

## THE WTO: IN THE TROUGH OF THE TRADE ROUND

*The meeting at Cancún saw the North-South divide take front stage in the multilateral trade negotiations. The proliferation of alliances by developing countries has given way to a clearer division. On the one hand, the trade and growth potential of the G22 countries allows this group to begin real “bargaining” with the countries of the North and become a key actor in the negotiations, alongside the European Union and the United States. On the other hand, the least developed countries are likely to be the overall losers within a general liberalisation process, given their trade preferences with Northern countries and trade specialisations. The Cancún meeting ended in failure as it did not take sufficiently into account the interests of the former group or provide an adequate response to the latter. This failure clearly shows up the need to reform the way in which negotiations are conducted.*

The so-called “Singapore issues” provoked the collapse of the negotiations in Cancún. Be it clumsiness or a lack of determination to tackle other disagreements, the issues of investment, competition policy, transparency in government procurement and trade facilitation were placed at the top of the list in the proposal for an accord, submitted by the Mexican Minister Luiz Ernesto Derbez, who was responsible for the negotiations. To be sure, some developed countries do indeed want to discuss these issues (notably the European Union, Japan and South Korea *etc.*). But they are rejected *en bloc* by the South, which is focussing on implementing the agreements signed in Marrakech in 1994, agreements that relate to market access for labour-intensive activities, and above all to agriculture.

The rich countries thus left Cancun with their hands empty. So, at the other extreme, did the least developed countries (LDCs), which had been looking for an agreement on the key issue of cotton. As for the developing countries, they saw the prospects of a rapid conclusion to the Round diminish, and hence the possibilities of quickly liberalising sectors they are interested in. Under the GATT, negotiations would frequently break down in the course of its trade rounds. But the Cancún showdown is different. Not only is the objective of liberalisation being challenged by part of civil society, but the institution itself, or more specifically the modalities of negotiation appear to be inappropriate. The WTO finds itself in a paradoxical situation. Its working rules probably make it one of the international

organisations which gives the greatest voice to the developing countries. It is the only organisation in which a complaint lodged by a poor country may lead to disciplinary action taken against the United States<sup>1</sup>. But the conduct of negotiations makes it difficult for weaker nations to push their demands. At Seattle, the developing countries already complained about the fact that essential areas of the negotiations took place in a *green room*, to which most of them did not have access. In the Doha Round, negotiations are carried out in commissions, with the result that the central role played by commission chairpersons is being contested. Similarly, the limited space attributed at “mini-ministerial” meetings (such as that in Montreal last July) to developing countries now seems unacceptable to them. From this point of view, the Cancún meeting, which saw new alliances emerge, at least has the merit of clarifying positions.

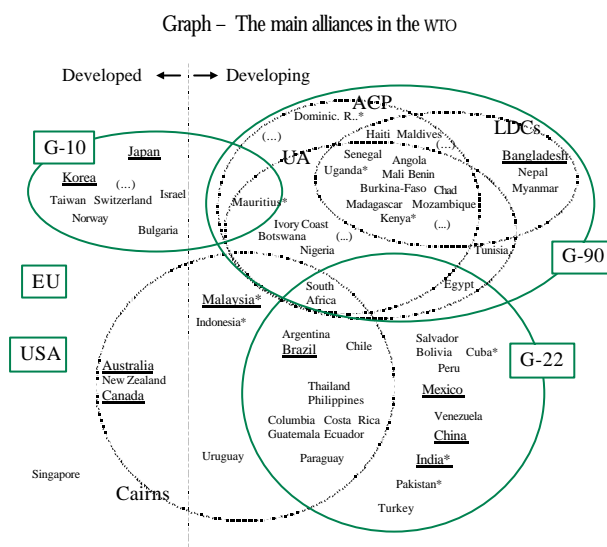
### ■ The New State of Play

Negotiations within the WTO are based on the principle of consensus. In addition, the rounds are henceforth also founded on the principle of a single signature. A country's commitment can only be made to all issues at stake, it cannot pick and choose<sup>2</sup>. Negotiations between 148 countries on 20 subjects are especially difficult to conduct: an ambitious round is doomed to failure as soon as it includes issues that are unacceptable to certain countries. In contrast, a limited round may lack support as it

1. According to a recent study, it may be considered that developing countries have benefited from favourable rulings in all the complaints lodged against the United States and the European Union with the Dispute Settlement Body (DSB), which were handled between 1995 and 2002. Broadly speaking, the study suggests that the workings of the DSB are unbiased with respect to a country's level of development: see P. Holmes, J. Rollo & A. Young (2003), “Emerging trends in WTO dispute settlement, Back to the GATT?”, *World Bank Policy Research Working Paper*, 3133, September.

