



TRADE AND  
DEVELOPMENT SYMPOSIUM  
Perspectives on the Multilateral Trading System

A Collection of Short Essays

**Competing with Regionalism  
by Revitalizing the WTO**

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The global trading system currently presents some strikingly contrasting pictures. Judged by the state of the Doha Round, the system seems to be in serious trouble. Despite the repeated lip-service paid by the G20 leaders instructing their negotiators to achieve “a balanced and ambitious agreement” the Round is clearly at an impasse. It has missed every deadline that has been set, and the prospects for resolution are bleak.

Yet, in many other respects the system is vibrant and thriving: the dispute system at the WTO is working well. With only a few exceptions countries have shown great forbearance by not raising trade barriers in the face of the global financial crisis -- in the case of most developed countries, this has meant maintaining applied tariff rates at levels far lower than required by WTO rules. In addition, new bilateral preferential agreements are being concluded with great vigor.

Clearly there are strong forces driving countries towards increased global integration. Reductions in transportation and communications costs have allowed firms to operate global supply chains that take advantage of differences in national comparative advantage both through intra-firm trade and through networks that link teams of producers. Increasingly, countries specialize in tasks rather than products, and this puts a premium on establishing governance mechanisms that reduce the transactions costs and risks that such operations entail. The firms that engage in this trade are concerned about far more tariffs. They seek rules and administrative and logistic facilities that enhance these operations.

A cumulative process has been set in motion as countries compete to become export platforms. As some offer foreign and domestic investors favorable domestic production environments combined with preferential access to foreign markets, others feel pressures to do the same. This has led to agreements in which countries agree to rules (e.g. for investment, competition policies, intellectual property protection) and market opening (in goods and services) that go considerably further than they have undertaken at the WTO.

A second key driver of these agreements has been the shift in global growth away from the developed countries towards the emerging markets. South-South trade has flourished and in response, developing countries have been signing agreements between themselves to regularize and promote their interactions. These South-South agreements have varied in depth and scope, with some that are quite comprehensive and detailed and likely to stimulate trade while others that are hortatory and vague and more symbolic and diplomatic in character.

If the Doha Round ends in failure, the contrasting states of the multilateral and regional parts of the system could become even greater, with regional initiatives flourishing while the multilateral system becomes an increasingly less relevant. To be sure the existing agreements will remain binding on all members, but there are dangers that there could be backsliding: One reason countries comply with existing agreements, is their interest in negotiating new agreements. Absent such prospects, their compliance incentives could be reduced. Moreover, thus far there are as yet no deep preferential arrangements between the largest trading nations the US, EU, China India and Brazil and since the WTO is the principle forum for their interaction, its weakening could damage their relationships with detrimental consequences for the system.

### Regionalism is here to stay

Some would like to see regional agreements eliminated. But this will not happen. Countries have already proceeded too far with their commitments. Moreover, they should not be eliminated. Some functions are in principle, better carried out at a sub-global level. Viewed simply as tariff reducing exercises, preferential arrangements are said to be “second best” because they can divert trade. But partial multilateral trade liberalization, the realistic alternative to preferential arrangements, is also “second best” in the same way. So the real choice is between two second-best approaches and it is an empirical matter as to which is superior. Indeed both can promote trade.

But only considering tariffs is too limited. Many of the regional agreements cover far more than tariffs, and they also implement rules and regulatory frameworks that not all countries are willing to sign. The optimal area for trade might be the world, but global federal government is not widely seen as the optimal area for governance. Thus viewed as joint governance arrangements, a mixture of multilateral and regional arrangements may actually be first best. Plurilateral and bilateral arrangements can thus be valuable in their own right and not only because they may be a stepping stone towards a more comprehensive system.

### Revitalizing the WTO

However, the drift towards a world in which all deeper integration takes place through regional arrangements while the WTO maintains a single undertaking that enforces the lowest common denominator needs to be resisted. Instead, we need a global trading order in which multilateral

and preferential arrangements operate in a complementary fashion. This requires a two-pronged approach that on the one hand, revitalizes the WTO and on the other improves the disciplines on preferential arrangements in order to reduce their discriminatory aspects.

The multilateral dimension involves successfully concluding the Doha Round and then launching a new series of plurilateral arrangements governed by a new protocol of understanding. The Doha Round has worthy objectives, but it also has serious problems. Its many delays have been costly because the world has changed. The prioritization of agriculture was questionable from the start and has become increasingly problematic. This is not an area in which most of firms who undertake trade and investment have interests -- the payoffs from reducing industrial tariffs, liberalizing services and investment are much larger. In 2001, global food prices were low and the major issues were import barriers and subsidies to production in developed countries. These problems remain, but in 2011, global food prices are high and volatile, and the key farm trade issue not covered by the talks is the export restraints imposed by many developing countries. In 2001, China was a newly acceding member that needed time to adjust and many developing countries in Africa and Latin America had experienced two decades of slow growth. But as of 2011, China is the world's largest exporting nation, and many developing countries have enjoyed a decade of unprecedented growth.

