provided for in the Agreement on Agriculture. More than 1300 TRQs have been notified to the WTO. Tariffs can be applied within or outside the quotas (in-quota and out-of-quota).

Furthermore, the range of instruments that could be used under this heading to provide protection to domestic industries is large. It is also diverse in the sense that they may be fiscal, quantitative, involving monitoring and sophisticated administrative procedures. They include, for instance:

- seasonal quotas, such as those applied to food staples that are produced in different periods of the year depending on the latitudes;
- import authorisations or non-automatic licensing;
- voluntary export restraints;
- minimum pricing or price surveillance, like the entry price system;
- some custom valuation procedures.
- Unbound tariffs.³

A recent WTO panel that considered the United States claims against Korea's requirements on imported beef⁴ provides examples of specific non-tariff measures that were ruled as inconsistent with the WTO obligations (art.XI:1 of the GATT 1994, art.4.2 of the Agreement on Agriculture, and art.1 and 3 of the Agreement on Import Licensing Procedures), such as the establishment of minimum import prices and delay of both invitations to tender as well as quota allocations. The same Panel also determined that the Korean's requirement to sell imported beef in separate displays, with specific signs and additional labelling requirements is inconsistent the provisions of art.III:4 of the GATT 1994.

Referring to tariff peaks in the context of quota tariffs, the OECD analysis quoted above indicates that *“average in-quota tariff rates are substantially lower than the out-of-quota rates and lower than the average tariff on products outside the TRQ regime. But, with an average of about 20%, in-quota tariff rates are not trivial. Rather, they represent a significant hurdle which may be one of the reasons for the relatively low fill rates (...). But, the tariff on potential imports outside the quota is extremely high, averaging 148% at the end of the implementation period. (...) the gap between the in-quota and out-of-quota tariffs is tremendous, greatly reducing the possibility of out-of-quota imports. (...) Whey powder is in a league by itself, with an average out-of-quota tariff of about 600% while butter is almost 300%.(...) on average, the difference between in-quota and out-of-quota rates is 124%, with the largest gap (580%) for whey powder and the smallest (30%) for pigmeat.”*⁵

³ Finger, M. et al “The Uruguay Round: Statistics on Tariff Concessions Given and Received”, Washington, The World Bank, 1996.

⁴ WTO, Korea - Measures Affecting Imports of Fresh, Chilled and Frozen Beef - AB-2000-8 - Report of the Appellate Body, Geneva, WT/DS161/AB/R and WT/DS169/AB/R, 11 December 2000.

⁵ *Ibid.*, p.7. The OECD document notes that *“preferential quota allocations and preferential tariffs are not included. While this may influence results for specific countries, it should not affect the overall outcomes, as preferential quotas represent only a small share of world trade for highly homogeneous products traded in competitive markets.”*: *ibid.*, p.10.

The following table shows some tariff peaks in the context of quota tariffs in OECD countries:

AVERAGE TARIFF IN 2000 BY IN, OUT AND NON-QUOTA PRODUCTS⁶

	In-quota	Out-of-quota	No-quota
coarse grains	15.59	271.69	22.06
Wheat	13.20	180.31	24.64
rice	10.14	108.47	21.67
beef	21.89	96.77	22.87
pigmeat	27.36	57.70	42.06
sheep meat	5.48	60.24	6.45
butter	38.59	286.15	44.52
cheese	23.47	107.59	37.39
skim milk powder	17.10	182.82	51.65
whole milk powder	21.15	236.75	67.96
whey powder	14.46	596.56	130.26
<i>ALL</i>	19.98	148.83	29.38

Source: OECD, AGR/CA/APM/CFS/MD (2001), 2000 p.9.

➤ ***Tariff escalation.***

A tariff escalation is a system of protection whereby the greater the degree of processing that a commodity undergoes, the greater the levels of protection that are applied to it in the form of a tariff. This system provides effective protection to domestic producers engaged in value added processes. It aims at discouraging supplying countries in developing a resource based industrialisation.

