

INTER-AMERICAN DEVELOPMENT BANK
Integration and Regional Programs Department



AID FOR TRADE

**THE INTER-AMERICAN DEVELOPMENT BANK'S
EXPERIENCE IN LATIN AMERICA AND THE
CARIBBEAN**

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Special Report on Aid for Trade

INTEGRATION AND REGIONAL PROGRAMS DEPARTMENT

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The opinions expressed herein are those of the authors and do not necessarily reflect the official position of the Bank or its member countries.

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ABBREVIATIONS

ADB	Asian Development Bank
CABEI	Central American Bank for Economic Integration
CAF	Andean Development Corporation
CAFTA-DR	US-Central America-Dominican Republic Free Trade Agreement
CARICOM	Caribbean Community
DFID	Department for International Development (UK)
DTIS	Diagnostic trade and integration study
ECLAC	UN Economic Commission for Latin America and the Caribbean
EU	European Union
FONPLATA	Financial Fund for the Development of the River Plate Basin
FSO	IDB Fund for Special Operations
FTAA	Free Trade Area of the Americas
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
IDB	Inter-American Development Bank
IF	Integrated Framework
IFI	International financial institution
IIC	Inter-American Investment Corporation
IIRSA	Initiative for the Integration of Regional Infrastructure in South America
IMF	International Monetary Fund
INT	Integration and Regional Programs Department (IDB)
INTAL	Institute for the Integration of Latin America and the Caribbean (IDB)
ITD	Integration, Trade and Hemispheric Issues Division (IDB)
LAC	Latin America and the Caribbean
LDC	Least developed country
MIF	Multilateral Investment Fund (IDB)
NAFTA	North American Free Trade Agreement
NLF	New Lending Framework (IDB)
OAS	Organization of American States
OECD	Organization for Economic Cooperation and Development
PBL	Policy-based loan
PDL	Performance-driven loan
PPP	Puebla Panama Plan
PRI	Private Sector Department (IDB)
RTC	Regional Technical Cooperation
SWAP	Sector-Wide Approach
TFFP	Trade Finance Facilitation Program
TFRP	Trade Finance Reactivation Program
UNCTAD	UN Conference on Trade and Development
WB	World Bank
WTO	World Trade Organization

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I. INTRODUCTION

The Inter-American Development Bank (IDB) is the main source of multilateral development finance in Latin America and the Caribbean (LAC).¹ From 2000 to 2005, total financing for economic, social and institutional development projects amounted to US\$38.7 billion, of which close to US\$35 billion was ordinary capital, US\$2.7 billion was concessional lending, and US\$1.1 billion was grant funding.² Concomitant with emerging demands in its borrowing member countries, the IDB has in recent years devoted a growing share of its financing to trade-related assistance, echoing a broader trend in aid flows across the world. Trade-related assistance, or aid for trade, encompasses both traditional trade-related capacity building and broader forms of assistance aimed at enhancing a country's capacity to trade (Box 1).

Box 1. What is Aid for Trade?

Aid for trade refers to the flow of development finance from developed to developing countries for the purpose of enhancing their participation in the world trading system. Narrowly defined, the term refers to trade-related capacity building to help countries formulate, negotiate and implement trade policy and related agreements; and trade development, including export promotion and trade finance. More broadly defined, aid for trade also covers support to strengthening a country's trade-related infrastructure (transport, energy, communications) and other supply-side capacities (for example, in the productive sector) to help it benefit from freer trade. It can also refer to trade-related adjustment programs (social safety nets, worker retraining).

While there is no universally agreed definition of the term, aid for trade is nothing new: bilateral donors, international financial institutions (IFIs) and other development agencies, including the IDB, have long engaged in the provision of such assistance. But the term has assumed prominence in the current Doha Development Round of multilateral trade negotiations, where discussions are underway on how to expand aid for trade. Several developed countries have pledged to increase their trade-related assistance in the coming years to help developing countries build the supply-side capacity and trade-related infrastructure they need to implement and benefit from WTO agreements and to expand their trade. WTO members view aid for trade not as a substitute for, but as a complement to the development benefits that would result from a successful conclusion of trade negotiations in the Doha Round.

¹ The IDB has 47 member countries: *Borrowing member countries* are: Argentina, The Bahamas, Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Suriname, Trinidad & Tobago, Uruguay, and Venezuela. *Non-borrowing member countries* include: Austria, Belgium, Canada, Croatia, Denmark, Finland, France, Germany, Israel, Italy, Japan, Korea, Netherlands, Norway, Portugal, Slovenia, Spain, Sweden, Switzerland, the United Kingdom and the United States.

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At the Sixth Ministerial Conference of the World Trade Organization (WTO), held in Hong Kong in December 2005, Ministers called for the establishment of a WTO task force to examine ways in which aid for trade could be made operational and might contribute to the development dimension of the Doha Development Agenda. The 13-member task force was created in February 2006. Half of its members are also member countries of the IDB (they are Barbados, Brazil, Canada, Colombia, Japan and the United States, with EU countries holding a joint seat).³ The task force has been asked to provide recommendations to the General Council of the WTO by July 2006, and has invited international organizations, including the IDB, to provide advice in the formulation of relevant proposals.⁴

The IDB is well placed to provide contributions to the current debate on aid for trade. Since its creation more than forty years ago, the Bank has actively supported the development of trade-related infrastructure and supply-side capacities in its LAC member countries. Over the last decade, moreover, the Bank has built a solid track record in trade-related capacity building in LAC, developing both country-focused and region-wide approaches to the provision of such assistance. Through regular interaction with government authorities, the private sector and other non-state actors, it has developed a sound reputation in the LAC trade community, based on technical expertise, working experience and mutual trust.

LAC is a diverse region comprising mostly middle-income countries, many of which no longer have access to concessional IDB or World Bank financing. Most LAC countries are moreover excluded from recent trade-related cooperation initiatives that target the least developed countries (LDCs) – such as the Integrated Framework (IF) or the EU Everything but Arms Initiative. Trade, however, is crucial for their development, and despite their relatively more advanced levels of development, LAC countries continue to face serious challenges in this area. For many of them, trade liberalization has been at the center of a significant structural reform process spanning the last two decades,

² Total funding approved for new loans and grants, including Multilateral Investment Fund (MIF). Another US\$1.1 billion in loans was provided by the IDB's sister organization, the Inter-American Investment Corporation (IIC).

³ The remaining members of the task force are China, India, Thailand, Mauritius, Benin and Zambia. The latter three currently act as coordinators, respectively, of the African, Caribbean and Pacific (ACP), African, and Least-Developed Country (LDC) groups in the WTO.

⁴ A version of this report was submitted by the IDB as a contribution to the WTO Task Force on Aid-for-Trade.

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but it has not yet delivered the expected results in terms of stronger export growth and economic development.

The challenges facing LAC in the area of trade are briefly reviewed in Section II of this document. Section III provides an overview of IDB support to trade in the past decade, examining institutional developments, efforts to integrate trade into the Bank's programming process, and innovations in the types of instruments and mechanisms used to deliver trade-related assistance. Section IV examines lessons learned and, based on these, highlights existing gaps in the provision of trade-related assistance. Section V looks to the future, offering some recommendations on how the IDB could contribute to global efforts at delivering aid for trade more effectively.

II. TRADE CHALLENGES IN LATIN AMERICA AND THE CARIBBEAN

Among developing regions, LAC has been one of the most active participants in multilateral, regional and bilateral trade initiatives. LAC countries recognize that trade can be a powerful engine of growth and that liberalization affords them with many opportunities for expanding economic welfare. Because many LAC countries are relatively small, they depend crucially on trade for their economic development. Even in larger economies, domestic market size is constrained by low income levels across large sections of the population. LAC countries need export income to create and sustain jobs, finance imports, pay off foreign debt, and maintain a healthy balance in their external accounts, all of which is necessary to achieve sustainable levels of economic growth. LAC countries also depend on the supply of competitively priced imports to support local production and satisfy consumer demands. In a global context marked by the emergence of new trade powerhouses such as China and India, LAC countries need to preserve their trade competitiveness to secure continued access to international markets and the associated welfare gains.

