Backgrounder

No. 2187
September 19, 2008
Revised and updated October 22, 2008

Published by The Heritage Foundation

Trade Liberalization Continuing Despite Doha Impasse

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The 2009 rankings of trade freedom in countries around the world, developed by The Heritage Foundation as part of its annual *Index of Economic Freedom* and released to the public today,[1] show many countries moving ahead on their own to lower tariffs and cut other barriers to trade. This is good news for consumers and businesses in those countries that will enjoy greater access to competitively priced goods from around the world. Countries standing still or moving backward in response to protectionist political pressures, however, are likely to find themselves falling behind, with lower growth rates and stagnating economies.

The Challenge

Trade restrictions can take the form of taxes on imports and exports (known as tariffs), quotas or outright bans on trade, and numerous other regulatory and institutional barriers to trade. The degree to which government hinders access to the free flow of foreign commerce can have a direct bearing on the ability of individuals to pursue their economic goals.

Tariffs increase the prices that local consumers pay for foreign imports, and these price distortions change incentives, often pulling producers away from specializing in some goods and toward the protected goods. By interfering with comparative advantage, trade restrictions impede economic growth. Also, tariffs hurt domestic consumers by raising prices. In many cases, trade limitations put advanced-technology products and services beyond the reach of local people, limiting their own productive development.

Talking Points

- Trade restrictions can take the form of tariffs, quotas or outright bans on trade, and numerous other regulatory and institutional barriers to trade. The degree to which government hinders access to the free flow of foreign commerce can have a direct bearing on the ability of individuals to pursue their economic goals.
- The *2009 Index of Economic Freedom*'s trade freedom rankings demonstrate that many countries understand that the absence of action by others is no reason to hold back on doing what they can to increase trade freedom for their own citizens.
- According to data from the *Index of Economic Freedom*, countries with freer trade policies experience higher per capita economic growth than countries that maintain trade barriers.
- The trade freedom scores demonstrate that there is ample room for trade reform and significant potential for expanding trade and economic freedom around the world.

This paper, in its entirety, can be found at:
www.heritage.org/Research/TradeandForeignAid/bg2187.cfm

Produced by the Center for International Trade and Economics (CITE)

Published by The Heritage Foundation
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Washington, DC 20002–4999
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While trade liberalization involves government policy decisions that are inherently unilateral, most progress in liberalizing trade has come about in the context of multilateral trade negotiations under the auspices of the World Trade Organization (WTO) and its predecessors.

The General Agreement on Tariffs and Trade (GATT) provided the context for significant trade liberalization among member countries from 1948 to 1994 and served as the foundation for the creation of the WTO in 1995. The rush of new members into the GATT during the Uruguay Round and after the establishment of the WTO demonstrates that the multilateral trading system has been recognized as an anchor for development and an instrument of economic and trade reform.

The multilateral trading system changed dramatically over the period of the GATT and has changed even more significantly in the little more than a decade since the WTO was formed. Most developing countries were not members of the GATT, and their involvement in trade negotiations was negligible. Those that were members benefited from the outcome of GATT rounds but were exempt from having to reciprocate with significant tariff concessions of their own. In a sense, they were passive members of the multilateral trading system.

As it turns out, this paternalistic benevolence on the part of richer countries toward their less developed brethren was no favor. It was the countries that liberalized by reducing tariffs and other economic barriers that prospered, while those that were allowed to keep their protectionist walls in place became ever less competitive.

Things are much different today. Among the WTO's 153 members, about three out of four are from the developing world, and all members—rich and poor alike—are responsible for the advancement of freer trade. One consequence of the growing number of developing countries in the WTO was the decision to premise the current Doha Round of multilateral trade negotiations on promoting economic development. In November 2001, the WTO formally initiated the current round of trade negotiations in Doha, Qatar: the "Doha Development Agenda."

After more than half a century of trade liberalization, the agenda for negotiations includes some of the most politically sensitive and difficult trade issues. Among the most important issues faced by WTO negotiators are reforms in agriculture, further reductions in non-agriculture tariffs, the expansion of market access for services, improving WTO institutional rules and procedures, and solving developing country issues, including the need to boost those countries' capacity to trade.

So far, negotiations have failed to result in a comprehensive agreement that is satisfactory to all WTO members. The latest collapse of the negotiations in July 2008 reflects both divergent thinking on the role that trade liberalization plays in advancing economic development and intransigence among some members with respect to upholding their commitments to eliminating trade barriers.

