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REVIEW OF THE ROLE OF TRADE IN THE WORK OF THE FUND

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- The **Staff Report** on Review of the Role of Trade in the Work of the Fund, prepared by IMF staff and completed on February 2, 2015 for the Executive Board's consideration on February 27, 2015.
- A **Press Release** summarizing the views of the Executive Board as expressed during its February 27, 2015 consideration of the staff report.

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International Monetary Fund
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REVIEW OF THE ROLE OF TRADE IN THE WORK OF THE FUND

EXECUTIVE SUMMARY

February 2, 2015

This review follows the Board-endorsed recommendation by the IEO in 2009 to have an assessment of the Fund’s work on trade every five years. In addition to reviewing past work, this paper discusses key issues going forward towards a future trade agenda for the next five years. This reflects the need to operationalize the implications of the changing trade landscape, including the changing drivers of trade—such as global value chains (GVCs)—and the movement of the fulcrum of trade policy from multilateral rounds to regional and plurilateral deals.

Growth in global trade has slowed as the benefits of past reforms and integration trends have matured and new reforms have languished. Trade grew more rapidly than global growth in the last few decades, contributing to higher growth and productivity by allowing countries to integrate and specialize in what they do best. But over the last few years global trade has slowed down as momentum has faded and GVCs in several regions have matured.

Trade is an essential component of the global policy agenda to bolster growth. A new momentum is needed in policies amid heightened risks to global growth and concerns over a “new mediocre.” At a country and global level, trade reforms can complement and augment the benefits of other structural reforms, are an important element of infrastructure investment, and support the strengthening of policy and institutional frameworks. These reforms would enable countries to participate in GVCs.

There are potentially important gains to be made from further trade integration and expansion of global supply chains. These gains come from traditional liberalization in many countries (in particular low-income countries and many emerging market economies, for which applied and bound tariffs remain about five times higher than advanced economies on average) and sectors (e.g., agriculture) including via unilateral efforts; from lowering barriers in new trade policy frontiers (services, regulations, investment); and from additional expansion of global supply chains, particularly to regions and countries that have missed out on these opportunities in the past.

Reigniting global trade integration would require an open architecture that allows different speeds and depths, but also coherence among preferential and multilateral

efforts. The finalization of the Bali agreement is welcome, but earlier impasses as well as the longstanding difficulties to advance the Doha Round have emphasized the need to buttress the governance of the multilateral trading system. With the fulcrum of trade policy moving to regional and plurilateral deals, new trade liberalization initiatives should seek to avoid fragmenting trade, even as renewed efforts are made to prop and retool the governance of the multilateral system, with the WTO at its center. Heightened and coordinated vigilance will also be needed to avoid new forms of protectionism as well as, in some cases, traditional tariff protection.

Better embedding macro-critical trade issues in the work of the Fund will require a concerted effort. This will involve clearer institutional views on trade and trade policy issues; continued analytical work; enhanced efforts to translate key implications of the trade and trade policy landscape, particularly for bilateral and regional surveillance; prioritizing bilateral work on macro-relevant areas specific to various country groups; revising guidance; and the review process. The Fund's work on trade will need to take into account resource constraints and limited trade expertise, thus requiring careful prioritization and continued collaboration with other international institutions.

The focus of surveillance in advanced countries, emerging market economies and low-income countries going forward should respond to their distinct macro-critical nature and differential needs.

- For most *advanced countries* a key issue will be the implications of their efforts to pioneer and advance the new trade policy frontiers, opening services markets and making their regulatory systems more coherent (i.e. better aligning domestic regulations through dialogue among regulators, mutual recognition and, in some cases, harmonization), with potential gains to themselves and to others if these initiatives minimize fragmentation and are eventually multilateralized.
- Many *emerging market economies*, for example in South Asia and Latin America, can still benefit greatly from integrating via traditional liberalization, including on a unilateral basis, and by anchoring their economies to GVCs, moving away from import-substitution policies that have failed in the past and avoiding protectionism through the use of non-tariff barriers. Trade liberalization complements and augments the benefits of structural reforms and supports the strengthening of policy and institutional frameworks.
- *Low-income countries* need trade and integration to GVCs as a central plank of their development and growth strategy, for which trade facilitation is critical. They can benefit by removing forms of protectionism that hinder job creation and export growth. For these economies, addressing traditional trade barriers, such as upgrading poor trade infrastructures, and improving economic institutions are still crucial. Technical assistance could be needed to support integration, including on how to adapt to a less protected environment (e.g., fiscal implications of lower tariffs); sequence, pace and coordinate reforms; and take advantage of improved access to advanced economies' markets.

Approved By
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INTRODUCTION AND KEY MESSAGES

A. Overall Context of the Review

1. This review follows the Board-endorsed recommendation by the IEO in 2009 to have an assessment of the Fund’s work on trade every five years.¹ The review of the role of trade in the work of the Fund is a deliverable under the implementation plan in response to Board-endorsed recommendations arising from the IEO Evaluation of IMF Involvement in International Trade Policy Issues (IMF, 2009; see Annex I). The IEO evaluation noted that the Fund had curtailed its work on trade, and the Board called to focus trade work on macro-relevant issues and to pay greater attention to trade in multilateral surveillance. The review provides a broad overview of the role of trade and trade policy issues in the work of the Fund over the past five years and proposes a work agenda for the next five years prioritizing key areas. In particular, the review will focus on systemic and macro-critical trade issues to: (i) lay out the changing trade and trade policy landscape and its implications for the Fund; (ii) review the role of trade in the work of the Fund with a view to assess any major gaps; and (iii) identify systemic/macro-critical trade issues towards a future trade agenda going forward.²

2. In addition to reviewing past work, this paper discusses key issues going forward towards a future trade agenda for the next five years. This reflects the need to operationalize the implications of the changing trade landscape, including the changing drivers of trade—such as global value chains (GVCs)—and the movement of the fulcrum of trade policy from multilateral rounds to regional and plurilateral deals.

3. In the last few decades, global trade growth raced ahead of GDP growth, supporting the latter and increasing interdependence. This exceptional trade growth has been due to the widening of WTO membership, notably China’s accession; rapid expansion of GVCs; and increasing role of South-South trade. This process, however, has been uneven across countries, with substantial room for further trade integration for many developing economies.

4. On the trade policy side, there have been two important shifts in recent years: (i) trade liberalization efforts have in part migrated from multilateral to preferential and plurilateral negotiations and (ii) the focus has moved from tariffs to non-tariff measures (NTMs). The post-war multilateral trading system allowed countries to rapidly integrate into the global economy. Meanwhile, this system has always interacted with regional trade arrangements. However, Preferential Trade Agreements (PTAs) are becoming more important in recent years, in part due to the slow progress at the WTO. NTMs such as divergent standards may be the main trade policy barrier going forward but are more difficult to measure than tariffs. Moreover, their welfare impact,

¹ See Annex I for an overview of the IEO Evaluation of IMF Involvement in International Trade Policy Issues.

² See Annex II for a description of The Legal Framework Underpinning the Fund’s Work on Trade Matters.

in some cases, is undetermined and they posit important challenges as they intersect public policy and trade policy.

B. Trade in Recent Years

5. Growth in global trade has slowed as the benefits of past reforms and integration trends have matured and new reforms have languished. Trade grew more rapidly than global growth in the last few decades, contributing to higher growth and productivity by allowing countries to integrate and specialize. But over the last few years global trade has slowed, as trade liberalization momentum has faded and GVCs in several regions have matured. Earlier, WTO membership allowed countries, most notably China, to rapidly integrate into the global trading system even as supply chains were built in Asia, Europe, and North America.

6. The Fund has done significant analytical work on trade, keeping up with the changing landscape, but uptake of such analyses has been uneven, including in bilateral surveillance. Over the last five years, significant analytical work has been done to understand the changing trade landscape and its implications. Some of the key issues included the great trade collapse in the wake of the Global Financial Crisis, the emergence of GVCs in several regions, spillovers through trade channels, and more recently the global trade slowdown. Amid an impasse in trade policy during this period, trade developments received greater attention than trade policy.

- **Trade received greater attention during the Global Financial Crisis and has increasingly played a greater role in the context of GVCs.** Issues such as the great trade collapse—and the need to avoid protectionism—and the advent of GVCs have tended to figure more prominently in bilateral surveillance, particularly for advanced and emerging market economies, although the depth of coverage has been uneven.
- **The integration of trade issues into the overall assessment and policy recommendations in bilateral surveillance has been limited.** This may have been due to a confluence of factors, including prioritization of issues during the Global Financial Crisis; a perception that trade was less relevant for the work of the Fund; and the significant change in trade landscape requiring time to understand its implications.

In general, the potential benefits of trade integration for global and country growth have received limited attention, both directly and as complement to other structural reforms.

C. Key Issues and Challenges Going Forward

7. Trade integration can be an essential component of country and global policy agendas. A new momentum is needed in policies amid heightened risks to global growth and concerns over a “new mediocre.” At a country and global level, trade reforms can complement and augment the benefits of other structural reforms, including by increasing external competition, forming an important part of infrastructure investment, and supporting the strengthening of institutional frameworks.

Towards a Future Trade Agenda: Some Key Considerations

8. There are potentially large global gains to be derived from further trade liberalization and integration. These gains come from traditional liberalization in many countries (in particular, low-income countries (LICs) and many emerging market economies, for which applied and bound tariffs are about five times higher than advanced economies on average) and sectors (e.g., agriculture); from lowering barriers in new trade policy frontiers (services, regulations, investment); and from additional expansion of global supply chains, particularly to regions and countries that have missed out on these opportunities in the past. Important reforms can be adopted on a unilateral basis, including not only traditional trade liberalization (e.g., reducing tariffs) but also improvements in trade facilitation (e.g., customs reforms and upgrades in trade infrastructures).

9. Reigniting global trade integration would require an open architecture that allows different speeds and depths, but also coherence among preferential and multilateral efforts. The finalization of the Bali agreement is welcome, but earlier impasses as well as the longstanding difficulties to advance the Doha Round have emphasized the need to buttress the governance of the multilateral trading system. With the fulcrum of trade policy moving to regional and plurilateral deals, trade liberalization initiatives should avoid fragmentation, even as renewed efforts are made to prop and retool the governance of the multilateral system, with the WTO at its center. The challenges and priorities ahead include:

- **New liberalization arrangements should be open, transparent and comprehensive.** Trade liberalization efforts are currently taking place mainly via preferential (e.g., Trans-Pacific Partnership (TPP) and Transatlantic Trade and Investment Partnership (TTIP)) and plurilateral negotiations (e.g., Trade in Services Agreement (TISA) and Information Technology Agreement (ITA)), which can help advance liberalization in new trade areas. To avoid fragmenting the global trading system such arrangements should be open (i.e., they should eventually be available to all comers who are willing to meet the standards of the agreements), transparent, comprehensive (in terms of coverage of sectors and issues), and minimize discrimination between members and non-members (particularly with respect to regulatory requirements). Over time, arrangements based on these principles can maximize the benefits of deals and ignite reciprocal opening efforts from non-members. They can also limit the risk of backlash to integration by avoiding a sense that trade is only advancing for a preferred “club” of countries.
- **Advancing integration in new trade areas (services, regulations, investment) may take new paths but also require retooling the global governance of trade.** These initiatives have large potential benefits but also intersect with legitimate national policies and regulatory concerns, making the process very different and much more complex than past trade negotiations that mainly focused on lowering tariffs. Moreover, the eventual multilateralization of these agreements would have major implications for the global governance of the trading system.
- **Traditional trade liberalization such as tariff liberalization and trade facilitation is still needed.** It is important for many low-income countries as well as a swathe of emerging market economies, as tariffs remain higher than in advanced economies. However, trade liberalization in LICs requires parallel efforts on revenue mobilization to offset for the lost tariff revenues and a

careful choice of proper sequencing and pace of market opening (including on the liberalization of financial services, taking into account financial stability considerations). Reducing trade costs for LICs also requires a sustained effort to improve trade facilitating infrastructures and reduce other impediments such as unnecessary border procedures.

- **Heightened and coordinated vigilance will be needed to avoid both old and new forms of protectionism.** The WTO has been effective in evidencing and limiting traditional protectionism through higher tariffs and other border measures but there is a risk that protectionism will increase through diverse non-tariff measures such as undue regulatory barriers, for which large data gaps exist.

10. The focus of surveillance in advanced countries, emerging market economies and low-income countries going forward should respond to their distinct macro-critical nature and differential needs.

- For most *advanced countries* a key issue will be the implications of their efforts to pioneer and advance the new trade policy frontiers, opening services markets and making their regulatory systems more coherent (i.e. better aligning domestic regulations, through dialogue among regulators, mutual recognition and, in some cases, harmonization), with large potential gains to themselves and to others if these initiatives minimize fragmentation and are eventually multilateralized.
- Many *emerging market economies*, for example in South Asia and Latin America, can still benefit greatly from integrating via traditional liberalization, including on a unilateral basis, and by anchoring their economies to GVCs, moving away from import-substitution policies that have failed in the past and avoiding protectionism through the use of non-tariff barriers. Trade liberalization complements and augments the benefits of structural reforms and supports the strengthening of policy and institutional frameworks.
- *Low-income countries* need trade and integration to GVCs as a central plank of their development and growth strategy, for which trade facilitation is critical. They can benefit by removing forms of protectionism that hinder job creation and export growth. For these economies, addressing traditional trade barriers, such as upgrading poor trade infrastructures, and improving economic institutions are still crucial. Technical assistance could be needed to support integration, including on how to adapt to a less protected environment (e.g., fiscal implications of lower tariffs); sequence, pace and coordinate reforms; and take advantage of improved access to advanced economies' markets.

Operationalizing a Future Trade Agenda

11. Better embedding macro-critical trade issues in the work of the Fund will require a concerted effort.³ This will involve clearer institutional views on trade and trade policy issues; continued analytical work; enhanced efforts to translate the key implications of the trade and trade

³ See Annex II.

policy landscape, particularly for bilateral and regional surveillance; prioritizing bilateral work on macro-relevant areas specific to each country and linking it to the overall assessment and policy recommendations; and review practices. The Fund's work on trade will need to take into account resource constraints and limited trade expertise, thus requiring careful prioritization and continued collaboration with other international institutions.

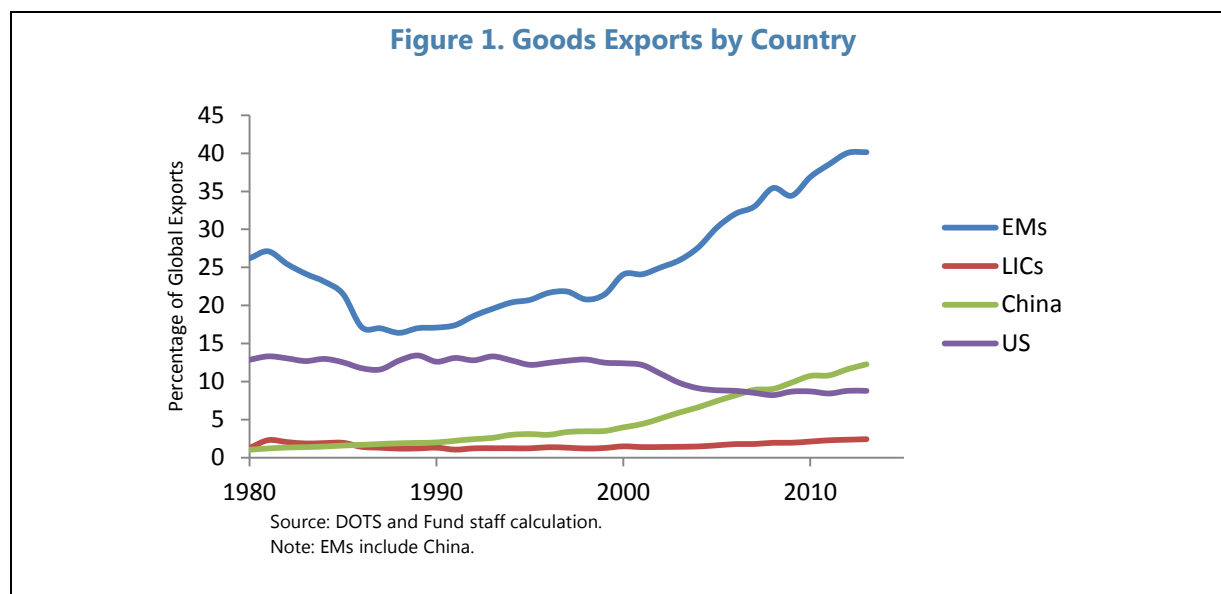
EVOLUTION OF TRADE AND TRADE POLICY LANDSCAPE IN RECENT YEARS

A. Changing Trade Landscape

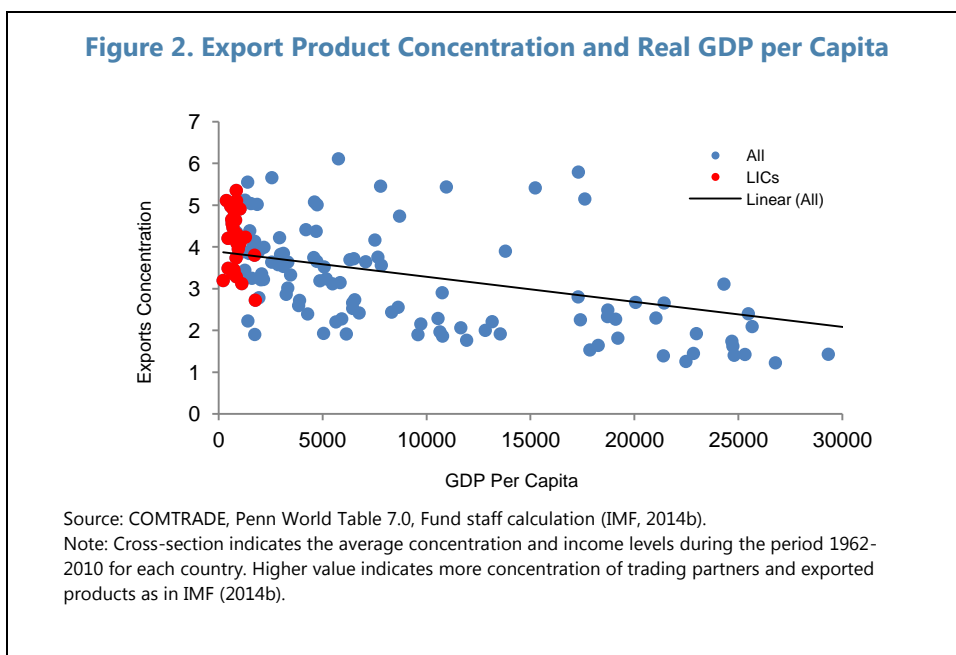
In the last few decades, global trade growth raced ahead of GDP growth, supporting the latter and increasing interdependence. This exceptional trade growth has been due to the widening of WTO membership, notably China's accession; rapid expansion of GVCs; and increasing role of South-South trade. This process, however, has been uneven across countries, with substantial room for further trade integration for low-income and emerging market economies.

Old and New Global Trade Players

12. Global trade has increased dramatically during the last three decades, particularly for emerging markets (EMs). The value of world goods exports increased from US\$2 trillion in 1980 to over US\$18 trillion in 2013, growing 6.8 percent per year. In turn, trade volumes became four times larger over the same period (WTO, 2013). The significant reduction of trade barriers due to technological, transportation, and policy changes made this possible. In 1980, developed economies represented nearly 73 percent of the world goods exports. The United States was the leading exporter with nearly 13 percent of global goods exports (Figure 1). Through this period, EMs and LICs increased their participation in total world goods exports from 27 percent in 1980 to 43 percent in 2013. In particular, China gained ground from 1 percent of global goods exports in 1980 to 12 percent in 2013. Higher exports led to higher GDP in EMs and LICs which nearly doubled their share of global goods imports from 23 percent in 1980 to 40 percent in 2013 (WTO, 2013).

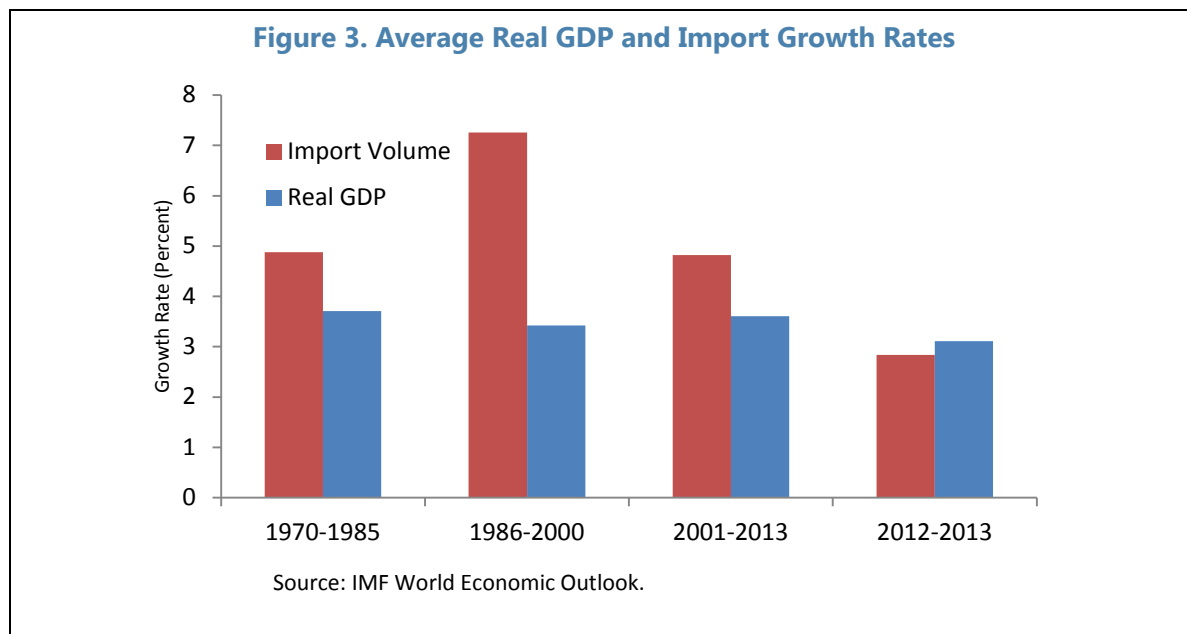


13. However, trade integration of EMs and LICs has been highly uneven and there is substantial room for further integration. The integration of EMs into the global trading system has differed substantially across countries. For instance, China's trade intensity (imports plus exports to GDP ratio) increased enormously from 13 percent in 1980 to 46 percent in 2013, while Brazil's trade intensity increased more moderately from 20 percent to 28 percent. In turn, LICs represented less than 3 percent of global exports in 2013, with substantial structural barriers to trade. Figure 2 shows a positive association between exports diversification and GDP per capita. LICs that invested in infrastructure, trading networks, and human capital increased the number of trading partners and exported products, with greater trade diversification associated with higher and less volatile growth (IMF, 2014b). Trade and trade integration play different roles in the growth strategy of different countries but there is substantial room for further growth of international trade across EMs and LICs.