⁶ OECD, *ibid.*, p.9, table 3. The tariff profile for selected countries and commodities are base on MFN rates found in their countries' schedules. Selected countries included Argentina, Australia, Canada, European Union, Hungary, Japan, Korea, Mexico, New Zealand, Poland and US.

Examples of tariff escalations on cocoa items (% tariff rates):

	Cocoa beans	Cocoa butter	Powder w/o sugar	Powder with sugar	Chocolate
European Union	1 (GSP=0)	9 (GSP=6.3)	10.7 (GSP=3.7) (ACP=0)	*(a)	*(b)
Japan	0	0	15.8 (GSP=10.5) (LDC=0)	31.5	16.7
South Africa	0	0	0	20	20

*(a) rates depend on sugar content

*(b) rates depend on sugar and other contents

Source: UNCTAD TRAINS.

➤ ***Sanitary, phytosanitary or technical standards or requirements.***

Despite the disciplines introduced by the Uruguay Round agreements, many sanitary and phytosanitary, and technical standards can represent an obstacle to trade when they respond to residual trade protection objectives. Similarly, the precautionary principles provided for in the SPS and TBT agreements can also be used as a way to hide trade protection objectives instead of a genuine sanitary protection goal.

Measuring the trade effect of sanitary and phytosanitary standards is particularly complex as it is to find a balance between the regulatory costs sustained by exporters with the possible gains in higher sanitary and phytosanitary levels attained by the importing countries. For instance, the sanitary requirements imposed by a group of countries on the imports of a determined fish have extremely high costs for the exporting countries, while the sanitary risk is extremely low for the importing countries.

➤ ***Rules of origin.***

Some rules of origin are so excessively stringent that they represent a market access barrier more efficient than a high tariff. In some cases, they target a specific, well-identified item, therefore providing a clear example of a residual trade protection.

Rules of origin are particularly important in the preferential trade regimes in favour of developing or least developed countries, where tariffs have been eliminated or significantly lowered compared to the MFN treatment.⁷ Therefore, a stringent rule of origin, applied unilaterally within the rules of each preferential regime given by a developed country, can have the same impact as a tariff peak.

Usually, as in the case of the implementation of tariff quotas or seasonal quotas and similar non-tariff barriers, the administrative procedures to implement these rules of origin are costly –from the point of view of the importing country-, and complex –from the point of view of the exporting country. The benefits of the trade preferences may be hampered by rules of origin that cannot easily be understood and fulfilled by the exporters. The situation is even

⁷ See UNCTAD, Options for Improving Market Access for LDCs in the QUAD countries (Forthcoming).

further complicated by the fact that each preferential regime has its own rules of origin, with its own criteria. Sometimes, as in the example below, the criteria to determine the origin of a product refer to the nationality of the ships used for its transportation rather than the nationality of the inputs of the product.

For instance, in one of the generalised system of preferences (GSP), the rules of origin for fish and fish preparations provide that only goods “wholly obtained” can benefit from preferential treatment. In order to be considered as “wholly obtained” in a beneficiary country, the vessels and factory ships used in sea fishing must comply with a detailed series of conditions related to ownership of the vessels and to the nationality of managers and crew, who have to be nationals of the beneficiary country or of the country(-ies) that gives the preferential treatment.

➤ ***Exceptions to trade preferences for developing countries.***

All preferential regimes for developing countries exclude some “sensitive” items (such as textiles and apparel, leather products, agricultural products) that usually coincide with those that are protected through some kind of high tariff or non-tariff measure in the MFN treatment. Usually, for these sensitive items, the GSPs provide for quotas or for tariffs lower than the MFN tariffs in favour of the beneficiary countries.

In other words, the residual trade protection implemented in the GSPs for the items considered as “sensitive” is lower vis-à-vis the imports coming from developing countries compared to the protection applied in the MFN regime. That can be explained because the competition represented by developing and least developed countries is perceived as less important for domestic producers, but not totally absent.

