

## **Handout on Developing Country Issues**

1. Debates on LDC trade policy
2. Developed country policy impacts on LDCs

### **1. Debates on LDC Trade Policy**

#### 1.1 Import substituting industrialization.

- Based upon the experience of the United States among others (Friedrich List, James Hamilton).
- In practice, some ISI was practical response, e.g., Argentina and autarky induced by WW II.
- Post-war planning envisioned a rational approach to substituting out for imports with domestic production.
- Tariffs and quotas would induce domestic production of final goods. Backward linkages would induce the development of domestic suppliers of inputs into the production of final goods. Forward linkages would also arise. Over time, firms would supply domestic demand, and average cost would decline as economies of scale exploited (or learning by doing occurred).
- Problems: (1) In order to keep final goods industries profitable, tariffs would have to be raised when input industries' protection was raised (remember "effective rate of protection" calculations); (2) most countries domestic markets not usually sufficiently large so that firms reached efficient scale of operation; (3) reliance on quotas, licensing, etc., provided extremely high levels of protection, and allowed monopoly power to be exerted by domestic firms, with resulting high prices.

#### 1.2 High Performing Asian Economies (HPAEs), and Export Led Development

- The experience of the East Asian economies – Korea, Singapore, Taiwan and HK – signaled the end of ISI as the preferred policies.
- These countries did not try to rely solely on domestic markets, but rather on world markets, where scale economies could be exploited.
- In contrast to ISI, extremely high levels of trade protection were seldom the case.

- Outward orientation was extolled in World Bank, *The East Asian Miracle: Economic Growth and Public Policy* (Oxford, 1993).

### 1.3 The Intellectual Counter Attack

- HPAEs suffered crises in the mid-1990s
- On intellectual level, it was clear that while HPAEs were less protectionist, they were not necessarily less interventionist. For instance, credit was directed in many cases. Korea had a “heavy and chemical” industries industrial policy, 1973-79.
- The HPAEs benefited from (1) High saving rate, (2) high rates of human capital accumulation.
- Since then, many countries have adopted what is sometimes called “the Washington Consensus” (term coined by John Williamson), which involves minimal price distortions and trade barriers,<sup>1</sup> but have not seen an acceleration of growth.
- This has led to a focus on institutional bases for economic growth (laws, etc.), recognizing that “getting the prices right” is not enough.

## 2. Developed Country Policy Impacts on LDCs

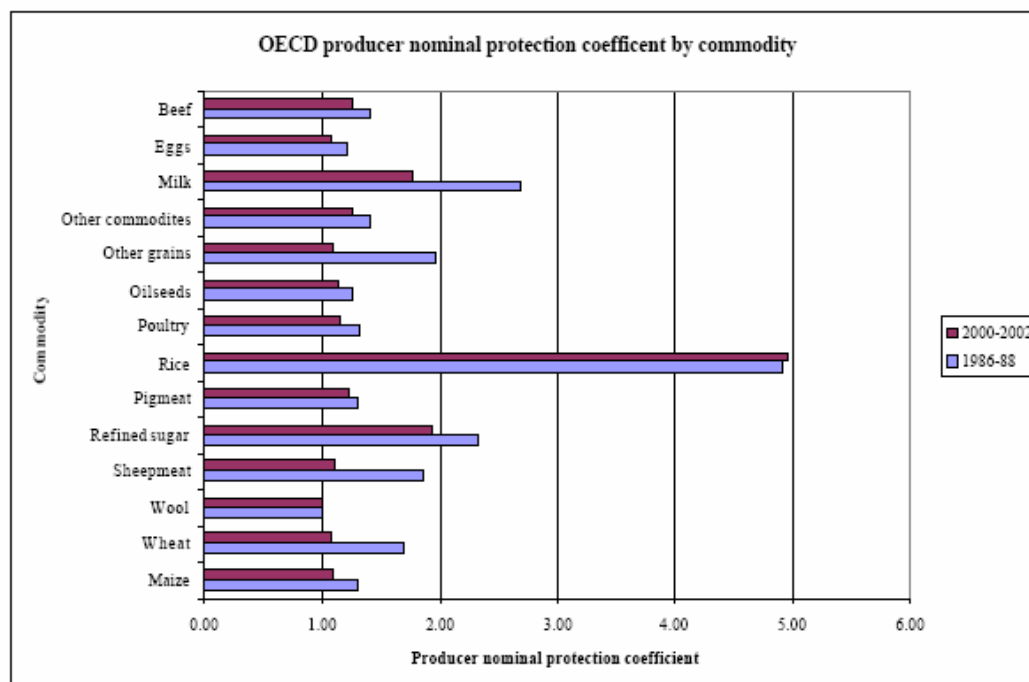
The biggest single concern of LDCs regarding developed country trade policies concerns agriculture. That’s because agricultural goods are exactly the ones that many LDCs have a comparative advantage in. Yet, developed country protection is now perhaps the highest in agricultural goods.

