Executive Summary

Over the last decade, countries have improved many aspects of policy relevant for trade. Worldwide, Most Favored Nation (MFN) average tariffs have fallen from 14.1 percent during 1995–99 to 11.7 percent during 2000–04 and further to 9.4 percent in 2007—a decline of more than 33 percent. In addition, a substantial amount of trade is conducted at a zero MFN tariff rate (MFN-0) or through preferential trade agreements. Both the severity of remaining restrictions and the importance of trade flows at duty-free or preferential rates vary among countries. The most recent estimates indicate that all regions and income groups have witnessed substantial real growth in trade during this time. In 2007, average real growth in trade, 7.7 percent for the world as a whole, is within the 7–9 percent growth range of the last decade. Groups that have the best policies and institutions overall also tend to have stronger and more consistent trade performance.

The trade reform agenda going forward is about rationalizing substantial tariff peaks (particularly in agriculture), reducing overall tariff levels in some groups or countries, reducing tariff escalation aimed at protecting special goods, liberalizing services trade, and improving the other behind-the-border factors that affect trade expansion and the gains from it. Tariff rationalization is particularly needed in high-income countries where there are high tariffs on products of particular interest to developing countries. In the Middle East and North Africa (MNA), South Asia (SAS), and Sub-Saharan Africa (SSA) regions, average MFN-applied tariffs are also greater than 10 percent (for MNA, more than 15 percent). Trade in services has not been liberalized to the same extent as trade in goods, especially in low-income countries. Locking in current levels of liberalization through the General Agreement on Trade in Services (GATS) would be a first important step toward a more ambitious reform agenda, especially for low-income countries. Improvements in domestic institutions could boost export performance, particularly in manufacturing and services, and help support new markets and new products. Overcoming inefficiencies in trade facilitation in developing countries would have a high payoff for trade performance, especially as tariffs have been reduced below trade costs in most countries.

Trade Policy

Tariff protection, both with and without the inclusion of preferences, has fallen consistently in all regions and income groups from the mid-1990s to 2007, and especially in low-income countries, where average MFN applied tariffs fell 46 percent (10 percentage points). High-income countries, which were earlier reformers, still have the lowest average tariffs at 6 percent compared to a developing country average of 11 percent. Other measures, such as the World Bank's Trade (MFN) Tariff Restrictiveness Index (MFN TTRI), confirm this pattern.

- Among developing countries, the EAP and SAS regions' performance is noteworthy for the large declines in their (simple) average MFN tariffs, which fell by 50 and 47 percent (10 and 12 percentage points) respectively. Although SAS's percentage decline is the largest, it also had the highest tariff levels, averaging 26 percent. Among developing regions, the smallest decline was in MNA (22 percent), which is the most restrictive region with average tariffs around 16 percent. It is followed by the SAS and SSA regions. The ECA region has the lowest average tariff (7 percent), followed by the LAC region (9 percent). When including preferences, applied trade-weighted tariffs are on average about 20 percent lower for high-income countries and 14 percent lower for developing countries than MFN counterparts, but trends over time and regional patterns are broadly similar.
- Developing countries that have seen the largest falls in import restrictions since the early 2000s as measured by MFN simple tariffs include the Arab Republic of Egypt (from 47 to 17 percent), the Seychelles (28 to 8 percent), India (32 to 15 percent), and Mauritius (18 to 3.5 percent). In China, tariffs also decreased from 14 to 10 percent. Among developed countries, overall tariff restrictions in the European Union (EU), Canada, Japan, and the United States came down slightly, but from already low levels.
- While the overall trend has been toward liberalization, in some years, some countries have raised their tariffs on particular products (and thus their average tariffs as well). Between 2005–06 and 2007, three countries raised tariffs by more than 1 percentage point: Mauritania raised the average MFN tariff from 11 to 12 percent, El Salvador's tariff went from 6 to 7 percent, and St. Vincent and the Grenadines raised its tariff from 4 to 10 percent. With respect to the early 2000s, 31 countries have increased their tariffs, of which 14 had increases between 17 and 42 percent. Kazakhstan almost tripled its tariffs, increasing the average from 2.8 to 7.8 percent.

But average tariffs do not reveal the whole pattern of protection. High-income countries have higher nontariff barriers, greater tariff escalation and dispersion, and much higher maximum tariffs than low-income countries; that is, they protect certain sectors much more than others. Many of these protected sectors and goods are of special interest to developing-country exporters.