Framing the negotiations as the development round has been a mixed blessing, especially as developed countries have stagnated. The European Union's priorities to cover the Singapore Issues such as investment, competition policy and transparency in government procurement failed to achieve the necessary consensus at Cancun. The developed country priority in the Round, obtaining meaningful market-opening concessions from the large emerging economies has been hard to achieve since developing countries have acted as a block to limit their concessions. From the developed country vantage point, the bargain currently on the table looks small and uncertain, while regional arrangements seem to offer better prospects.

Increasingly there are calls for the members to terminate the negotiations by admitting failure or by harvesting the concessions that have already been made. Some argue, for example, for a "Doha lite", in which the concessions already agreed for the least developed countries are granted and the agreements on trade facilitation adopted. But others resist making even these concessions,

claiming they were made under the assumption that more would put more on the table.

However, failure would damage the system, and a final effort should be made. It should start with the largest members stepping forward and exercising the leadership needed to reach a meaningful agreement. One example: China could agree to join the Government Procurement Agreement for example, in return for developed countries granting it market economy status.

## New Approaches

Part of the final deal could involve a trade in which concessions to developing countries are made in return for them agreeing to a new protocol that would set the rules for negotiating new plurilateral agreements that would counter the attraction of deeper preferential arrangements.

WTO members are diverse and one size does not fit all. Some would prefer therefore to have WTO rules that deal mainly with the reductions in tariffs and subsidies and indeed to eliminate the TRIPs. But this could be costly in terms of opportunities foregone. There are strong reasons to believe that additional rules could aid in the integration required for fully exploiting the potential of the global economy. Ample evidence indicates that, even when tariffs are removed, border effects continue to impede the free flow of goods and services. Indeed, this evidence can be seen in more extensive agenda's that are covered by many regional trade arrangements.

The desire for deeper integration and the concerns for policy space for some developing countries should both be respected. Instead of a system in which all members, both developed and developing, are required to adhere to all rules, a more attractive approach would entail a variable geometry with mandatory core commitments supplemented by plurilateral agreements to which only some members belong. These agreements could take a variety of forms. They could involve new rules, the full liberalization of sectors, and agreements on trade facilitation. Some agreements could extend most-favored-nation treatment to all members, other agreements would grant privileges only to those who sign up. Some could become binding on members only when a critical mass sign up.

These agreements would end the simplistic distinctions between developed and developing countries and allow members from both groups to adopt rules that met their interests. Examples might include foreign investment, rules for state-owned enterprises, restrictions on export

barriers, restrictions on energy subsidies, competition (anti-trust) policies, regulatory practices, customs procedures, liberalization of key services sectors, and additional intellectual property protection.

The prospects of agreements in these areas would help attract participants that have lost interest in the current system while it would give all some say in developing the rules. Important benefits could result from conducting the negotiations under the WTO aegis: namely, the legitimacy conferred by the stamp of approval of the organization, access to WTO resources and dispute settlement facilities, the ability for other members in the future to join an arrangement with rules that they had previously endorsed, and the ability to group negotiations on several agreements at once to allow for cross-issue trades.

### Tougher Disciplines for FTAs

A second prong of the approach to regionalism would be to tighten the disciplines on Free Trade Agreements. The best solution to the trade diversion caused by regionalism is of course to go to full free trade. The problem is we might never get there if we create vested interests in the current arrangements. But the next best approach is to focus on the diversion and additional costs that are created by complex and restrictive rules of origin. The idea would not be to prevent members from signing free trade agreements but to reduce their discriminatory effects and enhance the ability to link them into more encompassing arrangements.

For the most part, it is not the WTO rules relating to preferential arrangements that are flawed but the failure to enforce them. The GATT Article 24 which deals with preferential trade agreements stipulates they should cover “substantially all trade” and not raise barriers on outsiders. But exactly what this means has never been clarified and it should be. A great service would be provided if one brave country was willing to step forward and bring a case that required that this be done.

In addition, however, there is one area in which the rules should be tightened. Conspicuous by their absence have been additional requirements on rules of origin in the case of Free Trade Agreements. This has led to protectionist

violations of WTO principles when rules such as “yarn forward” for apparel are used in FTAs. These rules prevent garments with any value-added from third parties from qualifying for duty-free access under the FTA. They are clearly discriminatory and present obstacles to cumulating value-added. Article 24 should be amended to allow only one rule of origin for all sectoral covered by any agreement, and members given five years to come into compliance.

### Conclusion

The WTO has a key role to play in helping nations reap the full benefits of deeper integration but as its mission and means have expanded it has become more controversial. The organization’s legitimacy has been attacked from many quarters and efforts to add new issues to the rules have foundered, as many members have refused to accept new obligations on a variety of grounds that include problems in implementation, fears of future trade retaliation, and apprehension that domestic policy space will be lost. However, the net result of this resistance has been to create an organization that is losing its relevance for the issues that are of direct concern to those actually involved in building supply chains that stretch across several countries. This requires dealing not simply with tariffs, but rules that relate to regulations, competition, investment, intellectual property and services.

Supplementing the core WTO obligations with plurilateral agreements could help to promote deeper global integration while at the same time alleviate the WTO’s institutional tensions. These arrangements offer a compromise in which diversity can co-exist with more extensive commitments among willing members and would help reduce the trends towards regionalism, not by preventing these arrangements but by creating a more attractive alternative. In addition though, disciplines on regional arrangements should be tightened.

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