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What Future for the WTO?

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Introduction

At the World Trade Organization in Geneva, summer 2007 is likely to be a reprise of summer 2006. WTO officials will point to the body's August adjournment as a deadline for agreeing the basic terms of a new trade deal. Failure to agree, they are likely to proclaim, risks a collapse of the Doha Round and irreparable harm to the WTO itself. The world financial press and other pundits will berate negotiators for letting slip through their fingers a deal that has the potential to alleviate world poverty on a grand scale. Many will blame the developing countries for intransigence and claim that they are hurting themselves and other poor countries more than wealthy countries. Without a deal, some will pontificate, countries will turn to bilateral free trade agreements and the WTO will become irrelevant.

Despite the number of times the scene is replayed and the lines are repeated, none of these claims are true. This article examines each of these propositions and finds the reality to be quite different:

- A new global trade bargain is unlikely to be completed this year. Crafting a new trade regime that reflects the emerging redistribution of global economic power will probably require several more years of negotiation.

- Failure to agree this summer, or this year, will neither slow world trade nor harm the WTO.

- There is no deal at hand: the agreements that have been reached to date are all at the conceptual level. Actual proposals are still very far apart; some contradict the agreements that have been reached in principle.

- Empirical studies show that several of the Doha proposals currently under consideration would have very differentiated impacts on developing countries and ambiguous impacts on poverty. Some poor countries would be net losers.

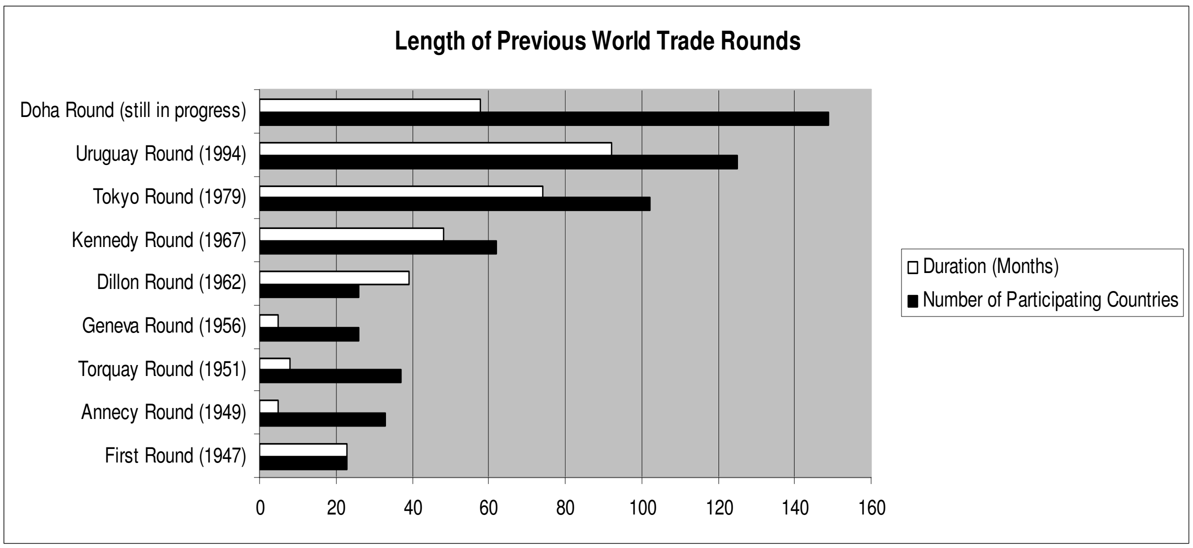
- Developing countries are resisting proposals that would channel most benefits to developed trading powers and do little to increase the benefits of global trade to less developed countries.

- Bilateral free trade negotiations, while problematic in themselves, do not pose a threat to the existence and relevance of the WTO.