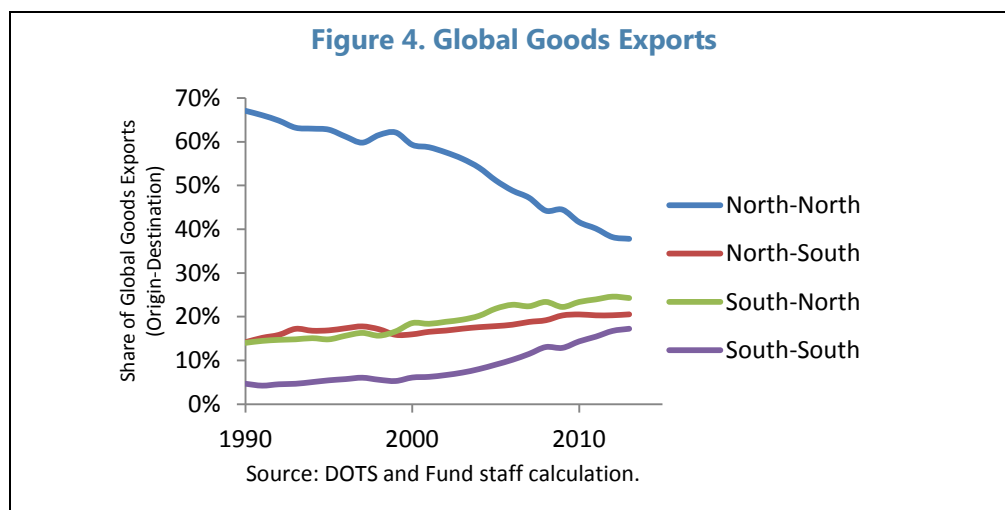
14. Trade growth suffered an abrupt, severe, and synchronized collapse in late 2008 and early 2009. The annualized drop in imports was 30 percent between the last quarter of 2008 and the first quarter of 2009 and affected advanced and developing economies equally (IMF, 2010a). Imports rebounded afterwards at an annualized rate of 20 percent during the next three quarters. However, the recovery left global trade below its pre-crisis trend. Moreover, imports remained below pre-crisis levels for countries directly affected by financial and banking crises, limiting the recovery of exports of countries not directly affected by financial crises.

15. Trade growth has been sluggish after the recovery from the Great Recession. Trade volumes grew about 3 percent in 2012 and 2013, substantially lower than the pre-crisis average of 7.1 percent (1987 to 2007) (Figure 3). Structural changes contributing to this global trade slowdown may have begun before the crisis: estimates of the long-run world elasticity of trade to GDP decreased from 2.2 in 1986-2000 to 1.3 in 2001-2013, matching the elasticity for the 1970-1985 period. Changes in the structure of trade, notably the rapid expansion of global value chains in the 1990s and the slower pace in the 2000s can help explain this pattern (Constantinescu, Mattoo and Ruta, 2015). Similarly, the slower pace of trade liberalization in the 2000s relative to the 1990s may have contributed to the global trade slowdown in recent years.

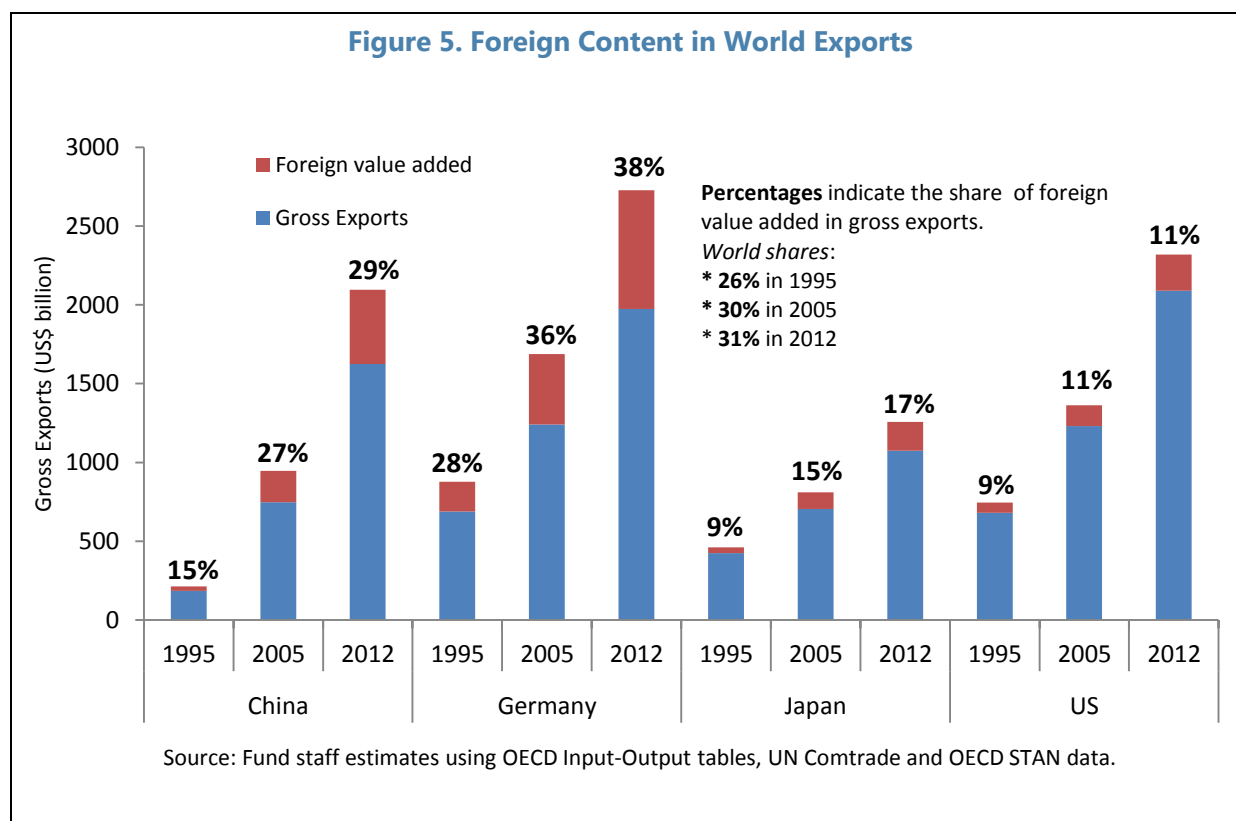


Changing Patterns of Trade

16. EMs and LICs did not only trade more in general but also more among themselves. The trade between advanced economies (AEs) as a share of global trade shrank over the last two decades, with the percentage of global goods exports among AEs (North-North trade) decreasing from 67 percent of total exports in 1990 to 38 percent in 2013 (Figure 4). Meanwhile, the share of global goods exports among EMs and LICs (South-South trade) rose steadily from 5 percent of total exports in 1990 to 17 percent in 2013. This remarkable growth of South-South trade coincided with a relatively stable share of global trade between AEs and EMs or LICs (North-South trade) (WTO, 2013).



17. GVCs expanded substantially in some regions, creating a trade-investment-service nexus. Technological advances in transportation and communication and trade liberalization reduced transaction costs and facilitated the unbundling of production across borders. These GVCs are one of the main reasons behind the growth of global trade and the increasing participation of some EMs such as China. World merchandise trade volume has grown much faster than global GDP during the last three decades (WTO, 2013). The advent of GVCs help to explain the rapid growth in gross global trade as exports increasingly contain more imported intermediated components, with inputs crossing borders multiple times before being assembled and sold to final consumers. Vertical specialization has increased since the mid-1990s (Figure 5). This increase has been particularly pronounced for China (where the share of imported content of exports increased by 12 percentage points from 1995 to 2005) and for Germany and Japan (8 and 6 percentage points, respectively), with the emergence of GVCs contributing significantly to their rise as major exporting powerhouses. In contrast, the share of foreign content in gross exports is lowest for the United States (IMF, 2011a). GVCs are highly concentrated in specific regions—North America, Europe and Southeast Asia—leaving out most LICs and many EMs.

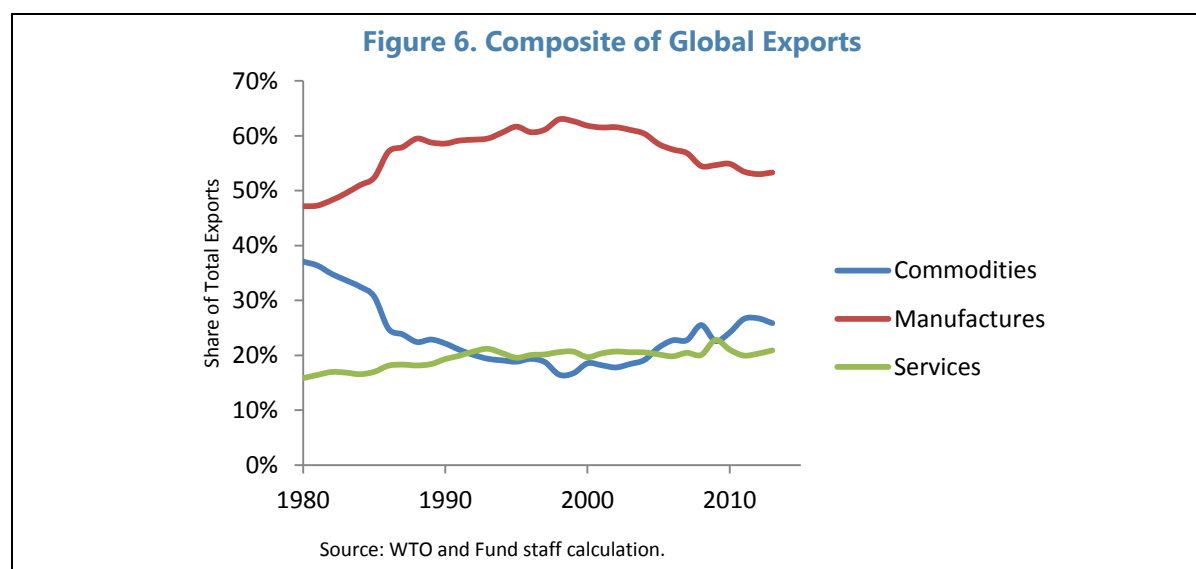


18. AEs and EMs/LICs play different roles in GVCs, with the latter having a greater downstream presence. AEs tend to be upstream in the supply chain with a smaller foreign content in their exports which are sent to downstream countries. EMs and LICs tend to be positioned downstream with relatively large foreign contents in their exports (IMF, 2011a). Thus total exports do not necessarily reflect the contribution to growth, with attention needed on the value added at each stage of production. However, the emergence of GVCs allowed some EMs to increase the

technological content of their exports and move upstream in the value added chain (IMF, 2011a), making those EMs' exporting sectors more similar to AEs.

Changes in the Composite of Trade

19. Commercial services trade grew slightly faster than goods trade during the last three decades. The value of world commercial services exports increased from US\$370 billion in 1980 (16 percent of total exports) to US\$4.6 trillion in 2013 (21 percent of total exports), growing about 8 percent per year (WTO, 2013) (Figure 6). Services such as transportation and financial services are closely related to goods trade, and have greater value added than manufacturing in GVCs.



20. Financial services are of particular importance, providing working capital and reducing payment risk in international trade (trade finance). Bank-intermediated trade finance supports one-third of global trade and has grown fast particularly for EMs and LICs (BIS, 2014). Trade finance declined suddenly during the Global Financial Crisis but also recovered rapidly suggesting that it was only a partial contributor to the trade collapse (Ahn, 2011, and Asmundson et al., 2011). Currently, the most rapidly growing and competitive trade finance services are related to GVCs, including management of the collection and funding of receivables within the networks (BIS, 2014).

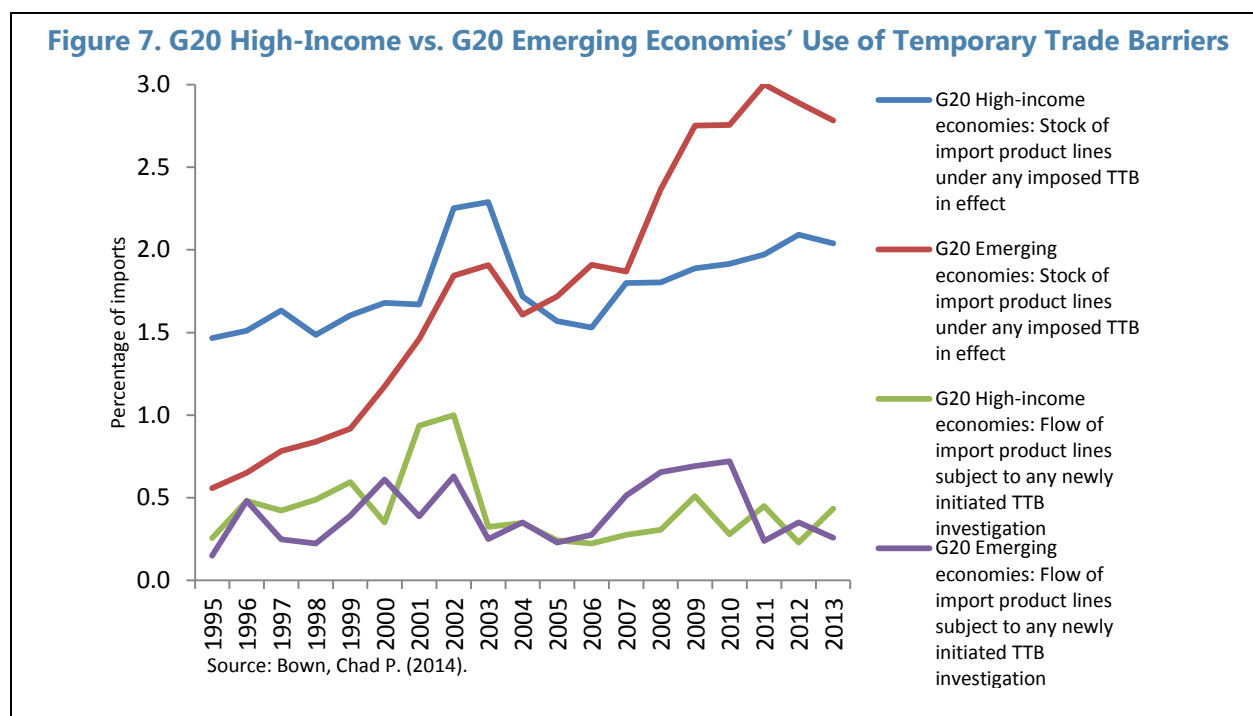
B. Changing Trade Policy Landscape

On the trade policy side, there have been two important shifts in recent years: trade liberalization efforts have in part migrated from multilateral to preferential and plurilateral negotiations, and the focus has moved from tariffs to non-tariff measures (NTMs).

The Crisis and the Risk of Protectionism

21. Despite initial fears, traditional trade barriers did not appear to rise significantly during the Great Recession, but there are concerns of a rise in less transparent forms of

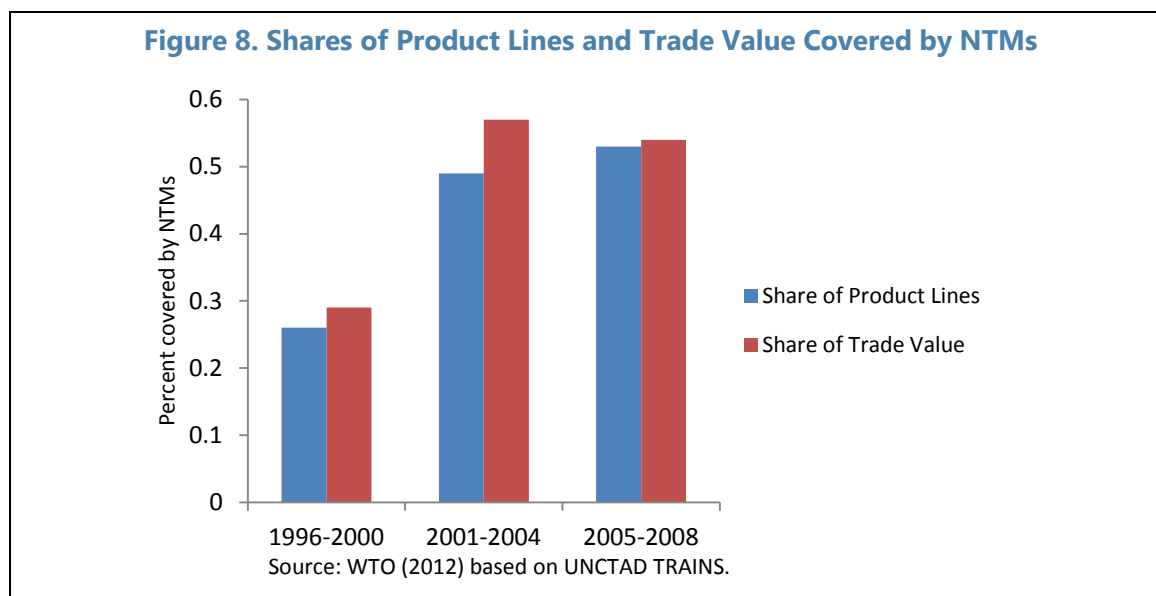
protectionism. The experience since the Great Depression showed that import tariffs and temporary trade barriers (e.g., antidumping and countervailing duties) tended to rise during periods of economic weakness. This however was not the case during the Great Recession in AEs (Bown and Crowley, 2013) and most EMs and LICs (Kee et al., 2013), although the latter implemented bilateral import restrictions more frequently than AEs through temporary trade barriers (Figure 7). This was perhaps one of the key collective actions taken by the international community at a crucial juncture to minimize the spread and amplification of the Global Financial Crisis aftershocks (IMF, 2010b). However, the Global Trade Alert reports an increase in less transparent protectionist measures, such as various forms of subsidies (e.g., bailouts, tax concessions, and export subsidies) and local content requirements (Evenett, 2014).



Tariffs vs. Non-tariff Measures

22. NTMs, such as divergent standards, are increasingly more important than traditional trade barriers and more difficult to measure. In the post-war periods, there was a significant reduction of trade barriers. The average tariffs in Western Europe and North America fell from 15 percent in 1952 to 4 percent in 2005, mainly in the 1950s and 1960s (WTO, 2007). Many developing countries followed this path only in the 1980s when their tariffs came down markedly as well (IMF, 2011a and 2011b). However, NTMs appear to have increased both in the number of products covered and the number of countries that utilize them (Figure 8). NTMs are classified into Technical Measures, such as Technical Barriers to Trade (TBT) or Sanitary and Phytosanitary (SPS) measures, and Non-Technical Measures, such as contingent trade protective measures (UNCTAD, 2013). The use of NTMs grew steadily since mid-1990s, rose sharply in early 2000s and flattened out afterwards (WTO, 2012), although this increase may in part reflect improved coverage of the

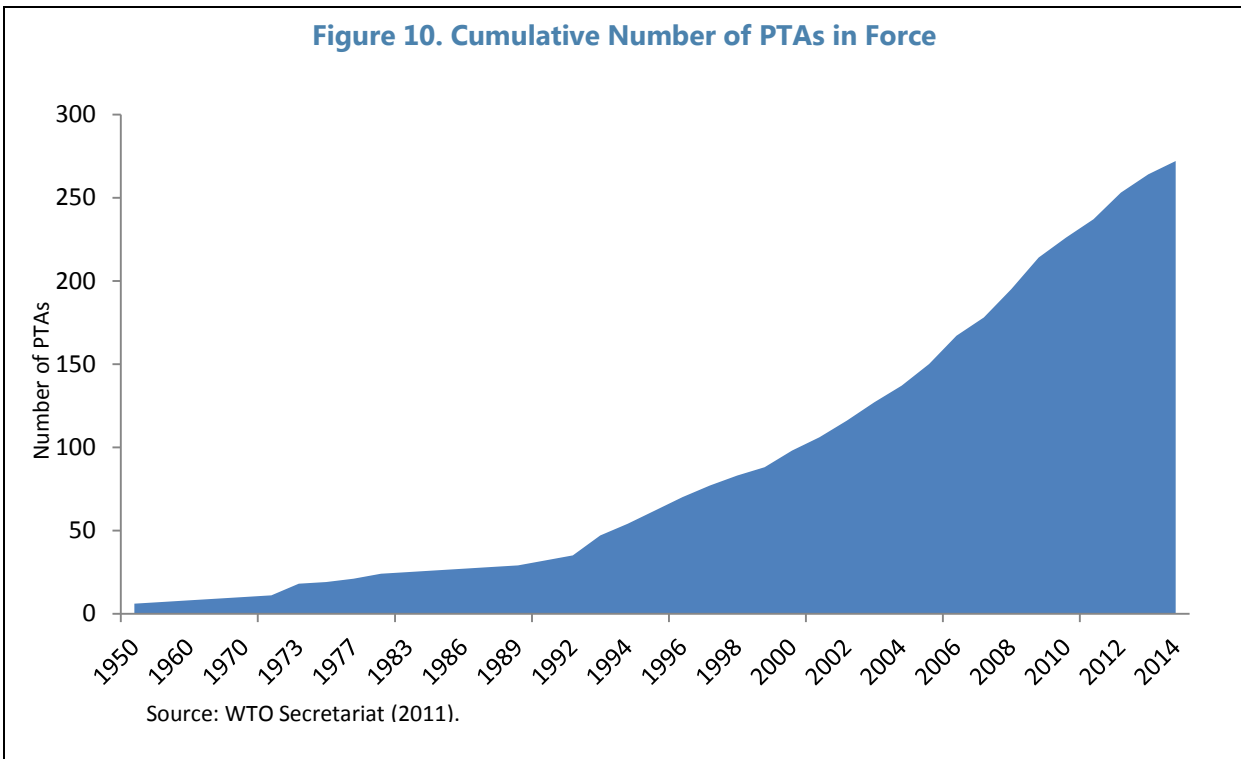
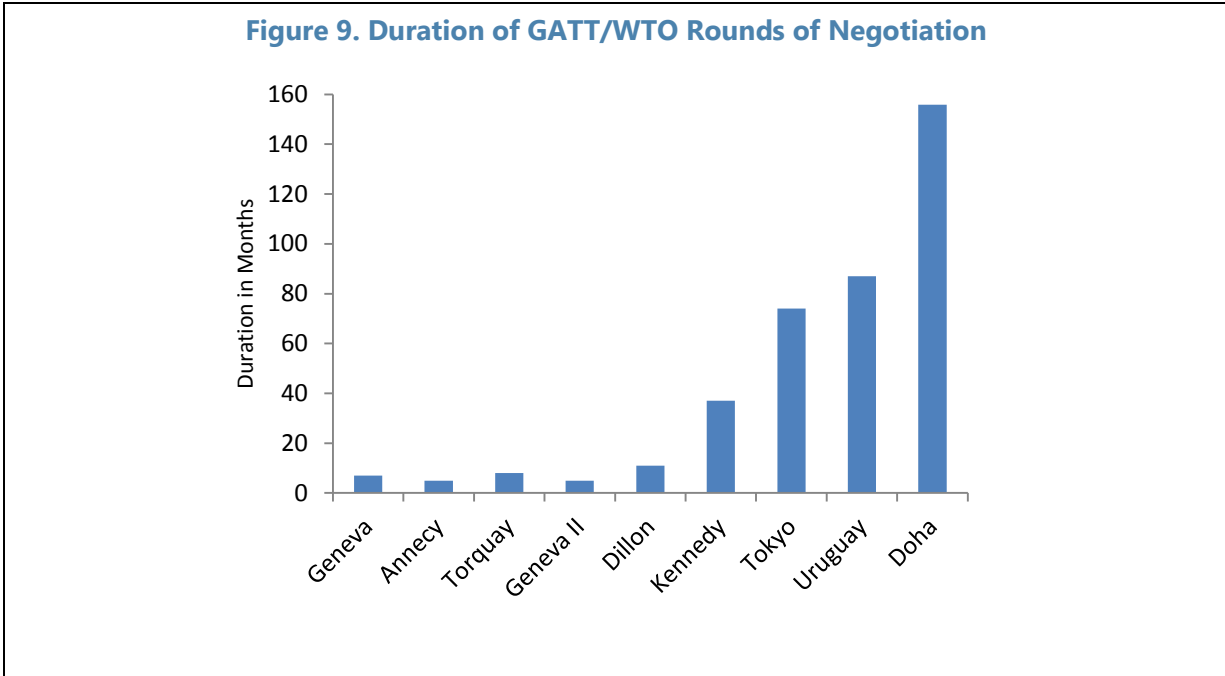
measures. However a thorough assessment is challenging since the quality of the data on NTMs is inadequate as NTMs differ across countries and are not recorded systematically (UNCTAD, 2013).