In the 1980s and 1990s, LAC countries undertook significant structural reforms to facilitate economic growth and development. Trade liberalization featured prominently in the reform process and was pursued through a multi-polar integration strategy.⁵ Unilateral trade liberalization helped raise efficiency in domestic markets, while reciprocal multilateral liberalization (GATT/WTO) as well as bilateral free trade agreements opened new markets for exporters and provided the means for establishing effective rules governing trade with external partners. Regional integration, meanwhile, offered easier access to neighboring markets and an opportunity for businesses to prepare for further global market integration. Import protection declined substantially during this period: the region's average tariff fell from 40 percent in the mid-1980s to 10 percent in 2000. However, liberalization was not systematically accompanied by complementary policies to help countries maximize the benefits of reform. A comprehensive strategy aimed at making trade work for development is even more urgent as the scope of global trade integration broadens.

⁵ Inter-American Development Bank. 2003. *Beyond Borders: The New Regionalism in Latin America – Economic and Social Progress Report*, Inter-American Development Bank, Washington, D.C.

Increase Welfare through Trade Performance. Despite the structural reforms, the region's trade performance displays some weaknesses and needs to be improved in most countries. Trade openness, measured as the ratio of a country's external trade to its GDP, is below levels prevalent in other regions of the world.⁶ Some of the smaller Central American and Caribbean countries do have high levels of trade openness, but in these and most other LAC countries, the quality of trade integration presents vulnerabilities. Exports are not very diversified, and consist mostly of commodities or resource-based manufactures with low technology content. In addition, several LAC countries - prominent among them the smaller Caribbean islands - have been exposed to significant preference erosion in recent years, adding to their difficulties of maintaining a competitive presence in world markets. After a decade of sluggish growth, the region needs stronger trade performance to achieve and sustain higher levels of economic growth.

Equitably Distribute the Gains from Trade. In the reform process, efficiency considerations overshadowed concerns regarding the distributional aspects of trade liberalization. As a result, trade opening was only rarely accompanied by mechanisms for compensating inevitable losers in the process and boosting the opportunities of potential winners. Few countries implemented broad adjustment programs to address the disruptions to local industries and labor markets resulting from trade liberalization. Such disruptions, along with rapid import growth unmatched by similar export performance, pressures on national trade balances and current accounts, and widespread perceptions of insufficient public consultation during the reform process have tested LAC countries' continued support for trade liberalization and reform. In some countries, a certain reform fatigue has heightened the risk of a backlash to further trade liberalization. Partly as a result of these developments, trade issues have assumed a much more prominent role in the public debate. At a time when further reform is needed to boost competitiveness, waning support for trade opening is a serious challenge.

Adapt to the Complexity of Modern Trade Agreements. For LAC countries, trade liberalization is not a linear process starting with negotiations at the bilateral, regional or multilateral level, then moving to implementation of commitments and, finally, to adjustment to a more open trade regime. Rather, it

⁶ For example, Colombia has roughly the same GDP as the Philippines, but its trade/GDP ratio is less than half that of the Philippines. Similarly, Venezuela's population and GDP are close to those of Malaysia, but its trade/GDP ratio is less than one fourth of Malaysia's.

is a circular and continuous process in which implementation and adjustment often raise the need for further negotiation and liberalization. In addition, LAC countries are often at various stages of implementing multiple agreements with different trade partners, which requires careful planning and adequate resource allocation across all stages of the reform process. Finally, trade agreements themselves have become more complex, increasingly covering behind-the-border issues in addition to traditional border issues such as customs tariffs and rules of origin. Behind-the-border issues such as investment, intellectual property, competition and standards are becoming standard features in modern trade agreements. To fulfill commitments in these areas, governments are often required to make significant changes to long-standing institutional, legal and administrative practices in their countries.

Promote Ownership of Trade Reforms. The combination of a more complex reform agenda and growing public debate about trade means that governments must increasingly involve multiple actors in the formulation and implementation of trade policy, with a view to creating a sense of public ownership of the reform process. This requires the development of efficient consultation mechanisms among relevant government departments, and between these and prominent civil society groups such as labor and the private sector.

Further Expand Trade-related Institutional Capacity. Technical capacity is crucial to managing a complex trade agenda, and not always readily available in the region. As in fact, there are significant variations in capacity and experience among LAC countries with respect to the negotiation and implementation of trade agreements. While several countries were actively involved in the Uruguay Round negotiations, others were less involved, their participation often constrained by the lack of permanent representation in Geneva. The speed of implementation of Uruguay Round commitments has also varied greatly across the region. On the regional and bilateral front, Chile and Mexico started liberalizing early and are now implementing complex North-South trade agreements with the United States, EU and Asian countries. Other LAC countries have gained most of their experience through less ambitious South-South agreements with neighboring countries, and have only recently begun to negotiate and implement bilateral trade agreements with developed countries (e.g., the US-Central America-Dominican Republic Free Trade Agreement, CAFTA-DR). Some countries are fairly new members to the WTO and one – The Bahamas – has not yet joined.

Secure Adequate Funding for Trade-related Assistance. LAC countries have limited financial resources to manage their trade agenda, particularly as the agenda expands to respond to emerging needs. Severe debt overhangs, sluggish economic growth during most of the past decade, loss of tariff revenue, difficulties in establishing alternative revenue sources, and growing social demands have all put severe pressure on fiscal resources to fund the various stages of trade-related policymaking. The concentration of some recent trade-support programs on LDCs has not been helpful for LAC countries, which are mostly middle-income countries. In some cases, such as the EU Everything but Arms Initiative, such programs have placed additional strain on LAC export efforts because they have affected relative market access conditions for many of the region's exporters. In others, such as the Integrated Framework, most of them are simply not included.

Implement Complementary Domestic Policies. Against this background, LAC governments increasingly recognize that trade policy can no longer be treated as a sectoral issue isolated from other aspects of economic policy. First, trade liberalization can induce macroeconomic shocks and thus requires broad-based macroeconomic responses to address the fiscal impact of liberalization and preserve price competitiveness through sustainable exchange rate policies. Second, trade liberalization is a necessary, but not sufficient condition for generating equitable economic growth. It opens doors and provides new opportunities for growth, but to help economic actors seize those opportunities, governments must create an enabling environment for enhanced productivity and competitiveness, particularly through the removal of red tape and other impediments to business development. This requires action in many areas of economic policy, both at the macro and micro level, and investments in infrastructure and related services. Finally, efforts to boost economic efficiency should be accompanied by policies that promote equity. Specific trade-related social policies aimed at protecting the most vulnerable and facilitating the transition of labor to expanding sectors of the economy should form an integral part of trade reform.

III. A DECADE OF IDB TRADE-RELATED ASSISTANCE IN LAC

For the IDB, as for its clients in Latin America and the Caribbean, 1994 marked a milestone in the area of trade. It was the year in which the Uruguay Round of multilateral trade negotiations was concluded, with LAC countries binding their tariffs for the first time in GATT history and agreeing to a comprehensive agenda of complementary, behind-the-border trade reforms to be implemented under the newly established WTO. It was also the year the North-American Free Trade Agreement (NAFTA) entered into force between Canada, Mexico and the United States. In South America, Mercosur countries signed the Ouro Preto Protocol, consolidating the group's institutional structure and moving it towards a customs union, the second largest in the world. In 1994, moreover 34 countries in the western hemisphere, all of them IDB members, decided to negotiate a Free Trade Area of the Americas (FTAA). Since then, LAC countries have concluded 39 bilateral and regional trade agreements with each other and with countries outside the hemisphere.

