

# Chapter 1

## Introduction

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While, in recent decades, the international community has recognised the structural changes in the way trade, production and marketing are organised – with production spread between firms in several countries organised into complex production networks and global value chains (GVCs) (WTO 2017) – only recently has the influence of trade policy regimes on value chain outcomes and upgrading strategies been analysed (Curran and Nadvi 2015). This includes measures applied at the border such as tariffs, as well as other product specifications such as rules of origin. This absence of critical analysis is surprising, since the success of export-orientated growth by emerging Asian countries achieved during the second half of the twentieth century was underpinned by shifting patterns of production and forms of trade preference (Keane 2013).

The implications for least developed countries (LDCs) of the rise of the Asian newly industrialised countries (NICs) as intermediaries within a triangular mode of manufacturing has only recently begun to be explored within the GVC literature. Essentially, the Multifibre Agreement (MFA) conferred a form of locational advantage on countries not party s to the agreement; this subsequently brought developing countries (notably in Asia) into production networks. The end result has been the creation of triangular trade arrangements between the USA, Europe, the Asian NICs and less developed Asian economies, as well as producers in Latin America, the Caribbean and sub-Saharan Africa.

The multilateral trading system rests on the principle of non-discrimination, as described by Hoekman et al. (2009). Notions of managed trade and ‘constrained upgrading’ and thus the strategic rationales underpinning trade policy began to be articulated as the MFA with its distributed system of quotas was replaced by the Agreement on Textiles and Clothing, under the auspices of the World Trade Organization (WTO) (Pickles et al. 2015). The General Agreement on Trade and Tariffs (GATT) allowed for exemptions from the most-favoured nation (MFN) rule in the case of reciprocal preferential trade agreements and the granting of unilateral (non-reciprocal) preferences to developing countries (Hoekman et al. 2009).

As quantitative trade restrictions have been removed in developed country markets, the end result is increased consolidation at the firm and country levels. Buyers have modified their strategies, making them more focused on lead time management, production flexibility, and product quality and delivery – and less focused on (tariff) rent capture (see Curran and Nadvi 2015). An economic rent is defined as the difference between the

price at which an output can be sold and its production costs, including normal returns. Essentially, when governments levy tariffs they drive a wedge between sale prices and create an economic rent over and above that which may be derived by the producer. Because of the profit maximisation behaviour of economic agents and the role of economic rents as conveyed by tariffs, when they are removed firms must offset economic losses elsewhere. Globally, these shifts have been expressed through a decline in unit prices and increased pressure in the sector, as geographies of global sourcing have become more complex and multilayered (Pickles et al. 2015).

The 1979 Enabling Clause (formally titled ‘Differential and more favourable treatment, reciprocity and fuller participation of developing countries’) agreed as part of the Tokyo Round of the GATT gave permanent legal cover for the Generalised System of Preferences (GSP). It also included references to ‘graduation’, thereby indicating that special and differential treatment (SDT) policies were to be phased out as recipient countries reached a certain level of economic development. However, criteria for SDT eligibility and for graduation remained undefined within the multilateral trading systems, and, as described by Hoekman et al. (2009), the major concern expressed by developing countries has been that SDT provisions are best-effort commitments and not enforceable through the dispute-settlement mechanism of the WTO; eligibility and graduation criteria, as well as product coverage and type of preference, are left to donor countries to determine unilaterally.

It is fair to say that the influence of trade preferences for development, which have conveyed important incentives for the integration of LDCs into global production networks and are a key type of international support measure, remains underexplored within the GVC literature. In view of the unprecedented number of countries anticipated to graduate from the LDC category in the coming years – mainly on the grounds of income – this guide seeks to redress this shortcoming. While by 2018 only five countries had graduated from LDC status since 1971, this situation is expected to change dramatically in subsequent years.

Over time, particular segments of the GVC and stages of production have become increasingly concentrated, which has served to consolidate the position of firms within particular stages and tiers of production. Developments in trade policy, including making trade more socially and environmentally responsible, have also begun to influence the institutional context of production (Pickles et al. 2015). In view of these trends, this handbook presents a conceptual framework and identifies research methods and tools, which, if applied, could assist policy-makers in adapting to the loss of tariff rents induced by graduation.

It does this through integrating conventional analysis of preference erosion with GVC analysis. This is because the modern export sector

is characterised by tightly co-ordinated production networks linked to end markets, highly organised within tiers of suppliers differentiated by their functions, spread geographically, including across sectors where the trade preference rent conveyed to LDCs is high, such as within the textiles and clothing, high value agriculture and processed fisheries GVCs.

## References

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