- All countries on average have higher trade barriers in the agriculture sector relative to mining and manufacturing; the SAS and EAP regions have the most restrictive policies, followed by the high-income Organisation for Economic Co-operation and Development (OECD) countries. The low-income countries' import-weighted average tariff on agriculture (including preferences) is 1.4 times that on other goods. For the high-income OECD group, it is 9 times higher. Among developing countries, the EAP and ECA regions protect agriculture 4 and 3.3 times more, respectively, than all other goods on average. By comparison, SSA protects agriculture just 1.4 times more than other sectors. Net food importers on average protect agriculture more relative to nonagricultural sectors than countries that are not net food importers.
- The level of protection may be significantly affected by nontariff measures, but information about nontariff measures is only available on a cross-country basis for 2001 or earlier. When considering these measures, the pattern of restrictiveness in agriculture changes: the most restrictive region is MNA, followed by the high-income OECD group, and the least restrictive is SSA.
- OECD countries have high maximum MFN-applied tariffs, averaging 347 percent (having dropped from 1,488 percent in the latter half of the 1990s), and low-income countries have the lowest at 122 percent. MFN tariff dispersion is 2.4 times higher in high-income countries than in low-income ones. Among developing regions, MNA has the highest MFN maximum tariff, averaging 716 percent in 2007, followed by EAP at 335 percent.
- Developing country exporters face higher export hurdles at the upper end of production than at the lower end. Most countries protect finished goods more than unfinished goods, but tariff escalation is higher in the high-income OECD countries than in developing countries. This pattern is amplified in the agriculture sector. However, tariff escalation is highest in the MNA region. The SAS region has the lowest tariff escalation both in agriculture and overall. It is followed by the LAC and SSA regions.

Tariff reform is closely linked to fiscal outcomes in many developing countries because of their high reliance on trade taxes for fiscal revenues.

- Revenues from import duties account for almost a quarter of fiscal revenues for low-income countries, compared to the high-income average of only 7 percent. In 2007, the SAS region obtained 26 percent of its fiscal revenues from import duties followed by the SSA region at 23 percent, compared with 0.8 percent for high-income OECD countries. In many cases, exemptions and inability to collect full tariffs mean lower revenues than implied by the statutory tariffs.

Barriers to services trade are still high across countries and especially in the low-income countries.

- Services trade liberalization can confer large gains to developing countries but low-income countries have made the fewest commitments to liberalize services in the World Trade Organization (WTO). Commitments under the General Agreement on Trade in Services (GATS) do not reflect actual liberalization since some countries have liberalized unilaterally or in the context of bilateral or regional agreements. However, GATS commitments do indicate whether countries are bound to a certain level of liberalization. Among the 20 countries that have made the most commitments to liberalize, at least half are in ECA.
- In terms of sectors, fewer commitments by all income groups were made in health and social services and transport sectors than in others. In other sectors, there is some variation by income group. For example, high-income countries have made stronger commitments in financial services, business, and distributional services but weaker commitments in tourism sectors. Many countries already allow a large degree of foreign participation in telecommunications, with the ECA countries being fully open and most other regions being very open except EAP.

Market Access

A substantial share of exports is subject to an MFN-0 tariff level. In addition, trade preferences, free trade agreements (FTA), or customs unions (CU) have lowered trade restrictions for many countries. But there are large differences across regions and income and product country groups in how much trade is restricted or conducted under a zero MFN tariff rate or through preferential arrangements. For instance, low-income country exporters face a weighted average tariff including preferences of 3.7 percent, which is higher than that faced by high-income country exporters at 2.8 percent. And garment exporters in developing countries face restrictions on their exports on average that are more than double those faced by the rest of the developing world.

- MFN-0 trade accounts for 26–45 percent of world exports; MNA and SSA have the highest percentage of exports at the MFN-0 tariff level, while SAS and LAC have the lowest. High-income countries have 40 percent of their exports in this category.
- MNA faces the lowest applied tariffs inclusive of preferences (1.2 percent) and SAS has the highest (4.7 percent). The value of EU and U.S. preferences, for which more complete data are available, is modest for low-income

countries, equivalent to only 3.2 percent of their exports to these two preference-granting countries. The average Latin American country benefits the most from such preferences and ECA the least. The value of such preferences is above 10 percent of bilateral exports for less than two dozen countries, with a high of 48 percent for Anguilla and 33 percent for Swaziland.

- Not only do the SSA and SAS regions have less favorable market access but they also have the lowest proportion of their total exports going to countries with which they have an FTA or CU. For the SAS region it is around 2 percent for 2006 and for SSA it is under 10 percent. EAP countries have 38 percent of their exports in this category, ECA has 43 percent, and high-income OECD countries have 57 percent.

Behind the Border

Improvements in countries institutional environments and in the quality of trade facilitation could support trade and export growth. The institutional environment varies widely across regional and income groups and among countries in the same group. Countries whose institutional environments are better tend to have a higher share of manufactures in their goods exports, have lower export concentration, and tend to be more integrated in the world economy.

- Among developing countries, the SSA, SAS, and MNA regions rank below the world average on institutional dimensions related to the business climate and general governance indicators as measured by the Doing Business (DB) indicators and the Worldwide Governance Indicators (WGI) of the World Bank.