2. Only agreements relating to public markets and aircraft are optional, in other words they are pluri-lateral rather than multilateral.

holds out few gains for all parties. These problems mean that the modalities of liberalisation must be sufficiently simple for them to be applied symmetrically. They also encourage participants to form alliances, often based on limited convergence on certain subjects. Piling these subjects up leads to a situation which, at first glance, is apparently inextricable. This is indicated in a very simplistic way by the diagram below.



*Note:* The groups are those of the alliances which have been formed by countries within the WTO. The most active groups at Cancun are indicated in dark green lines. Countries marked by an asterisk are members of the Like-Minded Group, led by India. Countries whose names are underlined were the most influential at Cancun. The diagram is not exhaustive, and does not show all alliances nor all countries.

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Finally, the weeks leading up to Cancun did allow for a certain amount of clarification. The text on agriculture, published jointly by the European Union and the United States on 13 August, did not appear to be a compromise that would lead to a general agreement, but rather as an attempt by the rich countries to impose their views on the international community. A group bringing together the main, influential developing countries was formed in reaction to this, becoming progressively the "Group of Twenty-Two" (G22). In contrast to the Cairns group (which was practically inactive as such, at Cancun), the G22 includes no rich members. For their part, the poorest countries came together in an alliance of the African Union - ACP - LDCs (AU - ACP - LDCs, also named the G90). Lastly, the countries most strongly protectionist in agriculture formed a G10, led by Japan and South Korea.

This reconstitution of alliances indicates the emergence of a new state of play. The European Union-United State split was traditionally at the centre of negotiations, with the Cairns group acting as a third protagonist. At Cancun, the G22 suddenly emerged as a key actor, alongside the EU and the United States, thus putting the North-South divide at the heart of the negotiations. The G90 and G10 played second roles, with less force but holding more radical positions. Another factor of new

importance is that these five groupings (the EU, the United States, G22, G90 and G10) actually divide up the WTO as they practically do not overlap and their combined members account for nearly the whole WTO membership. They were the only audible parties present at Cancun.

## ■ The Heterogeneity of the South

The claims of the Southern countries may, at first glance, be explained by the sectoral protection of Northern markets. This results from nearly half a century of negotiations among the rich countries within the GATT. The trade liberalisation pursued since the World War II has also focussed mainly on products of interest to the industrialised countries, leaving pockets of strong protectionism, in agriculture and labour-intensive industries (especially, clothing-leather-footwear). Overall, the level of protection in the Quadrilateral (Quad: United States, Canada, Europe and Japan) is especially high in these sectors (Table 1), which are precisely the strong points of the developing countries.

Table 1 – Average customs duties faced by exporters to the Quadrilateral (% , 2001)

Exporter	Agriculture			Clothing		
	All North developing countries	LDCs	LDCs	All North developing countries	LDCs	LDCs
Canada	30.8	19.5	1.3	17.4	17.8	18.2
EU	12.6	12.0	0.3	11.0	7.9	0
Japan	12.6	10.2	1.4	7.6	3.0	0.5
United States	9.9	8.6	20.8	12.4	13.7	15.3

*Note:* Customs duties at the level of tariff headings are aggregated by using trade between groups as a weighting. For example: Japanese duties are weighted on products exported by Pakistan according to imports of these products to the Quadrilateral which originate in the LDCs. This method makes it possible to avoid biases of underestimating protection induced by weighting based on flows of bilateral trade. The AGOA was not yet fully in place in 2001.

*Source:* A. Bouët, L. Fontagné & M. Mimouni, "Direct Measure of Protection: a Rehabilitation", *CEPR Working Paper* forthcoming.