23. The use of NTMs presents a challenge as they intersect with legitimate public policy and regulatory concerns. NTMs are an important component of trade costs, almost doubling the trade restrictiveness of tariffs (WTO, 2012). This is particularly important for AEs (compared to EMs and LICs) and for agricultural products (compared to manufactured goods). However, many NTMs address legitimate national policies and regulatory concerns such as food safety or environmental issues, making it more difficult to assess the intent. More transparency in the use of NTMs and a more unified institutional framework across countries are therefore imperative (WTO, 2012).

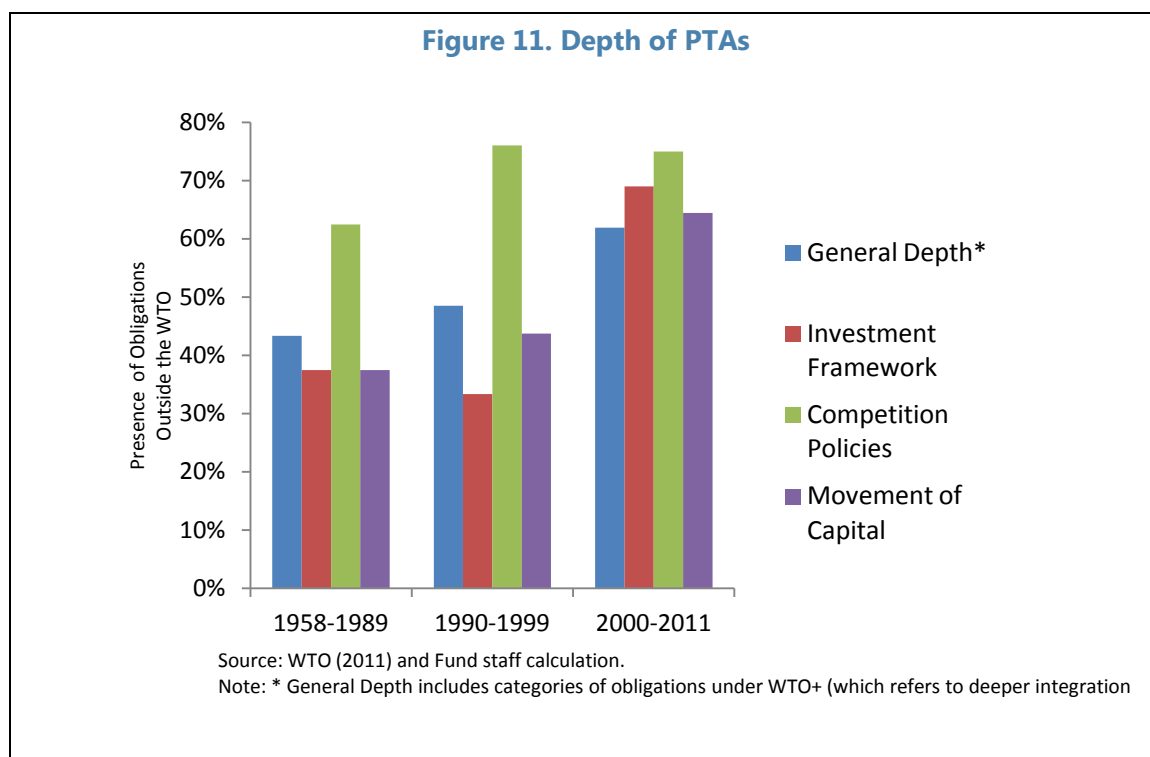
Difficulties of the Multilateral Trade Regime and the Rise of “Deep” Preferential Trade Agreements (PTAs)

24. Trade liberalization efforts have in part migrated from multilateral to preferential and plurilateral negotiations. The General Agreement on Tariffs and Trade (GATT) in 1947 was one of the main forces behind the significant reduction in tariffs in the post-war period. However, each round of negotiation has been taking more time than the previous one (Figure 9). The Doha Round, which started in 2001, is not yet concluded with the recent difficulties to deliver on the Bali agreement highlighting the challenges of multilateral negotiations. Meanwhile, PTAs, which grew steadily to 70 agreements in 1990, expanded rapidly since then to reach almost 300 PTAs in force by 2014 (Figure 10). All except for one WTO member belong to at least one PTA, increasingly transcending regional boundaries with the most recent PTAs being cross-regional. This trend has led to higher trade within PTAs members: intra-PTA trade increased from 18 percent of total world merchandise trade in 1990 to 35 percent in 2008 (WTO, 2011).



25. PTAs are increasingly “deep” as they cover issues beyond tariffs and in the realm of domestic policy and regulation. The increasing importance of NTMs and the advent of GVCs have led to “deeper” PTAs (Figure 11). These PTAs sought to provide the necessary institutional framework to handle more complex NTMs and facilitate the integration of production processes

through greater regulatory coherence in services, investment, competition policies and intellectual property.



THE WORK OF THE FUND ON TRADE ISSUES

In the past five years, trade has played different roles in the work of the Fund in multilateral and bilateral surveillance, research, trade-related technical assistance, and collaboration with the WTO and other institutions. The review of the Fund's work suggests that while analytical work has kept up with the changing trade landscape, covering key issues such as the great trade collapse, GVCs, and trade spillovers, coverage of trade and trade policy issues in bilateral surveillance has been limited, with scope for better integration with multilateral surveillance.

A. Methodology

26. The analysis is based on three complementary evaluation approaches aiming at reviewing systematically bilateral and multilateral work vis-à-vis the main trade issues between 2009 and 2013 (see Annex III for details of the methodology). The first pillar relies on *textual analysis* of all staff reports over the last five years, using a simple search engine to extract the number of times trade-related words and key phrases have been used in a particular country document in order to estimate the overall coverage of trade and trade policy issues and coverage of specific issues. The second pillar involves a *structured review* by Fund staff of a representative sample

of staff reports using a common template.⁴ The third pillar entails a review of multilateral and research work in collaboration with *external experts* (Avinash Dixit of Princeton University and Douglas Irwin of Dartmouth College), as well as other areas (e.g., technical assistance and collaboration with other institutions). In addition, *interviews with stakeholders* were conducted, including the WTO, World Bank, OECD and International Trade Center. These inputs have provided useful information, helping to identify the key issues and priorities going forward.

B. Review of Multilateral Surveillance and Research

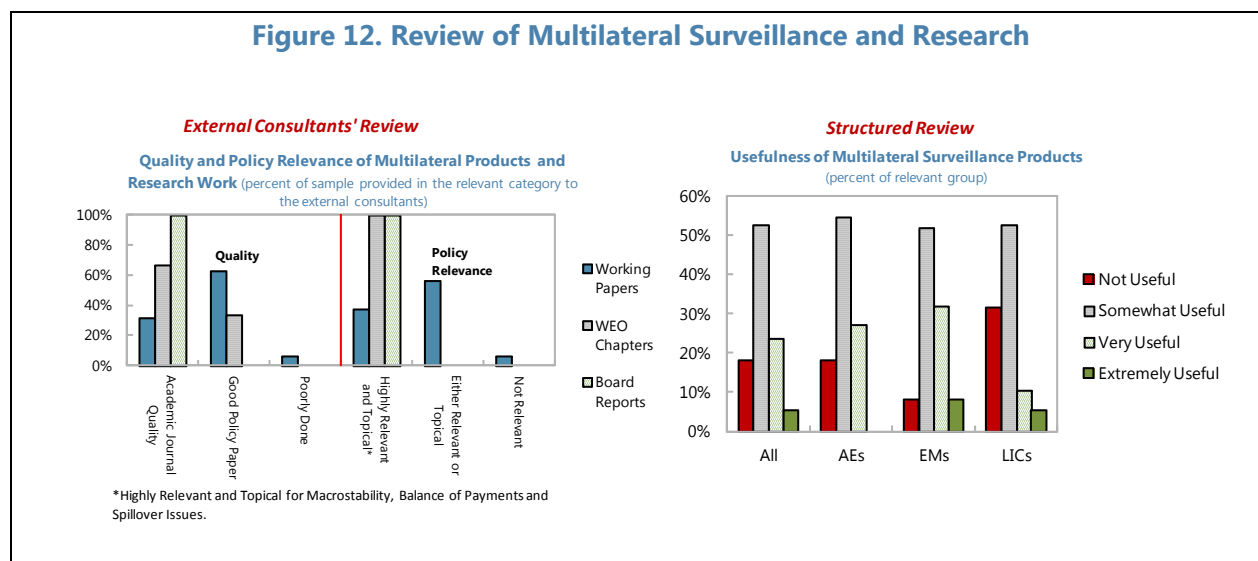
Multilateral products and research were of high quality and policy relevance, but were not well used in bilateral surveillance.

27. The Fund’s analytical work was considered to be of high quality and policy relevance.

According to the external experts, the Fund’s multilateral surveillance and research work have successfully identified the key issues in trade and trade policy that overlap with the Fund’s macroeconomic focus. These include changes in trade patterns (new trade players; GVCs; and rise of services trade, particularly financial services) and changes in trade policy (the crisis and the risk of protectionism; non-tariff measures; free trade agreements; and the difficulties of the multilateral trading system). A summary of the experts’ views on the Fund’s research work is provided in Box 1.

28. In the structured review, however, staff often saw the multilateral surveillance products as not directly useable. While most reviewers found the trade-related parts of these products at least “somewhat useful,” only a minority found them “very useful” or “extremely useful”, and this perception holds across the board (Figure 12). Some reviewers reported difficulty in tailoring the general policy implications from multilateral products to country specific conditions.

⁴ The main text presents the results of the structured review by income groups. See Annex IV for the results by regional groupings.

Figure 12. Review of Multilateral Surveillance and Research


Box. 1. Views of External Experts on Fund's Research Work

There seemed to be an inverse relationship between academic quality and policy relevance in the Fund's Working Papers, which may reflect appropriately the diverse nature of Fund's research. These papers exhibited great diversity of talents and interests among Fund staff. However, the higher the academic quality (i.e., suitability for journal publication), the lower was the policy relevance, in the sense that high quality work tends to focus on relatively narrow, well-defined topics. The most policy relevant work were surveys that brought together results from various studies and synthesized them into broad messages that were useful for policymakers. This diversity can be appropriate given the varying objectives of Fund's research.

The specific chapters on trade issues in the World Economic Outlook reports were of high quality and policy relevance. The first chapter adequately discussed relevant trade issues, and, when appropriate, provided boxes with excellent surveys and analyses. The second chapter, covering regional perspectives, could benefit from a discussion of interactions and spillovers among the various regions. In addition, some of the Regional Economic Outlook reports brought out trade policy issues that were missing in the broader multilateral products.

The Board papers brought to the fore the relevant trade and trade policy issues and highlighted the changing trade landscape. These papers often provided a useful overview of relevant trade issues, though could be more focused in several cases.

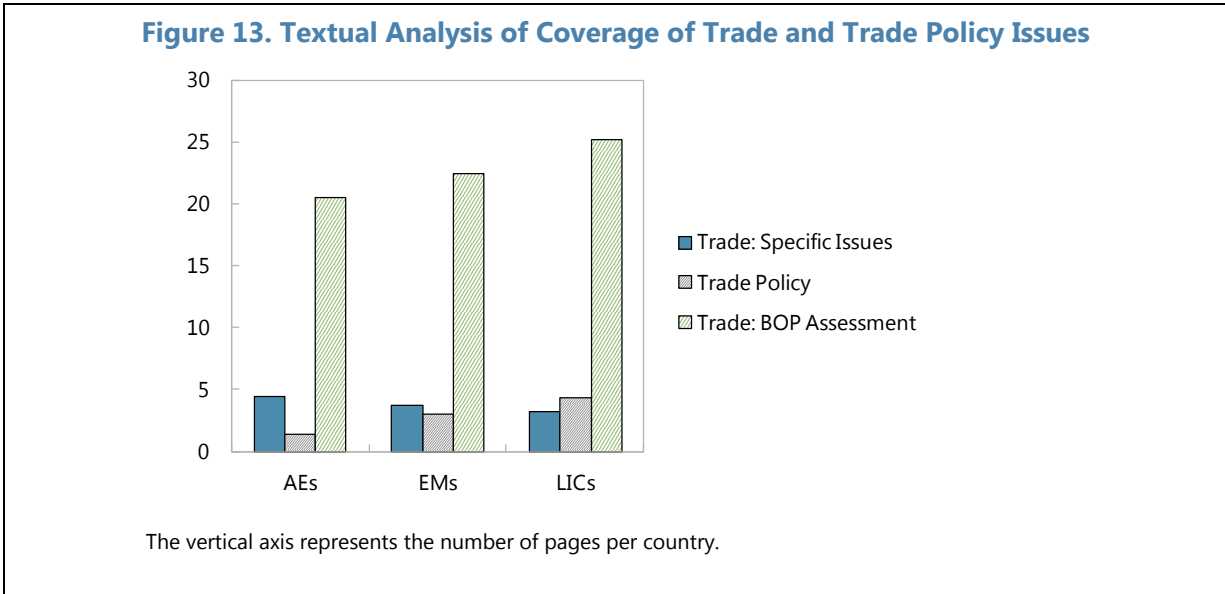
Several areas of trade for further analysis were identified:

- *Effects of supply-side shocks.* The spillovers of trade examined are mostly macroeconomic and on the demand side. The spillover analysis done at the Fund generally employs VAR methods to determine how negative growth shocks in EMs will affect exports of various AEs. Supply-side shocks, for example productivity improvements, and their welfare effects could be studied.
- *FDI and trade.* FDI is an important concomitant of GVCs, as well as a key factor in bringing new technology and competition to the domestic market in a way that can improve economic performance. FDI also has implications for inequality.
- *Relationship between exchange rate regimes, exchange controls, and trade policy.* This is related to work on trade because some countries still use import controls rather than allow the exchange rate to adjust to external imbalances.

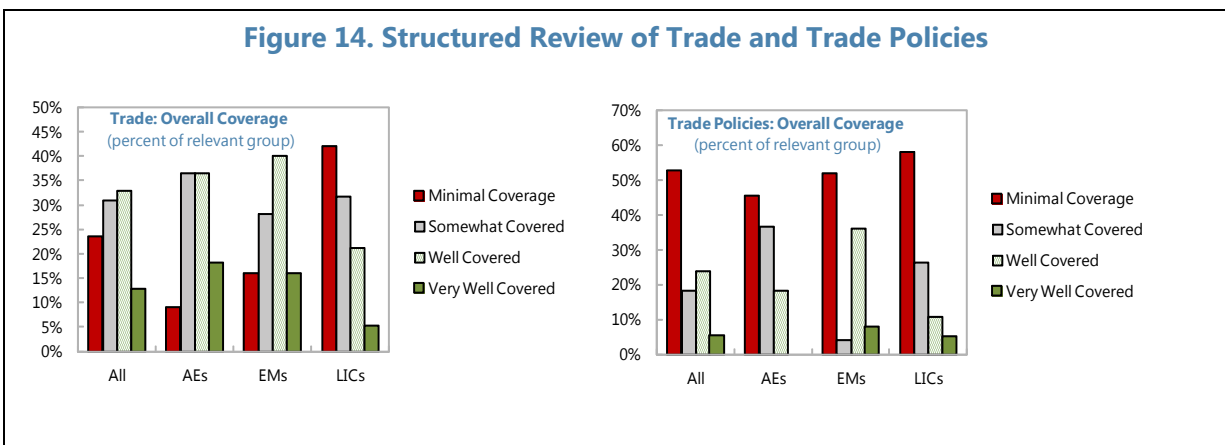
C. Review of Bilateral Surveillance

There is limited coverage of trade and trade policy issues in bilateral surveillance, with trade policy receiving less attention than trade developments.

29. The textual analysis indicates that trade developments receive more attention than trade policy in staff reports. Most of the focus is, however, on BOP assessment, with the average number of pages around four times more than other trade and trade policy issues (Figure 13).

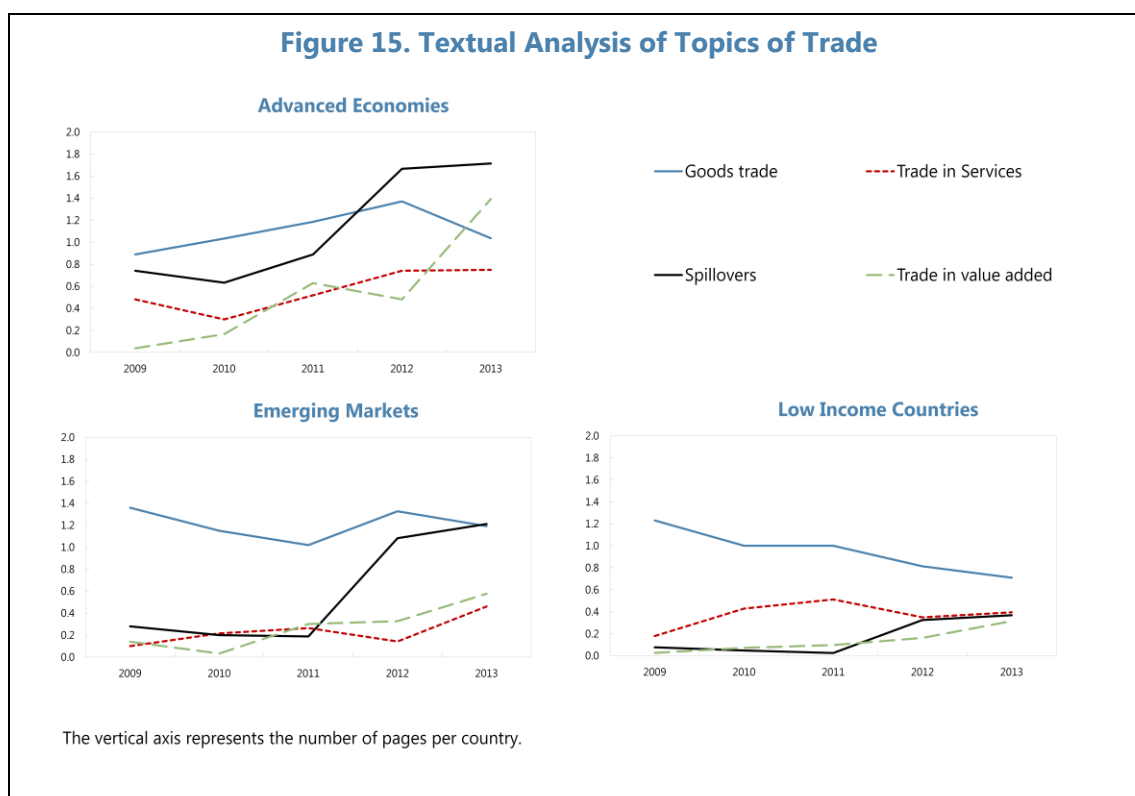


30. The structured review also suggests that the coverage of trade policy is lower than trade issues. The proportion of reviewers responding “minimal coverage” and “somewhat covered” is larger than those responding “well covered” and “very well covered” (Figure 14). Moreover, compared to the assessment of trade issues, the proportion responding “minimal coverage” and “somewhat covered” is higher for trade policy issues.

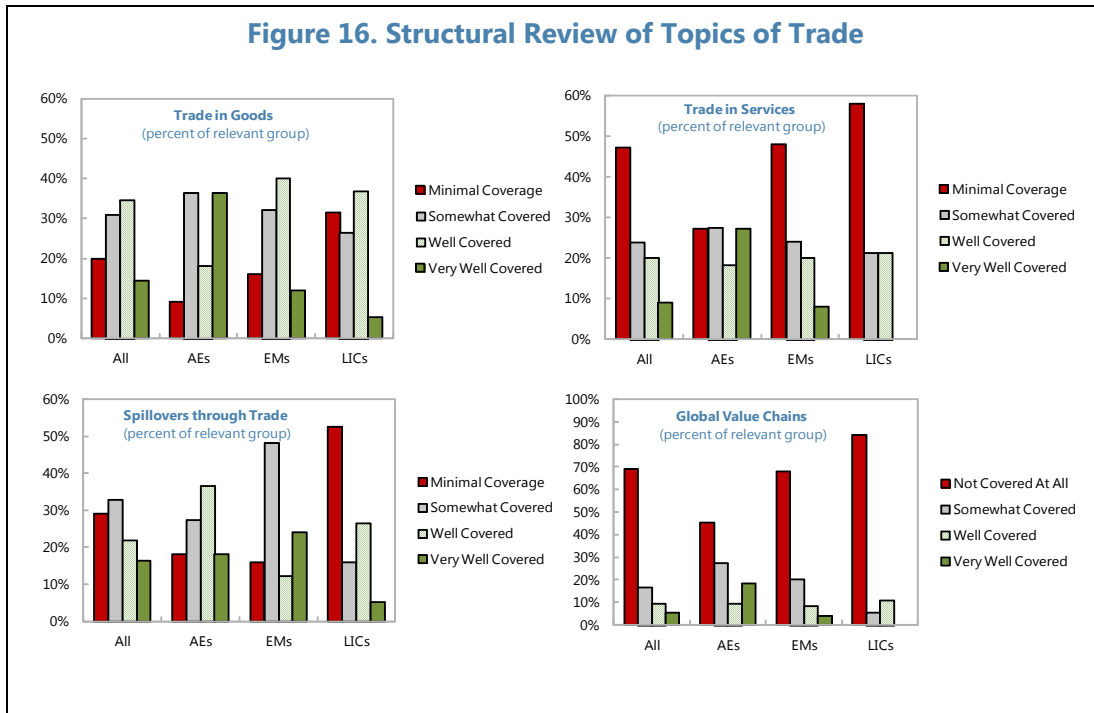


Specific trade topics such as spillovers and GVCs are increasingly covered for certain AEs and EMs, but there is scope for greater analysis of trade potential (e.g., GVCs in EMs and LICs and services trade in AEs).

31. In line with the evolving trade landscape, the textual analysis suggests that coverage of specific trade issues has gradually shifted from a focus on trade in goods to trade in services, trade in value added and spillovers. Though coverage of specific trade issues is low, it has increased over time. In particular, since the global financial crisis the Fund has stepped up efforts to better understand the spillover effects through trade in AEs and EMs (Figure 15). As discussed in detail in Box 2, the coverage of trade in value added has increased in certain AEs and EMs, but remains low in other EMs and LICs.