Therefore, the product coverage of preferential regimes needs to be assessed in this context. The proposals discussed before and after the WTO Third Ministerial Conference at Seattle that provided for duty free/quota free market access for “essentially” all products of LDCs implied that the product coverage of the proposed preferential regime included some exceptions for the “sensitive” items. Similarly, the recent European Commission proposal on free market access for LDCs products called “Everything but Arms” provides for a special schedule of liberalisation for the imports of rice, bananas and sugar.

All preferential regimes applied by developing countries in favour of LDCs show similar residual trade protection through the exceptions imposed on determined items.

➤ ***Residual trade protection in services.***

In so far as the national schedules of commitments agreed in the framework of the General Agreement on Trade in Services can be compared to national tariff regimes, they also show specific trade protection for services that are perceived as “sensitive” for the importing country.

Many exceptions to the MFN treatment for specific services follow into this category. But the main exception to the general trend of liberalisation of trade in services refers to the lack of commitments in the mode 4 (movement of natural persons), showing that the mode rather than the service *per se* raises sensitive issues in the importing country.

The lack of commitments on mode 4 can equally be found in developed as well as developing countries' schedules of commitments. Sophisticated procedures and requirements for the qualifications of some professional services (for instance nurses, designers, engineers) can have a trade impact similar to a stringent rule of origin in the case of goods.

B. THE POLITICAL ECONOMY OF RESIDUAL TRADE PROTECTION.

This section aims at providing to the researchers some guidelines on the methodological tools required to identify and to understand the roots of the residual trade protection measures such as those mentioned above, both in his own country as well as in the trading partners. The rationale for residual trade protection is basically the same in any country, whatever may be its level of development, but it is obvious that the impact on the trade flows and on the market access may differ, depending on the relative importance of the goods or services involved.

International trade policy is quintessentially a multidisciplinary area and analytical tools and approaches in any political economy issue should not be confined merely to the “economic” or “political”. Economic indicators, equilibrium models (which are particularly useful for analysis of the impact of tariff peaks, for instance), econometric calculations and simulations, and other analytical economic instruments need to be combined with political considerations. Quantitative data regarding, for instance, the contribution of a particular sector towards domestic output need to be considered alongside qualitative judgements regarding the significance of the sector in the trade-related decision making process.

Determining, therefore, the sensitivity of a tariff reduction, the scope of a trade measure, and/or the margin of manoeuvre available to a negotiator requires the use of analytical tools of various disciplines: international trade, macro and microeconomics, econometrics, sociology and political science.

The purpose of adopting such a multidisciplinary approach is to provide the trade negotiator and policy-maker with a better understanding of the precise mix of economic and political factors that determine both domestic sensitivities and those of his trading partners.

Trade negotiations and policy making are not precise arts. The trade negotiator and the policy-maker need to interpret data in an evolving context, which can and does unfold as negotiations are under way. Equally, from the political economy point of view, analysis on future trends and scenarios are at least as important as data on the current situation.

B.1- THE ECONOMIC ORIGINS OF THE RESIDUAL TRADE PROTECTION.

The impact of trade liberalisation on the interests of local firms (at the individual level as well as for economic sectors as a whole) is a political challenge for all countries for all countries, developing or developed. The adoption of the Uruguay Round radically changed the conditions under which the trade protection can be formulated and applied by policy-makers. The general reduction of tariff levels and the prohibition of virtually all forms of non-tariff barriers had therefore great implications for the domestic firms that relied on such instruments to protect themselves against external competition and that were widely implemented by governments all around the world. In spite of the trade liberalisation that characterizes current trade policies, one of the traditional sticking points regarding trade policy-making and trade negotiations continues to be the use of these trade measures to protect specific domestic firms.

