What Does Globalization Mean for the WTO? A View from Economics

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Introduction

- Globalization means many things
  - sometimes hard to pin down
  - but in the words of U.S. Supreme Court Justice Potter Stewart
  - ...we know it when we see it
  - and we are seeing a lot of it
- Individuals are the ultimate drivers of globalization, but governments set the rules of the game
  - the rules can be very important to the outcome
- The WTO (and GATT before it) is where governments come to agree on the rules of globalization

Introduction

- Over the past decade, WTO member governments have attempted to adjust the rules so that
    - developing countries can share in more of the gains from globalization under these rules, and
    - the rules can be extended to cover agriculture
    - ...the Doha Round
- But the Doha Round is on the ropes
- Why? What can be done about it?

Introduction

- Why? I will focus here on three contributing factors:
  - a "latecomers" problem plagues efforts to help developing countries share in more of the gains from globalization under the rules
  - attempts to liberalize agriculture have strayed from the tried-and-true methods that worked for industrial goods over the GATT era
  - the rise of offshoring may have changed the nature of problem that WTO is being asked to solve
- I will describe these factors in intuitive terms here; more formal detail can be found elsewhere
- What can be done about it?
  - answer is not obvious
  - I will suggest some possibilities
  - a proper diagnosis is critical

WTO DG Pascal Lamy (TNC meeting, July 26, 2011)

What we are seeing today is the paralysis in the negotiating function of the WTO, whether it is on market access or on the rule-making. What we are facing is the inability of the WTO to adapt and adjust to emerging global trade priorities, those you cannot solve through bilateral deals.

This risks overshadowing the achievements in other parts of the WTO functions, such as monitoring, surveillance, dispute settlement or even Aid for Trade...There is, therefore, an urgent need to develop a shared diagnosis over the current impasse and what went wrong as a means to prepare a discussion over possible solutions as well as over emerging issues.

What's the problem and how did we get there?

- Many developing countries have been GATT/WTO members for a long time, some since the very beginning
- Aren't they already sharing in the gains from globalization under GATT/WTO rules?
- Evidence suggests they are not

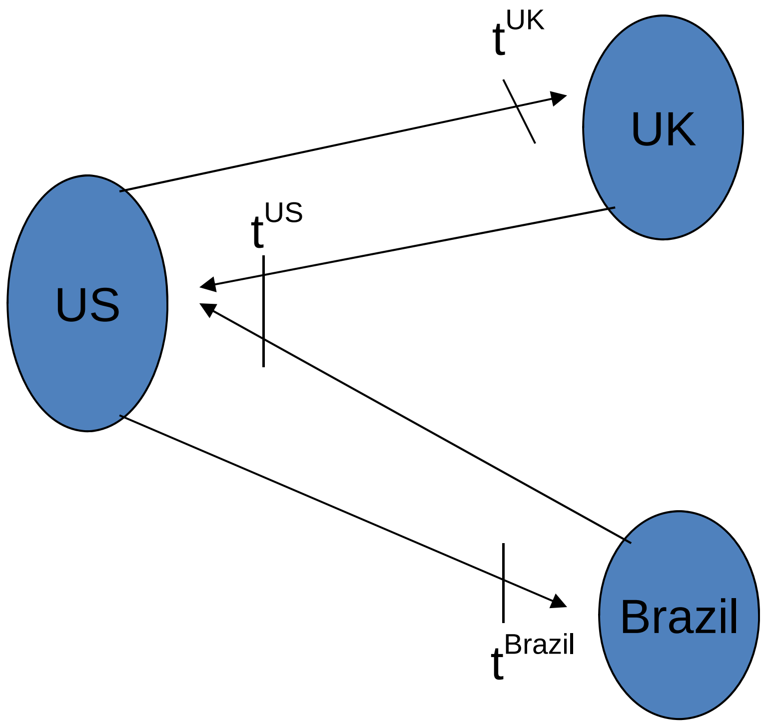
What's the problem and how did we get there?