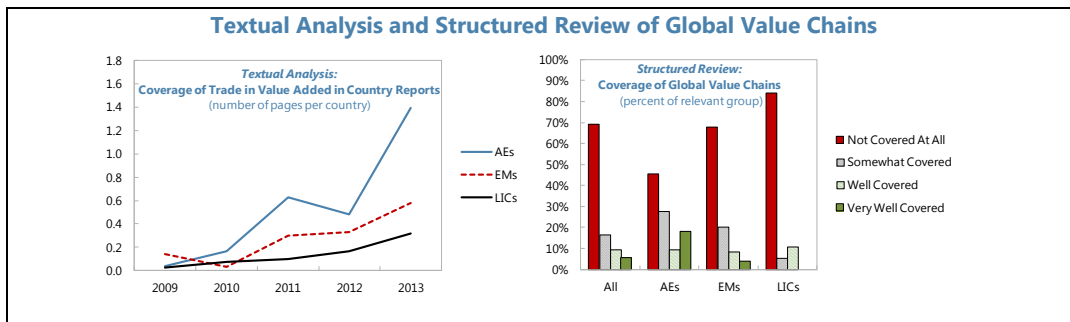
32. The structured review suggests that issues such as spillover effects, trade in services and GVCs are also relevant for EMs and LICs. In line with the textual analysis, in the structured review, staff indicates that the coverage of trade topics such as services and GVCs is low for all country groups, perhaps due to data limitations, while there is also little coverage of spillovers in LICs (Figure 16). As highlighted in Box 2, the potential benefits of trade integration for EMs and LICs have received limited attention and there is scope for more analysis of trade potential in staff reports. In addition, important trade events such as the great trade collapse in 2009 were covered extensively in multilateral products, while their coverage in bilateral surveillance reports was relatively low but concentrated within those countries that were most affected by the events (see Box 3 for details).



Box 2. Coverage of Global Value Chains (GVCs) in the Fund’s Work

The rise of Global Value Chains (GVCs) has been one of the most important trade developments with tremendous macro implications. As mentioned in Section II, one of the underlying reasons for the rapid growth in trade volumes in the past thirty years is the increasing unbundling of production across borders, due to the decrease in trade barriers and the technology-led decline in transportation and communication costs (IMF, 2011a). The rise of GVCs implies that gross trade data do not accurately capture the value added exchanged between countries because gross exports include both domestic value added and foreign value added that vary both over time and across countries (Figure below).

In line with recent trade developments, GVCs have been extensively covered in Fund’s multilateral and regional products. In a series of policy papers, the Fund has discussed in depth the recent trend of growing importance of global value chains and its macro implications (see, for example, IMF, 2011a, or IMF, 2013a). The expansion of GVCs has also been documented in regional reports, particularly in regions where such developments have been strong such as in Southeast Asia and Central and Eastern Europe (see, for example, IMF, 2011c, or IMF, 2013b), and in multilateral research reports (see, for example, IMF, 2013c). According to the external consultants, IMF reports on this topic scored highly in terms of both policy relevance and quality of the empirical analysis.



Box 2. Coverage of Global Value Chains (GVCs) in the Fund’s Work (concluded)

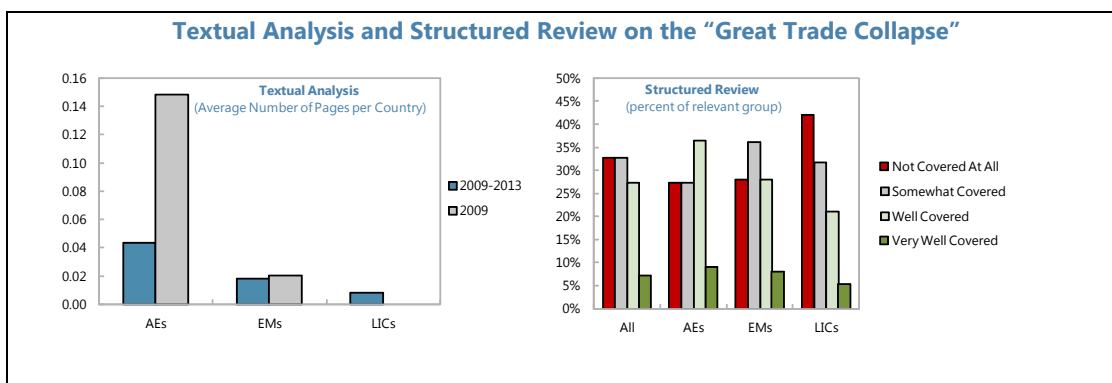
Fund’s coverage of GVCs in bilateral surveillance reports has improved over the years, but may not have been adequate all across the board. The results of the textual analysis and structured review appear inconsistent. The first reveals that the coverage of global value chains has increased remarkably in the past five years, particularly in AEs. However, the review shows that GVCs were not well covered (the proportion of “not covered at all” and “somewhat covered” is substantially higher than “well covered” and “very well covered”). The discrepancy may be due to the fact that GVCs are unevenly distributed, with many EMs and LICs not well integrated. The review supports this view, with indication that GVCs were not relevant for the individual countries. Having said that, the results indicate that country reports tend to focus on the description of existing trade patterns, but do not address the issue of how many EMs and LICs that would benefit from greater trade integration could anchor their economy to expanding GVCs.

Box 3. Coverage of the “Great Trade Collapse” in the Fund’s Work

International trade presented a sudden, severe and synchronized collapse in late 2008 and early 2009. The annualized drop in global imports was 30 percent between the last quarter of 2008 and the first quarter of 2009 and affected advanced and developing economies equally (IMF, 2010a). This contraction was substantially larger than the drop of global GDP that decreased by 6 percent during the same period. The rise of uncertainty after the bankruptcy of Lehman Brother in September 2008 and the subsequent contraction of credit suddenly depressed global demand, particularly for trade-intensive durable goods. This fact, along with other factors such as inventory adjustments and constraints to credit supply, determined the Great Trade Collapse (see, Bems, Johnson, and Yi, 2013).

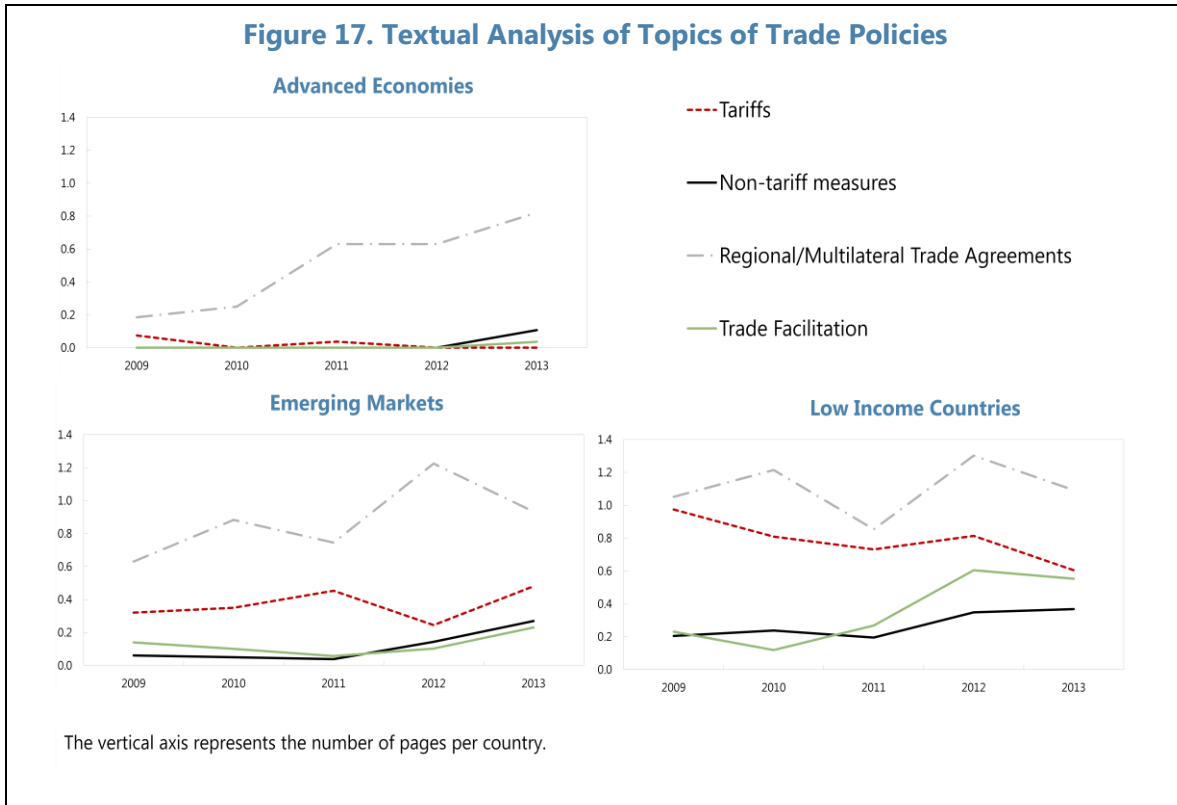
Multilateral products covered the Great Trade Collapse extensively and with high detail and quality, according to external consultants. The WEO devoted a chapter to answer the question “Do Financial Crisis Have Lasting Effects on Trade?” (IMF, 2010a). This chapter used standard techniques from research on international trade to highlight the interaction of trade flows and banking and debt crisis. It was built on the work of Fund’s research such as the analysis decompositions of demand spillovers during the “Trade Collapse” (Bems, Johnson and Yi, 2010) or the impact of financial crisis on subsequent international trade developments (Abiad, Mishra and Topalova, 2014). The IMF’s staff also discussed more specific issues surrounding the “Trade Collapse” such as the role of trade finance (Ahn, 2011, and Asmundson et al., 2011).

The coverage of the Great Trade Collapse in bilateral surveillance reports was relatively low but concentrated within those countries that suffered it the most. First, textual analysis across the universe of Article IV consultations from 2009 to 2013 showed that the trade collapse was on average only marginally covered. Similarly, the results from the structured review showed that more than 60 percent of all staff reports reviewed fell into the two lowest categories of coverage while less than 10 percent of the countries covered the topic “very well”. This relatively low coverage of the Great Trade Collapse in bilateral products is somewhat surprising given the size of the decrease in trade, but it may also reflect the fact that the phenomenon coincided with other major macroeconomic developments. On the other hand, the pattern across income groups indicates that coverage was concentrated in those countries that were at the core of the Great Trade Collapse (AEs and several EMs) and was lower for LICs, which were less affected by the pronounced fall in trade.

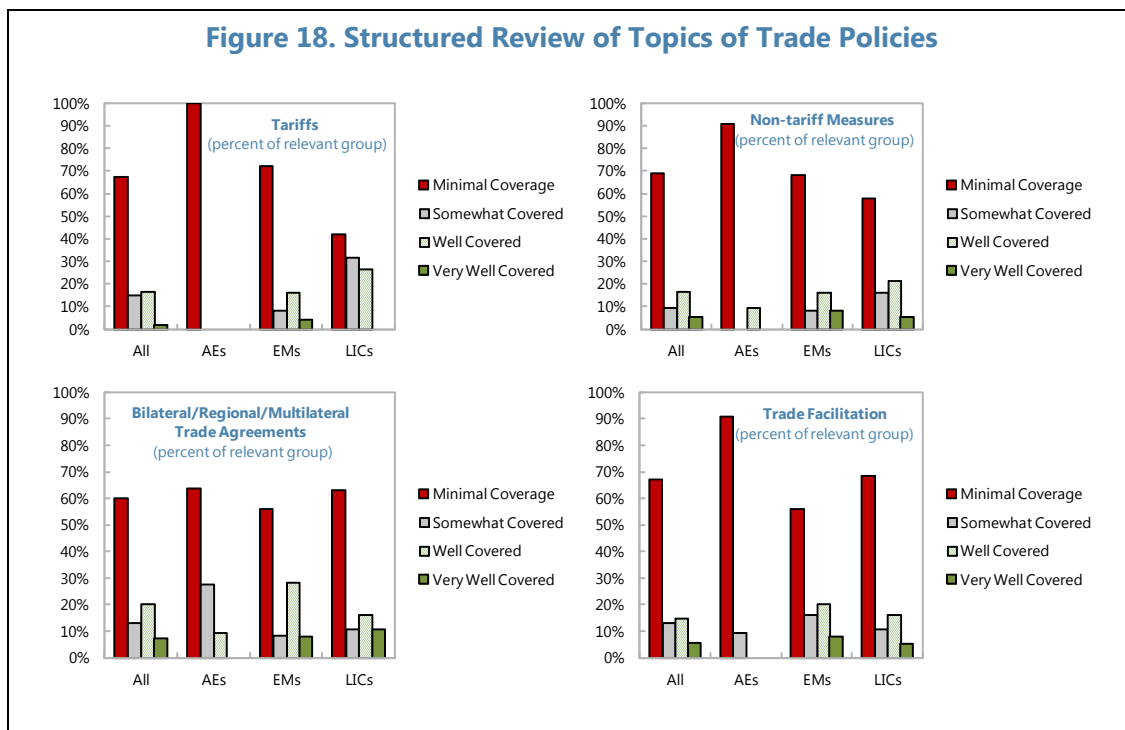


Coverage of trade policy issues is low across the board even in important areas (e.g., trade facilitation in LICs), and there are gaps in understanding the potential macroeconomic impact of trade policies.

33. The textual analysis suggests that coverage of trade policy issues is generally low, though discussions in EMs and LICs staff reports cover a wider range of issues than those of AEs. In contrast with the changing landscape of trade policy, there is little coverage of non-tariff measures for all country groups (Figure 17). Trade agreements are the main focus across all country groups, while issues such as trade facilitation remain minimally covered even for LICs.

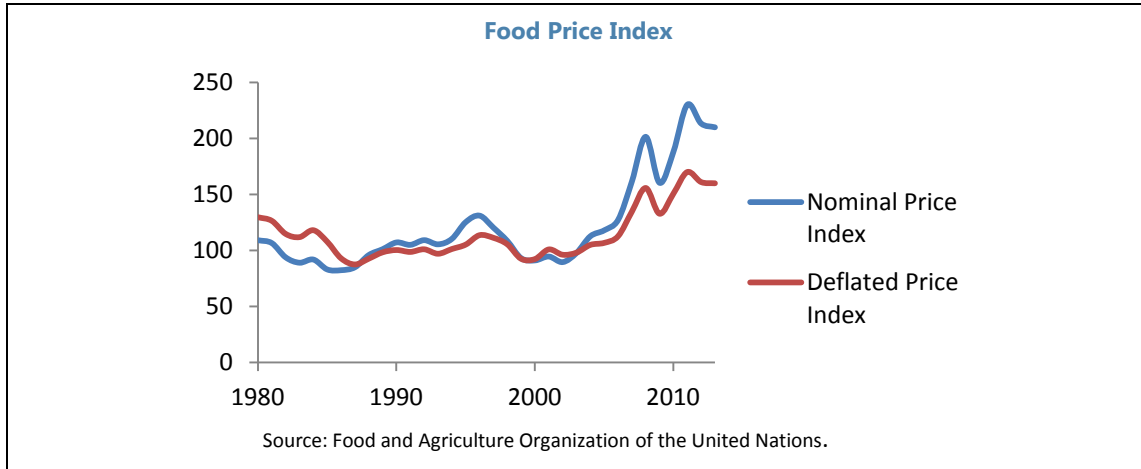


34. In addition, the structured review suggests that the macro impacts of critical trade policies are not adequately covered in staff reports. Issues such as tariffs and non-tariff measures receive wider coverage in EM and LIC staff reports, but discussion remains minimal (Figure 18). Coverage is usually not specific and the potential macroeconomic impact of trade policies (such as trade agreements) is usually not analyzed. For instance, as highlighted in Box 4, despite the importance of the role of trade policy in the food crisis of 2010-11, reports did not cover the issue in depth.

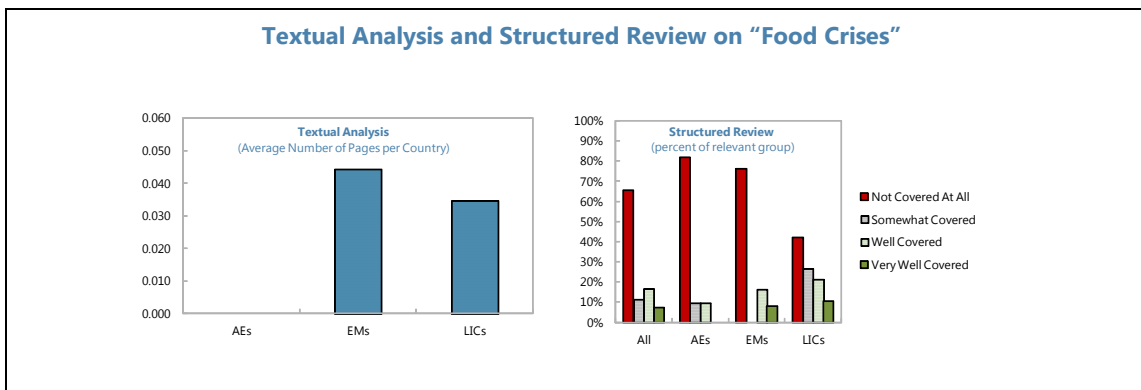


Box 4. Coverage of “Food Crises and Trade Policy” in the Fund’s Work

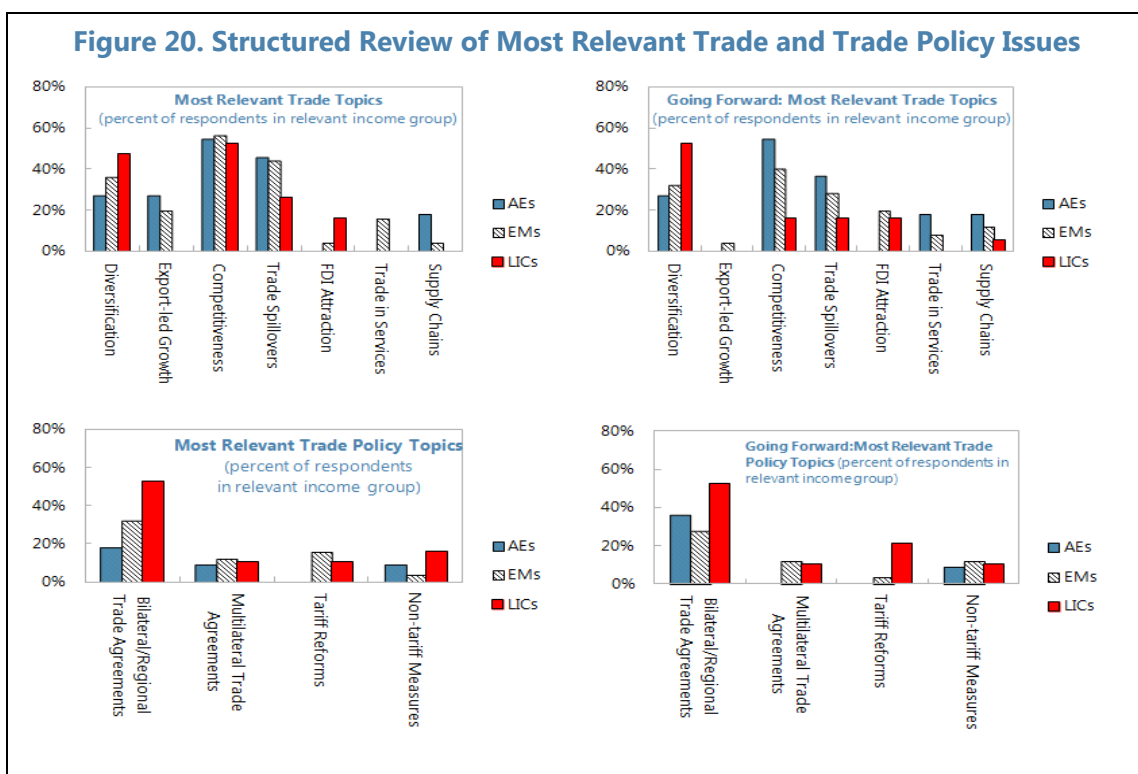
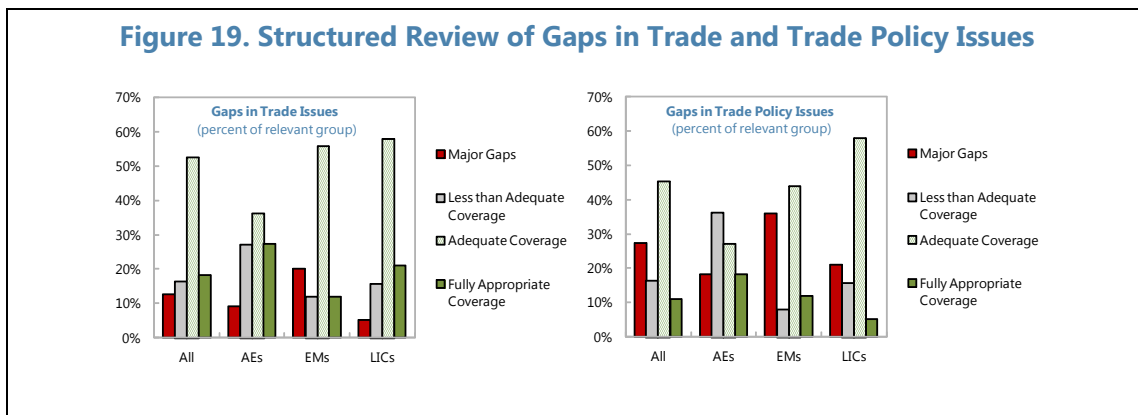
International food prices have been a key policy concern in recent years, uncooperative trade policy has contributed to their volatility. Food prices after 2006 differ from the preceding two decades, justifying the labeling of “food crises” in 2006-08 and then in 2010-11. A number of factors may have contributed to the sudden and rapid spikes in food prices such as reduction in key food stocks, increasing demand in emerging economies, financial speculation. Uncooperative trade policy is widely seen as a contributing factor. Specifically, if governments use trade policy to shield the domestic economy from large food price shocks, a complementarity emerges between the price of food in international markets and trade policy: when a shock drives up the price of food, exporters respond by imposing restrictions while importers wind down protection, thus exacerbating the initial shock and soliciting further trade policy activism (Giordani, Rocha and Ruta, 2014).



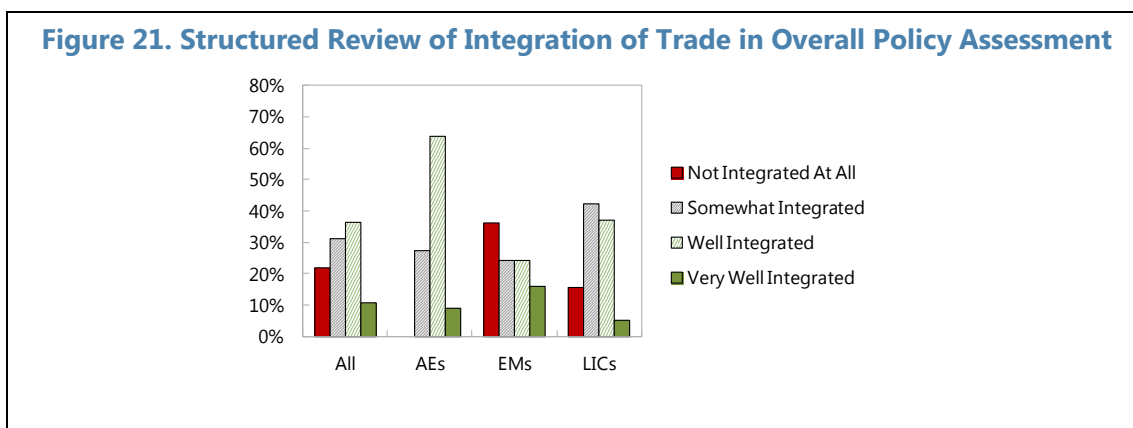
Despite the importance of the role of trade policy in the food crises, neither multilateral surveillance nor bilateral surveillance reports seem to have covered the issue in depth. While both the World Bank and the WTO largely covered these issues, the Fund’s staff reports had little or no discussion of the impact of trade policy on escalating food prices. Textual analysis across the universe of Article IV consultations from 2009 to 2013 showed that the food crisis in 2010-11 was covered up less than any other category in the general analysis. The low coverage is consistent with the fact that this issue affects developing economies to a larger extent: in fact, AEs’ reports present no mention of the topic in the textual analysis, while EMs and LICs devote at least some, very marginal, attention to the issue. The structured review confirms both the lack of coverage of the topic with more than 60 percent reporting that the issue was not covered at all. Even for LICs and EMs, trade policy and the 2010-11 food crisis was “very well covered” for less than 10 percent of the countries.



