



TRADE AND DEVELOPMENT SYMPOSIUM

Perspectives on the Multilateral Trading System

A Collection of Short Essays

The Future of the Multilateral Trading System and the WTO

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A recent study into the attitudes of the global trade community came to a conclusion which was striking: “it is much more divided than it was ten years ago, influenced by conflicting interests and with no leading group capable of bringing the Doha Round to a successful end, in fact a community fragmented into multiple different segments”.¹ The present paper attempts to address the questions posed by this analysis and to suggest some partial solutions.

This note starts by considering the changing pattern of world trade and the shifts in power among the major trading nations, and assessing what these trends imply for the multilateral trading system. To use more populist language, I am looking at the impact of global supply chains and the rise of the ‘emerging economies’, and what this may mean for the WTO as an institution.

The multilateral system in context

But before we address challenges and opportunities for the future of the system, we should review some of the elements of the existing system which are not generally much emphasised. I am assuming an audience that knows the basics: the **multilateral** system is - by convention - the rules put in place in the GATT in 1947 and now incorporated - with some additions - into the WTO.

For some, these rules are based on an **essential antithesis** between the multilateral approach and other avenues that lead to trade agreements or policy measures, whether bilateral or regional or unilateral. This might be characterised as a clear division between activity within the WTO framework and in Geneva and other activities elsewhere around the world which contribute to a global system.

For others this is an artificial analysis, the multilateral and the bilateral are **two sides of the same coin**. How could it be otherwise when there is an “immediate and unconditional” application of the MFN rule to all WTO members, together with a rule, some GATT Articles later, that permits preferential import treatment within free trade areas? Or when a general prohibition on all quantitative restrictions on imports is followed by rules that identify permissible exceptions to this and by rules that define in some detail how restrictions are administered.²

The point here is that the **trade system** contains within itself various **elements** which might appear

to be **contradictory and antithetical**. Activities that are apparently outside the system can be, and have been, accommodated without tearing it apart. Many think that it is precisely these built in flexibilities that have enabled the system to survive so long in a marriage of political imperatives with legal requirements. International rules in the financial or developmental fields have not endured so well.

This history becomes particularly relevant when we discuss the future of the system. The first question is therefore why there are so many trade policy observers who suggest the system should be reformed. It was always thus: if we go back to the 1960s, when GATT Part IV was added and when the UNCTAD was established, there were repeated criticisms that the GATT was skewed in favour of the developed countries and that its trade liberalisation efforts which were unfair to “the third world”. In the 1970s and into the 1980s, when the GSP was a major issue and when the ‘Enabling Clause’ was agreed, this was still an underlying theme among the critics.

With the arrival of the **WTO some changes** have been made, with a stronger emphasis on the legal aspects, the contractual nature of the commitments, the **rights and obligations** of the members; as well as a clear recognition that there are indeed several **tiers of membership** with tangible differences in the import treatment applied to each group.³ This is an indicator of a pragmatic approach to new circumstances and is in essence a proof of flexibility.

However, further reform of the system is now on the agenda. The continuing failure to close off the Doha Round is a part of the picture; when a core part of the institution’s agenda is not working, there is inevitably a response that reform is needed. But it goes back further, and we could usefully examine why exactly the system has become largely dysfunctional (and thus what needs to be fixed)?

- A first indication of trouble was the **deadlock** in the succession process for a new Director General in early 1999. This had all the appearance of a traditional North-South divide, with the developing world feeling that it was time (overdue?) for them to have a turn.
- Shortly after this, a second disaster struck in **Seattle** where a WTO Ministerial was abandoned without an agreed declaration, and without

1 Messerlin and van der Marel, World Trade Review, October 2011.

2 I refer to Article XI, together with Articles XX and XXI and Article XIII.

3 It is remarkable that the WTO does not yet have a clear definition of which members are developing countries although the rules allow specific measures (such as GSP) to assist development in such countries.

launching the new Round which had been the stated objective.

- In addition to these WTO internal events, the organisation was facing two major challenges from outside: the Internet and the spread of electronic data and payments systems, and the impact of globalisation on business and trading patterns. Many people attributed the economic changes that occurred to the new organisation. The general support that had existed for GATT was eroded.
- The success of the Doha conference was a brief-lived respite; but the WTO then faced a further setback in **Cancun**. While outside factors (the US political situation) had affected the efforts at Seattle, Cancun revealed that the WTO membership was fundamentally split. Major differences were emerging about the end points that could be negotiated in the three core areas of the agenda - NAMA, agriculture and services - and what would be contributed by all members.
- The declarations by Zoellick after Cancun that the US would pursue regional and bilateral agreements are another indicator that the system was under strain. The fact that these were aiming at WTO-plus agreements, going further than the Doha proposals and including elements that had been excluded from Doha agenda, confirmed that the division of opinion on how to move forward had become deep rooted.
- Finally, the exponential increase in trade in services which resulted from the developments mentioned above has led to a much broader distribution of trade among countries. China, India, Korea and Brazil are the WTO members that have benefitted most.

Possible challenges

Three broad areas of WTO activity can be identified where reform could be relevant in the current context: institutional issues (which covers decision-making, small groupings and promoting leadership), 'the negotiating forum' (which clearly needs rethinking), and shifts in world trade patterns and global trading power (and the consequences). This third area - the impact of external events - needs emphasis even if the facts about the changing pattern of world trade are well known. China has risen to be the third largest trading nation in goods

and services in the decade since it joined the WTO (and second if the EU is not treated as a group). India has followed, now joining the top echelon, thanks to its successes in the services sector.⁴ Countries such as Korea, Mexico and Brazil have also been rising up the ladder.⁵

One economic feature which underlies this shift is the development of the global supply chain business model, also called the industrial value chain. This is definitely due to globalizing factors such as the Internet, leading to a pattern of input supply-final assembly which has brought many smaller economies into the world trade system. In turn that puts emphasis on the role of foreign direct investment in changing trade patterns. China is universally recognized to have won the lion's share of the growth in FDI in the last decade; but other Asian countries have also taken their share, and in more sophisticated industries the role of Korea and Taiwan should not be ignored.