A "Development Round"

When the current round of negotiations was launched in Doha, Qatar in 2001, it was officially named the "Doha Development Agenda," indicating the priority placed on helping developing countries gain more from trade liberalization. This priority was in part an outgrowth of the global solidarity that emerged in the wake of the September 11, 2001 attacks on the United States. The "Development Agenda" also reflected the reality that developing countries now constitute the majority of World Trade Organization members and can determine whether new trade rules are adopted or not. Large developing countries, notably India and Brazil, are among the chief *demandeurs* in the talks, insisting that any deal must address their development concerns.

This new distribution of power and interests within the WTO makes it harder to reach a deal. The previous round of negotiations, called the Uruguay Round, took seven and a half years to conclude. The current round has been underway for only about five and a half years. As the figure below shows, global trade rounds have taken longer to complete as more countries join the negotiations. Most of the new members are low and middle-income countries at very different stages of economic development. They have highly differentiated export interests as well as defensive concerns for their own firms, workers and farmers. It was never likely that a round with more players, and more diverse players, would take *less* time than previous rounds. If the pattern seen below is any indication, this round could take eight to ten years, concluding in 2009 or later.



Neither the WTO nor World Trade Are at Risk

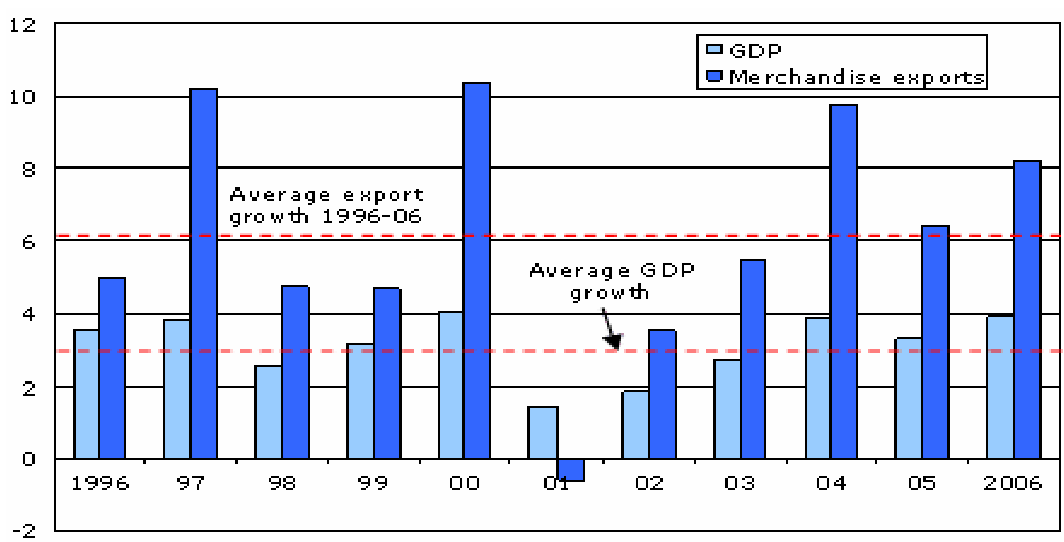
Notwithstanding failure to agree to new trade rules this year, the WTO will continue to function under the rules negotiated in previous rounds, which continue to bind all 150 member countries. Existing WTO agreements will still set the rules for trade between the major players, including the United States, the EU, Japan and major emerging powers such as China. There is little prospect that these countries will negotiate separate free trade agreements among themselves, partly for the same reasons that make a Doha deal difficult. The WTO will continue to attract new members, as seen in the recent accession of Vietnam and hard work by Russia to join the organization.

The WTO dispute settlement mechanism will continue to function and will be used to resolve disagreements that arise under existing rules. It is not at risk because it provides a real benefit to all member states in solving their trade disputes. Rather than being forced to use political and diplomatic capital to resolve disagreements through direct negotiations, countries can rely on panels of specialists to determine whether commitments have been honored or breached by their trading partners. The dispute settlement mechanism will need to be improved over the years to address shortcomings, such as a lack of transparency. Nonetheless, it is a reasonably well-functioning institution that provides impartial adjudication between countries of differing power and influence.