For the IDB, responding to this upsurge in trade policy developments in the region was an urgent priority. The Bank faced three challenges in this regard: how to adapt its institutional strategy and structure to growing demands for trade-related assistance; how to integrate trade into its programming process; and how to deliver trade-related assistance effectively through traditional and new instruments.

A. Institutional Adjustments to Meet Client Needs

Trade and the IDB Institutional Strategy. In 1994, the IDB's Board of Governors increased the Bank's financial resources and reaffirmed regional integration as an important strategy for enhanced global integration and one of the institution's foremost operational priorities. These priorities are developed in greater detail in the Bank's Institutional Strategy, approved in 1999. The strategy defines sustainable economic growth, poverty reduction and promotion of social equity as the institution's overarching goals. These goals are advanced through action in four priority areas: modernization of the state, regional integration, competitiveness and social development.

Trade is deeply embedded in each of these four areas. Modernization of the state includes trade-related capacity building and institutional reforms in the public sector aimed at fostering more efficient trade policymaking and implementation. Regional integration covers support to regional trade agreements and institutions, the development of regional infrastructure, and the fostering of regional public goods. Competitiveness operations target supply-side capacities and adjustment, infrastructure and trade finance, and support to business development activities that improve a country's ability to compete in the global economy. Social development encompasses the creation of safety nets as well as compensatory programs such as re-training of displaced workers.

Restructuring of the Bank. The year 1994 also saw a major restructuring of the Bank, aimed at improving its lending operations and enhancing its capacity to respond to rapidly changing circumstances in its borrowing member countries.⁷ The restructuring included the creation of the Department for Integration and Regional Programs (INT) and, within that Department, a new Bank unit dedicated exclusively to trade and integration issues, the Integration, Trade and Hemispheric Issues Division (ITD). As part of the restructuring, the Bank's Buenos Aires-based Institute for the Integration of Latin America and the Caribbean (INTAL) was made part of the new Integration Department. The aim was to bring together the Bank's headquarters and field-based expertise in the area of trade.

A New Bank Unit Specialized in Trade. The new Trade Division, ITD, was given three mandates: (i) to deliver trade-related technical assistance directly to LAC countries and sub-regions; (ii) to provide technical support services to the Bank's main operational units and departments (both its public and private sector lending windows); and (iii) to act as the Bank's focal point of contact and coordination with other organizations working on trade.

- a. ***Provision of technical assistance to governments.*** One of the Trade Division's most important initial tasks was to provide assistance to the launching of the FTAA process in 1994. ITD provided significant technical support in the areas of market access, agriculture and government procurement both in the preparatory phase (1994-1998) and during the actual trade negotiations, which

⁷ The IDB Group comprises the Inter-American Development Bank (IDB), the Multilateral Investment Fund (MIF) and the Inter-American Investment Corporation (IIC). For information regarding the Bank's organizational structure see www.iadb.org.

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began in 1998. More recently, ITD has also provided direct technical support to LAC countries in their multilateral, sub-regional and bilateral negotiating processes, including WTO, CAFTA and US-Andean free trade negotiations, and to implementation of resulting agreements.

- b. *Technical support services to Bank operational departments.* The Division assists the Bank's operational departments in the design and implementation of trade-related operations, ranging from comprehensive programs of institutional strengthening spanning several ministries and trade-related agencies, to more specific interventions in areas such as customs, technical standards, and trade-related fiscal reform. The Division also provides non-operational support in the form of regional papers and national trade and integration sector studies that feed into the Bank's regional and national programming cycles (see below). Over the years, the Trade Division has established close links with the Bank's operational departments in all stages of the programming process.
- c. *Coordination with other agencies.* The Trade Division is a focal point for the Bank's contacts and coordination with other institutions in the area of trade. Collaboration between the IDB and the WTO was formalized through a Memorandum of Understanding between the two institutions in 1999, and covers such areas as training, research and support to the preparation of WTO Trade Policy Reviews in Latin American and Caribbean countries. Other institutions with which the Bank collaborates in the area of trade include the Asian Development Bank (ADB), the World Bank (WB), International Monetary Fund (IMF), European Commission, Organization of American States (OAS), UN Economic Commission for Latin America and the Caribbean (ECLAC), and UN Conference on Trade and Development (UNCTAD).⁸ Over the years, the Bank has conducted many joint research, outreach and training activities with these agencies.

To help fulfill its mandate, ITD launched a comprehensive research program aimed at providing the basis for informed policy recommendations and

⁸ ITD has represented the IDB on the Tripartite Committee of Technical Support to the FTAA process, comprising the IDB, the OAS and ECLAC.

decisions. The Division has produced numerous policy-relevant studies on a broad range of trade and regional integration issues, including market access negotiations (tariff, non-tariff measures and rules of origin); analysis of major trade agreements (e.g., FTAA, Mercosur bilateral free trade agreements); economic impact of trade liberalization and regional integration (computable general equilibrium modeling and sector studies); the interplay between regional and multilateral trade negotiations; regional cooperation; and regional public goods.

A Revitalized field-based Integration Institute. In 1995, the Bank gave INTAL additional resources to support its trade and integration-related work in the region. Since then, ITD and INTAL have partnered on a wide variety of activities and initiatives supporting trade in the region, combining ITD's technical expertise with INTAL's field experience, operational skills and know-how in the areas of training, publications and outreach. In 1997, INTAL began to collaborate with the WTO in the organization of training courses for trade negotiators in the region. To date, the two institutions have jointly organized over 100 training events in LAC countries, often with direct participation by the Bank's Trade Division. INTAL has also been instrumental in executing regional projects and disseminating Bank research on trade and integration-related issues.

B. Integrating Trade into the Bank's Programming Process

Beyond building institutional capacity in the area of trade, the Bank has made efforts to integrate trade more strongly into its policy dialogue with governments and the programming of its regional and country-specific operations. This has required attention to the various stages of the programming process, and the provision of specific trade-related inputs in each stage. The Bank's programming process is increasingly based on technical analysis. This feeds into policy dialogue with governments and other relevant partners, which, in turn, informs the development of a Bank strategy and related project pipeline. This is then followed by the design and implementation of specific interventions. The process is circular in that lessons learned from programming and the delivery of development finance feed into new technical analysis and policy dialogue. The Bank conducts two types of programming, regional and national, with the latter proving to be the more challenging in terms of integrating trade into the various stages of the process.

Regional Programming focuses on the four main integration groups within LAC: the Andean Community, Caribbean Community (CARICOM), Central American Common Market and Mercosur. Approximately every five years, the Bank prepares new strategies for support to regional integration in each of the four groups. Because of the importance of trade in these integration processes, and the multiple initiatives of regional cooperation in this area among LAC countries, trade has always dominated the Bank's regional strategies. In coordination with the operational departments, the Integration and Regional Programs Department undertakes diagnostic studies to identify the key challenges in each sub-regional integration process, as well as in the group's trade integration with the rest of the world, and on the basis of this assessment proposes priority areas for Bank support. Policy dialogue with regional secretariats, national authorities and relevant non-state actors is crucial throughout the process. The regional strategy facilitates the formulation of regional programs and activities, which are then implemented mainly through grants and direct non-financial support. Regional secretariats and other regional agencies often act as executing agencies for these programs, and over the years, the IDB has developed close working relationships with these agencies. Lending for regional programs is very limited owing to the difficulties in securing appropriate guarantees for multi-country loans.