This situation arises when a poorer country becomes successful in exporting a good that was “*just marginally competitive in the richer one, causing those industries there to contract and shut down. Someone there will necessarily lose, the identity of the losers depending on the mobility of factors. If in the short run factors are industry specific, then those industry-specific factors in the declining industries will find their livelihoods undermined by trade with the advancing developing world. If instead factors are mobile across industries, then the shifting fortunes of industries based on factor intensities will cause the relatively scarce factors in the developed world to suffer decline in real wages. Either way, then, someone is worse off, and they can be expected to resist this change by lobbying for protection. If they get it, market access for the growing developing world will be curtailed.*”⁸

Therefore, the perceived need for a high tariff or a non-tariff measure that protects the domestic market in favour of a firm appears when there is a lack of factor mobility in the importing country, and when the trade policy-maker decides to introduce this kind of measures to protect the “loser firm” – even if he is aware that the trade protection introduced will not improve the lack of factor mobility that originates the problem.

The same reasoning applies for developing countries compared to least developed countries, when the latter improve their export capacity and threaten the declining industries of the former. In all countries, similar political economy reasons explain why policy-makers accept to introduce residual trade protection for the “losers”, even if the ways and means of lobbying and the nature of the measures adopted may differ among countries.

The perceived need for the trade protection is also generated by the difference between what is labour-intensive and what is capital-intensive: “*growth through capital accumulation expands the poor country’s capacity to produce what for it are capital-intensive goods. But these same goods are at the labor-intensive end of the spectrum in the developed world, and the effect is thus to lower incomes in those labor-intensive industries. Because the effect is felt unevenly in the developed world, the pressure for protection is arguably larger than it would have been if spread more thinly across the whole population. And it also tends to be the poorer groups within the rich North that feel this effect, which increases even more the incentive for protection as a social policy. (...) If there are many countries, (...) and the very poorest countries may stimulate protection not in the richest but only in some just a bit less poor than they. Wherever a country lies in the path of economic development, for it to move ahead it must tread on the heels of those ahead of it, and those heels are likely to kick back, using trade protection, and make progress more difficult.*”⁹

⁸ Deardorff, Alan V., *Market Access for Developing Countries*, Paper presented at the Center for Business and Government, Harvard University, June 2000.

⁹ *Ibid.*, p.5.

B.2- THE ROLE OF DOMESTIC CONSTITUENCIES IN RESIDUAL TRADE PROTECTION.

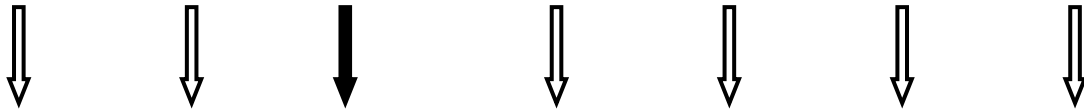
For a policy-maker, the sustainability of almost any trade reform depends on the successful management of the reform from the point of view of the political economy. Analytical tools, such as impact studies, should help to reveal by how much tariff protection may be reduced without provoking serious socio-economic damage to individual firms or to economic sectors, and without disrupting the political equilibrium that sustains the trade policy. Yet, the policy-maker must also anticipate the use, by certain economic actors, of sufficient political influence and lobbying to bring about a shift in his trade policy.

Therefore, analyses that provide insights from the political economy perspective will enhance the policy maker's assessment of the best course of action to take when formulating the national trade policy.

The range of domestic constituencies that may bring some influence to bear on the formulation of the national trade policy may potentially encompass all sort of actors: from the public opinion as a whole to the trade unions, or from political parties to the transnational interests. Each one has its own position and goals regarding the trade policy, and each one may be lobbying the policy-maker to obtain measures corresponding to its goals. For instance, the exporting firms may support a lowering of trade barriers so as to obtain similar conditions in foreign markets. On the opposite, some trade unions may be in favour of tariffs or non-tariff measures to protect the domestic firms that generate employment. Non-governmental organizations may represent a variety of interests, in favour or against an open trade policy, and their influence can greatly differ depending on the country, the circumstances, and their internal or external allies.