There is a complication of course (keeping in mind the heterogeneity of the countries). Some LDCs are food exporters and some are importers. To the extent that developed countries protect their markets and exclude LDC food exports, food prices are driven down in LDCs. This helps consumers, but hurts producers.

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<sup>1</sup> The consensus included ten broad sets of recommendations: (1) Fiscal policy discipline; (2) Redirection of public spending from indiscriminate (and often regressive) subsidies toward broad-based provision of key pro-growth, pro-poor services like primary education, primary health care and infrastructure investment; (3) Tax reform – broadening the tax base and adopting moderate marginal tax rates; (4) Interest rates that are market determined and positive (but moderate) in real terms; (5) Competitive exchange rates; (6) Trade liberalization – liberalization of imports, with particular emphasis on elimination of quantitative restrictions (licensing, etc.); any trade protection to be provided by low and relatively uniform tariffs; (7) Liberalization of inward foreign direct investment; (8) Privatization of state enterprises; (9) Deregulation – abolition of regulations that impede market entry or restrict competition, except for those justified on safety, environmental and consumer protection grounds, and prudent oversight of financial institutions; and, (10) Legal security for property rights. Source: [http://en.wikipedia.org/wiki/Washington\\_Consensus](http://en.wikipedia.org/wiki/Washington_Consensus)

**Figure 1 Producer nominal protection coefficients by commodity**



Source: OECD PSE/CSE database.

Source: Ashraf, McMillan and Peterson-Zwane, “My policies or yours?”

<http://www.nber.org/~confer/2004/gpif04/ashraf.pdf>

**Table 1: Agriculture’s importance in economies by income classification**

Countries	Agriculture value added (% of GDP)	Rural population share (%)	Arable land under cereal production (%)
High income OECD	2	21	38
Low & middle income	12	58	53
Least developed countries	33	76	60

Source: World Development Indicators. Notes: Low and middle income classification uses World Bank definition (income below about \$9,000); least developed countries uses United Nations (UN) classification (44 poorest members of the UN).

Source: Ashraf, McMillan and Peterson-Zwane, “My policies or yours?”