35. The structured review does not offer clear pointers for major gaps in trade and trade policy coverage. Despite the low coverage of trade and trade policy issues, in the structured review, staff indicates that the coverage is adequate (as shown in Figure 19, the proportion replying “adequate coverage” and “fully appropriate coverage” is more than the proportion replying “major gaps” and “less than adequate coverage”). Competitiveness, trade spillovers, diversification and bilateral/regional trade agreements are considered key issues for all income groups both now and going forward (Figure 20). Finally, data limitations, particularly on trade agreements, are seen as one of the main reasons that hinder further analysis in country reports.



36. The integration of trade issues in the overall macro assessment has been limited, particularly in EMs and LICs. This may have been due to a confluence of factors, including prioritization of issues during the Global Financial Crisis; a perception that trade was less relevant for the work of the Fund; and the significant change in trade landscape requiring time to understand its implications. On the other hand, the structured review indicates that trade has been “well integrated” in overall policy assessment for AEs (Figure 21). This reflects in part that staff reports for AEs have incorporated issues such as trade spillover effects in their analyses.



D. Other Trade-Related Work in the Fund

Apart from trade work in bilateral and multilateral surveillance and research, in the past five years the Fund has also: i) provided trade-related technical assistance to member countries on trade facilitation, tariff reform and external sector statistics; and ii) collaborated with the WTO and the World Bank on relevant trade and trade policy issues.

IMF Technical Assistance⁵

37. The Fund has offered considerable tax policy advice with a trade facilitation component over the recent years. For instance, ample technical assistance (TA) by the Fiscal Affairs Department (FAD) in tax policy has dealt with the removal or reduction/simplification of tariffs and export subsidies, sometimes in countries acceding to the WTO. TA often dealt with the ways to recover the revenue losses from such reforms.⁶ Also excise policies that are akin to import tariffs have been addressed, as well as certain business tax incentives with an important trade impact (such as income tax exemptions for exporting companies). TA work in Sub-Saharan Africa has encountered interactions between tax and customs reform and regional trade agreements, such as overlapping requirements within COMESA, SADC and SACU (as many countries belong to at least two of these

⁵ Prepared by the Fiscal Affairs Department and Statistics Department.

⁶ For analytical Fund work on this issue, see Baunsgaard and Keen (2010) and Keen and Lockwood (2010).

agreements). Country coverage of this TA work is broad, and ranges from the Caribbean, East Asia, and Sub-Saharan Africa to the Middle East.

38. Substantial capacity building TA in customs administration has been given by FAD, contributing to improved trade facilitation outcomes. TA has targeted legislation improvements, dealing with the administrative implications of customs unions, implementing function-based organizational structures, strengthening human resources, streamlining and automating the import clearance process to eliminate paper import declarations, and improving the performance and integrity of core customs operational functions.⁷ Since 2009 FAD has undertaken 37 dedicated customs administration missions and 73 general revenue administration missions comprising both a tax and customs administration component. To support implementation of FAD customs mission recommendations, 140 short-term expert visits have been fielded from IMF headquarters and through the IMF's Regional Technical Assistance Centers. Africa, Asia Pacific, and Western Hemisphere countries have been the largest recipients (Table 1).

Headquarters missions (dedicated customs administration)						
	AFR	APD	EUR	MCD	WHD	Total
FY2009	2	2	3	1	3	11
FY2010	0	0	0	0	1	1
FY2011	1	1	0	1	0	3
FY2012	4	1	0	0	0	5
FY2013	5	0	0	1	1	7
FY2014	5	1	0	2	2	10
Total	17	5	3	5	7	37
Headquarters missions (combined tax and customs administration)						
	AFR	APD	EUR	MCD	WHD	Total
FY2009	5	1	2	1	1	10
FY2010	5	0	0	0	4	9
FY2011	2	1	0	1	10	14
FY2012	8	2	0	1	7	18
FY2013	0	1	1	0	7	9
FY2014	3	1	0	1	8	13
Total	23	6	3	4	37	73
Customs short-term expert visits						
	AFR	APD	EUR	MCD	WHD	Total
FY2009	7	14	0	0	2	23
FY2010	5	4	0	2	2	13
FY2011	3	7	0	2	3	15
FY2012	4	9	0	1	10	24
FY2013	8	4	0	3	27	42
FY2014	5	1	0	0	17	23
Total	32	39	0	8	61	140

39. The Fund has also provided trade-related TA to member countries through missions on external sector and national accounts statistics and price statistics. The Statistics Department's (STA) TA is characterized by the promotion of internationally accepted statistical methodologies and compilation practices, emphasis on regional projects, and working with regional

⁷ See also Montagnat-Rentier and Parent (2012).

institutions. To complement TA into the full spectrum of capacity development (CD), STA also conducts training in these two statistical areas. CD activities in external sector statistics have increased significantly during the last five years mainly due to the conversion of the balance of payments data to the basis of the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)* and the *System of National Accounts 2008 (2008 SNA)*. Compilation guidance on conversion of balance of payments and SNA rest of world sector data to the latest format covers the principal conceptual changes in the goods and services accounts in the most recent manuals. Recent work on statistical methodology has focused on the statistical implications of emerging developments in trade, particularly the increasing importance of GVCs and trade in intellectual property.

40. The traditional focus of TA on external sector and national accounts statistics has been on low-income and post-conflict countries. With the recent global financial crisis, however, TA has expanded to cover emerging and advanced economies as well. STA also attached priority on providing TA to countries with serious data shortcomings that hamper the effectiveness of Fund's surveillance and lending operations.

41. STA addresses the measurement of external trade in goods and services as well as export and import price indices through its capacity building activities (TA and training missions) and through participation in international task forces. Notable cases on recent trade-related TA include: JSA Project on the Improvement of External Sector Statistics in the Asia and Pacific Region (which benefits 22 economies in the region); Harmonization Project of External Sector Statistics of CAPTAC-DR (which includes seven Central American countries); as well as STA regional workshops and through BOPCOM, where trade in goods and services issues are discussed and analyzed, among other external sector statistical issues. STA is also actively contributing to the work of international task forces, such as the Task Force on Global Production (TFGP) and the Inter-Agency Task Force on International Trade Statistics (TFITS). National accounts TA also may address measurement of external trade in goods and services when significant issues are encountered. The development of export and import price indexes supports analysis of an important aspect of trends in trade. These data are also used in national accounts to improve the measurement of the price and volume dimensions of exports and imports.

Collaboration with the WTO and the World Bank

The Fund, WTO and World Bank have worked together in the past five years with the goal of ensuring a sound system for global trade and payments. Some of the main channels of collaboration are summarized below.

42. The Fund and WTO have engaged regularly in both formal and informal consultations regarding trade policy and global economic developments, as well as on advice for individual countries. Examples of consultations include visits by senior IMF staff to the WTO, and vice versa, to make presentations and attend discussions on issues of common interest. The IMF has observer status in certain WTO bodies, and may participate in meetings of certain WTO committees and working groups. The WTO Secretariat attends meetings of the IMF Executive Board or the Board

Committee on Liaison with the World Bank, and other international organizations on matters of common interest. In addition, the IMF surveillance reports are important inputs to the WTO's periodic reports on member countries' trade policies (Trade Policy Reviews).

43. The joint Annual IMF/World Bank/WTO trade workshops bring together experts in the three institutions to discuss topical trade issues and relevant research projects. The trade workshop started in 2011 and has become an important platform of discussion among leading experts on trade and trade policy issues. In past events key issues included: agricultural trade policies, value added trade, trade protectionist responses to the Global Financial Crisis, services trade, trade and exchange rates, and diversification in trade and trade finance. The workshop has also included a segment where the future trade work of the three institutions was discussed, with a view to facilitate collaboration.

44. The IMF, the World Bank, the WTO, and other international organizations and donors have worked together to help countries improve their ability to trade via TA and training. The Enhanced Integrated Framework for trade-related TA to Least Developed Countries seeks, among other priorities, to ensure that poorer member countries incorporate appropriate trade-related reforms into their Systematic Country Diagnostics. As recommended by Executive Directors, the Fund has had a selective involvement in this area through TA.

45. The IMF and the World Bank started producing jointly a Trade Watch report, an internal analytical note focusing on recent developments in trade and trade policy. The Trade Watch (IMF and WB, 2014a) follows international trade flows from a global perspective. It contains up-to-date data from an array of sources along with analysis covering relevant trade issues. The goal of the Trade Watch is to provide high quality and timely information to IMF and World Bank staff on a regular basis.

TOWARDS A FUTURE TRADE AGENDA FOR THE FUND

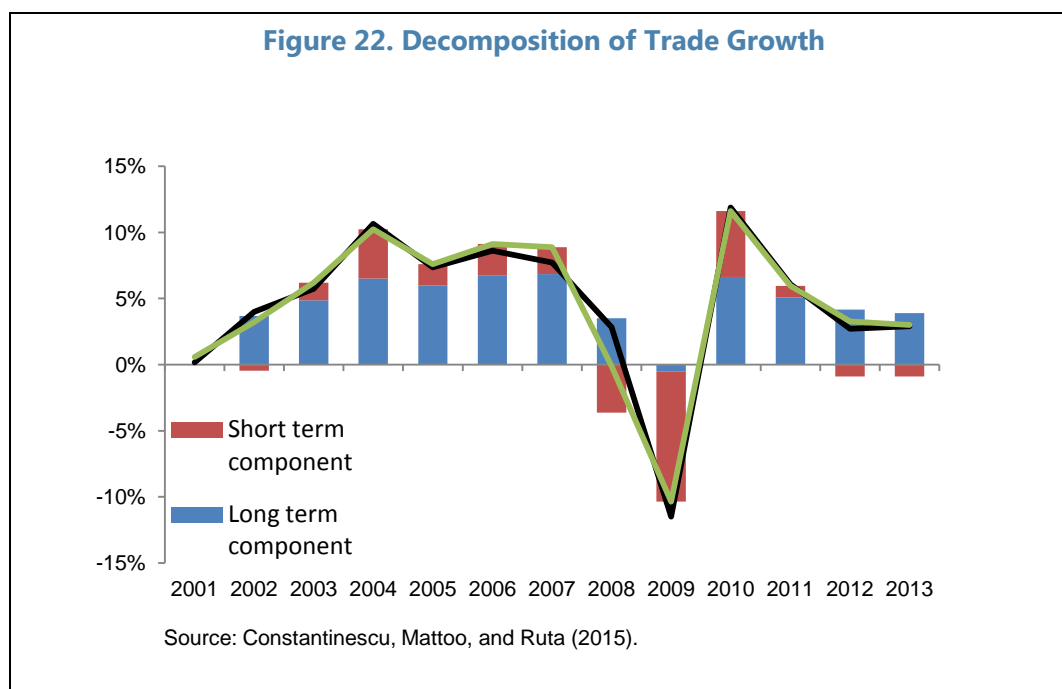
This section discusses the trade and trade policy landscape going forward and highlights key issues, with a view to identifying main considerations for a future trade agenda that would serve to prioritize the Fund's trade work, including under multilateral and bilateral surveillance and for different groups of countries.

A. Trade and Trade Policy Landscape

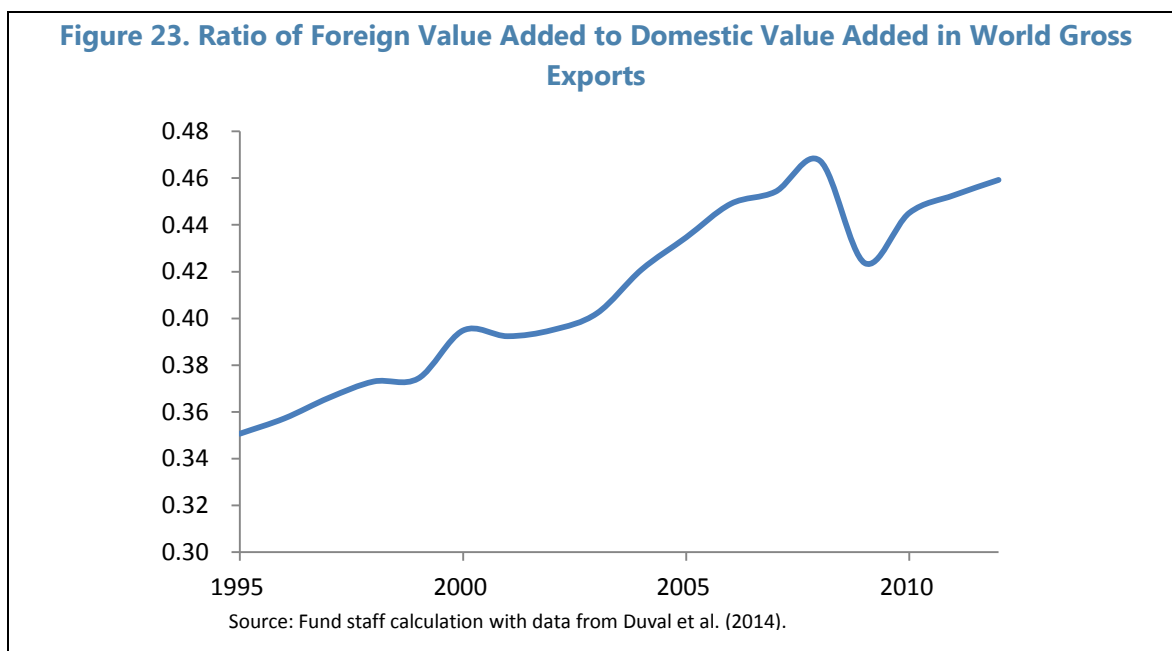
Trade Landscape going forward

Past trends of trade integration are likely to continue, but with no simple extrapolation. The global trade slowdown that began in 2012 has in part structural determinants, as GVCs in some regions and gains from past trade liberalization may have matured. The nature of trade interconnectedness and potential spillovers will continue to evolve with changing trade patterns.

46. The recent global trade slowdown is likely to persist, as it is in part driven by structural factors. The slowing of global trade in recent years was more pronounced than output. The rate of growth of trade slowed to 3.4 percent in 2013 from 6.1 percent in 2011, while global output growth decelerated to 3.3 percent from 3.9 percent over the same period. Latest WEO estimates for 2014 confirm this trend, with world output growth at 3.3 percent and trade volumes growing at 3.1 percent. The underperformance of trade relative to output would require close monitoring. Recent analysis shows that, while cyclical factors dominated the Great Trade Collapse in 2009, structural factors such as slower pace of expansion of GVCs and of trade liberalization in recent years also contribute to explain the current global trade slowdown (Figure 22), implying that the weak performance of trade is likely to persist (Constantinescu, Mattoo and Ruta, 2015).



47. GVCs are expanding at a slower pace, but there is untapped potential. The ratio of foreign value added to domestic value added in world gross exports increased by 8.4 percentage points between 1995 and 2005, but by only 2.5 percentage points between 2005 and 2012 (Figure 23). The growth of GVCs in the 1990s reflected the increasing unbundling of production driven primarily by the United States and China. That particular engine appears to have matured, reflecting a number of factors such as the diminishing labor cost advantage of China, its increased ability to move up the value chain, and reduced cost of energy in the US. However, the scope for further unbundling of production and increasing trade in tasks is still strong in Europe and could be important going forward for regions that have not yet been heavily involved in GVCs, such as Sub-Saharan Africa, Middle East and North Africa (MENA), South America and South Asia.



48. Hindrance to GVC participation includes distance, but also lack of infrastructure and policy barriers. Distance to the hub can be an important factor limiting integration in GVCs. For instance, the average distance to the United States for Latin American countries is 40 percent higher than the average distance to Japan for Asia-Pacific countries, which partly explains the lower participation of Latin American countries to GVCs relative to countries in the Asia-Pacific region. However, other factors such as quality of infrastructures and sound policies and institutions can play a key role as well. Countries thus need trade and other structural reforms to enhance their participation in GVCs.

49. The nature of trade interconnectedness and potential spillovers will continue to evolve with changing trade patterns. Notwithstanding the trade slowdown and the slower pace of expansion of GVCs, the world economy is still much more interconnected today than it was in the past and will remain so in the coming years. In this context, various contingencies can have potentially large implications for global trade and growth. At the same time, diversification would imply less disruption from more idiosyncratic shocks. Trade channels and spillovers risks, however, will also evolve with changing patterns of trade. In particular, the changing structure of GVCs will affect how shocks are transmitted both through demand and supply channels, and may have localized amplifying effects in some regions and sectors, issues that still require analytical work.

50. Traditional trade issues will remain important, particularly for LICs and several EMs. Poor integration with the rest of the world, weak competitiveness, and lack of export diversification are often the result of high trade costs (e.g., inadequate infrastructures, see for example Nordas and Piermartini, 2004, and tariff and non-tariff barriers). These challenges for developing economies, coupled with data and capacity constraints, will persist over the coming years. The rise of nationalism and cross-border conflicts could also have an adverse impact on international commerce.

Trade Policy Landscape Going Forward

There is a significant degree of trade policy uncertainty ahead. Preferential and plurilateral agreements will likely continue to move the trade policy frontier into new areas such as services, regulations and investment. Open, transparent and comprehensive trade integration initiatives will be needed to minimize fragmentation, even as renewed efforts are made to prop and retool the governance of the multilateral system. There are potentially large global gains from further trade liberalization and integration, including because trade reforms complement and augment the benefits of other structural reforms.

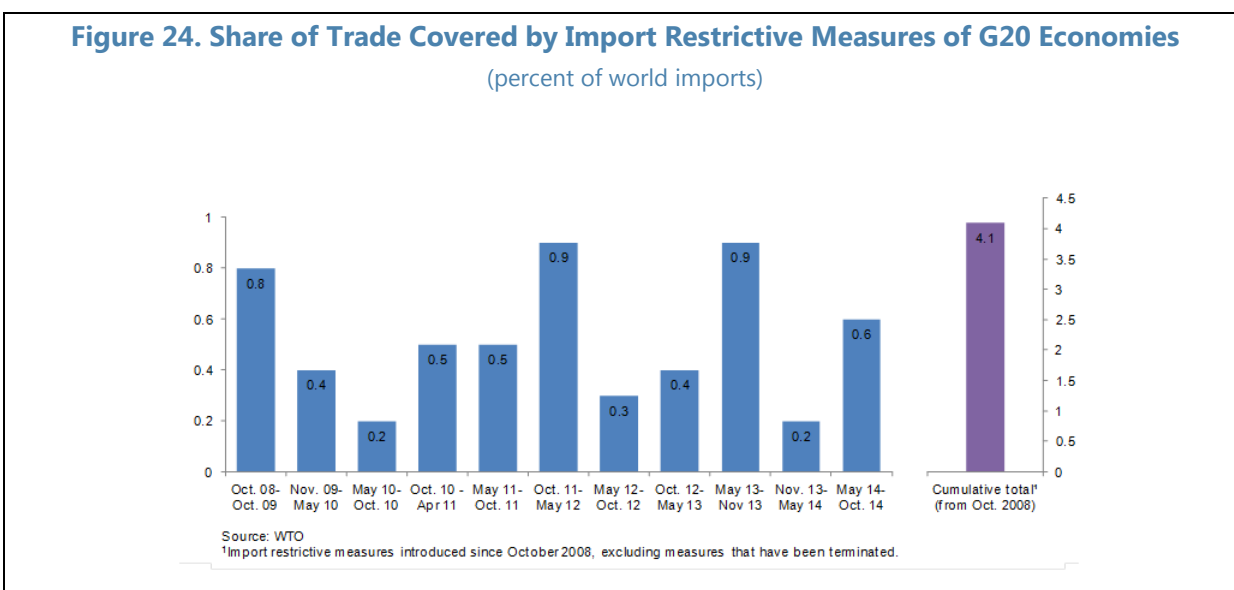
51. The earlier impasse with the WTO’s Bali agreement highlights the difficulties in multilateral trade negotiations. The finalization of the Bali agreement is welcomed, but the impasse as well as the longstanding difficulties to advance the Doha Round, have emphasized the need to buttress the governance of the multilateral trading system. The Bali package focuses on a small set of issues from the Doha Round, most prominently the Trade Facilitation Agreement (TFA), but the deal is particularly important to EMs and LICs and key to renewing the international community’s commitment to the WTO.

52. Reliance on PTAs and plurilateral agreements will likely persist, but the endgame is not yet clear. The process of multilateral negotiations that defined the world trading system in the post-war period has proven very challenging in recent decades. Trade rules in the foreseeable future are likely to be either preferential (such as the mega-regional Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP)) or plurilateral (such as the Trade in Services Agreement (TISA) or the recently reinvigorated Information Technology Agreement (ITA)). These agreements aim at breaking new grounds in areas such as services, regulatory cooperation, and investment rules. The endgame of these negotiations is, however, uncertain at this stage. Similarly, LICs are increasingly granted access to advanced economies’ markets through preferential agreements such as the Economic Partnership Agreements (EPA) of the EU or the African Growth and Opportunity Act (AGOA) of the US.

53. Open, transparent and comprehensive trade integration will be needed together with renewed efforts to prop and retool the governance of the multilateral system. Deep PTAs can improve coherence of institutional frameworks and increase trade between partners as well as efficiency of GVCs, with positive effects on third parties when these initiatives are multilateralized. To avoid fragmenting the multilateral trading system such arrangements should be open (i.e., they should eventually be available to all who are willing to meet the standards of the agreement), transparent, comprehensive, and minimize discrimination between members and non-members (particularly with respect to regulatory requirements). Over time, arrangements based on these principles can maximize the benefits of deals and ignite reciprocal opening efforts from non-members. They can also limit the risk of backlash to integration by avoiding a sense that trade is only advancing for a preferred “club” of countries.

54. While traditional trade barriers are still relevant in certain cases, the focus will increase on NTMs. Tariffs and bottlenecks to trade facilitation are important trade costs for many countries

(e.g., regional trade in Africa) and for certain sectors (e.g., agriculture), but traditional forms of protectionism did not appear to grow significantly during the Global Financial Crisis. Nevertheless, some countries continued to impose new trade restrictions, while previous measures were not rolled back (Figure 24). Trade costs are increasingly affected by NTMs, such as divergent regulatory standards (e.g., safety tests for cars), investment rules, and intellectual property protection. Trade negotiations will focus increasingly on these issues and will be complex and challenging as divergent NTMs often reflect genuine differences in policy preferences and regulatory concerns. NTMs are also the areas where protectionism may hide, with less transparency relative to tariff measures.