It may be assumed that all actors in the domestic constituency are interrelated and influence each other's positions to a greater or lesser extent. It is also commonly assumed that the occurrence of a tariff peak is an indication of domestic firms with a determinant position in the overall domestic constituency, and with a lobby capacity on the policy-maker more convincing than the influence of other actors.

DOMESTIC CONSTITUENCY OF COUNTRY X:



In this context, the policy-maker will consider, for instance, the following economic, legal and political elements when assessing the lobby made by the domestic producer firm:

- the current and potential competitiveness of the firm, i.e. the economic rationale of the residual trade protection;
- its importance in the overall domestic economy and its role in the support to the national trade policy;
- the capacity that the firm may have in mobilizing other social and political actors in favour of its arguments, at the national and the international level;
- the regional and multilateral commitments of the country regarding trade measures;
- the general level of trade protection being implemented at the country-level.

In the trade negotiations, the position of country X aiming at preserving the residual trade protection will be based on similar elements. However, the trade negotiator of country X will also have to consider that in order to defend the residual trade protection (that represents a contradiction compared to the general level of openness of its domestic market), he may be asked to pay a “price” to the trading partner(s). At this stage, the negotiating capacity of the country X will be determinant to minimize the value of the concessions or trade-offs that may be requested by the trading partner(s).

Therefore, when deciding to implement a targeted trade protection such as those mentioned in the previous section, both the policy-maker and the trade negotiator of country X need to assess the economic and political costs and benefits of two decisions: (i) the maintenance to a specific trade protection for a domestic firm whose competitiveness may be declining in the international market; and (ii) the concessions or trade-offs that the country may be asked to give to its trading partner(s) in order to maintain the residual trade protection.

From the point of view of country Y, which is a trading partner of country X, the situation regarding the residual trade protection is seen as in a mirror: the trade negotiator of country Y has the mandate to obtain the elimination or the lowering of the trade protection of country X. In exchange to the elimination of its trade protection, country X may request some concessions to country Y. As previously noted, the value of the “price” to be paid either to

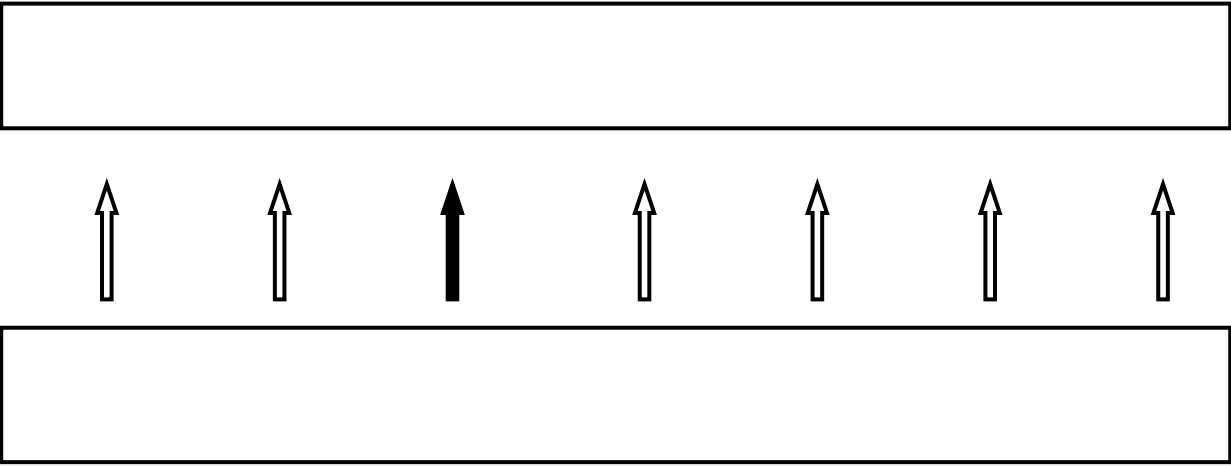
maintain the trade protection or to obtain its elimination will depend on the negotiating capacity of the trading partners and on the overall context of the negotiation.