National Programming is the Bank's main programming instrument. It follows a similar process as regional programming, but the focus is not necessarily on trade. Rather, trade is one of several issues analyzed in the preparation of the Bank's country strategies. The challenge of mainstreaming trade into national programming has been three-fold: first, to support Bank country teams in their efforts to focus more on trade integration in their diagnostic work; second, greater emphasis needed to be placed on trade issues in the Bank's policy dialogue with governments and relevant non-state actors; and third, subsequent to approval of country strategies, trade specialists had to provide technical support to the Bank's operational units during the development and implementation of trade-related operations. To address these challenges, ITD began in the late 1990s to provide specific inputs to the national programming process. Over time, these contributions have evolved into comprehensive trade and integration sector studies (or Diagnostic Trade and Integration Studies, DTIS) that serve as a basis for policy dialogue and feed into the formulation of country strategies. Trade specialists from the Bank have increasingly participated alongside country teams in the Bank's high-level, closed-door policy discussions (*encerronas*) with newly elected governments in

the region. ITD has also assigned some of its trade specialists to work exclusively on operations, helping the Bank to translate technical expertise into operational benefits for its clients.

Efforts to integrate trade into national programming have already yielded results. Whereas country strategies produced by the Bank in the mid-1990s contained few specific references to trade, today many strategies devote significant attention to trade and global market integration, and strengthening of related institutions. This, of course, also reflects the fact that trade is increasingly mainstreamed into the national development agendas of the Bank's client countries. Requests for trade-related assistance have increased as a result, and the Bank has used both existing and new instruments to respond to this growing demand.

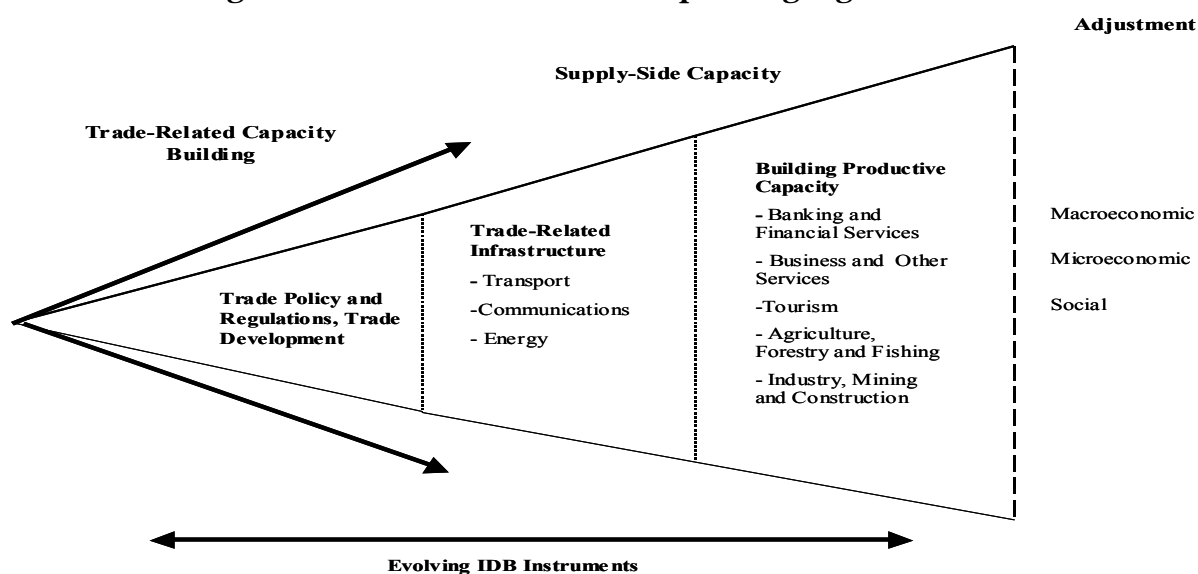
C. Adapting the Bank's Instruments to a More Complex Trade Agenda

Aid for trade is not new for the IDB: many of the Bank's traditional lending instruments were designed to support the very elements of what is today perceived as the broader aid-for-trade agenda, including infrastructure development (transport, energy and communications) and strengthening of countries' productive capacities. The Bank also has a long track record of providing adjustment-related lending, some of which has been directly related to trade. What was new in the 1990s was that the Bank began to build institutional capacity and deepen its operational support in the area of trade-related capacity building (Figure 1). The Bank also began to explore ways of better linking the various components of trade-related assistance (capacity building, supply-side development and adjustment), and to design new grant and lending instruments to this effect.⁹

⁹ The section provides a broad overview of the Bank's trade-related operations; specific projects are mentioned only for illustrative purposes.

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Figure 1. Aid for Trade: The Expanding Agenda



Source: IDB adaptation of figure presented in OECD, *Aid for Trade: Support for an Expanding Agenda* (COM/DCD/TD), 2006

Traditional Financial and Non-Financial Support. During the 1990s, the IDB relied on existing lending and grant instruments to deliver trade-related assistance. The Bank's most important lending instruments, investment and policy-based loans, continue to finance the vast majority of the Bank's operational activities in LAC, including operations to improve trade-related infrastructure and supply-side capacities. Investment loans are the Bank's most widely used lending instrument and span the whole range of the expanded aid-for-trade agenda.¹⁰ Policy-based loans disburse against the implementation of agreed policy changes.¹¹ While most loans are non-concessional, some are

¹⁰ Examples of such loans include Productivity Support and Development of New Livestock Products in Uruguay (US\$19.8 million), Improvement of the Competitiveness of Tourism in Argentina (US\$56 million), SIEPAC Central American Electric Interconnection (US\$50 million), Rural Roads National Program II in Paraguay (US\$89.5 million), Northern Coastal Highway Improvement in Jamaica (US\$85 million), Program for Institutional Strengthening of the Tax and Customs Administration in Nicaragua (US\$12.5 million) and Modernization of the National Customs Bureau in Uruguay (US\$1.1 million).

¹¹ The Bank has developed a number of policy-based loans to help strengthen the institutions in charge of competitiveness and trade negotiations, simplify trade and custom procedures, enhance business and labor productivity and improve the regulatory framework for the provision of infrastructure services. An example of a PBL is the Peru Competitiveness Reform Program (US\$300 million) with three areas of action: i) long-term approach to addressing and resolving impediments to competitiveness ii) policy and institutional reform to improve the climate for private sector investment as well as reduce costs and

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provided on a concessional basis from the Bank's Fund for Special Operations (FSO). Only five countries – Bolivia, Guyana, Haiti, Honduras and Nicaragua – have access to this type of financing.¹² The Bank lends to both the public and private sector. The latter operations are managed by the Bank's Private Sector Department (PRI) and its sister organization, the Inter-American Investment Corporation (IIC).¹³

Grants and non-financial support were the main instruments for the Bank's assistance to trade-related capacity building during this period. Grant funding came from the FSO and the various trust funds managed by the Bank on behalf of its non-borrowing member countries. None of these funds was dedicated exclusively to trade. The Multilateral Investment Fund (MIF), established in 1993 and administered by the IDB, focused its assistance on private sector development, using both grant and investment mechanisms to undertake small, targeted development projects to build the capabilities and skills standards of the workforce, broaden the economic participation of smaller enterprises and strengthen the environment for doing business – but the connection to trade, and trade policy, was still precarious. During the 1990s, the Bank moreover maintained a limited Export Finance Program, which, however, was terminated in 2001 amidst calls for alternative, more efficient mechanisms to address the continuing and growing need for trade finance in the region. Assistance provided directly by the Bank through its administrative budget (defined as non-financial support) was delivered mainly through the Bank's Trade Division and INTAL.

The majority of trade-related capacity building programs funded during this period were regional projects. The Bank's main instrument for regional grant projects is the Regional Technical Cooperation (RTC) Program, which uses both FSO and trust fund resources to finance a wide range of initiatives that span the entire aid-for-trade agenda, including supply-side capacity and adjustment. In the area of trade-related capacity building, RTC projects and

improve efficiency at the enterprise level and iii) public-private cooperation activities at the local level through the development of *clusters*.

¹² The FSO has US\$9.8 billion in paid-in contributions from all Bank member states. The net income of the FSO enables the IDB to approve on average over US\$400 million per year in grants and concessional lending.