Such a presentation is, however, somewhat simplistic, given the diversity of Southern countries. For the last thirty years, the major powers have used trade preferences (reduced or zero customs duties for "preferred" countries) to help the developing countries with which they have historical links. As part of the efforts to reduce poverty, such preferential policies have recently been extended to all LDCs<sup>3</sup>. The barriers facing developing countries are therefore very heterogeneous and the LDCs generally suffer from little tariff protection in Quad markets. The historical trade partners of the United States have generally been intermediate-income countries, so that the American market has been an exception from this point of view. This situation is tending to disappear with the measures taken in favour of the African countries (African Growth Opportunity Act, AGOA). That said, the interests of developing countries as a whole are not necessarily the same as those of the LDCs in particular. Were the suppression of all tariff peaks (i.e. tariffs of more than 15%)

3. The EU's "everything except arms" initiative, the GSP-LDC of the United States and Japan's 99% initiative, etc.

for Quad markets to be offered to all developing countries, it would lead to a substantial rise in the exports of the products in question<sup>4</sup>. But the LDCs would only really profit from such market opening if they were the only ones to benefit from it (Table 2). For these countries, the generalised opening of markets to all developing countries would erode their preferences. Were this to occur, it raises the particular problem of accompanying measures. These could take the form of new trade advantages or development aid. Furthermore, the very limited diversification which characterises developing-country exports makes certain issues very contentious, such as cotton for west African countries, sugar and bananas for small ACP states, or clothing for Bangladesh.

Table 2 – Gains for developing countries from the suppression of tariff peaks (the progress of exports for the countries concerned, in %)

Exporter	Suppression benefiting all developing countries		Suppression benefiting LDCs only
	LDCs	Other developing countries	LDCs
EU	0.9	18.5	37.5
Japan	8.4	20.3	62.8
United States	20.5	20.4	35.1
Canada	16.2	21.7	29.2

Source: B. Hoekman, F. Ng & M. Olarreaga (2002), "Eliminating Excessive Tariffs on Exports of Least Developed Countries", *World Bank Economic Review* 16(1): 1-21.

An analysis of the consequences of liberalising all world trade in manufactured goods<sup>5</sup> confirms this statement. World exports of manufactured products would rise by more than 12% and this growth would be more than 30% for Argentina, India, the Maghreb, South Asia and Brazil. In contrast, exports from sub-Saharan Africa would not rise by more than 11%, given the disappearance of the trade preferences from which this region benefits.

These different outcomes create the conditions leading to the observed coalitions, especially in agriculture.

## The Agricultural Issues at Stake

Agriculture in most industrialised countries is characterised by heavy protection at borders, internal support and even export subsidies. The rich countries support their agricultural producers to the tune of more than \$1 billion per day, six times the amount provided in development aid. Such support, which is justified by collective preferences and considerations of rural development planning, is clearly subject to political economy considerations and results from effective action by powerful lobbies. But it is

not just a cost to the countries in question, as it lowers world prices and holds back developing country exports<sup>6</sup>.

Simulations carried out with the MIRAGE model allow the impact of agricultural liberalisation to be gauged, according to the modalities of the Harbinson proposition<sup>7</sup> (Table 3). The industrialised countries will benefit from a real gain in wealth, linked to the reduction of distortions induced by protection, especially in Europe (the EU and EFTA) and developed Asia. In contrast, they will not witness any substantial rise in their agricultural exports, with the notable exception of the developed countries in the Cairns group<sup>8</sup> (Australia, Canada, New Zealand). World trade in agricultural products would grow by more than 5% in volume terms, essentially due to a surge in exports from developing countries.

Table 3 – The impact of the application of the Harbinson\* proposal for liberalisation in agriculture (variation in %)

	Agricultural imports (volume)	Agricultural exports (volume)	Terms of trade	Real wealth
EU-25	9.9	-0.5	0.13	0.11
United States	4.6	0.5	0.15	0.09
Developed Cairns	4.6	11.1	0.09	0.04
Cairns developing	-3.6	7.8	0.27	0.15
Sub-Saharan Africa	-3.8	3.9	-0.01	-0.32
Developed Asia	8	27.5	-0.35	0.12
China	-6	8.7	0.21	-0.1
EFTA	30.2	0.3	-0.25	0.69
Mediterranean countries	-4.8	13.3	0.01	-0.48
EX-USSR	10.5	16.3	-0.92	-0.18
World	4.7	4.7	-	0.1

\* Cf. note 7.

Source: A. Bouët, Y. Decreux & S. Jean (2003), "Developing Countries Faced with Multilateral Agricultural Liberalization: Contrasted Fortunes", *CEPII Working Paper* forthcoming.

Liberalisation is likely to lead to contrasting effects among the developing countries, due to the way support is targeted in the rich countries and to the strong heterogeneity of the formers' specialisations.