- As a group developing countries have experienced little in the way of trade gains from 50 years of GATT/WTO-sponsored tariff negotiations
- For example, central message of Jawara and Kwa (**Behind the Scenes at the WTO: the real world of international trade negotiations**):
- *"Developed countries are benefitting from the WTO, as are a handful of (mostly upper) middle-income countries. The rest, including the great majority of developing countries, are not. It is as simple as that."* (P. 269).
    - ...based on interviews with WTO delegates and Secretariat staff members
    - but this position is also supported by the data (Subramanian and Wei, JIE, 2007, and confirmed subsequently by many others)

What's the problem and how did we get there?

- Why has this happened?
- Fact: most developing countries have committed to few tariff cuts over 8 GATT multilateral negotiating rounds spanning 50 years
  - a result of exception to reciprocity norm, extended to developing countries and codified under "SDT" clauses
  - were supposed to get a "free pass" on the MFN tariff cuts that the developed countries negotiated with each other: Figure 1
  - apparently, it didn't work out that way
  - some simple economics suggests that we might have expected this

Figure 1: Reciprocal MFN Tariff Cutting



What's the problem and how did we get there?

- Key mechanism: a country's own tariff cuts stimulate its exports
- In context of reciprocal MFN tariff negotiations:
  - if a country agrees to cut its own import tariffs in exchange for MFN tariff cuts in the markets served by its exporters (reciprocity),
  - it's exporters will gain more export volume from the additional access in those markets than exporters from countries that did not reciprocate (i.e., did not agree to tariff cuts of their own); Figure 1
- Evidence on this mechanism? Plenty, but perhaps most convincing...

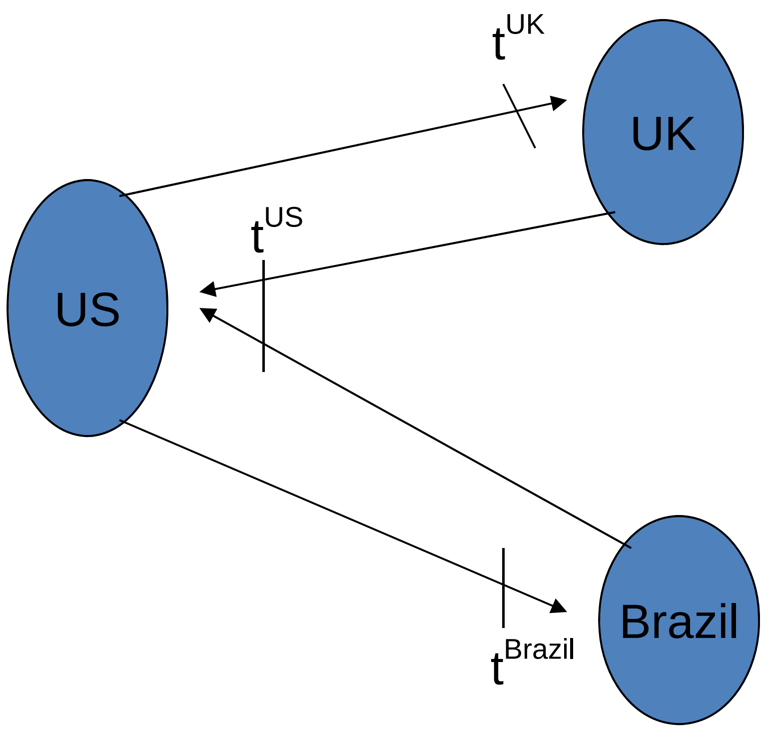
An exception that proves the rule?

- China's accession to the WTO in 2001

What you get is what you give

- $\therefore$ In GATT/WTO bargaining, what you get is what you give
- $\Rightarrow$ Doha's current non-reciprocal approach anchored in SDT will not deliver meaningful trade gains for developing countries, just as this approach did not do so over the previous half century
    - developing countries must come to the bargaining table and negotiate reciprocally with each other and with developed countries; Figure 1
- But there is a bigger problem

Figure 1: Reciprocal MFN Tariff Cutting



The latecomers problem

- Developed countries may have already achieved through 8 GATT rounds the degree of "openness" that they desire