**Table 2 Leading net importers and exporters of OECD-supported commodities, 2000 ( '000s of Metric Tonnes)**

Rice		Maize						Refined Sugar						Wheat			
Net importers	QM	Net exporters	QX	Net importers	QM	Net exporters	QX	Net importers	QM	Net exporters	QX	Net importers	QM	Net exporters	QX		
Indonesia	1,500	Australia	552	Japan	16,340	Moldova	50	Iran	720	Belarus	230	Brazil	7,201	China	428		
Philippines	1,410	Burma	670	Korea	8,743	Thailand	166	Algeria	700	Korea	348	Iran	6,284	Hungary	963		
Nigeria	1,250	Egypt	694	Mexico	5,911	Ukraine	371	Nigeria	685	Colombia	349	Egypt	6,050	India	1,128		
Iraq	959	Uruguay	736	Egypt	5,268	Paraguay	458	Indonesia	542	Poland	363	Algeria	5,600	Turkey	1,135		
Saudi Arabia	942	China	1,580	Taiwan	4,924	Hungary	717	Israel	490	China	367	Japan	5,431		3,654		
Iran	765	India	1,685	Canada	2,624	S. Africa	886	Sri Lanka	449	U.A.E.	521	Indonesia	4,020		11,265		
Senegal	735	U.S.	2,245	E. U.	2,591	Brazil	5,938	India	413	Turkey	613	Morocco	3,534		12,066		
Bangladesh	672	Pakistan	2,429	Malaysia	2,365	China	7,187	Syria	375	Thailand	1,802	Iraq	3,300		15,856		
E. U.	641	Vietnam	3,488	Colombia	1,857	Argentina	9,653	Uzbekistan	313	Brazil	3,900	Philippin	3,050		17,117		
Brazil	632	Thailand	7,521	Algeria	1,600	U.S.	49,140	Bangladesh	310	E.U.	6,019	Korea	2,999		26,459		
Cotton		Oilseeds						Dry Whole Mild Powder									
Net importers	QM	Net exporters	QX	Net importers	QM	Net exporters	QX	Net importers	QM	Net exporters	QX	Net importers	QM				
Indonesia	574	Burkina	113	E.U.	17,392	Ukraine	2	Algeria	110								
Mexico	389	Mali	125	China	13,037	Hungary	5	Brazil	108	Colombia	0						
Russia	359	Cote d'Ivoire	131	Japan	4,767	Uruguay	14	Venezuela	65	Poland	0						
Turkey	353	Benn	136	Mexico	4,381	Ecuador	30	Philippines	52	Canada	4						
Thailand	342		147	Taiwan	2,330	Zimbabwe	39	China	41	Ukraine	4						
India	321	Tyrosaniet Syria	229	Korea	1,404	Canada	316	Taiwan	38	U. S.	12						
Korea	306	Greece	306	Thailand	1,290	Paraguay	2,550	Mexico	34	Argentina	103						
Italy	289	Uzbekistan	739	Indonesia	1,127	Argentina	6,995	Egypt	30	Australia	164						
Japan	248	Australia	850	Israel	617	Brazil	14,570	Thailand	26	N.Zind	407						
Taiwan	226	U.S.	1,464	Malaysia	592	U.S.	27,006	Peru	22	E.U.	568						

Source: USDA/FATUS. Countries in bold are rich-country OECD members. Data excludes food aid.

Source: Ashraf, McMillan and Peterson-Zwane, "My policies or yours?"

**Table 5: Do rich country agricultural policies affect the incomes of the poor?**

Dependent variable: Log income per capita of first quintile						
	(1)	(2)	(3)	(4)	(5)	(6)
	OLS	OLS	OLS	OLS	OLS	OLS
OECDPOLICY	0.073 [0.046]	-0.036 [0.058]	-0.325 [0.130]**	-0.373 [0.210]*	-0.254 [0.226]	-0.390 [0.185]**
OECDPOLICY squared			0.099 [0.033]***	0.120 [0.053]**	0.104 [0.054]*	0.124 [0.048]**
Log average income per capita	1.049 [0.046]***	0.950 [0.051]***	0.948 [0.052]***	0.960 [0.061]***	0.936 [0.074]***	0.959 [0.060]***
SOI anomaly	-0.016 [0.035]	-0.021 [0.030]	-0.012 [0.030]	-0.002 [0.030]	-0.005 [0.030]	-0.004 [0.031]
ECE*OECDPOLICY				0.596 [0.313]*	0.504 [0.304]	0.533 [0.387]
MENA*OECDPOLICY				0.155 [0.187]	0.049 [0.189]	0.100 [0.259]
LAC*OECDPOLICY				0.203 [0.134]	0.140 [0.139]	0.160 [0.191]
SSA*OECDPOLICY				-0.197 [0.098]**	-0.259 [0.115]**	-0.194 [0.103]*
SA*OECDPOLICY				-0.080 [0.172]	-0.166 [0.179]	-0.124 [0.246]
Arable land per capita					-0.045 [0.039]	
Non-program crops share, 1970						-0.131 [0.320]
<b>REGIONAL FIXED EFFECTS</b>						
East and Central Europe		0.419 [0.077]***	0.486 [0.084]***	-0.029 [0.321]	0.205 [0.364]	0.042 [0.404]
Middle East North Africa		-0.031 [0.085]	0.029 [0.086]	-0.095 [0.209]	0.116 [0.271]	-0.029 [0.299]
Latin America Caribbean		-0.394 [0.067]***	-0.315 [0.070]***	-0.573 [0.209]***	-0.413 [0.247]*	-0.515 [0.278]*
Sub-Saharan Africa		0.257 [0.069]***	0.269 [0.071]***	0.703 [0.231]***	0.835 [0.264]***	0.681 [0.250]***
South Asia		-0.509 [0.127]***	-0.468 [0.128]***	-0.347 [0.268]	-0.167 [0.300]	-0.287 [0.343]
Constant	-1.797 [0.377]***					
Observations	143	143	143	143	141	143
R-squared	0.79	0.88	0.88	0.89	0.89	0.89
F-stat	188.30	164.55	122.59	122.42	124.94	108.28