Moreover, the Doha process of multilateral trade negotiations is based on the idea that it is easier for countries to lower their tariffs and other trade barriers if others do so as well. There is some political merit to the idea. The actual negotiations, however, involve a dynamic that runs counter to the goal of freeing trade. Countries hold jealously to protectionist measures that hurt the efficiency of their own economies, offering them up only in exchange for similar "concessions" from others. The psychology of the process could not be worse, because it encourages countries to value things that hurt themselves, like tariffs, import quotas, or domestic subsidies.

The 2009 Trade Freedom Scores

The *2009 Index of Economic Freedom* trade freedom rankings demonstrate that many countries understand that they benefit from removing restrictions that they have imposed on trade. Of course, they may also benefit from other countries' liberalizing measures, but the absence of action by others is no reason to hold back on doing what they can to increase trade freedom for their own citizens.

1. The *2009 Index of Economic Freedom* will be published in January 2009. The trade freedom rankings, which account for 10 percent of a country's overall economic freedom score, were released early at the request of the Millennium Challenge Corporation, which uses them as part of its criteria for determining countries' eligibility for MCC grants.

2009 Trade Freedom Scores

(t) – Tie

Rank	Nation	Score
1	Hong Kong	95.0
2(t)	Singapore	90.0
2(t)	Macao	90.0
2(t)	Libya	90.0
5	Norway	89.2
6	Namibia	88.4
7	Canada	88.2
8	Iceland	88.0
9(t)	Croatia	87.6
9(t)	Kyrgyz Republic	87.6
11	Papua New Guinea	87.2
12(t)	Mauritius	86.8
12(t)	United States	86.8
14	Turkey	86.6
15	Armenia	86.4
16	Kazakhstan	86.2
17	Israel	86.0
18(t)	Austria	85.8
18(t)	Belgium	85.8
18(t)	Bulgaria	85.8
18(t)	Chile	85.8
18(t)	Czech Republic	85.8
18(t)	Denmark	85.8
18(t)	Estonia	85.8
18(t)	Finland	85.8
18(t)	Germany	85.8
18(t)	Hungary	85.8
18(t)	Ireland	85.8
18(t)	Latvia	85.8
18(t)	Lithuania	85.8
18(t)	Luxembourg	85.8
18(t)	Malta	85.8
18(t)	The Netherlands	85.8
18(t)	Poland	85.8
18(t)	Portugal	85.8
18(t)	Romania	85.8
18(t)	Slovak Republic	85.8
18(t)	Slovenia	85.8
18(t)	Spain	85.8
18(t)	Sweden	85.8
18(t)	United Kingdom	85.8
42	Switzerland	85.4
43	Taiwan	85.2
44	Australia	84.8
45	New Zealand	84.6
46	Ukraine	84.0
47(t)	Oman	83.6
47(t)	Paraguay	83.6
49	Uruguay	83.4
50	Tajikistan	82.6
51	Japan	82.0
52(t)	Bolivia	81.8
52(t)	Costa Rica	81.8
52(t)	El Salvador	81.8
52(t)	Saudi Arabia	81.8
56(t)	Macedonia	81.6
56(t)	Moldova	81.6
56(t)	Qatar	81.6
59	Mongolia	81.2
60(t)	Kuwait	81.0
60(t)	Micronesia	81.0
62(t)	Cyprus	80.8
62(t)	France	80.8
62(t)	Greece	80.8
62(t)	Italy	80.8
62(t)	Lebanon	80.8
62(t)	United Arab Emirates	80.8
68	Georgia	80.6
69(t)	Mexico	80.2
69(t)	Montenegro	80.2
71	Bahrain	80.0
72	Trinidad and Tobago	79.8
73(t)	Haiti	79.4
73(t)	Peru	79.4
75(t)	Nicaragua	79.2
75(t)	Turkmenistan	79.2
77	Jordan	78.8
78	The Philippines	78.6
79(t)	Azerbaijan	78.4
79(t)	Guatemala	78.4
81	Malaysia	78.2
82(t)	Honduras	78.0
82(t)	Serbia	78.0
84	Bosnia and Herzegovina	77.2
85	Indonesia	76.4
86(t)	Panama	76.2
86(t)	Yemen	76.2
88	Albania	75.8
89(t)	Mauritania	75.6
89(t)	Tanzania	75.6
89(t)	Thailand	75.6
92	Uganda	75.2
93	South Africa	74.8
94	Dominica	74.2
95	St. Vincent and the Grenadines	73.6
96	Mozambique	73.4
97(t)	Dominican Republic	73.0
97(t)	East Timor	73.0
97(t)	Mali	73.0
100(t)	Madagascar	72.6
100(t)	Ecuador	72.6
100(t)	Guyana	72.6
103	Colombia	72.4
104	Burma (Myanmar)	72.2
105(t)	Angola	72.0
105(t)	Saint Lucia	72.0
107	Kenya	71.8
108(t)	Brazil	71.6
108(t)	Swaziland	71.6
110	China	71.4
111(t)	Senegal	71.2
111(t)	Zambia	71.2
113	Sri Lanka	71.0
114(t)	Jamaica	70.6
114(t)	Togo	70.6
116(t)	Burkina Faso	70.4
116(t)	Ivory Coast	70.4
116(t)	Niger	70.4
119	South Korea	70.2
120(t)	Argentina	70.0
120(t)	Samoa	70.0
122(t)	Belize	69.6
122(t)	Fiji	69.6
124	Eritrea	69.2
125	Botswana	69.0
126	Malawi	68.8
127(t)	Algeria	68.6
127(t)	Ethiopia	68.6
129	Morocco	68.0
130	Benin	67.4
131	Belarus	67.2
132	Guinea-Bissau	66.8
133(t)	Laos	66.4
133(t)	Solomon Islands	66.4
135	Sierra Leone	66.0
136	Pakistan	65.6
137(t)	Cape Verde	65.4
137(t)	Uzbekistan	65.4
139	Barbados	64.6
140	Cuba	64.4
141	Suriname	64.2
142(t)	Cambodia	63.4
142(t)	Egypt	63.4
142(t)	Vietnam	63.4
145	Nepal	63.2
146(t)	Burundi	63.0
146(t)	Ghana	63.0
146(t)	Vanuatu	63.0
149	Democratic Republic of Congo	62.2
150	Nigeria	61.8
151	Rwanda	61.2
152	Russia	60.8
153	Sao Tome and Principe	60.0
154(t)	The Gambia	59.6
154(t)	Guinea	59.6
154(t)	Venezuela	59.6
157	Equatorial Guinea	59.4
158	Chad	58.4
159	Iran	57.4
160(t)	Gabon	57.0
160(t)	Lesotho	57.0
162(t)	The Bahamas	56.0
162(t)	Cameroon	56.0
162(t)	Tonga	56.0
165	Republic of Congo	55.4
166	Kiribati	55.0
167	Syria	54.0
168	Liberia	53.8
169	Tunisia	53.0
170	India	51.0
171(t)	Central African Republic	50.4
171(t)	Zimbabwe	50.4
173	Maldives	44.0
174	Bhutan	42.0
175	Bangladesh	40.2
176	Dijibouti	31.8
177	Seychelles	28.4
178	Comoros	27.2
179	North Korea	0.0