These developments are part of a general shift of trade power away from the West and towards Asia, with China's GDP overtaking Japan in the region and Korea and India also experiencing rates of growth much higher than any in Europe. This phenomenon, with the rise of emerging economies elsewhere in the world, has led to the creation of the G20 to replace the G8 and to calls for reform of institutions such as the IMF and World Bank whose management and voting power still reflects the situation in the post-World War II period. There is no good reason why the WTO would be isolated from such change.

The challenge is therefore how to introduce changes to the system which might help to meet these points of deadlock and failure, and which might respond to the shifts occurring in the global economy.

To take the broader issue first, how should we give greater recognition in the WTO to the shifting trade power of the members? This is not a straightforward issue, there are not the same kinds of governance questions as arise in bodies like the IMF and World Bank. There are no differences in the way countries are represented in WTO (each one has an Ambassador, and each of them has a single vote); and this clearly distinguishes its practices from those of the other institutions where representation of a country in the Governing Bodies is usually indirect and voting rights reflect a member's (historic) weight in the world economy and its financial contribution to the funds of the institution.⁶

4 As an importer India is at 13 for goods and at 7 for services in 2010 (at 8 and 5 if intra-EU trade is excluded). It stands a little further back as an exporter but still in the top 10.

5 It is true that the US and Japan and five or six EU member states still occupy places in the top 10, but Canada and smaller European states have been displaced and nations such as Thailand, Malaysia and Indonesia have moved ahead of them.

Reform in those institutions is seen to be a matter of adjusting current practice, to bring it into line with the evolution of the global economy, but also to keep control of key decisions in the hands of the main financial contributors. Within those parameters, a more equitable spread of responsibility for the leadership of the financial and development systems is also desirable. For the WTO, on the other hand, a broader division of leadership responsibility is the first requirement, with a greater role for the emerging economies which have been rapidly increasing their shares of world trade.

We are not starting from zero in this process. As already mentioned the WTO does explicitly recognize three groups of members, and has allowed members to introduce policies which give advantage to one or other group. Long standing examples of measures are the GSP schemes and more recently the duty-free, quota-free treatment for LDCs applied by several developed members. In the rules area these actions are covered by the Enabling Clause. During the Doha Round a major shift has already occurred with the *de facto* recognition of the central role that China, India and Brazil can play as a developing country presence in the G5 group steering negotiations.

What more could be done? In purely institutional terms it seems difficult to invent new mechanisms which would in some mysterious fashion create new leaders: presence and participation is one element, leadership in the general systemic interest is another thing. I would however support one change, to set up an intermediate body between the members acting individually and the membership acting together in the General Council, with executive functions on similar lines to those that exist in almost every other International Organisation. This might be represented as a "G20 trade group" reflecting the broader composition of the G20 summit meetings but giving it a defined role in the WTO hierarchy.

Such a group would permit more open, in-depth discussion of the main policy issues than is possible

with around 120 representatives in the room and would lead to greater efficiency in the decision making process.⁷ This may well be needed as the WTO moves forward towards a post-Doha world and begins considering what the elements of its work programme should be.

This would yield institutional benefits, but would not address the problems of how to achieve a wider responsibility for the future of the system. In the area of trade negotiations the primary job of every national representative is to secure changes in rules (or reduce trade barriers) which are in his/her country's interest; but it is also necessary for those at the centre that are crafting the final deal - and the compromises inevitably needed - to agree upon and promote systemic objectives. Recalling the quotation at the start of this paper, it is no easy task to agree upon these objectives if the trade community is fragmented and split.

In consequence there is no single reform approach which will ensure success. The composition of the G5 is reasonably balanced and representative; it could be expanded in various ways, but would that be an improvement? Some of the missing ingredients are the political will in major trading nations to pursue the primary objectives of opening markets, eliminating barriers and expanding trade; and close behind is the absence of a cooperative spirit as opposed to an adversarial approach. It will take some time to bring the trade community back to such first principles; and it is the members themselves that need to reshape the institution rather than the other way round.

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6 In the World Bank, five major economies (but not China or Brazil or India) are permanent members of the Executive Board and the others are elected for a fixed term and organised in groups represented by one member of the group. The members of each group are selected based on regional criteria; but the method to choose the country that represents them is arcane and varies from group to group. Voting rights reflect the weight of each member in the world economy when the Bank was set up (with relatively minor adjustments since), as well as the donations made to the Bank's funding (eg. to the IDA). The five permanent members have more than 37% of the voting rights, but to take one example, China, Russia and Saudi Arabia each have less than 3% of the votes while many middle rank European countries enjoy more voting power than they do. Fourteen leading members command a clear majority in the Bank's decision-making which is skewed in favour of the 'old' Western nations (who also have contributed more to the funding).

7 This preparatory role is at present performed by an exhaustive round of informal consultations carried out by the Director General in the 'Green Room' and by the Chairmen of various Councils and negotiating groups; but there is still from time to time criticism that not everyone can make his voice heard. In earlier years a middle level group was established but it was limited to an advisory role and was discontinued after a short period of life.