¹³ Examples of PRI projects include support to Ecuador's Quito International Airport (US\$610 million) that includes the construction of a connector road to the new airport and the Inter-oceanic highway, and the development of a free trade zone in the area; and six highway concession projects in Brazil since 1996 (nearly US\$1.7 billion) as part of the IDB contribution to Brazil's highway concession program.

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non-financial support were used to finance the Bank's significant support to the FTAA process.¹⁴ The Bank also provided grant funding for a number of sub-regional trade initiatives.¹⁵ The Bank moreover stepped up its non-financial support in the areas of policy research, technical workshops, and other outreach activities. Many of these initiatives were also regional in nature.

New instruments. As LAC demands for trade-related assistance increased, it became clear that new instruments were needed to respond rapidly and efficiently to those demands. More funding was needed for policy research, policy dialogue and direct assistance to governments. Grant funding alone was not adequate to meet the demands, and the Bank's existing loan instruments were tailored more towards large-scale investments -requiring a substantial preparation process- than to urgent needs for technical cooperation to assist in ongoing negotiations and implementation of trade agreements. The region's private sector also needed more targeted assistance to cope with a rapidly changing external environment. Starting in 2000, therefore, the Bank began to develop a number of new instruments and mechanisms to strengthen its trade-related assistance. Some are designed for national interventions, while others focus on regional support; several instruments can cover both types of intervention.

- a. Starting in 2000, the Bank instituted a regular **Regional Policy Dialogue** on trade as part of a broader program that also includes other thematic areas. The objective was to create a trade forum or network through which LAC countries could share experiences, learn about practices outside the region, and explore opportunities for regional cooperation in areas related to trade. The regional policy dialogue meetings bring together vice-ministers and other senior trade officials from LAC countries to explore pressing trade issues, based on a previously agreed agenda and technical work prepared by

¹⁴ RTC projects financed the FTAA Secretariat and the Bank's technical support to three of nine FTAA negotiating groups. Further technical support to the process was provided directly by the Bank's Trade Division; meanwhile, a MIF grant financed implementation of customs-related business facilitation measures agreed by the countries in 1999.

¹⁵ In the Andean Community, for example, the Bank financed several border development initiatives, while in CARICOM it supported the creation and operation of the Caribbean Regional Negotiating Machinery, and implementation of member states' Uruguay Round commitments. In Central America, the Bank provided assistance in such areas as services trade liberalization and customs. In Mercosur, the Bank supported institutional strengthening of the Mercosur Secretariat, as well as the building of a computable general equilibrium model to measure the impact of various trade liberalization scenarios on the group's economies.

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the Bank. A total of six regional meetings and six sub-regional meetings have so far been held.¹⁶

- b. In 2000, the IDB created a **Trade Sector Facility** that provides fast track approval for ordinary or concessional loans up to US\$5 million to strengthen the capacity of trade ministries and other trade-related institutions to formulate, negotiate and implement trade policy. Ten of the Bank's borrowing member countries have so far accessed the facility, with approved funds totaling US\$46.6 million.¹⁷
- c. In 2002, MIF launched its **Facilitation of International Trade and Investment** project cluster, the aim of which is to foster greater participation of smaller enterprises in international trade and investment. Projects in this cluster support trade facilitation activities related to customs reform, technical standards and certification, as well as strengthening the private sector's participation in the formulation of trade policy. Many projects are regional, rather than national in scope. Since 2002, the MIF has approved 17 grant projects under the cluster with a total contribution of US\$28.2 million.¹⁸ The cluster is supported by technical experts who regularly visit projects, facilitate project implementation and foster the sharing of experiences among beneficiary agencies.

¹⁶ The last two regional meetings focused on the negotiating agenda for the WTO Hong Kong ministerial meeting and on macroeconomic implications of trade liberalization, respectively, while sub-regional meetings have covered such issues as bilateral negotiations with the United States and special and differential treatment.

¹⁷ The ten countries are: Bolivia, Chile, Dominican Republic, Ecuador, Guatemala, Nicaragua, Panama, Peru, Suriname and Trinidad and Tobago. Although each project is tailored to the specific needs of the client, these operations typically comprise the following components: (i) institutional reform to improve trade policymaking; (ii) implementation of effective information and communications systems for the Ministry of Trade and other trade-related agencies; (iii) technical support to negotiations and implementation of trade agreements, and training in all areas related to trade; (iv) sector-specific support in such areas as agriculture, sanitary and phytosanitary standards and intellectual property rights; (v) modernization of export promotion and investment attraction agencies; and (vi) support for outreach activities and stakeholder consultations.

¹⁸ Project examples include a US\$1.1 million regional grant to support the private sector's participation in CARICOM's external trade negotiations; a US\$2.48 million grant to support small rural producers in Argentina in overcoming technical barriers to trade; and a US\$2.14 million regional grant to raise awareness and facilitate application of sanitary and phytosanitary standards in Mesoamerica.

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- d. In 2002, the Bank created the **Special Initiative on Trade and Integration**, providing additional funding to the Trade Division over a four-year period (2003-2006). The aim was to (i) strengthen the Bank's capacity to influence the policy debate on trade and integration; (ii) provide technical support to governments, particular in response to urgent, time-sensitive requests; and (iii) conduct more public outreach.¹⁹
- e. In 2003, responding to growing needs for adjustment-related assistance, the Bank established a **Lending Program for Trade, Integration and Competitiveness**, which allows a country to combine components of the Bank's policy-based, investment and technical assistance lending into a single loan operation to address the broader range of sectoral adjustments that it must make in the transition to freer trade. This program, coupled with the availability of loans focused on competitiveness, provides support for all the critical issues in the transition to free trade, including infrastructure, labor market adjustment, worker re-training, rural agriculture, small and medium enterprise development, tax reform, customs modernization, and trade-related capacity building.²⁰
- f. In 2003, the **International Trade Finance Reactivation Program (TFRP)** was approved, allowing the Bank to commit up to US\$1 billion for projects, programs and other actions aimed at supporting the availability of trade finance in LAC countries. Initially created on a two-year trial basis, the program was made permanent in 2005. The Bank's private sector department, PRI, has developed several instruments to implement the TFRP. In 2005, it launched one such instrument, the Trade Finance Facilitation Program (TFFP). Under the TFFP, the IDB extends guarantees to cover risks associated with

¹⁹ The Special Initiative has allowed the Bank to expand its trade-related research, technical assistance and outreach activities substantially. For example, it has enabled the Bank to provide direct support to Central American and Andean countries in developing and implementing national action plans for trade-related capacity building. It has also facilitated the Bank's policy research into crucial areas such as rules of origin; asymmetries and distributional effects related to trade liberalization, and the implications for LAC of China's emergence as a major trading power. Finally, it has helped expand the Bank's outreach activities, for example by funding orientation workshops on trade for parliamentarians and civil society.

²⁰ Costa Rica was the first to develop a multi-sector loan under the program, comprising foreign trade, science and technology and rural roads rehabilitation. The US\$116.8 million investment loan was approved in 2005.

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trade-related instruments (e.g., letters of credit, documentary collections, promissory notes) issued by banks in the financing of international trade transactions.²¹ The Bank has also approved several loans to investment funds that provide trade financing to under-served exporters and importers in the region.

- g. Bilateral donors have increasingly channeled trade-related assistance through the IDB. The **IDB-Canada Trade Fund**, established in 2003, provides grants to relevant ministries or regional agencies to support trade-related capacity-building programs agreed by LAC countries under the FTAA Hemispheric Cooperation Program. The Fund has expanded the Bank's possibilities of offering grant assistance at the national level. So far, ten countries and one regional agency have accessed the fund, for total financing of CAN\$1.65 million (US\$1.5 million). The **Trade and Poverty Trust Fund**, established in 2005 as a multi-donor trust fund from the United Kingdom (DFID), supports Bank efforts to respond to increased demands for analysis of the distributional effects of trade integration, as well as the formulation and implementation of strategies, policies and instruments aimed at enhancing the impact of trade integration on the poor.