Note: *2008 Index of Economic Freedom* Trade Freedom scores may be obtained at *http://www.heritage.org/index.*

Table 1 • B 2187 heritage.org

The rankings show that for the world as a whole (counting those countries measured in both the 2008 and 2009 editions of the *Index*[2]), average tariffs dropped from 8.1 percent in 2008 to 6.7 percent in 2009. The average trade freedom score for these countries improved from 72.0 in 2008 to 74.4 in 2009.[3] The progress made is certainly not a breakthrough, but it does indicate that many countries are resisting protectionist pressures and moving forward with liberalization.

Action to improve trade freedom was broad-based throughout the world, with 67 countries scoring at least a point higher in 2009 than in 2008.[4] Thirteen countries scored at least 10 points higher, with Libya recording an amazing 50 point increase in trade freedom by virtually eliminating all tariffs.

Trade Freedom—Top Ten Winners and Losers

Gaining Freedom: Country	2008 to 2009 Score Change	Losing Freedom: Country	2008 to 2009 Score Change
Libya	+50.4	Tunisia	–18.8
Bangladesh	+40.2	Rwanda	–9.4
Cape Verde	+24.2	Madagascar	–7.0
The Bahamas	+24.0	Zimbabwe	–5.0
Russia	+16.6	Fiji	–4.6
Belarus	+15.0	Kenya	–3.2
Burundi	+12.8	Uzbekistan	–3.0
Haiti	+12.4	The Gambia	–3.0
Cambodia	+11.2	Egypt	–2.6
Qatar	+10.8	Bosnia and Herzegovina	–2.6

Note: *2008 Index of Economic Freedom* Trade Freedom scores may be obtained at *http://www.heritage.org/index.*

Table 2 • B 2187 heritage.org

By contrast, only 18 countries experienced a decrease in trade freedom of at least one point. Only one country, Tunisia, showed a drop of more than 10 points, falling from 71.8 to 53.0. Rwanda was not far behind with a 9.4 point drop in trade freedom.