- Two issues then follow:
  - preservation of bargaining power – developed countries may have little to offer developing countries in reciprocal bargains, hence difficulty in negotiating reductions in developing country tariffs
  - globalization fatigue – existing MFN tariffs of developed countries may be too low for world in which developing countries are fully integrated into world trading system
  - Figure 1

- These two issues not unfamiliar: a struggle with accommodating latecomers in evidence from very early in GATT/WTO history

The latecomers problem

E. Wyndham White on the *bargaining power* issue faced in the 1950-51 Torquay Round...

> *"...A number of European countries with a comparatively low level of tariff rates considered that they had entered the Torquay negotiations at a disadvantage. Having bound many of their rates of duty in 1947 and 1949, what could these low-tariff countries offer at Torquay in order to obtain further concessions from the countries with higher levels of tariffs?"*

...and on an early version of *globalization fatigue*:

> *"The Torquay negotiations took place under conditions of much greater stress than those which prevailed at the time of the Geneva or Annecy Conferences. Besides, ...many of the countries...felt they needed more time to digest and to assess the effects of the concessions already made before making further cuts in their tariffs." (ICITO, 1952, pp. 9-10).*

The latecomers problem

- And even *The Economist* coming around to the view that the latecomers problem is the central sticking point at Doha:

"...the real bone of contention is the aim of proposed cuts in tariffs on manufactured goods. America sees the Doha talks as its final opportunity to get fast-growing emerging economies like China and India to slash their duties on imports of such goods, which have been reduced in previous rounds but remain much higher than those in the rich world. It wants something approaching parity, at least in some sectors, because it reckons its own low tariffs leave it with few concessions to offer in future talks. But emerging markets insist that the Doha round was never intended to result in such harmonisation. These positions are fundamentally at odds." (April 28, 2011)

The latecomers problem

- Accommodating latecomers may pose familiar problems for GATT/WTO negotiators
- But *scale* of latecomers problem in Doha is unprecedented in history of GATT/WTO
- This, rather than sheer numbers of members, may be biggest problem for Doha
- $\therefore$ Moving away from non-reciprocal SDT norm can help break Doha impasse and deliver meaningful trade gains for developing countries
    - but at this point it is not enough
    - this is where agriculture comes in

Agriculture

- In *The Misadventures of the Most Favored Nations*, Paul Blustein describes the terms of the agriculture bargain that emerged from Doha in 2005:

  "The package was based on a hardheaded political calculation, in the finest tradition of WTO- and GATT-style mercantilism. Curbing farm subsidies might be a desirable policy for the United States as a whole, but it was a 'sacrifice' that American politicians could accept only if most farm groups were assured that their export opportunities would burgeon. A Kansas wheat grower who might ordinarily rebel at seeing his federal check shrink would presumably acquiesce provided his crops stood a better chance of gaining access to European consumers or the booming emerging markets of India and China." (pp. 205-206)

Agriculture

- But with suspension of the round in 2008, Blustein observes:

  "Agriculture groups felt that the deal on the table simply wouldn't provide enough new market access for U.S. farm exports to compensate for the reduction in the cap on U.S. subsidies...the handwriting seemed to be on the wall: Although U.S. exporters would gain additional sales in high-income markets, such as the European Union, for beef, pork, and some other products, they wouldn't gain much, if anything, in the world's emerging markets, because the loopholes granted to developing countries were too large." (p. 269)

- Why hasn't Doha's approach to agriculture succeeded?

Agriculture

- In fact, contrary to Blustein's assertion,
- exchanging cuts in **export subsidies** for cuts in **import tariffs**
  - departs from the "tradition of WTO- and GATT-style mercantilism" in a number of crucial respects
  - for one thing, the traditional political tradeoff of export interests against import-competing interests is absent

Agriculture

- Result: no one to push for the Round

> *"It was really sobering to hear the ag and NAM [National Association of Manufacturers] people say, 'Hmmm, this isn't worth the trouble," recalls one congressional staffer who attended the meetings. "How would you get that passed in Congress?" (Blustein, p. 270).*