Beyond specifically trade-related instruments, several broader initiatives launched by the IDB in recent years support the institution's efforts to deliver aid for trade more effectively. Noteworthy are three infrastructure initiatives aimed specifically at supporting the region's intra-regional and global integration.

- a. **Initiative for the Integration of Regional Infrastructure in South America (IIRSA)**. Launched in 2000, IIRSA supports the development and integration of energy, transport and telecommunications infrastructure across 12 South American countries to facilitate trade integration both intra-regionally and with the rest of the world. The IDB, along with the Andean Development Corporation (Corporación Andina de Fomento, CAF)

²¹ The TFFP currently comprises a network of over 60 confirming banks belonging to 26 different international banking groups in 20 countries, and 11 issuing banks in seven LAC countries with over US\$270 million in approved credit lines. To date, the IDB has issued guarantees for over US\$30 million in support of approximately 50 international trade transactions totaling over US\$66 million.

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and the Financial Fund for the Development of the River Plate Basin (Fondo Financiero para el Desarrollo de la Cuenca de Plata, FONPLATA) forms part of IIRSA's technical coordination committee, which provides support to countries in all IIRSA-related topics. IIRSA has developed physical infrastructure requirements for eight integration hubs in the region, and identified 335 related projects with an estimated value of US\$37.5 billion.²² From this portfolio, governments have selected 31 additional priority projects worth US\$5.9 billion for implementation over the next five years.²³ Under the IIRSA initiative, the IDB has so far financed seven strategic infrastructure projects for a combined value of US\$515 million. In 2005, moreover, the IDB created a US\$20 million Fund for the Financing of Technical Cooperation Operations for Regional Infrastructure Integration Initiatives under IIRSA.

- b. The **Puebla-Panama Plan (PPP)**, launched in 2001, seeks to improve the trade, growth, and economic development potential of southern-Mexico and Central America. The PPP focuses on a number of areas including trade facilitation, infrastructure development (roads, energy, telecommunications), and tourism services. The core PPP structure is comprised of the IDB, the Central American Bank for Economic Integration (CABEI), and ECLAC, as well as the national governments. IDB acts as financial coordinator of the program and is also a member of its technical committee. Envisioned as a multi-billion, multi-year program with stated goals until 2020, the PPP is financed by contributions from participating countries, the private sector, and bilateral and multilateral donors, including the IDB.²⁴
- c. The Bank approved a new US\$20 million **Infrastructure Project Preparation Fund (InfraFund)** in early 2006. The fund, which is not exclusive to either IIRSA or the PPP, supports the preparation of

²² To date 29 projects with an estimated value of US\$3.8 billions have been approved or are under financial planning by IDB-CAF-FONPLATA

²³ One example of an initiative directly related to trade is the four-country project to pave the Carmelo Peralta–Loma Plata route and build the Carmelo Peralta–Porto Murtinho bridge, which will interconnect productive areas in Chile, Bolivia, Brazil and Paraguay and ensure access for isolated, landlocked regions to Pacific ports.

²⁴ Two recent IDB operations are a US\$50 million loan to Honduras and two loans for a total of US\$80 million to Nicaragua in 2004 to support PPP-related road projects.

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pre-investment studies (e.g., financial and environmental assessment) for infrastructure projects.

- d. The Bank has also supported improved provision of infrastructure services for trade with technical cooperation grants in areas such as port security, institutional strengthening of port authorities, and strengthening of border crossing logistics.

The Bank's **Business Climate Initiative (BCI)**, launched in 2003, aims to identify and then reduce or eliminate critical barriers to growth, promoting the expansion of private sector activities through legal and regulatory changes in the institutions and policies that affect the investment climate. The BCI seeks to identify areas where there is consensus among public officials and private business leaders that significant barriers to private sector-led growth exist, and to define priority actions to address those barriers. The initiative has three phases: (i) signature of an aide memoire between the IDB and the government reaffirming the importance of a sound environment for private sector development, and defining the scope of action for identifying the appropriate reform agenda and support program; (ii) diagnostic assessment based on consultations with a broad range of stakeholders to identify issues that should be addressed as a matter of priority to maximize the impact of any policy action on the country's business climate; and (iii) business climate reform financing. Once identified in the country strategies, the specific action plans are then supported through the IDB's operational programs.

Not exclusively linked to trade, but important for its potential to facilitate larger-scale regional interventions is the Bank's new **Regional Public Goods Initiative**, launched in 2004. This initiative aims to support the development of goods, services, rules systems or policy regimes that generate shared benefits for the participating countries as a result of cooperation and collective action by those countries. The Bank provides non-reimbursable resources of up to US\$10 million a year to finance demand-driven projects that develop regional public goods in LAC. Based on a competitive selection process, the IDB approved US\$8.9 million in grants in 2005 and has a 2006 pipeline of 11 projects for 23 borrowing member countries in areas such as environmental protection, education, modernization of the state, financial markets, information and communication technologies, agriculture, health and social development. The Bank has already approved several trade-related projects under this initiative, and there is good potential for developing more such projects in the future.

Importantly, moreover, this instrument could be used to provide seed money and as an incentive for countries to cooperate around larger regional projects that also require lending for the implementation of national components.

D. Addressing Future Challenges in Trade-related Assistance

A Regional Development Bank Positioned to Deliver Aid For Trade. As the above demonstrates, the Bank's institutional structure and support for trade-related assistance have evolved over time to meet growing demand in LAC countries, for which global trade integration is emerging as a priority. Historically a supplier of technical and financial assistance to what are perceived today as the broader components of the aid-for-trade agenda, the Bank more recently also established a solid track record in the delivery of assistance for trade-related capacity building. The combination of a critical mass of technical expertise in trade-related issues, operational know-how to deliver development assistance, and a presence in each country of the region, along with a wide representation of donors in its shareholding structure, put the Bank in a good position to contribute to the delivery of trade-related assistance to LAC.

A "New Lending Framework" to Improve Development Effectiveness. In 2005, the IDB adopted a New Lending Framework (NLF) to support the region's need for more effective spending and higher returns on investment within the context of narrowing fiscal space. The NLF favors a programmatic (rather than individual project) approach to lending, more flexibility in terms of lending criteria, increased reliance on national fiduciary and evaluation systems, and greater focus on results. The NLF includes the use of sector-wide approaches (SWAPs), new lending instruments such as programmatic policy-based loans (PBLs) and performance-driven loans (PDLs), and a wide range of other measures to make lending more flexible and execution of projects more efficient.²⁵ In 2006, moreover, the Bank relaxed its conditions for lending to the private sector. Several elements of the NLF may prove to be critical for delivering trade-related assistance more effectively.

²⁵ A *sector-wide approach* can be supported by any type of investment loan. In a SWAP, all development partners involved in a sector collaborate to support a single government-led sector policy and expenditure program, and relying increasingly on government procedures to disburse and account for all funds. A *programmatic policy-based loan* comprises a series of individual operations set within a medium-term framework of reform, approved on a phased basis to support a country's reform program, and with specific triggers for moving from one operation to the next. A *performance-driven loan* is an investment loan that disburses once the program's actual developmental results or outcomes are achieved, and the Bank has verified the expenditures incurred by the borrower to reach the outcomes.

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A Dynamic Institution Aligned with Client Needs. Along with upgrading its operational instruments and procedures, the Bank is currently engaged in a process of institutional realignment to increase its effectiveness in the delivery of development finance. With Bank operations now covering the whole range of trade-related assistance, and using many different instruments to deliver such assistance, the challenge is to ensure that all interventions are closely linked with and complement each other, and that the region's trade concerns are effectively addressed in all areas of Bank intervention, and through all available instruments. The Bank's proven capacity to adapt to changing demands in its borrowing member countries, its New Lending Framework, and its long-established presence in the region provide good tools for addressing this challenge. So do the lessons learned from its past experience in providing trade-related assistance.

