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CHOOSING SENSITIVE AGRICULTURAL PRODUCTS IN TRADE NEGOTIATIONS

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NON-TECHNICAL SUMMARY

Systematic rules, often based on formulas, have been found useful in achieving trade liberalization, especially where trade negotiations are complex and involve large numbers of participants. When this approach is used, however, there are widespread demands for exceptions from, or flexibility in, the application of these systematic rules. The Doha-Round negotiations are a good example: from the industrial countries, the demands for "sensitive" products in agriculture seem likely to result in agreement that countries can subject a specified percentage of tariff lines to reduced tariff cuts. Some developing countries have, in addition, sought latitude to subject an additional set of products to much-reduced or zero cuts on the grounds that they are "special" products.

In contrast with a specific tariff reduction formula, there is no mechanical way to identify the implications of allowing countries to designate a set of self-selected tariff lines as 'sensitive'. This paper assesses what choices countries are likely to make in using this flexibility. Based on a political-economy model of protection, we consider initial protection as an equilibrium, that can be used to reveal policy-makers' preferences. With this assumption, we show that the likely choices of these sensitive products can then be predicted using a simple indicator based on the value of the import at domestic prices; the squared, proportional cut in the price of the import brought about by the formula; and the extent to which sensitive product status reduces the size of this price cut.

This framework is applied to the Doha Round negotiation on Agricultural Market Access, based on trade and tariff information at the six-digit product level. While the sensitive-product exceptions in the current agricultural negotiations have long been considered as a minor deviation from the disciplines being discussed, we find that the discretion allowed for these products may greatly diminish the effect of these disciplines. We estimate that allowing 2 percent of tariff lines to face only 50 percent of the formula cut would reduce the cut in weighted average industrial-country tariffs from 7.5 percent to 3.5 percent. Increasing the share of sensitive products to 4 percent reduces the cut in average tariffs only slightly more, to 3.1 percent.

Two standard rules of thumb frequently used to guess possible sensitive products identify them as the products with the highest bound or applied duties. We find these shortcuts to understate severely the possible consequences of sensitive products because they overlook the trade weight of each product. An alternative of using the tariff revenue loss as a criterion appears to provide a far better approximation to the results obtained with our political economy framework. In addition, we examine the potential impact of excluding “sin” tax commodities from the sensitive product group. While these products are prominent in the list defined as sensitive, particularly in developing countries, it is possible that they have high tariffs because of a desire to discourage their consumption, rather than the mix of protection and revenue goals that apply on other products. Whatever the cause, it appears that excluding them from the sensitive list has relatively little impact on the resulting cuts in average tariffs. We also find the magnitude of the deviation from formula cuts allowed for sensitive products to matter significantly, even when it is merely changed from half to two-thirds or one-third. This result suggests that this "depth" of flexibility is an important dimension—frequently more important than the much-discussed “breadth” in terms of the number of tariff lines covered.

A problem for exporters associated with allowing a certain number of tariff lines to be treated as sensitive is that this criterion does not take into account the importance of these tariff lines to the exporter. If the sensitive products are restricted on the basis of their share in total imports, we find a dramatic reduction in the loss of market access. With the tiered formula, the cut in average tariffs after allowing 2 percent of imports to be exempted is 6.3 percent, only 1.2 percentage points less than in the absence of sensitive products.

Sensitive product exceptions adversely affect both welfare and market access. However, since these exceptions increase the variance of tariffs relative to the formula outcome, we show that their effects on economic welfare are much worse than their effects on market access. In this sense, the combination of steeply progressive tariff formulas and exceptions may be much more rational from a mercantilist point of view than when examined from the perspective of economic welfare and development.

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