- More fundamentally, where are efficiency gains from this deal that can ensure mutual benefits to negotiating partners? Figure 2
- A traditional market access bargain exchanges tariff cuts for tariff cuts: Figure 3
- ∴ The agricultural package on the table is *not* in the tradition of GATT bargains
  - can help explain lack of Doha success in liberalizing agriculture
  - but also might suggest a way out of the Doha impasse

Figure 2: Exchanging Cuts in Export Subsidies for Cuts in Import Tariffs

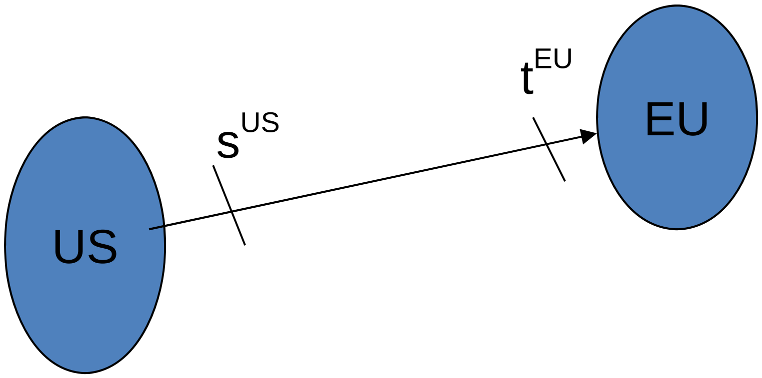
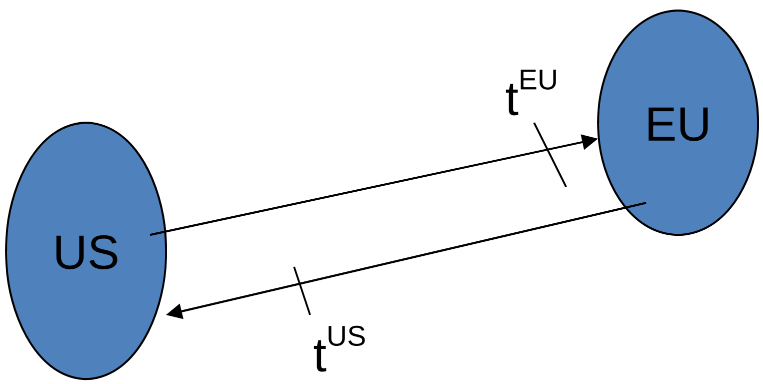


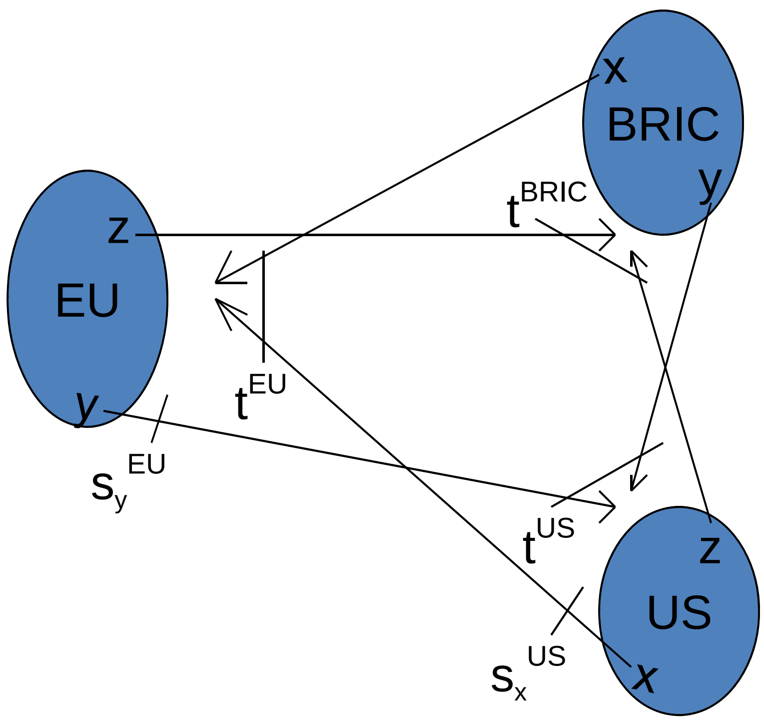
Figure 3: Exchanging Cuts in Import Tariffs for Cuts in Import Tariffs