For instance, in a multilateral context where it is being agreed that *all* residual trade protection of all countries will be dismantled, the negotiating capacity of an individual country has to be assessed in a different way, and the value of the concessions may change because of possible wider trade-offs. From the point of view of the negotiating strategy, the scope of potential agreement on the dismantling of the residual trade protection will vary depending on the bilateral or multilateral nature of the negotiation.

Similarly, in a context where a multilateral preferential regime for all the LDCs is being discussed, the relevance of an individual trade measure will be seen in the context of the multilateral cooperation with LDCs. The role of the domestic constituencies will also be affected by the context where the residual trade protection is being discussed: the lobby of a domestic firm to maintain the trade protection may be more influential in the context of a bilateral negotiation than in a multilateral forum. However, no general assumptions nor forecasts can be made in this regard.

In the domestic constituency of country Y, the exporting firm(s) play a determinant role in supporting a negotiating position that targets the trade protection of country X. But other domestic actors of country Y may also be interested and supportive, such as the trade unions linked to the exporting firms, or the political parties that advocate for trade liberalisation.

DOMESTIC CONSTITUENCY OF COUNTRY Y:



When preparing its negotiating strategy, the trade negotiator of country Y will take into account, for instance:

- the importance of the residual trade protection of country X from the point of view of the exporting goals of country Y;
- the importance of the residual trade protection of country X from the point of view of the political economy of country X, i.e., the economic and political role of country X's protected firm(s);
- the scope of the negotiating capacity he may have to achieve his goal of dismantling or eliminating country X's measure;

- the potential concessions he may be requested to give in order to achieve its goals, as well as the concessions he will ask to country X in case the residual trade protection will not be removed;
- the alliances with other trading partners to support country Y's negotiating goals, particularly in a multilateral context;
- the actors of the domestic constituency of country X that are opposed to the residual trade protection and that may support country Y's goals;
- the economic rationale behind the residual trade protection of country X, in order to identify the weak points of country X's argumentation.

It is worthwhile noting that country Y may find external allies –both in the domestic constituency of country X as well as in other countries or among transnational NGOs- in favour of the dismantling of the residual trade protection of country X. Likewise, the domestic firm of country X may be able to find “allies” in other countries in order to enlarge its political pressure on the policy-makers and negotiators. Nowadays, the transnationalization of non-governmental organizations may lead to various cross-border and cross-sectorial alliances. It is therefore quite difficult to foresee the evolution of lobbies regarding trade policy issues. Section D provides other analytical tools for the identification of the protected firm's interests and strategy¹⁰.

¹⁰ “Syllogism: the political economy of differentiation”, and “Varying paths in the product cycle and an industry's policy preferences”, in Craig VanGrasstek, *The Political Economy of Residual Trade Protection*, unedited version, Washington 2000.

C. CRITERIA TO BE CONSIDERED WHEN ANALYSING THE POLITICAL ECONOMY OF ANY TRADE POLICY AND ANY TRADE NEGOTIATING STRATEGY

There are many similarities between the analytical tools needed to identify the interests that sustain the residual trade protection and those needed to understand the political economy of any trade policy in general. In both cases, a “mix” of economic and political science instruments help to the fine-tuning of the research work, and provides to the negotiator a better understanding of the trading partner’s objectives.

The analysis of trade policies and negotiating strategies is useful for both the policy-maker and the trade negotiator: the former needs to identify the domestic sensitivities that may undermine the sustainability of its trade policy; similarly, the trade negotiator needs to know the sensitivities of the trading partner to avoid a negotiating strategy that aims at unrealistic goals.