There is a significant gap in the quality of trade facilitation between the high-income countries and even the best-performing developing countries. Better trade logistics, as measured by the World Bank's Logistics Performance Index (LPI), are correlated with positive changes in trade integration.

- At the bottom of the rankings are low-income countries that are geographically isolated or beset by conflict or other internal problems. Landlocked developing countries, especially in Africa and in Central Asia, are the most constrained in terms of trade logistics, as they typically suffer from difficult geography, poor access to logistics services in neighboring countries, and high coordination and transportation costs. Among developing regions, the ECA and EAP regions score the highest, while the SAR and SSA regions lag significantly behind them.

Trade Performance

According to World Bank preliminary estimates as of December, developing countries' trade growth slowed down in 2007 while developed countries' trade growth increased, so that for both groups on average trade grew at 7.7 percent in real *terms. There has been some change in the structure of world exports, with agriculture's share falling 31 percent over the last decade.*

- In the early years of the 2000s developing countries' trade and export growth (both around 8 percent) was significantly higher than that of high-income countries (both around 6 percent). In 2007, the ECA region had the fastest growth in trade and exports (10 percent) on an unweighted basis, followed by the EAP region (both just under 9 percent). The developing region with the lowest estimated growth in trade during 2007 was the SSA region, followed by the SAS region.

- The weakest export performance was exhibited by the MNA region, followed by SSA and LAC. China with 23 percent real growth and Sudan, a mineral exporter, with 39 percent are among the countries with the highest export growth. Algeria and Mauritania are at the bottom (−6 and −17 percent, respectively).

- For the world as a whole, real growth in services exports has been higher than growth in merchandise exports until the mid 2000s but has slowed down in recent years. The largest services exporters in 2007 were Poland, with real growth in services exports estimated at 48 percent, Azerbaijan at 30 percent, and the Czech Republic at 25 percent. Low-income countries with growth above 10 percent included the Democratic Republic of Congo, Bangladesh, Haiti, Burundi, and India. Several African countries, among them Eritrea, Sudan, and Angola, have seen declines in services exports.

- High growth in trade has meant increasing levels of integration: MNA's increase of 39 percent in its trade-to-GDP ratio since 1995–99 is the highest among the regions, and ECA and OECD countries follow with a 21 percent increase. Surprisingly, the slowest integrators have been the LAC (6 percent) and SAS (13 percent, despite its recent high export and trade growth rates) regions. Differences in integration among regions and income groups are large: SAS, the least integrated region (73 percent of GDP) is about half as integrated as the EAP (116 percent) or ECA regions (105 percent). As expected, smaller economies tend to be more integrated than larger ones**.** Among the larger countries that have the lowest trade-to-GDP ratios are Brazil, the United States, Australia, and India. Among the smaller countries that are the most integrated are Singapore, Hong Kong (China), Malaysia, and Swaziland.

- The composition of world and regional exports has changed over the last decade. Agriculture's share in world exports has dropped 31 percent from 1995–99 to 2006 (and 19 percent since the early part of this decade). Manufacturing and mining have grown while services exports have remained fairly constant as a share of total exports (and relative to GDP). In 2005–06 services have accounted for 28 percent and manufacturing for 34 percent of world exports. The LAC and SSA regions and high-income

OECD countries (from a low base) have seen the largest increase in the mining share of exports. EAP and OECD countries have the highest share of manufacturing in exports (just over 50 percent) and SSA has the lowest (not quite 18 percent). The SSA and SAS regions have the highest share of agricultural exports at 27 and 21 percent, respectively. High-income non-OECD countries have the highest share of services exports (37.4 percent), followed by SAS, EAP, and MNA (around 30 percent).

- Countries seek to diversify their export structures to manage risk arising from volatility of export earnings as demand or supply conditions change. Export concentration tends to change only slowly over time, and countries with higher income tend to be more diversified. Among developing countries, the SSA and MNA regions have the most concentrated export structures. In the former, the top five exports have accounted for almost 80 percent of exports, in the latter almost 70 percent for SSA. Export concentration is positively and significantly correlated with volatility in real export growth. The 20 least diversified countries have 2.3 times greater volatility in real export growth relative to the 20 most diversified countries. The most specialized countries tend to be either mineral resource-abundant economies or very small islands.

Effective assessments of global trade policies and outcomes are dependent on good-quality data. The WTI database is useful in highlighting in one place the many policy factors that together influence trade as well as data gaps and fluctuations in country coverage. The existing data show that countries with poor endowments and geographical constraints can overcome bottlenecks to trade. The database, by allowing benchmarking and ranking of country performance in various policy and outcome areas, provides a clearer picture of where each country stands and should support incentives to implement policy reforms.