Excluded dummy variable in regressions with regional fixed effects is East Asia and Pacific. Huber robust standard errors in parentheses. Significantly different from zero at 90% (\*), 95% (\*\*) 99% (\*\*\*) confidence. SOI is Southern Oscillation Index. Income measured in \$1985, PPP. MENA is Middle East and North Africa, ECE is Eastern and Central Europe. LAC is Latin America and Caribbean, SSA is Sub-Saharan Africa, SA is South Asia. Program crops are defined as those for which a NPC estimate is calculated by the OECD.

Source: Ashraf, McMillan and Peterson-Zwane, "My policies or yours?"

**Table 6: Determinants of agricultural support in the OECD**

Dependent variable: OECDPOLICY <sub>it</sub>					
	(1)	(2)	(3)	(4)	(5)
	OLS	OLS	OLS	OLS	OLS
EU Budget year? (0/1)	0.135 [0.214]	0.217 [0.193]	0.134 [0.195]	-0.089 [0.163]	
Japanese election year? (0/1)	-0.203 [0.164]	-0.189 [0.133]	-0.144 [0.133]	-0.200 [0.107]*	
US election year? (0/1)	-0.048 [0.158]	-0.070 [0.156]	-0.014 [0.144]	0.043 [0.116]	
France election year? (0/1)	0.459 [0.207]**	0.362 [0.186]*	0.409 [0.187]**	0.338 [0.131]**	
Output per farm, US		1.457 [0.279]***	0.967 [0.304]***	0.219 [0.276]	0.081 [0.382]
Output per farm, EU			11.793 [3.221]***	6.574 [3.280]**	6.670 [3.463]*
Concentration of production in US				9.859 [1.069]***	11.750 [2.440]***
Concentration of production in EC					-0.691 [0.842]
SOI anomaly	-0.056 [0.067]	-0.062 [0.059]	-0.091 [0.061]	-0.092 [0.045]**	-0.030 [0.039]
Constant	1.305 [0.092]***	0.716 [0.159]***	0.277 [0.179]	-0.337 [0.162]**	-0.301 [0.155]*
Observations	143	143	143	143	143
R-squared	0.04	0.17	0.23	0.55	0.53
F-stat	1.11	5.30	8.31	21.31	31.69

**Output per farm and concentration of production variables are weighted averages across commodities like the dependent variable where weights are country-specific and defined as fraction of agricultural production in each commodity class in 1970. Huber robust standard errors in parentheses. Significantly different from zero at 90% (\*), 95% (\*\*), 99% (\*\*\*) confidence. SOI is Southern Oscillation Index.**

Source: Ashraf, McMillan and Peterson-Zwane, “My policies or yours?”