Seventy-three countries show little movement at all, with modest increases or decreases in score of less than one point. By essentially standing still, these countries fell behind the better performers but improved their standing vis-à-vis those that succumbed to protectionism.

Economic Gains from Trade

The evidence linking economic growth to trade freedom is strong. According to data from the forthcoming edition of the *Index of Economic Freedom*, countries with freer trade policies experience significantly higher per capita economic growth than countries that maintain trade barriers. The top 10 percent of countries in terms of trade freedom had five-year compound per capita GDP growth rates averaging 5.6 percent.[5] By contrast, the 10 percent of countries with the lowest levels of trade freedom[6] had five-year per capita GDP growth averaging just half as much, or 2.8 percent.

2. The *2009 Index of Economic Freedom* includes 21 countries not measured previously. The newly added countries are Afghanistan, Bhutan, Comoros, Dominica, Eritrea, East Timor, Kiribati, Liberia, Liechtenstein, Macao, Maldives, Micronesia, Papua New Guinea, Saint Lucia, Saint Vincent and the Grenadines, Samoa, Sao Tome and Prinicipe, Seychelles, Solomon Islands, Tonga, and Vanuatu. Because of data constraints for Afghanistan, Iraq, Sudan and Liechtenstein, only 179 countries are fully scored and ranked. For accuracy in discussing year-to-year trends, such comparisons in this paper look only at countries measured in both 2008 and 2009 unless otherwise noted.
3. The average tariff rate for all countries evaluated in 2009 was 7.3 percent. The average trade freedom score for all countries ranked in 2009 was 73.2. These figures are less impressive than those cited in the year-on-year comparisons in the text because of the addition to the rankings of 21 new countries, many of which maintain relatively high tariff rates and thus have lower than average trade freedom scores.
4. While data constraints make it impossible to fully grade Afghanistan and Sudan, we are able to compute trade freedom scores. The trade freedom score for Afghanistan is 73.2, and the trade freedom score for Sudan is 54.4.
5. Compound average growth rate of per capita income from 2002–2006, the most recent years for which data are available.
6. Excluding North Korea, for which income data were not available.

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Changes in trade freedom were also important to GDP growth. The 20 countries whose trade freedom has improved the most over the 15-year history of the *Index* enjoyed per capita GDP growth from 1995 to 2006 averaging 3.35 percent. The 20 countries whose trade freedom scores improved the least (or actually fell in a few cases) saw their per capita GDP grow at an average rate of only 1.37 percent.

Because of the vital link between economic prosperity and trade freedom, it is important that countries strive to advance liberal trade rules and dismantle trade-distorting non-tariff barriers. Countries that have already made significant progress in reducing tariff rates receive higher trade freedom scores than those that still impose high tariffs on trade at the border, but they should not look at these ratings as a reason to rest on their laurels. Instead, these countries should turn their attention to eliminating the non-tariff measures that add to the cost of international trade.

However, the biggest gains to freer trade and economic freedom would be for countries—especially in the developing world—to eliminate what are the world's highest average tariff levels. The impact of freer trade on growth rates and poverty is telling: Real per capita income levels grew about 3 times faster in developing countries that lowered trade barriers than in those countries that did not.[7] The level of tariff protection in developing countries is four times higher than in higher-income countries, and 70 percent of the tariff burden developing country exports face is from other developing countries.[8] These statistics demonstrate that there is ample room for trade reform and significant potential for expanding trade and economic freedom around the world.

Methodology

The trade freedom score reported in this paper is based two inputs:

- Trade-weighted average tariff rates and
- Non-tariff barriers (NTBs).

Different imports entering a country can, and often do, face different tariffs. The weighted average tariff uses weights for each tariff based on the share of imports for each good. Weighted average tariffs are a purely quantitative measure and account for the basic calculation of the score using the following equation:

$$\text{Trade Freedom}_i = (((\text{Tariff}_{max} - \text{Tariff}_i)/(\text{Tariff}_{max} - \text{Tariff}_{min})) * 100) - \text{NTB}_i$$

where Trade Freedom_i represents the trade freedom in country *i*, Tariff_{max} and Tariff_{min} represent the upper and lower bounds for tariff rates, and Tariff_i represents the weighted average tariff rate in country *i*. The minimum tariff is naturally zero, and the upper bound was set as a score of 50. An NTB penalty is then subtracted from the base score. The penalty of 5, 10, 15, or 20 points is assigned according to the following scale:

- **20**—NTBs are used extensively across many goods and services and/or act to impede a significant amount of international trade.
- **15**—NTBs are widespread across many goods and services and/or act to impede a majority of potential international trade.
- **10**—NTBs are used to protect certain goods and services and impede some international trade.
- **5**—NTBs are uncommon, protecting few goods and services, and/or have very limited impact on international trade.
- **0**—NTBs are not used to limit international trade.

