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My Dear Margaret

During our recent conversations in London, I promised that I would have prepared for you a paper highlighting the significance for developing countries of protectionism, including an assessment of the contribution of the recent MTN.

The enclosed paper does just that. I think you will agree with its central message that the issue remains a very live one and of significant concern to us all, whether developed or developing. Indeed I believe the analysis set out in this paper to be sufficiently important that all of our colleagues attending the CHOGM meetings in Melbourne should receive a copy, and I am taking steps for it to be distributed to them in the near future.

I look forward to hearing of your reactions to the analysis, and to our forthcoming meetings in Australia.

Yours Sincerely

Malcolm Fraser

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THE IMPACT OF PROTECTION ON DEVELOPING COUNTRY TRADE

SUMMARY

1. The trade of developing countries with developed countries, both for industrial goods and for agricultural products, suffers from protectionist attitudes of major developed countries.

2. Contrary to popular opinion, the Tokyo round of MTN conferred only limited benefits on developing countries.

3. Agricultural protection, because it is so extensive and because agricultural trade is so important, seriously affects the growth and development prospects of most developing countries.

4. There are potentially significant gains to developed countries, as well as to the developing countries themselves, from further trade liberalisation - especially, but not exclusively, in relation to agricultural products.

A. OUTCOME OF THE TOKYO ROUND OF MTN

(i) Tariffs and Developing Countries' Trade

The MTN was regarded as successful in reducing trade barriers, especially in relation to industrial tariffs. However, while substantial reductions were achieved, the benefits fall unevenly. In particular, GATT studies have shown that the average tariff reduction on industrial products of export interest to developing countries was less than the overall average reduction - namely, about one quarter compared with one third.

This undoubtedly stems in large part from the greater component of so-called "sensitive" products in the export mix of developing countries. Nevertheless, the end result is that in the post-MTN situation, tariff averages on industrial products of export interest to developing countries are about 20% higher than the tariffs on all industrial products (i.e. 5.7% versus 4.7%).

Thus, even in the context of industrial tariffs, where the record of major developed countries in liberalising trade is at its best, developing countries are still significantly disadvantaged.

(ii) Non-Tariff Barriers, Codes of Conduct and Developing Countries

The range of non-tariff barriers (NTBs) is much more extensive than those identified in the MTN. For example, voluntary export restraint and variable levies were never discussed there, though they rightly comprise part of the list of NTBs assembled by UNCTAD.

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The MTN attempted to deal with non-tariff barriers through the negotiation of Codes of Conduct aimed at achieving stronger discipline especially on subsidy and other similar practices. In fact the Subsidies Code largely ignored problems of agriculture; and in relation to industrial produce subsidies, the Code discriminates heavily against developing countries since their main subsidy practices are outlawed, while those of the US, the EC and Japan (who together drafted the Code) are effectively exempt.

B. AGRICULTURAL PROTECTIONISM

Of fundamental importance for developing countries is the lack of progress in liberalising trade in agricultural products.

For example, MTN concessions covering products exported by developing countries to nine of their largest markets (Austria, Canada, E.C., Finland, Japan, Norway, Sweden, Switzerland and the U.S.) covered nearly $40 billion worth of traded goods - but only $12 billion of that total represented agricultural products. And while the MTN reduced, overall, the weighted average tariff on industrial products from 7.0% to 4.7%, the average level of tariffs, non-tariff barriers and subsidies on agricultural products, processed and unprocessed, is almost 70% in the EC, 80% in Sweden and a little over 100% in Norway and Switzerland. For industrial countries as a whole agricultural protection is more than <u>three times</u> that on industrial products.

In this context, UNCTAD has examined the variable levies applied by the EC and has concluded that in some cases the level of protection they afford reaches 500%.

C. SPECIFIC EFFECTS ON DEVELOPING COUNTRIES OF AGRICULTURAL PROTECTION

Agriculture is the largest sector of developing countries' economies, typically accounting for 30% to 40% of their GDP. This is generally two to three times more than the share of industrial production. Agricultural exports often provide between 50% and 80% of their foreign exchange earnings and between 50% and 90% of the labour force in developing countries work in agriculture.

With this in mind, a number of studies have demonstrated that there could be considerable and specific gains for developing countries by removing or diminishing agricultural protection.

(i) A joint <u>UNCTAD/FAO</u> study in 1972 estimated the gains in export income to developing countries of removing all barriers to their agricultural trade could be 17 billion 1972 dollars annually (equivalent to about 34 billion in 1981 dollars)

(ii) The WORLD BANK in 1977 identified nine key agricultural commodities (beef, fresh vegetables, sugar, maize, wine, rice, bananas, vegetable preserves and coffee) where full trade liberalisation could yield developing countries by 1985 a gain in export returns of 5.2 billion 1975 dollars (equivalent to some 8 billion 1981 dollars).

(iii) The INTERNATIONAL FOOD POLICY RESEARCH INSTITUTE in 1979 estimated that even a 50% reduction in agricultural trade barriers covering some 46 products could increase developing country export receipts by 30% or 3 billion 1977 dollars (a little over 4 billion in 1981 dollars).

In all of these cases, the final impact on the level and the growth of GDP in developing countries would be considerably larger - because of the multiplier effects of increased export incomes; and because of the increased ability of developing countries to meet the foreign exchange costs of imports of equipment and/or materials necessary to sustain and increase their productive potential.

The short-term costs to developed countries from allowing increased import penetration would be at least in part offset by reduced domestic prices of both imports and import substitutes; and the developed countries would also benefit from growing world trade, including expanded markets in developing countries for developed countries' exports.

CONCLUSIONS

1. Significant barriers, both tariff and non-tariff, exist against agricultural and industrial exports of developing countries.

2. The MTN settlement overall provided few gains for developing countries compared with those for developed countries, and in the case of some Codes of Conduct actively discriminated against them.

3. Agricultural protectionism, which is especially disadvantageous to developing countries, continues at exceptionally high levels and is not being seriously addressed.

4. Specific studies have shown that national income and foreign exchange earnings of developing countries could benefit significantly if agricultural protectionism (both in terms of product coverage and protective impact) could be eliminated or even partially reduced.

5. Long term gains to developed countries themselves would also ensue from any liberalisation of barriers to trade with developing countries. Developing countries would be in a position to buy more from developed countries; cheaper sources of goods would become available in developed countries, thereby reducing inflationary pressures; and resources could be allocated from import competing industries into more efficient uses in developed countries, resulting in higher production and incomes. The benefits of trade liberalisation to both developed and developing countries would clearly be substantial.