Bearing in mind this “mix”, the main criteria to be considered when analysing the trade policy and negotiating strategy of any country (developed or developing) can be grouped in two categories:

- **The economic (quantitative) indicators**, i.e. the tools that identify the economic interests of the firms or the productive sectors concerned, their economic sensitivity and their capacity to adjust to changes introduced by the trade liberalisation. In this category, the indicators are usually quantitative (statistical data concerning the evolution of import and export flows in the relevant good(s) and service(s); data concerning the productivity of a firm; the number of employees in an exporting sector; competitiveness indicators; factor mobility, the role of domestic and foreign capital, etc.).
- **The political (qualitative) criteria**, i.e. the tools that can determine the capacity of a firm, group of firms, or a productive sector to influence a government’s or trade negotiators’ decisions. These criteria are usually subjective, in the sense that the researcher has to interpret them, and generally “hidden”, in the sense that they require a good knowledge of the domestic political system to be identified. The ability of a firm to lobby successfully in favour of its interests is not simply determined by considering its importance to the domestic economy as a whole. Small local firms may be more effective at defending their interests than transnationals firms. The ability of an economic sector to influence the governmental decision-making process may be disproportional to its actual economic importance. Other qualitative indicators fall into this category, such as the degree of awareness of the WTO commitments and the perception of their implications at the level of local firms.

The following is a general overview of the kind of criteria that need to be considered in order to arrive at an accurate analysis of the political economy of a trade policy or a trade negotiating strategy.

➤ ***The economic criteria***

The objective being to determine the economic rationale of specific trade interests, the analysis should incorporate at least some of the following data:

- The likely impact on the exports and/or imports of the firm or the sector concerned of the proposed trade policy and negotiating position.
- The new trade opportunities that will be generated by the envisaged trade policy or negotiation in terms of market access for exports, as well as the effects on investment and technology flows.
- The trade diversion vs. trade creation effects brought about by a change in the level of a tariff, for instance, or by the introduction of a non-tariff measure.
- The level of competitiveness of the firm(s) or sector concerned by the trade policy, and the impact of the trade policy on the competitiveness level.
- The degree of influence of the firm or the sector concerned over the domestic or the international price formation.
- The level of the domestic and foreign indebtedness of the firm or the sector concerned.
- The alternative trade measures that may be envisaged to offer a “compensation” or to facilitate the adjustment of the concerned firm (for instance, anti-dumping rules, fiscal incentives, domestic support, investments, etc.).

➤ ***The political criteria.***

The objective being to identify how (and if) the trade interests can be channelled through the trade policy and negotiating decision-making, criteria such as the following may be considered:

- The historical background and the influence exerted by the firm or the sector concerned in the political system of the country.
- The capacity of the firm to mobilise other economic and political actors, within or outside the country, in favour or against the envisaged trade policy.
- The links between the firm or the sector and the local trade unions (in many countries, the trade unions of some economic sectors such as the automotive may act as leaders of the whole national working class).
- The nature of the firm and the sector concerned in terms of size and potential links with transnational interests.
- The extent to which the geographical concentration of the firm or the sector concerned may influence the decision-making process on the trade policy.

- The capacity of the firm or the sector concerned (through a private sector association, for instance) to be involved in trade negotiations by providing reactions and proposals to the government trade officials.
- The perceived impact of the trade policy and negotiations by the firm or the sector concerned, that may be as important as the real economic impact. The information provided by the media and by the interest groups may be intentionally or accidentally misleading and can generate unjustified, yet effective, political pressure on policy makers and trade negotiators.

D. ELEMENTS FOR THE DESIGN OF A TRAINING SIMULATION EXERCISE ON NEGOTIATIONS ON RESIDUAL TRADE PROTECTION

The simulation of a real decision-making process or a trade negotiation (bilateral, regional, or multilateral) is a useful training tool that complements a theoretical understanding of trade measures. It is a particularly efficient means of examining the political economy dimension of trade policies, especially if trainees are used to be confined to purely economic analyses where qualitative criteria are usually absent.