Many of the commitments undertaken in the Uruguay Round of negotiations have only recently been implemented, including the phase-out in 2005 of the global quota system that had governed apparel and textile trade. China has just finished implementing deep changes to its tariffs and other policies that it agreed to enact over five years as a condition of accession to the WTO in 2001. These changes mean that broad swaths of the world economy are still adjusting to new trade rules and relative price changes arising from earlier agreements.

There is ample room for world trade to continue to grow under the existing rules, as demonstrated by the impressive expansion of trade since the conclusion of the last round, seen in the figure below.

Growth in the volume of world merchandise trade and GDP, 1996-2006
(Annual percentage change)



Source: WTO, *WORLD TRADE 2006, PROSPECTS FOR 2007*, Chart 2

Businesses feel that they have the market access they need for the foreseeable future, as evidenced by the lack of engagement by the private sector in this round. Powerful corporate interests have never been shy about pressing their governments for new trade deals when they felt constrained by existing rules.

The only risk to the WTO—and it is minor—is from a self-inflicted loss of confidence caused by repeatedly setting premature and unachievable deadlines for reaching a new trade deal, thus producing one artificial "failure" after another. The guardians and supporters of the WTO should dampen, not fan, anxiety about the organization.

Wide Gaps on All Major Issues

Some officials and commentators characterize the Doha Round as close to agreement, with only small variances separating the parties' positions. This is far from the truth. Profound differences exist in all of the sectoral negotiations.

In the agriculture talks, there are stubborn and ongoing disagreements between the US and the EU on the level of US subsidies and depth of European market opening. Wider still are the disagreements with the developing world. By way of illustration, Brazil, on behalf of the G20 group of developing countries, insists that the US cap it trade-distorting domestic support at US$12 billion annually. The US has signaled that it could move from its current proposal of a $22.6 billion cap to a range of $17-$19 billion—still far from satisfying G20 demands. India, on behalf of the G33 group of developing countries with large agricultural sectors dominated by small-scale farming, insists that they must be allowed to shield up to 20% of agricultural tariff lines as "special products" that are important to the livelihoods of poor farmers, the food security of the nation, or rural development plans. The EU has hinted it might grant exceptions for 8% of tariff lines, while the US insists that less than 1% be designated as "special products". With 58% of its workforce in agriculture, India states categorically that it will not negotiate away the livelihoods of a majority of its population. It is staunchly backed by heavyweights such as Indonesia in the G33.

Turning to manufacturing talks, there is little cause for short-term optimism. Here the US and EU have joined forces to propose that developed countries agree to a maximum tariff of 10% on manufactured goods, while developing countries' maximum tariff would be 15%. The latter point out that in practice this would require much deeper cuts in their tariffs than in those of already industrialized countries. This would contradict an agreement reached earlier in the round that developing countries will be allowed to make smaller tariff reductions than richer countries. United in resistance are Brazil, India, China, South Africa and Argentina, among others.

Deep differences also plague the services negotiations. For example, proposals to increase visas for temporary workers, an important goal of developing countries, are contested in many developed countries where charged debates on immigration are underway. These and other major differences have proven intractable to date.

Distribution of the Gains from Doha

Recent empirical studies that model the impact of Doha proposals show that the greatest gains are likely to flow to high-income countries, with middle-income developing countries experiencing very differentiated impacts. Among that group, China is generally projected to gain the most. The models show the poorest countries receiving the smallest gains, with some emerging as net losers from the Round. A summary of the studies prepared by the European Commission notes that most models show the largest gains arising from manufacturing and/or services liberalization, with World Bank modelers alone in claiming that agriculture would be the most important source of gains.

Each of the studies differs somewhat in its definition of the likely outcome of the Doha Round. However none of the simulations supports the claim that the Round is on track to significantly alleviate poverty in the developing world. That claim, although still repeated today, is based on older and questionable models that used out-of-date data and failed to take account of existing preference programs that provide benefits to developing countries, the implementation of the Uruguay Round, the end of the apparel quota system, and the accession of China to the WTO.

Bilateral Free Trade Agreements: A Serious Threat to the WTO?

