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The tide of free trade will not float all boats

By ARVIND PANAGARIYA

Thanks to the advocacy of a few pressure groups and many international institutions, there is now a near-universal agreement that developed country subsidies and protection in agriculture hurt the poorest, least developed countries. **This is a telling example of how political correctness can lead to the acceptance of an economically incorrect proposition.**

The rich country subsidies and protection seriously distort the global trading system and must therefore be eliminated. But it is also true that, barring a few exceptional cases such as **cotton**, the least developed countries will actually be hurt by this liberalisation. The biggest beneficiaries of the rich country cuts in farm subsidies will be the rich countries themselves, which bear the bulk of the cost of the associated distortions, followed by the Group of 20 middle-income or larger developing countries led by Brazil, which will emerge as the main exporters of the liberalised products. Unless we recognise this fact, we shall fail to convert the Doha framework deal reached by the World Trade Organisation this weekend into a just final agreement for the poorest countries.

Current production and export subsidies flood world markets with the subsidised products and drive their prices down. The removal of these measures will raise the prices of the products in question. This will benefit the exporters and hurt the importers of these products. Food products happen to be among the most heavily subsidised items and as many as 45 of the world's least developed countries are net food importers, according to calculations by the economists Alberto Valdes and Alex McCalla. Even when we consider all agricultural products, 33 least developed countries are net importers.

A counter-argument may be that, once the subsidies are eliminated and world prices increase, the least developed countries will become net exporters of the products. But this is doubtful for two reasons: such a change can turn at most only a handful of these countries into net exporters and the switch from net importer to net exporter status by itself is not enough to bring an overall benefit. As food prices rise, so will losses on food imports. Only if a country becomes a sufficiently large exporter will it be able to offset these losses.

Some may argue that, even if the least developed countries as a whole lose, their farmers will still benefit from the price increases. And in so far as the farmers are poor, the change will be for the better. But this is a treacherous argument: if the objective is to prevent farmers being undercut by cheaper imports, a countervailing duty against the subsidised imports, which is entirely legal under WTO rules, is a better instrument since it also generates revenues. But the decision by the countries not to impose this duty suggests that they prefer the lower prices for their consumers.

What about the net agricultural exporters? Surely they would benefit from liberalisation? Even here the story is more complicated. Protection keeps agricultural prices inside the European

Union high. The Everything But Arms (EBA) initiative currently gives the least developed countries duty- and quota-free access to the EU market for all products except rice, sugar and bananas. Poor country exporters can therefore benefit from the higher prices prevailing in the EU. Opening up the EU markets to all comers will lower EU internal prices and hurt the least developed country sellers as well as the EU sellers.

Another reason why exporters in the least developed countries may lose out from liberalisation is that less transparent regulatory policies, ostensibly for food hygiene and safety, may eventually replace more conventional barriers such as tariffs and quotas. The relatively richer G20 countries will be far better placed to overcome these barriers than the least developed countries. While this outcome is not a certainty, it is a strong possibility.

Why have the numerous studies of agricultural liberalisation failed to reveal these losses? There are three reasons. First, with rare exceptions, the studies simply ignore the fact that the EBA gives the least developed countries free access to the EU market. Second, some studies lump liberalisation by poor countries in with liberalisation by rich countries. In so far as the benefits to the least developed countries from their own liberalisation outweigh the losses inflicted on it by rich country liberalisation, the innocent reader is left believing that all liberalisation must be beneficial. Finally, some studies put the countries that lose into a broader region (for example, Bangladesh into South Asia) such that the gains to other countries in the region offset their losses.

The failure to recognise the adverse effects of trade liberalisation on poor countries poses two dangers as we move to the final stage of the Doha negotiations. First, without such recognition, we shall fail to design the compensation and adjustment programmes that such countries will need to adapt to liberalisation. Second, when the least developed countries, promised huge gains, find themselves badly damaged instead, they will be disillusioned about the benefits of trade. That could be fatal to the cause of future liberalisation.

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