IV. LESSONS LEARNED AND GAPS IN THE DELIVERY OF AID FOR TRADE

A. Recognizing the Context and Defining the Scope of Assistance

The ultimate objective of aid for trade is broad-based economic growth and development. Achieving this outcome requires, first, recognizing the context in which such aid is being delivered, particularly if it involves further trade liberalization as envisaged by the Doha Development Agenda. While trade has assumed a much more prominent place in the public debate and on the policy agenda of LAC governments, trade is not yet sufficiently mainstreamed into national development agendas. Past experience has moreover shown that to sustain support for trade liberalization, adequate attention must be paid to supply-side capacity and adjustment issues in conjunction with future liberalization efforts. Finally, most LAC countries are highly indebted and face serious fiscal constraints. All this has implications for what kind of trade-related assistance LAC countries now need, and how it should be delivered.

Demand for traditional trade-related capacity building continues to be acute in many LAC countries, but there is also a growing need for trade-related assistance to address the broader aid-for-trade agenda. In particular, such assistance should increasingly help countries eliminate supply-side constraints that inhibit them from realizing the opportunities of trade liberalization and that weaken their capacity to respond efficiently to trade-related adjustment shocks.²⁶ The IDB has provided such assistance for decades both at the national and regional level, but is now making efforts to link it more effectively with the countries' trade agendas. At the same time, trade-related assistance must seek to address the distributional effects of liberalization and the problems of asymmetry, which, if left unsolved, can intensify as a result of liberalization. Aid for trade could make an important contribution towards changing attitudes about trade liberalization and mitigating the risk of a backlash against further trade reform in LAC.

²⁶ Overcoming supply-side constraints requires both physical investments and regulatory reform. In the area of infrastructure, for example, it is important not only to focus on building roads, ports or communications systems, but also on related policy and regulatory improvements. For trade-related infrastructure, it is moreover important to address questions of policy consistency across countries, and to prioritize cross-border linkages.

B. Delivering Aid for Trade: Experiences and Lessons Learned

Technical Analysis and Diagnostic Work. The best way to identify a country's trade-related needs is through comprehensive and broad-based technical analysis. The preparation of diagnostic trade and integration studies presents several challenges. First, developing countries often lack the capacity for doing their own diagnostic work, and their action plans tend to be somewhat narrow, focusing on short-term capacity building rather than considering trade challenges within a broader, long-term development perspective. Lack of sufficient data and adequate methodologies for preparation of trade and integration studies often contribute to this outcome. Second, and as a consequence of the above, trade and integration studies are often supply-driven, prepared by IFIs or other development agencies. Here, however, is another challenge in that staff, time and budget constraints in these agencies may prevent them from conducting the kind of in-depth analysis that is needed to prepare a comprehensive diagnostic study. Effective coordination in the preparation of analytical work, both at the country level (inter-agency) and within the development agency (inter-departmental) is crucial to ensure that trade strategies encompass all relevant sectors and aspects of the economy. This, too, may present a challenge. The way forward is to support the preparation of diagnostic studies that are demand-driven, have local ownership, and are effectively integrated into national development plans.

Policy Dialogue and Programming. Analytical work feeds into policy dialogue with governments and other relevant stakeholders. Here, the challenge is to move beyond traditional constituencies in the trade community to target decision-makers in the country more broadly. It is important to expand dialogue on trade issues with finance and planning ministries, who have crucial responsibilities in deciding future macroeconomic and development policy and prioritize funding requests for external assistance. Ideally, policy dialogue should encompass all relevant ministries (e.g., finance, planning, trade, agriculture) as well as the legislative branch of government (Congress, Parliament), the private sector and other important civil society groups, including labor. Without such dialogue, trade strategies run the risk of being unbalanced and unsustainable (because of insufficient political support and lack of "ownership").

Broad-based dialogue is also necessary to mainstream trade into national development agendas. Trade ministries are often aware of the significant

challenges that lie ahead, but finance or planning ministries may be less attuned to the specifics of those challenges given their much broader policy mandates. As a result, they may undervalue the importance of trade for economic development, and of well-functioning institutions for trade development. Continued efforts to integrate trade into country dialogue and programming are urgently needed.

Identification and design of operations. For IFIs and other development agencies, one important challenge in the design of operations is to ensure efficient coordination between staff engaged in strategy and policy formulation on trade for a specific beneficiary country or region, and the operational staff that will design and help implement programs in the field. In other words, it is important to establish a close working relationship or link between “trade practitioners” and “aid practitioners” in the identification, design and development of trade-related assistance. The Bank has made efforts in recent years to strengthen this link, aiming to ensure that policy research feeds seamlessly into operational support.

Implementation. One challenge related to the implementation of trade-related operations is the limited absorptive capacity of local executing or “beneficiary” agencies in LAC, some of which execute multiple donor projects at the same time. Donor coordination can go some way towards easing the pressure on these agencies, but capacity problems will remain a serious issue for the foreseeable future, particularly in the region’s smaller and/or poorer countries. Trade ministries and other relevant agencies in these countries are often inadequately staffed and too weak to implement operations without outside technical and administrative assistance.

To help countries execute projects, development agencies often establish specific project implementation units in such agencies, staffed by consultants. The availability of a broad pool of international experts who can assist in implementation is crucial to achieving beneficial outcomes. However, it has sometimes been difficult to attract such expertise, particularly for longer-term assignments in the region; language has also been an issue. The problem of limited implementation capacity could become even more pronounced with the planned increase in aid for trade. There is thus urgent need to build local expertise in all areas of trade as a first step in expanding such aid. This is also crucial to ensure the consolidation and sustainability of aid-for-trade development outcomes over the long term.

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In terms of the Bank's own processes, it is worth noting that IDB operations, similar to those of other IFIs, are developed by staff in headquarters and, once approved, are administered by field-based staff. In the IDB, trade specialists from headquarters provide regular advice on the technical aspects of implementation, but field office staff is in day-to-day contact with local executing agencies. The presence of field offices in each of the IDB's borrowing member countries provides a good opportunity for the Bank to participate in the delivery of expanded aid-for-trade flows. Their responsibility in the administration of such flows also highlights the importance of further developing technical expertise on trade in these offices, and of ensuring effective coordination between headquarters and field offices.

Instruments for delivering aid for trade. As mentioned earlier, most LAC countries are highly indebted and face serious fiscal constraints. This places limits on how much they can borrow to facilitate trade integration and adjustment.²⁷ In such a context, the limited availability of grant funding for trade-related assistance to middle-income countries is a serious challenge. In the IDB, for example, 21 of the 26 borrowing member countries have no access to Bank grant funding beyond trust fund, MIF and regional FSO resources, which are scarce. The Bank's specialized trust funds for trade-related assistance have emerged as important instruments for channeling resources to countries engaged in trade reform; expanding their scope could help LAC countries overcome their binding financial constraints in addressing trade-related adjustment.

Grant funding is not only limited, but often also programmed on an annual basis. This makes it difficult to support programmatic, long-term approaches to trade-related assistance. The scarcity of grant funding also limits the scope of activities that can be undertaken. There has been a significant amount of support for short-term training in LAC countries, perhaps crowding out other important trade-related priorities. Coordination among donors has not always been optimal and short-term training also raises the question about the sustainability of its outcome. Grant funding is sometimes tied to specific nationality requirements for consultants, country eligibility criteria, and thematic priorities, limiting the flexibility of its use. Grant funding, of course,

²⁷ The Caribbean countries are a good example of this dilemma: they have relatively high per capita income levels, but their high debt ratios limit the amount of borrowing they can do. These countries, nevertheless, are highly vulnerable to further multilateral trade liberalization and are struggling with the consequences of preference erosion in their main export markets.

must also grapple with the question of ownership – some counterpart funding may be warranted to ensure that beneficiary countries have sufficient incentives to work towards optimal outcomes of such aid.