Some argue that failure of the Doha Round will unleash a frenzy of bilateral and regional trade deals. These deals would exclude some countries, and if negotiated between unequal partners, might be even worse for the weaker countries than the deal on offer at the WTO. That much is true, and indeed a few headlining-grabbing negotiations have been launched, such as those between the EU and India. However, it is not at all clear that negotiations for bilateral deals have accelerated. Over 200 bilateral deals had been reported to the WTO by last year, and numerous other negotiations have been underway for several years. The newly announced negotiations barely expand the number in play.

In Europe, an ambitious negotiating agenda has been underway for several years to replace current preferential trade arrangements that benefit countries in Africa, the Caribbean, and the Pacific with free trade agreements by the end of 2008. These talks have run into substantial obstacles because of development concerns on the part of the ACP countries, similar to the issues that bedevil the global talks. Europe has announced new negotiations with ASEAN and Korea, in addition to India. There is little reason to think that these big agreements will be easy to achieve, again due to the same disagreements and differences of interest that make the Doha Round so complex.

In Asia, regional and bilateral trade pacts proliferated over the last ten years, even before the Doha Round was launched. The trade talks in Asia are meant either to facilitate integrated production in the region or to consolidate the economic interests of major Asian powers. Those countries depend on outside markets, particularly the rich markets of the United States and Europe, to take their exports, so they have no incentive to turn away from the WTO, regardless of how many regional pacts they conclude.

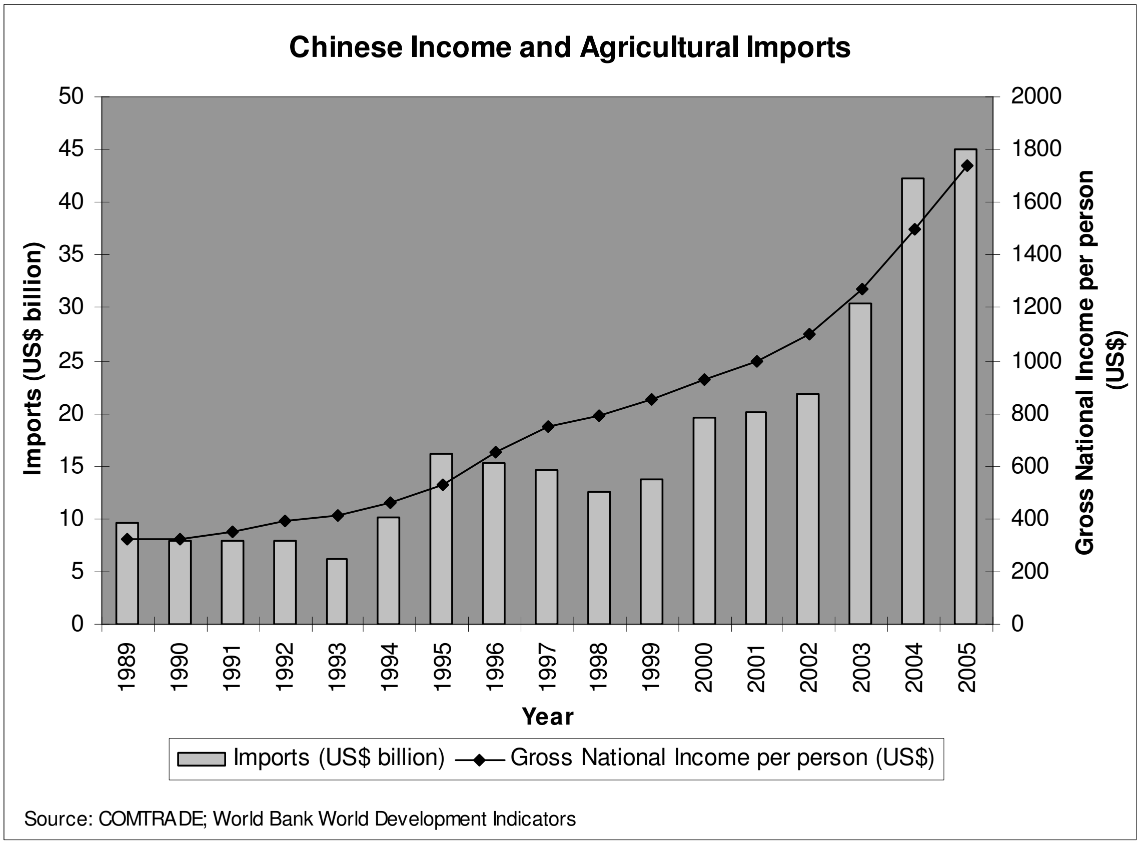
The U.S. has concluded several bilateral trade deals in the last five years, but each has produced a contentious debate and close vote in the US Congress. It is not clear whether the Congress will renew trade negotiating authority for the Bush Administration. If not, it will be impossible for the U.S. to conclude new bilateral free trade agreements.