Making the Doha Round a development round

- How can the Doha Round become a development round?
- Suppose Doha moves away from SDT, *and* reorients agriculture negotiations
  - away from cutting US farm subsidies in exchange for cuts in EU/China/India agricultural tariffs
  - and instead toward cutting US farm subsidies in exchange for cuts in BRIC tariffs on *manufacturing goods*
  - Figure 4

Figure 4: How the Doha Round Could Work



Making the Doha Round a development round

- This bargain could be understood as a way to engineer trade volume gains for developing countries by using the elimination of agricultural subsidies
- to entice developing countries to agree to lower their tariffs
  - thereby generating bargaining power for the low-tariff developed world
- and to mitigate the overall trade effects of integrating developing countries into the world trading system
  - thereby addressing the issue of developed-world globalization fatigue
- and in this way provide a solution to the latecomers problem
- Note: a truly multilateral deal required (Figure 4)

Offshoring and Doha

- The third issue (adjusting to rise of offshoring) less-clearly central to Doha, but could be behind this recent statement by WTO DG Pascal Lamy:

"...we have not yet figured out how to deal with the interdependent world economy we have created. This [GATT] system was initially designed to tackle problems specific to the mid-twentieth century... The basic architecture of the system reflected its origins in an Atlantic-centric world of shallow integration. The question now is what is needed to manage a globalized world of deep integration..." (Speech at the WTI, 10/01/10).

Offshoring and Doha

- A third theme: As the prevalence of offshoring rises, effective trade agreements and the institutions that support them will have to evolve;
- from a "shallow" market-access focus to "deep" integration,
- and from a reliance on simple and broadly-applied rules such as reciprocity and non-discrimination/MFN,
- toward a collection of more-individualized agreements that can better reflect member-specific idiosyncratic needs.
- Perhaps striking lack of Doha progress in services, and recent proliferation of FTAs, are manifestations of institutional shortcomings of the GATT/WTO architecture for a world of offshoring.
- Some suggestive evidence:
  - rise of deep-integration FTAs (Orefice and Rocha 2011)
  - signs of greater difficulty liberalizing trade through WTO negotiations in sectors where customized inputs are especially prevalent (Figure)

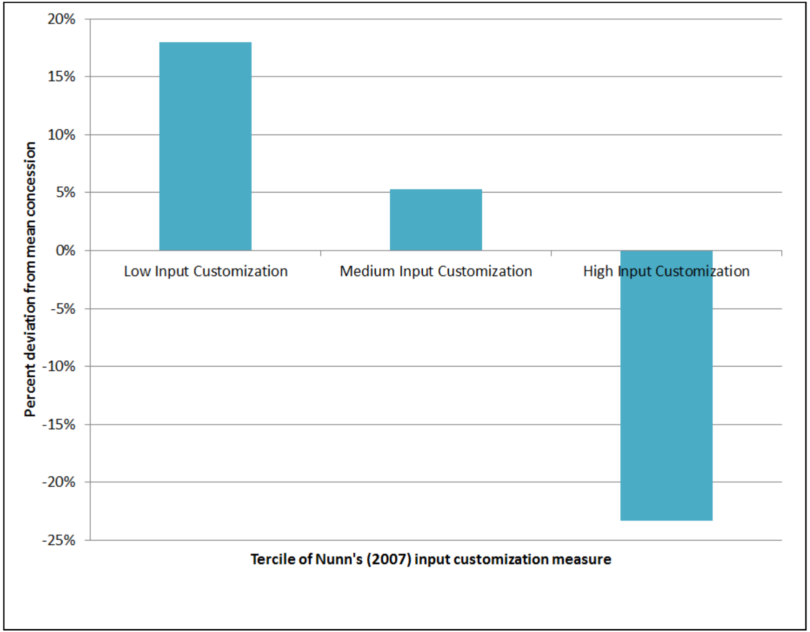


Figure 1: Percent deviation from mean concession by tercile of input customization measure