As regards specific lending instruments, one lesson learned is that a multi-sector approach to trade-related assistance is crucial. Hybrid programs covering multiple sectors and combining multiple lending instruments and executing agencies have all the requisites for addressing the complexity of the aid-for-trade agenda. They can, however, be difficult to design, implement, monitor and evaluate. Meanwhile, sector-wide interventions involving multiple donors could provide significant benefits to a country if implemented effectively (through SWAPs or similar mechanisms). They could also provide a vehicle through which to combine loans with technical assistance grants. The grant element could be used for purposes of strengthening local execution capacity, which, as noted above, has been a serious challenge in some LAC countries. SWAPs, meanwhile, present their own challenges in terms of donor coordination and attribution of development outcomes.

There is a clear gap in financing for large-scale regional interventions, particularly those involving the public sector. The Bank has a lot of experience working with LAC governments at the regional and sub-regional level, but its regional interventions are necessarily small owing to the scarcity of funding for such programs. The current level of grant funding that is available to LAC countries cannot cover the cost of large-scale regional infrastructure or public goods initiatives in the region, and lending instruments continue to focus almost exclusively on national interventions. It may be worthwhile for development banks to explore the possibility of combining national loans with a regional grant component that provides incentives for countries to approach problems from a regional perspective. To a certain extent, the Bank's IIRSA experience suggests that regional infrastructure projects can be financed through separate national projects, but perhaps the provision of grant funding could facilitate greater use of such regional approaches. The Bank's Regional Public Goods Initiative, by providing seed money for the development of new regional public goods, presents one possibility to foster greater use of regional approaches in the delivery of aid for trade. At the national level, a combination of grant and loan financing could be used to lower the effective cost of borrowing for countries.

Finally, in terms of instruments, the Bank's experience also points to the need for a flexible "rapid response" facility to address short-term, urgent requests from governments. When countries are already negotiating, and need urgent technical assistance within a week or two there is little time to develop even a small grant-financed project. Flexible funds would also allow timely identification and execution of pilot projects that could subsequently be scaled up and replicated in other countries or regions. To date, the Bank has sought to address urgent, very time-sensitive requests through deployment of its own staff and administrative budget resources.

Monitoring and Evaluation. There is much need to strengthen this aspect of aid for trade delivery. In the current context of serious fiscal constraints, many LAC countries are reluctant to borrow for projects that do not have an immediate or easily measurable development outcome. However, measuring outcome is very difficult in trade-related assistance, particularly assistance related to institutional strengthening and capacity building. This partly owes to the difficulty of establishing baseline indicators for measuring progress in trade-related assistance that is not related to physical infrastructure or investment. It also owes to the difficulty of establishing attribution in countries where many donors are involved in trade-related assistance.

One area where donor coordination could be very effective would be in the development of well-designed results-based frameworks for trade-related assistance. A "Results Framework" comprises goals, objectives, baseline indicators, target indicators, and an assessment of identified risks and mitigation efforts. Common frameworks, agreed and used across IFIs and donor agencies for the various types of trade-related assistance (ranging from training and institutional reform in trade ministries, to improved customs procedures, export promotion, infrastructure development, business development and adjustment efforts) would strengthen monitoring and evaluation capacities in individual institutions, and would also make it easier to monitor trade-related assistance at the regional and global level.

Role of the Private Sector. The private sector should play an active role in identifying countries' trade-related needs and in implementing adequate responses. The Bank has been active in this area with its MIF project cluster and Trade Finance Facilitation Program. In 2006, moreover, the Bank relaxed its conditions for lending to the private sector. Previously, such lending was limited to infrastructure, capital markets and trade finance. The Bank can now

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lend to private companies in any sector, and can also support public-private partnerships, where public sector involvement can be at both the national and sub-national level. This expanded mandate could substantially strengthen the Bank's role in supporting aid for trade, particularly as it relates to infrastructure and supply-side capacity.

In an effort to expand and better coordinate its support to private sector development in LAC, the Bank has recently launched the preparation of private sector development strategies for all its countries. These strategies, which feed into the Bank's country programming, guide the activities of the Bank's public and private sector lending departments and seek to provide a more coordinated approach to the Bank's support to the private sector. One challenge in the area of trade is that private sector agents in many LAC countries lack awareness of the benefits and consequences of trade liberalization. Particularly in the smaller countries of the region, they are often inadequately informed about public sector initiatives in the area of trade, and have little influence on the development of national trade policy. Outreach activities and awareness building for the private sector are therefore important activities that should be covered in trade-related assistance. It would naturally lead to improved capacity for preparing private sector needs assessments in the area of trade.

Donor coordination. Donor coordination in the delivery of aid for trade must be strengthened to avoid duplication of efforts, streamline reporting requirements for executing agencies and facilitate greater use of SWAPs. The IDB has taken a number of steps to coordinate its trade-related assistance, not least in conjunction with the FTAA Hemispheric Cooperation Program and the donor meetings organized during the bilateral trade negotiations between the United States and Central American and Andean countries. In delivering aid for trade, donors should adhere to the principles outlined in the 2005 Paris Declaration on Aid Effectiveness - ownership, harmonization, alignment, managing for results and mutual accountability. These principles are particularly relevant in view of the trade challenges outlined above and the planned expansion of aid for trade in the future.

V. LOOKING AHEAD: LAC, AID FOR TRADE AND THE IDB

One of the most important lessons learned by the IDB in its efforts to supply trade-related assistance to its borrowing member countries is that there is overwhelming need for such assistance in LAC. Despite being mostly middle-income, LAC countries face serious resource constraints that have created significant gaps in their capacity to respond to trade-related challenges and to exploit the opportunities of more open markets. Aid for trade, appropriately tailored to their more advanced levels of economic development (relative to other developing regions) could make an important contribution towards closing those gaps.

In the past decade, the IDB has made significant efforts to align its institutional structure, technical expertise and financial and non-financial instruments with client needs in the area of trade. It has established a solid reputation for the delivery of trade-related assistance to LAC countries and can draw on valuable lessons learned in designing its future interventions in this area. Along with new instruments for trade-related assistance, the Bank has also added greater flexibility to its overall lending process, making it easier and faster for countries to access its resources. Perhaps most importantly, working with trade-related assistance has given the Bank a keen sense of where the current bottlenecks to the provision of such assistance lie, and what gaps need to be filled to make aid for trade a truly effective instrument for helping developing countries participate more effectively in the multilateral trading system and, ultimately, to achieve stronger and more sustained economic growth.

This experience makes the Bank a natural partner for LAC - and for the wider global trade community - in the design and implementation of an expanded aid-for-trade package under the Doha Development Agenda. In developing its own expertise in trade-related assistance, the Bank has grappled with many of the issues that now confront the WTO Task Force on Aid for Trade: identifying the gaps, finding effective means of delivery, involving the private sector and strengthening monitoring and evaluation mechanisms, to name just a few.

As the previous section on lessons learned showed, there is clearly a need to develop better analytical tools and diagnostic capacities, more effective dialogue and programming, more appropriate operational instruments and stronger

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monitoring and evaluation mechanisms for trade-related assistance. But in terms of institutions for managing additional aid, the existing global and regional architecture appears to be adequate, at least on the supply side. Regional development banks, in particular, should play a prominent role in the future delivery of aid for trade. They offer a number of advantages in this respect, regional experience and proximity to clients being among the most important ones, not least because trade is often a politically sensitive issue. On the demand side, greater efforts should go into strengthening the absorptive capacity and sustainability of institutions that implement trade-related assistance. In fact, this aspect of managing aid for trade may be the most important issue for ensuring effective delivery of aid, and it deserves greater attention in the current debate on aid for trade. The role of the WTO Task Force on Aid for Trade is therefore crucial in ensuring a balanced debate between the supply and demand sides of aid for trade on how best to operationalize this important initiative in order to contribute to the development dimension of the Doha Development Agenda.