Simulation exercises provide a better understanding of the residual trade protection issues and help formulate an appropriate trade policy and negotiating position. Two main processes can be simulated:

- **The domestic decision-making process on the adoption of a residual trade protection (a tariff peak, for instance):** the simulation may consist of a ministerial cabinet where the decision to maintain or to remove the tariff peak has to be taken. Based on individual instructions and on the information regarding the relevant economic data, certain trainees assume the role of government ministers (e.g. trade, finance, development), while others take the role of non-governmental actors and private sector representatives.
 - **The negotiation with one or more trading partners regarding the elimination of the residual trade protection (tariff or non-tariff measures in order to adopt a preferential regime for developing countries, for instance):** the trainees should receive the information regarding the countries (real or imaginary) that they will represent, as well as the instructions regarding their negotiating goals.
- *Some pre-conditions required for a successful simulation exercise:*
- Trainees need to be fully aware of the scope, the implications and the nature of the residual trade protection that is being considered from the point of view of both the importing and the exporting country.
 - The instructions need to include meaningful quantitative and qualitative information (either replicating real situations, or using imaginary countries inspired by real situations), a description of the economic and political factors that are relevant for the instance of residual trade protection being considered, as well as an overview of the economic and trade policy of each country (the degree of economic openness, the existing trade commitments, the priorities in terms of export goals, etc.).
 - The instructions must emphasize the need to achieve a politically and economically sustainable outcome. For instance, for some highly sensitive goods, it is unrealistic to think that the tariff peak will be immediately eliminated to reach the average level of tariff protection of the sector. The trainees should be encouraged to explore imaginative solutions regarding the trade-offs that could be envisaged in this kind of trade negotiations. They should also consider what kind of international mechanisms should be put into place to monitor the implementation of a preferential regime that eliminated all quotas and non-tariff barriers, for instance.

- The instructions to the trainees could spell out the concessions that they are allowed to make during the negotiations without jeopardising national trade goals. Alternatively, they could be allowed to decide this for themselves and an assessment of the political and economic costs of their concessions would then be provided at the end of the exercise.
- The trainees need to understand the scenario of the simulation exercise as well as their instructions in advance so as to be able to fully assume their roles and defend the arguments for or against the trade measure. It is important for the trainees to assimilate the idea that being a good policy-maker and a negotiator is as much a matter of grasping the political and technical issues at stake as it is possessing good negotiating skills.

➤ ***Conditions to be fulfilled during the training simulation exercise:***

- The organizers – and particularly the “chairman” in the case of a simulated negotiation- need to keep in mind that the main objective of the exercise is to provide greater insight into the issue of the selected trade measure rather than to reach a pre-determined decision or agreement: the trainees should feel free to arrive at an outcome that has not been planned in advance.
- From the point of view of the training, the role of the chair-person should be to lead the exercise as close as possible towards an outcome that is likely in a real situation. Therefore, the best trainer for the simulation exercises would be a practitioner: a trade official who knows the background of the issue concerned; a diplomat who has been involved in similar negotiations; a businessman who has been a trade policy-maker or a negotiator, etc.

At the end of the simulation exercise, it is important for the trainers as well as the trainees to reflect on the process and the outcome of the exercise. The trainers should analyse how the economic and political factors were taken into account; how participants behaved, and how well they assumed the role they were given, the involvement of the various interest groups; the costs and benefits of the final decisions or agreements from the point of view of the individual country(ies) concerned; the alliances between different interest groups or countries made during the process, etc.

ANNEXES

1. [THE POST-URUGUAY ROUND TARIFF ENVIRONMENT FOR DEVELOPING COUNTRY EXPORTS: TARIFF PEAKS AND TARIFF ESCALATION](#)
2. [EXTRACTS FROM: THE POLITICAL ECONOMY OF RESIDUAL PROTECTION IN THE TRADE REGIME OF THE UNITED STATES OF AMERICA \(CHAPTERS 1 AND 5\)](#)
3. [EXTRACTS FROM: MERCOSUR AND THE WTO NEGOTIATIONS IN AGRICULTURE: A FIRST ROAD MAP](#)