B. Key Issues for Multilateral Surveillance and Analytical Work

Trade can be an essential component of a global policy agenda to bolster growth and avoid a “new mediocre.” Trade reforms complement and augment the benefits of other structural reforms, are an important element of infrastructure investment, and support the strengthening of policy and institutional frameworks. There are potentially large global gains of further trade integration, including from traditional liberalization and unilateral efforts; lowering barriers in new trade policy frontiers; and additional expansion of global supply chains. Reigniting global trade integration would require an open architecture that allows different speeds and depths, but also coherence among preferential and multilateral efforts to avoid fragmentation. Evolving trade linkages and spillover channels need heightened attention.

55. Further trade integration can bolster global growth. The potential contribution of trade to global and country growth should continue to be a priority area of analysis. The case for open trade rests on the existence of static and dynamic gains from trade. The literature shows that trade can boost growth through a number of channels including improved resource allocation, knowledge spillovers, enhanced competition, and increased market size. While the macroeconomic evidence on trade and growth is often challenged by questions on the causality of this relationship (Rodriguez

and Rodrik, 1999), a large number of microeconomic studies provide evidence of the positive impact of trade reforms on economic growth through these various channels.⁸

56. Increased integration of goods and services markets should be a key element of countries' growth strategy based on structural reforms. This is because trade reforms can complement and augment the benefits of other structural reforms. On one hand, rigidities in labor and product markets lower the gains from open trade and can sometimes make trade reforms painful and politically unsustainable, as they make it more difficult to reallocate resources across sectors and firms. On the other hand, trade liberalization can facilitate the implementation of structural reforms by improving an economy's growth prospects. Trade infrastructure, in particular for LICs, can have major positive effects, supported by improving policy and institutional frameworks.

57. A better grasp on the sources of trade costs is important to understand how to move forward on trade integration. A large literature in recent years has shown that "distance is not dead" and that trade costs are still large, even for countries that are highly integrated such as the United States and Canada (Anderson and van Wincoop, 2004). Understanding the diverse policy and non-policy components of trade costs, their varying relevance for countries in different regions and at different levels of development is relevant to pin down areas where a trade agenda may need to focus on in coming years. In particular, while academic work spent more time in assessing costs of trade in goods, little is known about services trade costs despite the presumption that barriers are prevalent in this area.

58. Managing risks and potential spillovers is important to maintain support for an open trading system. Increased integration can generate spillover channels in some regions and sectors. Shocks propagate internationally through demand and supply channels and can be further amplified, at least locally, by deeper trade linkages. To reap the benefits of integration and contain risks and potential spillovers, collaboration at the multilateral level is critical beginning with the recognition of the cross-border implication of domestic policy, including through trade.

59. Monitoring changing patterns of trade and their implications. The Fund has done substantial work in previous years in documenting and analyzing the evolution of trade patterns at the regional and global level, the rise of GVCs and some of the key implications of the changing trade structure, such as developing methods to estimate the value added real effective exchange rates. This useful monitoring work should continue and possibly be extended to account for the increasing interaction of trade with other structural reforms, foreign direct investment, and international labor mobility.

⁸ See Costinot and Rodriguez-Clare (2013) for a discussion of the recent academic literature that focuses on estimating the static gains from trade. Key studies on the dynamic gains from trade include Frankel and Romer (1999), Pavcnik (2002), Alcalá and Ciccone (2004), Bustos (2011). WTO (2008) reviews the different channels through which trade can affect growth and the macro and microeconomic evidence of this link.

60. Deep PTAs can contribute to advance liberalization in new trade areas, but a key question is how to achieve eventual multilateralization. Deep PTAs and plurilateral negotiations (e.g., TTIP, TPP, TISA, and ITA) can push forward trade policy frontiers in sensitive areas such as services, regulatory cooperation, investment rules, thus reducing trade costs and improving the institutional framework for GVCs.⁹ But with trade liberalization efforts taking place mainly in these settings, it is essential to avoid fragmenting the global trading system, including through open, transparent and comprehensive arrangements, and efforts for eventual multilateralization. Assessing the macro impact of preferential agreements on members and non-members, particularly in areas such as services, would be an important area of analytical work. The eventual multilateralization of these agreements would also have major implications for the global governance of the trading system.

61. Traditional trade liberalization, including on a unilateral basis, is still relevant both for goods and services markets. Traditional trade barriers still constitute a large share of the costs of trade for many countries (LICs and EMs), including the excessive use of instruments under the WTO such as antidumping and countervailing duties. Average applied tariff rates for LICs and EMs are above 10 percent, while average bound rates are above 29 percent, both nearly 5 times higher than average rates of advanced economies (WTO, 2014). Further liberalization and trade facilitation (e.g., customs reforms and improvements in trade infrastructures), including through unilateral efforts, are essential to better integrate these countries into the world markets and anchor their economies to GVCs.¹⁰ The pace of opening services markets, particularly financial services, should also account for the impact that these reforms may have on financial stability in the short term, notably in countries with financial vulnerabilities and weak prudential frameworks.

62. There is a need to remain vigilant about new and old protectionism. The WTO has been effective in keeping in check traditional barriers to trade, particularly since the global financial crisis. But given the diverse nature of NTMs, along with large data gaps, heightened and coordinated vigilance across different international institutions will be needed to avoid new forms of protectionism as well as, in some cases, traditional tariff protection (e.g., use of trade policy to prevent BOP adjustment). Finally, assessing the macroeconomic impact of NTMs on trade costs would be an important area of analytical work.

⁹ Deep PTAs cover more areas than traditional trade agreements and significant gains could come from greater regulatory coherence that reduces non-tariff barriers and bolsters FDI and services trade, increasing productivity through specialization and knowledge spillovers. Petri et al. (2014) show that TPP may increase the GDP of its members by 3.7 percent above the baseline by 2025. Felbermayr et al. (2014) estimate the existing trade costs between the U.S. and the EU and show that the reduction of these costs due to TTIP could increase real income of the U.S. by 4.9 percent and of the EU by 3.9 percent. Francois et al. (2013) find similar impacts of TTIP using an alternative approach. While few would disagree on the positive impact of these agreements, gains are difficult to predict and estimates could contain either an upward or a downward bias. For example, Krugman (2013) questions the size of gains from further trade liberalization of U.S. trade, while Kehoe (2003) shows that ex-post gains from NAFTA were higher than ex-ante estimates due to the growth of unanticipated trade channels.

¹⁰ For a discussion and collection of case studies on policies that help countries connect to GVCs, see OECD-WTO (2013).

C. Key Issues for Bilateral Surveillance

Better embedding trade in surveillance work, including its role in growth-enhancing reforms and as part of the overall assessment, will require a concerted effort: clearer institutional views on trade and trade policy; continued analytical work; enhanced efforts to translate key implications from the trade landscape; prioritizing bilateral work on macro-relevant areas specific to various country groups; revising guidance; and review process.

63. Clearer institutional views and better translating the implications of the trade landscape for bilateral work are important for enhancing surveillance. Several efforts could contribute to better channel multilateral and research analyses into bilateral surveillance, in line with the recommendation in the 2014 Triennial Surveillance Review (IMF, 2014c). There is a need to continue assessing and explaining the evolving trade and trade policy landscape and its implications for the work of the Fund, including for specific country groups. This should be supported by the development of institutional views on key macro-relevant trade and trade policy issues, along the lines of the staff reference note on trade (IMF, 2010c). Trade issues should be given particular attention in bilateral surveillance to the extent that they are relevant for domestic and external stability. The work of country teams can be facilitated by improved guidance and the review process, including knowledge exchange on similar cases. The Fund's work on trade will need to take into account resource constraints and limited trade expertise. Prioritizing trade work for different types of countries will respond to their distinct macro-critical nature and differential needs. The Fund will continue to collaborate with the WTO and other international institutions, drawing on their expertise on macro-critical trade issues.

64. Trade reforms could be analyzed as part of the broader macro-structural agenda. As trade reforms complement and augment the impact of other structural reforms such as in the product and labor markets, country teams could for instance consider trade measures as an integral part of the discussion of the growth strategy of the country linked to other structural reforms; and pay attention to potential new forms of protectionism, most notably discriminatory non-tariff measures.

65. In some instances, analysis at the regional level would be needed—and resource-efficient—to inform bilateral surveillance. Policy discussions on trade issues are frequently complex given that relevant responsibilities often lie with regional bodies, some of which the Fund has a formal surveillance dialogue. Even in the case of some of the monetary unions (e.g., Euro Area, West African Economic and Monetary Union, and Central African Economic and Monetary Community), trade policy issues cannot be fully covered in formal regional surveillance because those unions themselves are part of wider economic unions (European Union, Economic Community Of West African States and Economic Community of Central African States) with significant trade policy responsibilities. In this complex environment, analysis at the regional level, for instance in the form of cluster reports, could be needed and resource-efficient as background work in the relevant dialogue with country authorities.

66. Trade priorities should vary across country groups, focusing on macro-critical issues.

- *Advanced economies* can pioneer and advance the new trade policy frontiers, opening services markets (e.g., completion of the single market for services in the EU) and making their regulatory systems more coherent, for instance through the TTIP, with potential gains to themselves and to others if these initiatives minimize fragmentation and are eventually multilateralized.
- Many *emerging markets*, including in South Asia and Latin America, can still benefit greatly from integrating via traditional liberalization, including on a unilateral basis, and by anchoring their economies to GVCs, moving away from import-substitution policies that have failed in the past and avoiding protectionism through the use of NTMs. Trade liberalization complements and augments the benefits of structural reforms and supports the strengthening of policy and institutional frameworks.
- *Low-income countries* need trade and integration to GVCs as a central plank of their development and growth strategy, for which trade facilitation is critical. They can benefit by removing forms of protectionism that hinder job creation and export growth. For these economies, addressing traditional trade barriers, such as upgrading poor trade infrastructures, and improving economic institutions (including data and capacity) are still crucial. Technical assistance could be needed to support integration, including on how to adapt to a less protected environment (e.g., fiscal implications of lower tariffs); sequence, pace and coordinate reforms; and take advantage of improved access to advanced economies' markets.

ISSUES FOR DISCUSSION

67. We would welcome Directors' views on the following questions:

- Do Directors agree with the main findings of this review on the role of trade in the work of the Fund, in particular that the trade landscape has changed rapidly in recent years—slowing global trade integration, expanding global supply chains, new forms of protectionism, and ongoing trade liberalization initiatives—while coverage of trade issues in bilateral surveillance has been limited?
- Do Directors concur that, at this trade and trade policy juncture, there is a need to bolster bilateral and multilateral surveillance by focusing on macro-critical trade issues?
- Do Directors view the main considerations towards a future trade agenda as appropriate to prioritize the Fund's trade work, including for the various country groups and their specific needs?
- Do Directors have other suggestions to help operationalize a future trade agenda, taking into account the resource implications?

Annex I. IEO Evaluation of IMF Involvement in International Trade Policy Issues

This annex provides an overview of the Board-endorsed recommendations and proposed implementation plan arising from the IEO Evaluation of IMF Involvement in International Trade Policy Issues (IMF, 2009).

IEO Recommendations	Proposed Follow-Up
<i>A. Reviews of the Fund's work on trade and guidance to staff</i>	
<p>"The Board should commit to periodic re-evaluation of its guidance on objectives of, approaches to, and modalities of staff work on trade policies. Regular reviews of guidance should be undertaken in the context of assessments of current global trends in trade and trade policy."</p> <p>"The Board should establish guidance on the role and approach of the IMF in PTAs."</p> <p>"The Board should establish guidance on the role and approach of the IMF in trade in financial services."</p>	<p>A1. Five-yearly reviews of Fund work on trade policy will be conducted. As the IEO Evaluation covers much the same ground as staff reviews, an early review of trade policy by staff would be duplicative. Taking the IEO Evaluation as the starting point for the cycle, the first five-yearly review would be expected in 2014.</p> <p>A2. Staff guidance on trade in financial services and PTAs will be developed and issued to the Board for information by July 2010. A review of the content and implementation of this and other guidance on trade policy would be considered by the Executive Board in the context of the 2014 Board reviews of trade policy in the Fund.</p>
<i>B. Trade policy in Fund-supported programs</i>	
<p>"The IMF must engage on [trade policy] issues with borrowing countries through a strong advisory role" to help them resist protectionist pressures, ensure adequate trade finance, influence decisions within PTAs, and reform trade policies to reduce business costs.</p>	<p>B1. Relevant general guidance notes, in particular the 1999 "Guidelines on Implementing Trade Policy Reforms" will be updated and revised by July 2010. This guidance would clearly distinguish between Board-endorsed guidance and other information such as best practices, to the extent that both were covered in a single document. All such guidance notes would be issued to the Executive Board for information upon completion. Their content and implementation would be expected to be covered in the five-yearly Executive Board reviews of trade policy (see A1 above).</p>

<i>C. Multilateral, regional, and bilateral surveillance</i>	
<p>"Trade policy—particularly involving PTAs—should be addressed periodically in multilateral and regional surveillance."</p>	<p>C1. Relevant trade-related topics would be covered in standalone papers and through collaboration between staff working on trade policy and departments responsible for WEO, REOs, and GFSRs as appropriate. The Executive Board guidance on macro-critical trade policy issues and evenhandedness in trade policy advice will be incorporated into general trade policy guidance notes and its applicability to bilateral surveillance as well as multilateral and regional surveillance will be emphasized (see B1 above).</p>
<i>D. Staffing-related issues</i>	
<p>"...a small but critical mass of trade policy expertise must be built..."</p> <p>"...a division solely devoted to trade issues is needed..."</p>	<p>D1. The Fund staff should attract and develop trade policy expertise while balancing the need for economist staff to work on macroeconomic issues and in country teams. Such a balance would also position staff working on trade policy well to integrate their expertise into the broader Fund work and keep open options for successful Fund careers. Maintaining trade policy expertise in a division with broader responsibilities may help to facilitate the latter goal.</p>
<i>E. Trade policy information</i>	
<p>"Fund staff need data and measures of trade protection... IMF staff should work with other organizations to improve data and tools on trade policy."</p>	<p>E1. Trade policy staff will prepare a guidance note for Fund staff on the availability and use of tariff and other trade policy information from existing databases by July 2010 (See also B1 above).</p> <p>E2. Fund trade policy staff will also explore possibilities for enhanced information sharing on trade policy information with the WTO Secretariat, World Bank staff, and other potential interlocutors. Staff will engage actively with WTO and others on the ongoing trade policy monitoring exercises.</p>
<i>F. Institutional cooperation</i>	
<p>"To spearhead such cooperation, Management and a small number of senior staff need to commit to regular and formal meetings—for example, once a year— with counterparts in other key international organizations involved with trade.... IMF management should report to the Committee on Liaison with the World Bank and other International Organizations and/or the Executive Board/IMFC on proceedings of these meetings and plans for staff level coordination."</p>	<p>F1. Occasional meetings on trade among senior staff of the IMF, World Bank, and WTO, and possibly other multilateral economic institutions will continue, and Fund staff will seek to focus these interactions on issues relevant to the Fund in general and current Fund concerns that are shared with the appropriate institutions. Whenever possible, these could be organized on the margins of other international meetings.</p>

Annex II. The Legal Framework Underpinning the Fund’s Work on Trade Matters¹

This annex provides an overview of the legal framework underpinning the Fund’s work on trade matters. The bottom line is that the Fund has quite a wide scope to undertake work on trade matters under the rubric of its main activities—surveillance, use of Fund resources and technical assistance. The question is often not whether the Fund has the legal authority to engage in trade matters, but whether and how it should engage, taking into account its core areas of expertise, resource implications and the role of other international organizations. Executive Board Directors have often stressed these latter considerations.

A. Background

1. From the Fund’s inception, trade matters have played a role in all of the Fund’s three main areas of activity—surveillance, use of Fund resources and technical assistance.
2. The Fund has focused on trade issues either directly as part of its core macroeconomic agenda or because trade policy influenced the environment for that agenda. In this regard, a key aim of the Fund’s trade work is to ensure economic stability and growth. Regarding economic stability, trade regimes that are distortionary or allow excessive discretion create a poor environment for economic performance, external viability, aid effectiveness and good governance. Regarding economic growth, trade policy reforms can be a crucial ingredient of growth strategies and can be instrumental for the success of reforms in other areas—such as locking in regulatory reforms through external commitments, strengthening market disciplines on enterprises and banks or reducing the scope for corruption. Further, trade policies and the global trade policy environment can give rise to balance of payments effects. Other links between trade and the macroeconomic framework include the effect of trade policies on government revenue and on financial sector stability.²
3. This annex provides an overview of the legal basis for the Fund’s involvement in trade matters.

B. Fund’s Purposes and Powers

4. Article I (ii) provides as a purpose of the Fund:

“To facilitate the expansion and balanced **growth of international trade**, and to contribute thereby to the promotion and maintenance of high levels of employment and real income

¹ This Annex was prepared by the Legal Department.

² See generally [Review of Fund Work on Trade](#), February 7, 2005.

and to the development of the productive resources of all members as primary objectives of economic policy.”

This purpose is expressed in broad terms. Unlike the purposes dealing with exchange rate issues and use of Fund resources, it provides no specification regarding the nature of the role that the IMF should play in facilitating the expansion and balanced growth of international trade.

5. In order to achieve its purposes, the Fund has been granted certain powers under the Articles. While not specifically spelled out in the Articles, the Fund’s legal authority to work on trade matters in the context of SUR, UFR and TA stems, respectively, from Article IV, Article V, Section 3 and Article V, Section 2(b).

C. Surveillance (SUR)

6. Article IV is the basis for the Fund’s surveillance mandate, which is further elaborated in the Integrated Surveillance Decision (ISD). The ISD provides as follows:

- In its bilateral surveillance, the Fund will focus on members’ policies that can significantly influence present or prospective BoP and domestic stability. The following considerations are applicable:
 - In view of the focus on members’ policies that can significantly influence present or prospective BoP and domestic stability, exchange rate, monetary, fiscal and financial sector policies will always be the subject of the Fund’s bilateral surveillance. Other policies—such as trade policies—will be examined **“only to the extent that they significantly influence present or prospective balance of payments or domestic stability.”**³ Accordingly, whether to include a discussion on trade policy in a particular Article IV consultation, requires a judgment as to whether trade policies “significantly” influence BoP or domestic stability. Typically, coverage of trade issues is only expected: (i) where serious trade distortions hamper prospects for stability; and (ii) where balance of payments are vulnerable to trade developments.⁴ The possible impact of trade restrictions in services (including financial services) should not be forgotten.⁵

In this context, surveillance may examine issues respecting the promotion of growth to the extent that growth is critical for the promotion of domestic stability, also defined as orderly economic growth.⁶ As performance relative to capacity is always a key ingredient of

³ Decision on [Bilateral and Multilateral Surveillance Decision, No. 15203-\(12/72\)](#), adopted July 18, 2012, para. 6.

⁴ [Guidance Note for Surveillance Under Article IV Consultations](#), October 10, 2012, para. 53.

⁵ [Guidance Note for Surveillance Under Article IV Consultations](#), October 10, 2012, para. 53.

⁶ For discussion on growth, see [Jobs and Growth: Analytical and Operational Considerations for the Fund](#), March 14, 2013 at Annex 7 - The Legal Framework for the Jobs and Growth Agenda in the Fund.

domestic stability and crucial for balance of payments stability, the ISD requires the Fund to always examine whether domestic policies are directed toward keeping the member's economy operating broadly at capacity; and in assessing whether members fulfill their obligation to seek to promote orderly economic growth, the Fund should pay due regard to members' circumstances. It is for this reason that the ISD recognizes that there are circumstances in which surveillance must pay particular attention to the need to promote higher rates of potential growth. Specifically, the decision requires the Fund to examine whether domestic policies are directed toward fostering a high rate of potential growth but only in those cases where such high potential growth significantly influences prospects for domestic and, thereby, balance of payments stability. To the extent that growth significantly influences prospects for domestic and balance of payments stability and trade issues are important for such growth, such trade issues may be discussed in the context of bilateral surveillance.

- In its multilateral surveillance, the Fund focuses on issues that may affect the effective operation of the international monetary system, including (a) global economic and financial developments and the outlook for the global economy, including risks to global economic and financial stability, and (b) the spillovers arising from policies of individual members that may significantly influence the effective operation of the international monetary system, for example by undermining global economic and financial stability. Thus, trade policies and developments could be covered in the context of assessing global economic developments as in (a) above or in the context of assessing spillovers as in (b) above.⁷ Whether to cover trade policies and developments in the Fund's multilateral surveillance requires the exercise of judgment.
- Even if important issues respecting trade fall outside the context of surveillance, it is legally possible to discuss them in an Article IV consultation with the agreement of the relevant member.⁸ While the surveillance framework defines the scope of issues that members are required to discuss with the Fund under Article IV, it is also possible for members to voluntarily agree to discuss other issues including trade issues with the Fund in an Article IV consultation. The Fund's policy advice on these issues would be – technical assistance under Article V, Section 2(b) and not bilateral surveillance, but could be included in the member's Article IV consultation.

⁷ Such spillovers may be from policies implemented by countries that are systemically important or by countries that suffer from large vulnerabilities, which could trigger a systemic crisis in certain broader circumstances, either directly through trade and financial linkages with other countries or indirectly through market contagion. [Guidance Note for Surveillance Under Article IV Consultations](#), October 10, 2012, para. 15.

⁸ For discussion on growth, see [Jobs and Growth: Analytical and Operational Considerations for the Fund](#), March 14, 2013 at Annex 7 - The Legal Framework for the Jobs and Growth Agenda in the Fund.

D. Use of Fund Resources (UFR)

7. Article V, Section 3 authorizes the Fund to use its general resources to assist members to solve their balance of payments problems in a manner that establishes adequate safeguards for the temporary use of those resources. As noted in paragraph 2 above, trade policies can have a BoP impact. Accordingly, Fund-supported programs have encompassed trade measures designed to resolve BoP problems. The criteria for whether to establish trade-related conditionality are the same as those that apply to any conditionality. In this regard, the Conditionality Guidelines require measures, in particular, to be established as conditionality where, in particular, they are of critical importance for achieving the goals of the program, provided that such measures must be reasonably within the direct or indirect control of the member.⁹

8. In addition, the Fund has adopted a policy to include in every stand-by and extended arrangement a standard continuous performance criterion on not imposing import restrictions for balance of payments reasons. The reason for this is that the Fund has judged that the imposition of import restrictions to resolve BoP problems is more likely to aggravate economic maladjustments than to correct them, thus increasing the likelihood that the use of Fund resources will not be temporary.

E. Technical Assistance

9. Pursuant to Article V, Section 2(b), upon request, the Fund may provide technical assistance, so long as such assistance is consistent with the purposes of the Fund. Accordingly, TA on trade issues can be provided so long as it is consistent with the purposes of the Fund and, in particular, with Article I (ii). Examples of such TA include FAD's work in the areas of tariff policy reform and modernization of customs administration, and policy advice in the context of surveillance (see paragraph 6, last bullet of this Annex). It should be noted that TA may provide more flexibility to engage where Fund engagement in trade matters is limited by the criteria set forth under SUR or UFR.