The Way Forward for the WTO

The world economy and world trading system have changed tremendously since the Uruguay Round concluded in 1994. New powers are rising and they plan to exercise their might and press their vital domestic concerns. The poorest countries, which lost ground under the last trade round, insist that they must do better this time. In the wealthy world deep unease has emerged over the impact of trade policy on employment. These positions have profound roots and must be acknowledged and addressed in the negotiations.

The common concern, cutting across all countries, is the question of employment and livelihoods. Opening an economy more deeply to trade will cause some sectors to expand and create jobs, while others contract and destroy jobs. Economic theory says that in an economy at full employment, the composition of jobs will change but there will be no long term unemployment. However most economies, particularly those in the developing world, are not at full employment. The end of the Cold War has also changed the system, as two formerly separate production and trading systems have now merged into one, adding two billion workers to the western production system. Under these circumstances, most countries are going through a period of adjustment.

The preoccupation of WTO members with trade's effect on jobs is based in reality and is completely legitimate. The daunting task at the center of the Doha Round is to find a trade deal that captures the positive potential of global trade to accelerate economic growth and job creation, while recognizing and allowing sufficient time and flexibility to deal with the reality of extensive job destruction. As a concrete example, it is counterproductive for US and other competitive agricultural exporters to insist on prizing open farm markets in developing countries on a scale and pace that could lower the incomes of poor farmers there by displacing their production and causing price drops for the commodities they produce. Only as large numbers of low-income households grow their way out of poverty will the world's agricultural exporters see sustained increases in sales to developing countries. The figure below shows the example of China, where agricultural imports have closely tracked the rise in per capita income.



A similar pattern prevails in India, although income levels there are still substantially lower than in China. Indian per capita income is still below the level (about $800 per year, at international exchange rates) at which Chinese agricultural imports started to climb sharply. Countries with most households at very low income levels simply cannot afford to buy all of the food and other products they need. As developing countries manage to achieve higher levels of growth, their imports will follow a similar pattern. Trade rules can facilitate this process or reverse it, as current aggressive market access proposals threaten to do.

The employment consequences of trade agreements should be simulated in advance and treated as valid negotiating concerns and objectives. Computable general equilibrium models are now available that can provide reliable approximations of the impact of trade policy changes. The sequencing and pace of liberalization should take into account the adjustments that will be imposed on members' economies and labor markets. Any new agreement should allow extended implementation periods and real flexibility for developing countries, with the degree of flexibility related to income levels and the extent of diversification and vulnerability in the economy. The goal should be to allow countries to foster greater job creation than job destruction, taking into account their very different capacities for adjustment.

The Doha Round can lead to a new set of trade rules that more accurately reflects the new global distribution of economic power and interests. It can and should realign rules to tilt less in favor of wealthy countries and instead offer opportunities to countries at all levels of development. It should recognize and accommodate the economic anxiety that has arisen in response to the relocation of production across the world since the end of the Cold War. Finding an appropriate mix of policies to accomplish these objectives will take time, effort and good faith but in the end will produce a more robust and resilient global trading system based on reasonable rules that all countries can embrace. Artificial deadlines and self-created crises contribute nothing to this enterprise and should be abandoned by those who truly believe in the potential of trade.