Both qualitative and quantitative information is used to determine the extent of NTBs in a country's trade policy regime. Restrictive rules that hinder trade vary widely, and their overlapping and shifting nature makes it difficult to gauge their complexity. The categories of NTBs considered in our penalty include:

- **Quantity restrictions**—import quotas; export limitations; voluntary export restraints; import–export embargoes and bans; countertrade; etc.
- **Price restrictions**—antidumping duties; countervailing duties; border tax adjustments; variable levies/tariff rate quotas.

7. Office of the United States Trade Representative, "Trade Facts: The Benefits of Trade for Developing Countries," July 2008, at *http://www.ustr.gov/assets/Document_Library/Fact_Sheets/2008/asset_upload_file226_15014.pdf* (September 18, 2008)
8. *Ibid.*

- **Regulatory restrictions—**licensing; domestic content and mixing requirements; sanitary and phytosanitary standards; safety and industrial standards regulations; packaging, labeling, and trademark regulations; advertising and media regulations.
- **Investment restrictions—**exchange and other financial controls.
- **Customs restrictions—**advance deposit requirements; customs valuation procedures; customs classification procedures; customs clearance procedures.
- **Direct government intervention—**subsidies and other aids; government industrial policy and regional development measures; government-financed research and other technology policies; national taxes and social insurance; competition policies; immigration policies; government procurement policies; state trading, government monopolies, and exclusive franchises.

As an example, in 2009, France received a trade freedom score of 80.8, based on the weighted average tariff of 2.1 percent common to all European Union countries. The tariff yields a base score of 95.8, but the existence of significant French NTBs reduces the nation's trade freedom score by 15 points.

Gathering data on tariffs to make a consistent cross-country comparison can be a challenging task. Unlike data on inflation, for instance, countries do not report their weighted average tariff rate or simple average tariff rate every year; in some cases, the most recent time a country reported its tariff data could have been as far back as 1993. To preserve consistency in grading trade policy, the authors have decided to use the most recently reported weighted average tariff rate for a country from our primary source. If another reliable source reports more updated information on the country's tariff rate, the authors note this fact and may review the grading if there is strong evidence that the most recently reported weighted average tariff rate is outdated.

The World Bank produces the most comprehensive and consistent information on weighted average applied tariff rates. When the weighted average applied tariff rate is not available, the authors use the country's average applied tariff rate; and when the country's average applied tariff rate is not available, the authors use the weighted average or the simple average of most favored nation (MFN) tariff rates.[9] In the very few cases where data on duties and customs revenues are not available, the authors use data on international trade taxes instead.

In all cases, the authors clarify the type of data used and the different sources for those data in the corresponding write-up for trade policy. Sometimes, when none of this information is available, the authors simply analyze the overall tariff structure and estimate an effective tariff rate.

The trade freedom scores for 2009 are based on data for the period covering the second half of 2007 through the first half of 2008. To the extent possible, the information considered was current as of June 30, 2008. Any changes in law effective after that date have no positive or negative impact.

Finally, unless otherwise noted, the authors used the following sources to determine scores for trade policy, in order of priority: World Bank, *World Development Indicators 2008* and *Data on Trade and Import Barriers: Trends in Average Applied Tariff Rates in Developing and Industrial Countries, 1981–2006*; World Trade Organization, *Trade Policy Reviews*, 1995–2008; Office of the U.S. Trade Representative, *2008 National Trade Estimate Report on Foreign Trade Barriers*; World Bank, *Doing Business 2008* and *Doing Business 2009*; U.S. Department of Commerce, *Country Commercial Guide*, 2004–2008; Economist Intelligence Unit, *Country Report*, *Country Profile*, and *Country Commerce*, 2004–2008; and official government publications of each country.

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9. The most favored nation tariff rate is the "normal," non-discriminatory tariff charged on imports of a good. In commercial diplomacy, exporters seek MFN treatment; that is, the promise that they will be treated as well as the most favored exporter. The MFN rule requires that the concession be extended to all other members of the World Trade Organization. MFN is now referred to as permanent normal trade relations (PNTR).

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