F. Cooperation with Other International Organizations

10. Article X provides that the Fund shall cooperate with other international organizations having specialized responsibilities in related fields. The Fund cooperates with the World Trade Organization (WTO) and the World Bank on trade matters. While all three seek to foster international trade, the WTO focuses on a rule-based approach to liberalization and transparency, the Bank on development and sectoral issues and the Fund on the overall policy framework.¹⁰ There are agreements that regulate the general cooperation between the Fund and the WTO and the Fund and the Bank touching on issues such as ensuring policy coherence and consistency of advice and

⁹ [Guidelines on Conditionality, Decision No. 12864-\(02/102\)](#), September 25, 2002, as amended.

¹⁰ See generally [Review of Fund Work on Trade](#), February 7, 2005.

obligations, information exchange, staff contacts and representation in meetings of each others' governing bodies.¹¹

11. With regard to the WTO, there is overlapping jurisdiction on certain policy measures that have both exchange and trade attributes. Moreover, certain provisions in the WTO Agreements specifically cover international current payments and transactions, which are also the subject of Article VIII, Section 2(a) of the Fund's Articles. As such, close collaboration is required between the two institutions to avoid imposing conflicting requirements upon their common membership.

G. Latest Board Summings Up on Trade Issues

12. 2009 Summing Up on IEO Evaluation of IMF Involvement in Trade Policy Issues (BUFF/09/91, June 11, 2009):

- The Board considered that the report provides a balanced view of the Fund's involvement in trade issues and welcomed the IEO's recommendations.
- However, many Directors also observed that trade policy issues are only peripheral to the core competency of the Fund and viewed engagement as best served through cooperation with the WTO.
- Directors agreed that the report gives useful impetus to discuss what the Fund's priorities for trade work should be within the existing resource envelope.
- On surveillance, Directors agreed that bilateral surveillance should discuss macro-critical trade issues and that multilateral surveillance has scope for paying greater attention to global effects of trade policies in systemically important countries. Trade policy should be addressed periodically in the WEO, GFSR and REOs. The Fund's role in assessing revenue implications of trade liberalization was also noted. Directors emphasized that, given resource constraints, attention to trade policy issues will require effective prioritization.
- On UFR, Directors welcomed the scaling back of conditionality on trade policy. They underscored that the emphasis should be on avoiding trade restricting measures. Trade liberalization should be promoted actively where necessary for achieving program objectives.

13. 2007 Summing Up on Aid for Trade—Harnessing Globalization for Economic Development (BUFF/07/133, September 28, 2007):

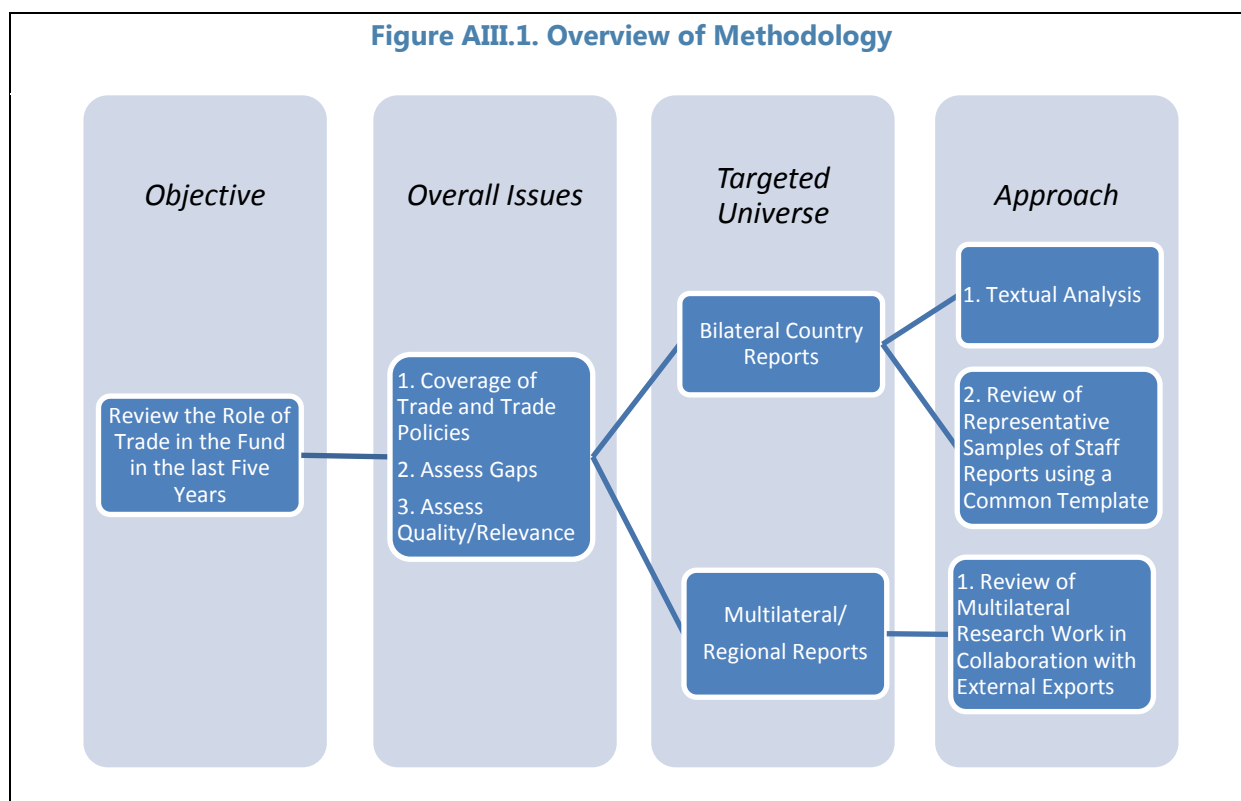
- Directors supported the Fund's selective involvement in the Enhanced Integrated Framework and the aid for trade initiative, especially with regard to TA in customs and tax reforms.

¹¹ For WTO, see [Fund-WTO Cooperation Agreement, Decision No. 11381-\(96/105\)](#), November 25, 1996; [Guidelines/Framework for Fund Staff Collaboration with the New World Trade Organization, Decision No. 10968-\(95/43\)](#), April 21, 1995. For World Bank, see 1989 [IMF-World Bank Concordat](#).

Annex III. Summary of Methodology

This annex summarizes the methodology that was used in the review of the role of trade in the work of the Fund in the last five years.

Overview. The analysis is based on three complementary approaches aiming at reviewing systematically the bilateral and multilateral work vis-à-vis the main trade issues between 2009-2013 (Figure AIII.1). The first pillar relies on *textual analysis* of all Article IV staff reports over the last five years. The second pillar involves a *structured review* by Fund staff of a representative sample of staff reports relying on a common template. The third pillar entails a review of multilateral and research work, in collaboration with external experts, as well as other areas (e.g., technical assistance and collaboration with other institutions). In addition, *interviews with stakeholders*, including the WTO, OECD and other institutions were conducted.



Approach 1: Textual Analysis. The textual analysis relies upon a simple search engine to extract the number of times trade-related keywords and key phrases have been used in a particular country document in order to estimate the overall coverage of trade and trade policy issues and the coverage of specific issues (e.g., trade in services, trade agreements) (Figure AIII.2). In addition, the search engine is run to find keywords related to other policies to understand the relative importance of trade issues compared to other issues.

Technically, the search is performed simultaneously on multiple documents, using Boolean queries in Adobe Acrobat XI that allows to combine keywords with logical operators like AND/OR to produce more relevant results. The search results are then processed in STATA to eliminate non-relevant occurrences (e.g., words such as “important” or “importance” instead of “import”), and to compute summary statistics. The keywords and key phrases were carefully chosen with the aim of exploiting the search engine facility to extract maximum information in the most systematic manner (Table AIII.1).

It should be acknowledged that such textual analysis using search engines has advantages and disadvantages. On the positive side, it provides a powerful method of targeting a large and comprehensive universe including all the country documents in the past five years when assessing the trade and trade policy coverage. On the negative side, it cannot assess the quality or relevance of the words searched and cannot by itself identify contexts. However, few measures—like the use of Boolean queries to somewhat identify the contexts—are taken to minimize these limitations as much as possible. In addition, the responses from the structured review provide a useful cross-check to the results of the textual analysis.

Figure AIII.2. Textual Analysis

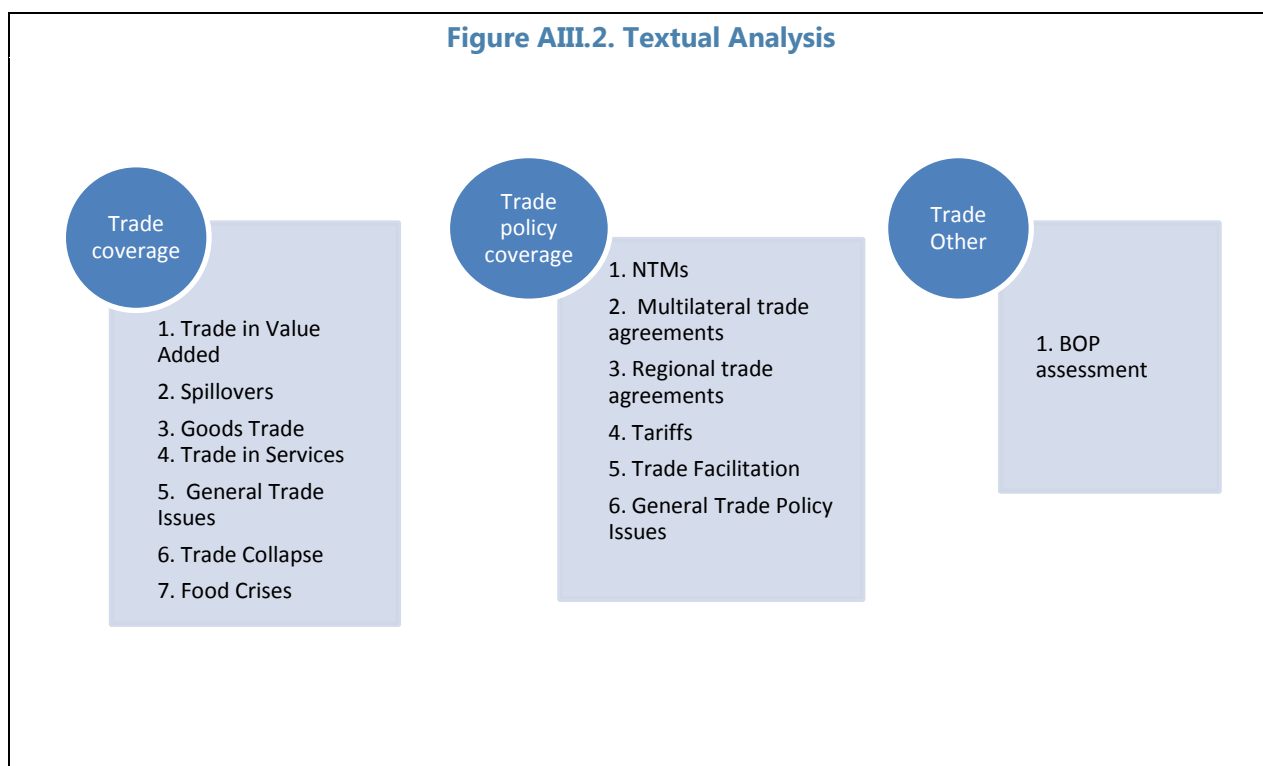


Table AIII.1. Keywords for Textual Analysis

Table AIII.1. Keywords for Textual Analysis			
Broad search areas	Category	Keywords and Keyphrases	
Trade and Trade Policy	Trade other		
	Specific Trade Issues	BOP assessment	import; export; trade
		Trade in value added*	gscs; gvc; intermediate export; intermediates trade; supply chain; supply-chain; trade in intermediate goods; value added chain; value chain; value-chain; intermediate imports; trade in tasks; effective protection; trade in parts and components; attracting foreign direct investment;
		Spillovers	border spillover; externality; inward spillover; outward spillover; through trade; trade channel; trade spillover
		Goods trade	goods trade; import flow; merchandise exports; merchandise imports; merchandise trade; trade in goods
		Trade in Services	services trade; trade in services; services import; services export; services flow
		General	comparative advantage; cross-border trade; export flow; trade center; trade environment; trade flow; trade officials; trade openness; transit trade; exporter; importer; trade collapse; trade crisis; trade integration
		Trade Collapse**	trade collapse; protectionism and the crisis; trade crisis; trade fall; export fall; import fall; trade slowdown; trade drop; export drop; import drop; global crisis and trade; fall in demand and trade; global downturn and trade
	Food Crises**	trade policy and food crisis; export restriction; export ban; export policy and food price; trade policy and food security; agricultural trade reform; trade policy and high food price; trade policy and volatile food prices	
	Trade Policy	Non-tariff measures	fdi regime; fdi restrictions; restrictive fdi; antidumping; anti-dumping; export subsidy; import quota; imposition of quota; nontariff; non-tariff; rules of origin; trade intellectual property; trade related intellectual property; quota system; import subsidy; services liberalization
		Multilateral trade agreements	gats; gatt; multilateral agreement; multilateral trade; wto accession; wto concerns; wto membership; wto obligations; wto observer; wto requirement; services agreement; doha round; agreement on subsidies and countervailing duties; intellectual property agreement; trade policy review mechanism; wto dispute settlement; wto procurement agreement;
		Regional trade agreements	free trade agreement; fta; gsp; pacific partnership; preferential market; preferential trade regional trade; tpp; trade agreement; trade partnership; trans pacific partnership; transatlantic trade and investment partnership; trans-pacific partnership; ttip; nafta; north american free trade agreement; mercosur; efta; european free trade association; ecowas; economic cooperation of west african states; eea; european economic area; eae; eurasian economic community; gsp; ; global system of trade preferences among developing countries; sacu; southern african customs union; caricom; caribbean community and common market; cefta; central european free trade agreement; cacm; central american common market; comesa; common market for eastern and southern africa; east african community; common economic space
		Tariffs	tariff regime; applied tariff; customs duty; customs tariff; decreasing tariff; duty drawback system; duty free; duty-free; export tax; external tariff; import duty; import tariff; increasing tariff; mfn tariff; tariffs on imports; trade tariff
		Trade Facilitation	border procedures; customs procedures; export cost; import cost; logistics performance; trade facilitation;
	General	protectionist trade; trade reform; trade regime; trade restriction; free trade; open trade; tariffs and nontariff barriers; trade barrier; trade freedom; trade liberalization; trade policies; trade policy; trade protection; trade policy and food crisis	

* Trade in value added or GVCs was also used in Box 2.
 ** These topics were only used in Boxes 3 and 4.

Approach 2: Review of Staff Reports using a Common Template. To complement the textual analysis, the same answers (trade and trade policy coverage) were sought by a structured review by Fund staff of a representative sample of staff reports using a common template (Box AIII.1). In addition, the knowledge of country teams was used to understand specific trade issues that were analyzed in the staff reports, and, more importantly, to get a sense of gaps—something that is difficult to understand with the textual analysis.

Box AIII.1. Trade and Trade Policy Structured Review

September 3, 2014

This structured review is an integral part of the review of the role of trade in the work of the Fund during 2009-2013, scheduled to be discussed at the Board early next year. The aim of this review is to evaluate the extent to which trade and trade policy issues were covered in country staff reports.

Country**Contact person****Extension**

This review will focus on the coverage of trade and trade policy issues in staff reports (SR). There are four sections:

- I. The first section is dedicated to *trade issues*, including (but limited to) changing patterns of goods and services trade, cross-border spillovers through trade, FDI, trade diversification, trade and growth.
- II. The second section concerns the coverage of *trade policy issues* such as tariff and non-tariff measures, regional trade agreements, protectionism during the crisis.
- III. The third section investigates the integration of trade and trade policy issues in the *overall policy assessment* of the country.
- IV. The fourth and final section focuses on the coverage of *three specific topics*: (i) the growing importance of global value chains in recent years, (ii) the global trade collapse in 2009, and (iii) the use of trade policy during the food crisis of 2010-2011.

Section I. Coverage of trade issues

A. *Coverage.* To what extent was trade covered in the staff reports in 2009-13? **Scale: 1-4¹.**

B. *Coverage of Topics of Trade.* How extensively were these trade-related issues covered in the staff reports? **Scale: 1-4.**

A. Trade in Goods	<input style="border: 1px solid red; width: 75px; height: 29px;" type="text"/>
B. Trade in Services	<input style="border: 1px solid red; width: 75px; height: 29px;" type="text"/>
C. Spillovers through Trade	<input style="border: 1px solid red; width: 75px; height: 29px;" type="text"/>
D. Foreign Direct Investment and Trade	<input style="border: 1px solid red; width: 75px; height: 29px;" type="text"/>
E. General trade issues (other than A-D)	<input style="border: 1px solid red; width: 75px; height: 29px;" type="text"/>

If E. General trade issues (other than A-D), please specify the trade issue.

C. *Relevance and Specific Example of Coverage.* Which trade issues were most relevant for the country during 2009-13 (e.g. trade competitiveness, diversification, export-led growth)?

¹ **Scaling system:** Unless otherwise specified, 1= minimal trade coverage (e.g. one or two sentences as part of required BOP assessment), 2= somewhat covered (e.g. required BOP assessment plus a box in SR or a SIP), 3= well covered (e.g. dedicated paragraph in SR plus a box in SR or a SIP), 4 =very well covered (e.g. more than one dedicated paragraph in SR / coverage in staff appraisal).

Please provide a specific example of how the relevant issue was covered in the SR. Name the specific country document, year, issue, title of the section, and provide a brief assessment of how well it was covered. (For instance, Box, SIP, section of SR, Staff Appraisal).

- D. *Gaps.* Are there any gaps in coverage of trade issues? For example, were relevant issues not covered adequately (e.g. trade finance during the financial crisis, spillover effects through trade of large macroeconomic shocks)? If so, please provide reasons. **Scale: 1-4**, with 1= inadequate coverage (major gaps), 2= less than adequate coverage, 3= adequate coverage, 4= fully appropriate coverage.

Scale:

- E. *Issues Going Forward.* What are the key trade issues for your country going forward if any?

Section II. Coverage of trade policy issues

A. *Coverage.* To what extent was trade policy covered in the staff reports in 2009-13? **Scale: 1-4.**

B. *Coverage of Topics of Trade Policy.* How extensively were these trade policy issues covered in the staff reports? **Scale: 1-4.**

A. Tariffs	<input style="width: 100%; height: 25px; border: 1px solid red;" type="text"/>
B. Non-tariff Measures	<input style="width: 100%; height: 25px; border: 1px solid red;" type="text"/>
C. Bilateral/Regional/Multilateral Trade Agreements	<input style="width: 100%; height: 25px; border: 1px solid red;" type="text"/>
D. Trade Facilitation (e.g. simplification of custom procedures)	<input style="width: 100%; height: 25px; border: 1px solid red;" type="text"/>
E. General trade policy issues (other than A-D)	<input style="width: 100%; height: 25px; border: 1px solid red;" type="text"/>

If E. General trade policy issues (other than A-D), please specify the trade policy issue.

C. *Relevance and Specific Example of Coverage.* Which trade policy issues were most relevant for the country during 2009-13 (e.g. lowering trade barriers, signing a trade agreement, promoting diversification)?

Please provide a specific example of how the relevant issue was covered in the staff report. Name the specific country document, year, issue, title of the section, and provide a brief assessment of how well it was covered. (For instance, SIP, box, staff appraisal, or other sections of staff report).

- D. *Gaps.* Are there any gaps in coverage of trade policy issues? For example, were relevant issues not covered adequately (e.g. use of protectionist measures during the crisis, impact of free trade agreements)? If so, please provide reasons. **Scale: 1-4**, with 1= inadequate coverage (major gaps), 2= less than adequate coverage, 3= adequate coverage, 4= fully appropriate coverage.

Scale:

- E. *Issues Going Forward.* What are the key trade policy issues for your country going forward if any?

Section III. Integration of trade and trade policy issues in policy assessment

- A. How well were trade and trade policy issues integrated in overall policy assessment? **Scale: 1-4**, with 1= trade and trade policy issues were not integrated with overall policy issues at all, 2= somewhat integrated, 3= well integrated, 4= very well integrated. Please first place your scaling and add any comments in the box below.

Scale:

- B. How useful were the multilateral surveillance products, including WEOs and REOs, in portraying the global and regional trade landscape for bilateral surveillance? **Scale: 1-4**, with 1= not useful, 2= somewhat useful, 3= very useful, 4= extremely useful. Please first place your scaling and add any comments in the box below.

Scale:

Section IV. Coverage of specific trade and trade policy issues

- A. *Global Value Chains*. Value chains (the range of activities to produce a good) are increasingly fragmented across multiple borders. The growth of these Global Value Chains has important implications for the Fund's surveillance work (*Board Paper "Trade Interconnectedness: The World with Global Value Chains*, August 26, 2013).

Were global value chains covered in country staff reports? **Scale: 1-4.**² In your comments, please give a sense if global value chains are relevant for your country. If possible, provide a specific example of how the issue was covered in the SR. Name the specific country document, year, issue, title of the section, and provide a brief assessment of how well it was covered. (For instance, SIP, box, staff appraisal, or other sections of staff report).

Scale:

- B. *Trade Collapse in 2009*. 'One of the most notable features of the Great Recession was the "sudden, severe, and synchronized" collapse in trade in late 2008 and in 2009. The annualized drop in world imports was more than 30 percent, with roughly equal declines experienced by advanced and emerging economies.' (*World Economic Outlook, Chapter 4 "Do Financial Crises Have Lasting Effects on Trade?"*, October 2010).

How well was trade covered in your country in 2009 relative to the other years in the period? Was there a specific coverage of the trade collapse and policy response? **Scale: 1-4.** If possible, provide a specific example of how the issue was covered in the SR. Name the specific country document, year, issue, title of the section, and provide a brief assessment of how well it was covered. (For instance, SIP, box, staff appraisal, or other sections of staff report).

Scale:

² **Scaling system:** In this section, 1= not covered at all, 2= somewhat covered, 3= well covered, 4= very well covered.

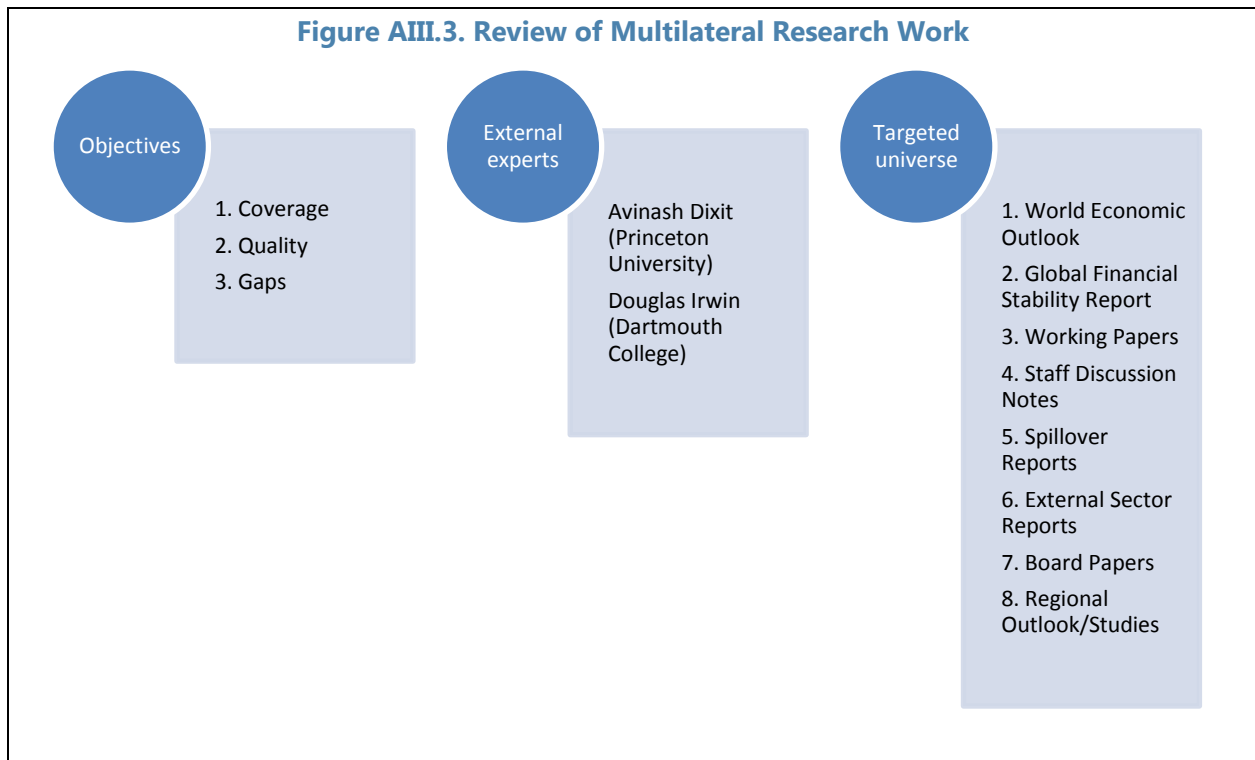
C. *Trade policy and the food crisis in 2010-11.* In 2010-11 prices of food products such as cereals rose by over 100 percent determining a food crisis in several countries. According to the WTO and the World Bank, trade policy was one of the underlying causes of rapid food price inflation, creating large cross-border spillovers. (*Export Restrictions and Price Insulation During Commodity Price Booms*, World Bank WP 5645, May 2011).

Was trade policy in the food sector covered in your country reports in 2010-11? Did the analysis cover both domestic and spillover effects of trade policy measures? **Scale: 1-4.** In your comments, please give a sense if trade policy in the food sector is relevant for your country. If possible, provide a specific example of how the issue was covered in the SR. Name the specific country document, year, issue, title of the section, and provide a brief assessment of how well it was covered. (For instance, SIP, box, staff appraisal, or other sections of staff report).

Scale:

- **(Optional) Other comments:**

Approach 3: Review of Multilateral Research Work. The multilateral and research work was reviewed in consultation with external experts (Figure AIII.3). The review has two stages. The first stage focuses on the universe of Fund multilateral products that relate to international trade and trade policy. The goal of this panoramic view is to assess the coverage of the issues and identify potential gaps in the analysis of the past five years. The second stage consists of an in-depth review of a representative subset of multilateral and research work to assess the quality of Fund trade analysis.



Annex IV. Results for Review of Bilateral Surveillance by Region

Figure AIV.1. Coverage of Trade Issues



Figure AIV.2. Coverage of Trade Policy Issues

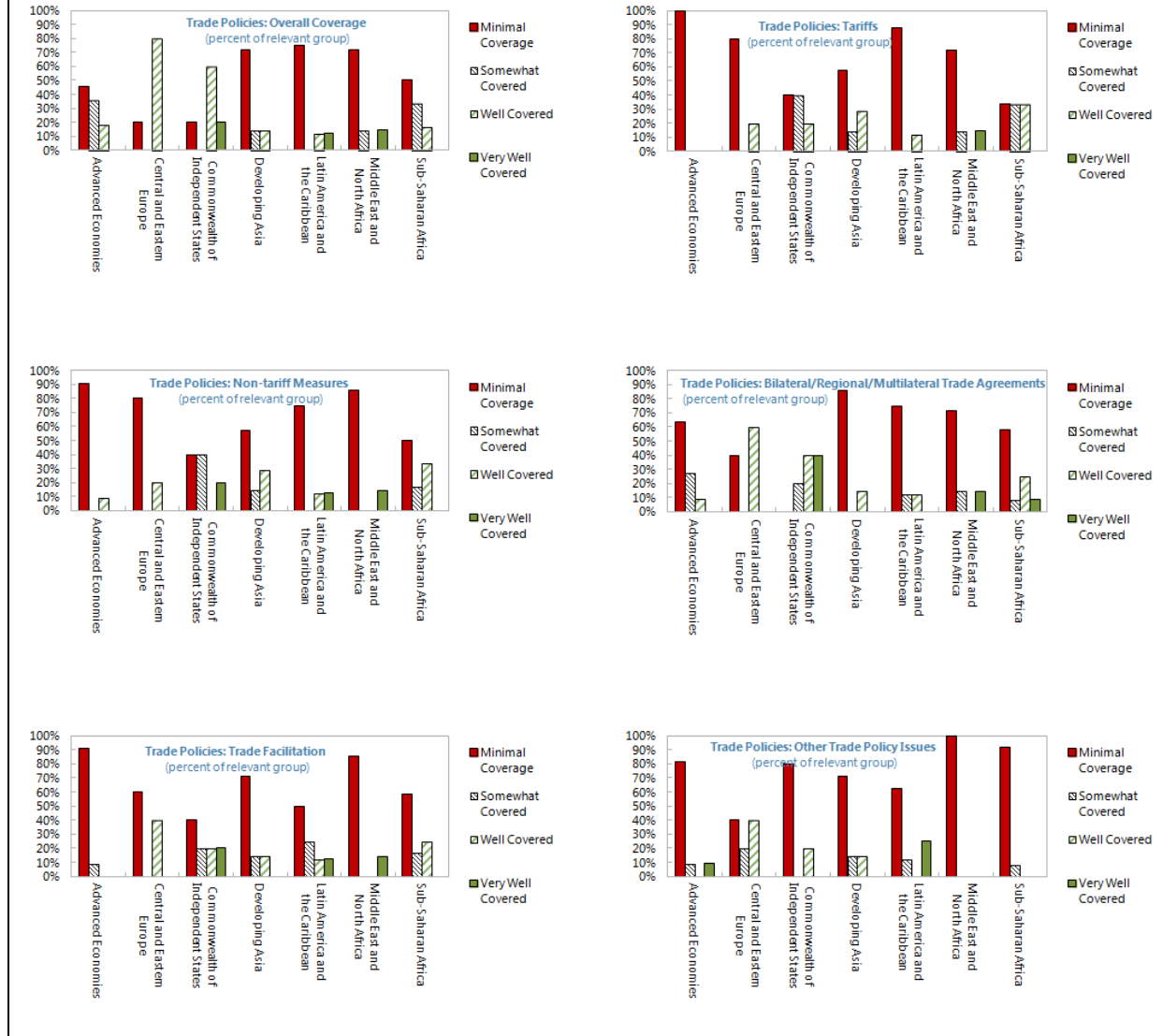


Figure AIV.3. Gaps in Trade and Trade Policy Coverage

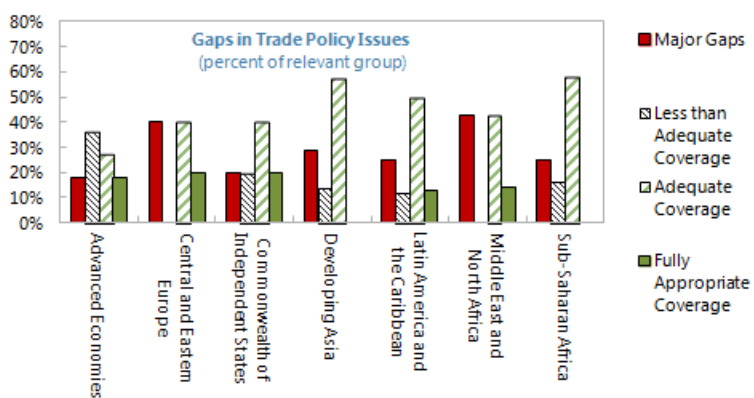
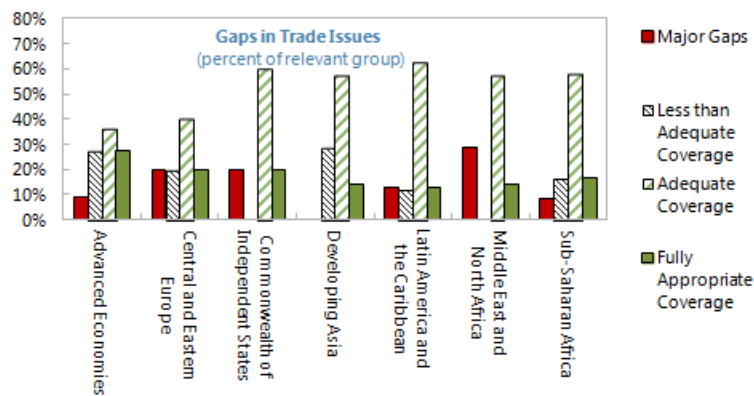


Figure AIV.4. Integration of Trade and Trade Policy Issues in Policy Assessment and Usefulness of Multilateral Surveillance Products

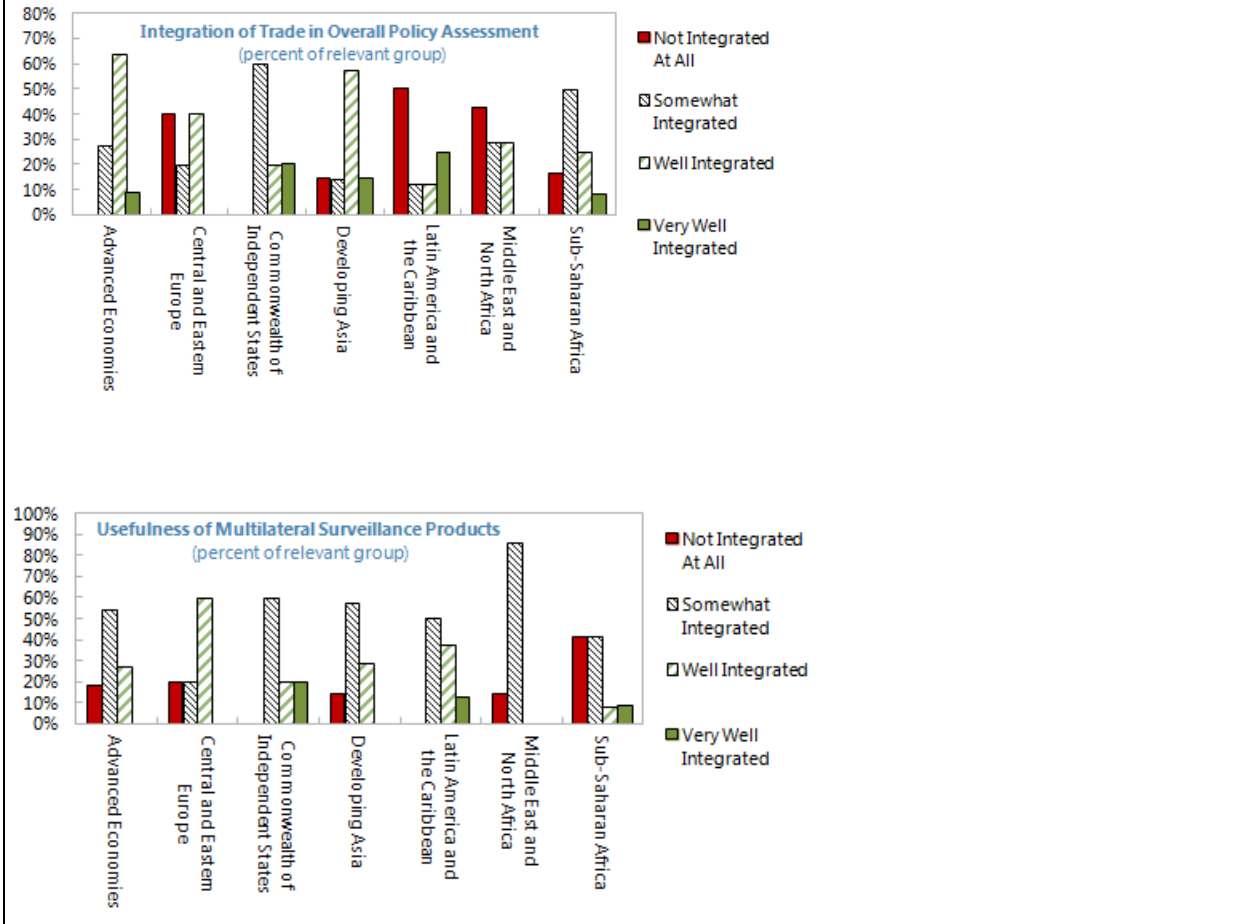


Figure AIV.5. Coverage of Specific Trade and Trade Policy Issues

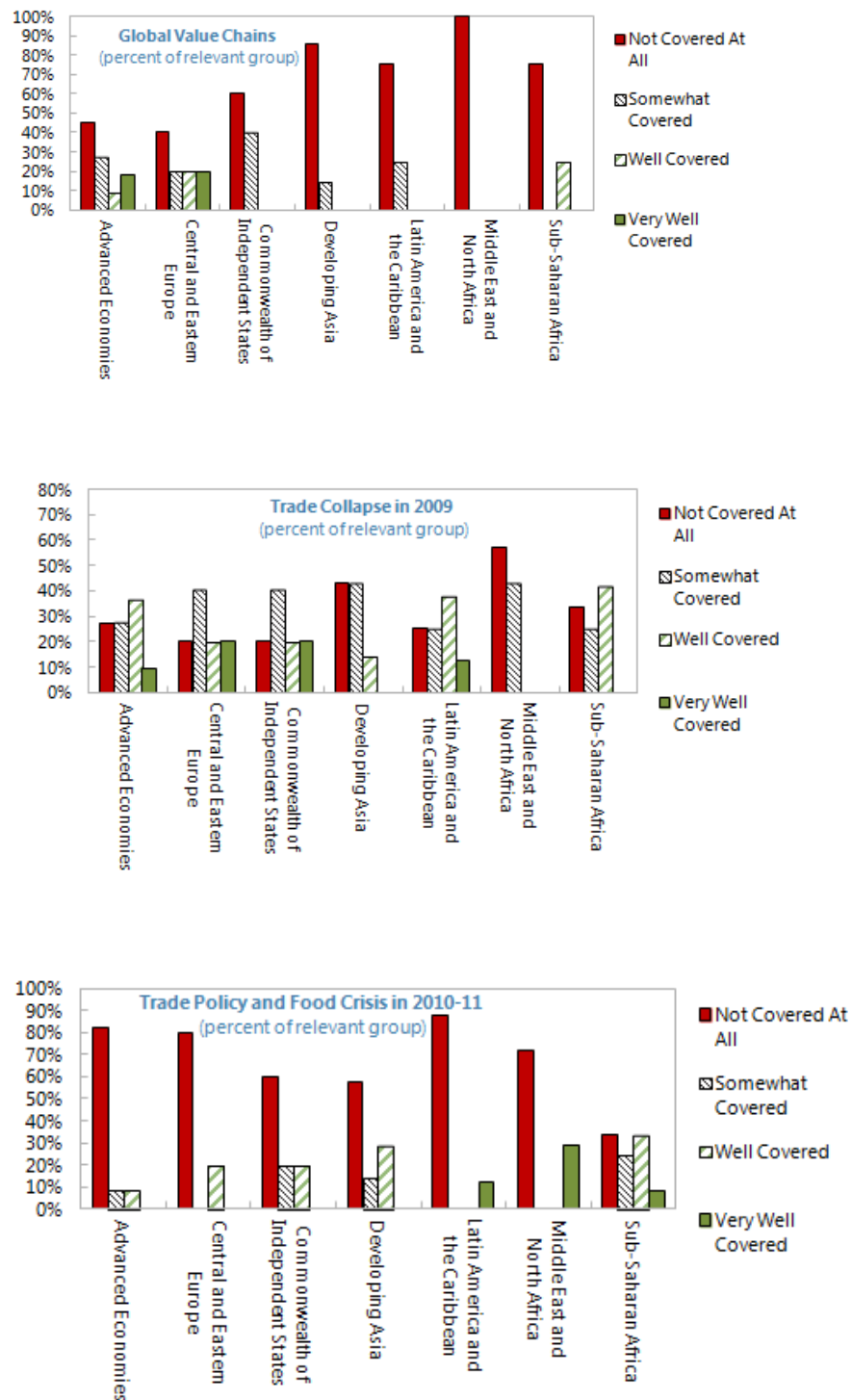
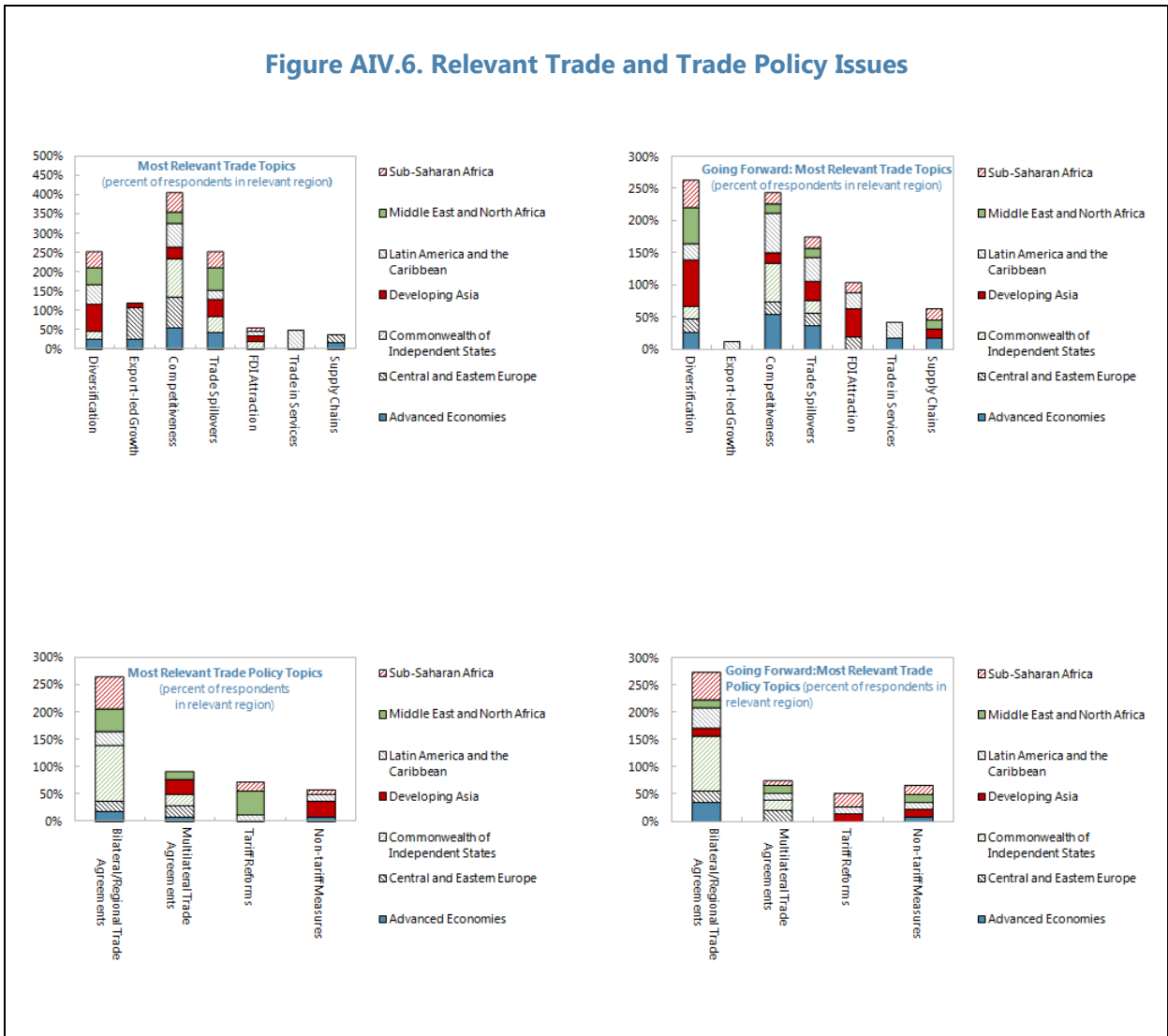


Figure AIV.6. Relevant Trade and Trade Policy Issues



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INTERNATIONAL MONETARY FUND



Press Release No. 15/132
FOR IMMEDIATE RELEASE
March 23, 2015

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Reviews the Role of Trade in the Fund's Work

On February 27, 2015, the Executive Board of the International Monetary Fund (IMF) discussed the five-yearly [Review of the Role of Trade in the Work of the Fund](#). This review follows the Board-endorsed recommendations and proposed implementation plan arising from the 2009 IEO Evaluation of IMF Involvement in International Trade Policy Issues. The staff paper provides a broad overview of the role of trade and trade policy issues in the work of the Fund over the past five years and discusses how to integrate and operationalize the implications of the changing global trade landscape at the Fund. The paper focuses on macro-critical trade issues and proposes to introduce a work agenda for the next five years. Based on the staff paper, the Board's discussion focused on how to make trade an essential element of the IMF's operational work and to further develop a work agenda for the Fund.

Following the Executive Board's discussion, Ms. Christine Lagarde, Managing Director and Chair, stated:

“Executive Directors welcomed the review of the role of trade in the work of the Fund and broadly agreed with its main findings. They noted that the trade landscape has changed rapidly in recent years. Directors considered that trade is an essential component of the global policy agenda to bolster growth and saw a need to reignite the multilateral trade system. They noted that there are potentially large global gains to be derived from further trade liberalization and integration, including from traditional trade liberalization in many countries and sectors, lowering barriers in new trade policy frontiers, and additional expansion of global supply chains. Directors also noted that trade reforms can complement and augment the benefits of other structural reforms, spur additional infrastructure investment, and support the strengthening of policy and institutional frameworks.

“Directors welcomed the high quality and policy-relevant work done by the Fund. They emphasized that the Fund's work in this area should remain within its mandate, addressing trade issues deemed macro-critical and taking into account resource constraints and limited trade expertise. This would require careful prioritization and continued collaboration with other international institutions, including the World Trade Organization and the World Bank.

“Directors emphasized that the coverage of trade issues in Fund surveillance should be tailored to the specific needs of individual countries. Recognizing differences across countries, Directors noted that for advanced countries, a key issue would be the implications of their efforts to pioneer and advance new trade policy areas such as services, regulations, and investment. For emerging market economies, there are still benefits from traditional liberalization and anchoring to global supply chains. For low-income countries, greater integration requires sustained efforts to reduce trade costs, including upgrading trade infrastructures and improving economic institutions both at national and regional levels, supported by relevant technical assistance.

“Directors agreed that better embedding trade in surveillance work would require a concerted effort on several fronts. They saw merit in enhancing efforts to translate key implications from the evolving trade landscape and continuing analytical work, and in further developing a work agenda for the Fund for the next five years based on the key considerations discussed. Several Directors suggested that staff should consider a range of issues for further work. Some Directors were open to having a clearer institutional view. In this regard, Directors noted that the 2010 reference note on trade policy will be updated to provide staff guidance on macro-relevant trade and trade policy issues. Directors stressed the importance of ensuring that the Fund’s approach to trade policies is evenhanded. Going forward, Directors considered it important to regularly review the role of trade in the Fund’s work.”