The impact of internal support is mainly sensitive for a limited range of products: cotton, rice, oilseeds and sugar<sup>9</sup>. Export subsidies are concentrated on milk products and sugar. For these products, the rise in world prices will be good news for the net exporting countries or those set to become so. But this is far from being the case for all developing countries. For other products, liberalising market access is the main issue at stake, leading to new outlets and hence gains for exporting countries.

A certain number of developing countries have become net agricultural importers in recent decades. This is especially the case for the LDCs, whose agricultural exports of food products only

4. For the European Union, this would mainly involve cereals, sugar, meat and footwear.

5. Assuming the suppression of the Multi-Fibre Arrangement, the implementation of the "Everything except arms" initiative, the consolidation of AGOA, and both China and Russia's entry into the WTO. Source: M.H. Bchir, L. Fontagné & S. Jean, "Market Access in Non-Agricultural Goods: What is at Stake in the Development Round?", *CEPII Working Paper*, forthcoming.

6. These efforts are all the stronger given that internal support is coupled, i.e. it is conditional to production volumes. This explains the stress placed on de-coupling within the agricultural negotiations.

7. This proposition, which was formulated by the Committee negotiating on agriculture, includes the suppression of export subsidies, a reduction of more than half in internal support coupled to production, and a cut in tariff duties according to a non-linear formula. Special and differentiated treatment is to be given to developing countries. The simulations presented here assume that the reform of the CAP which was voted in June 2003 is implemented prior to the simulated liberalisation. This assumption limits significantly the impact on world prices induced by the Harbinson proposition.

8. The strong, relative rise of Asian exports is not especially significant, given the initially low level of exports.

9. This situation described here will occur after the CAP reforms agreed in June 2003.

cover 20% of the value of their imports. These countries are caught between industrial competition from emerging countries and heavily subsidised agriculture in the North. Their economic specialisation structure is often hemmed in to producing raw materials, especially as moving up the production chain in transforming agricultural products is made difficult by the progressive nature of customs duties<sup>10</sup>. Such specialisation only aggravates their difficulties, as export earnings fluctuate, terms of trade tend to worsen, there are no spill-overs to other sectors and it is difficult distributing the corresponding economic rents. That said, for many of them agricultural liberalisation would not lead to substantial gains. Improved market access would not much benefit them, due to the erosion of preferences discussed above. Their dependency on food imports would cancel out, or reverse, in their case, the terms of trade appreciation which is to be expected for the developing countries as a whole. As for tropical goods, which are among the main export products of the most African countries, they are in any case little protected, as rich countries do not produce similar products. Liberalisation would not have an impact on their prices. It is therefore hardly surprising that the simulations of agricultural products only suggest very limited growth for exports from sub-Saharan Africa and even have a negative impact on their real wealth and on their terms of trade.

## Structures in Need of Reform

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The major powers were used to seeing the GATT as a rich countries' club, since its creation in 1947. They have underestimated the rise of the South in multilateral negotiations. But the creation of the WTO changed the rules of play: it transformed the Club into a structure capable of integrating the developing countries. This transformation was sought by the rich countries, and has succeeded beyond hopes, as the new entrants have become active partners in the WTO. But the present system is incapable of preventing gridlock in negotiations. This is probably due to failure to give sufficient weight to the interests of intermediate countries. It also stems from failure to reassure those countries most protective of agriculture and, lastly, from failing to provide specific answers to the problems of the LDCs.

However, the terms of the debate now seem clear. The intermediate countries have much export potential, which would allow them to benefit strongly from liberalisation, especially in agriculture. At the same time, these countries have the most promising markets, and solicit the greatest interest from the North. These cross-interests could provide the basis for "bargaining", that may be seen as mutually beneficial, at least for the main actors which are henceforth the EU, the United States and the G22. In addition, the emergence of five, well-identified and well-represented actors provides a clarification which should allow the heterogeneity of the South to be taken into account.

From this point of view, the context of Cancún would seem to be favourable to new advances in multilateral openness. The failure is only symptomatic of the inappropriateness of the structures for conducting negotiations and of the necessity of reforming them. This could include, for example, creating an institutional mechanism for allowing negotiations to be carried out in more limited, representative committees that are duly mandated.

Failing this, the most rapid negotiations within the WTO are likely to occur outside the Rounds, on a pluri-lateral<sup>11</sup> or regional basis. This could then lead the major issues of interest for the developing countries (tariff peaks, agriculture) to be frozen out of liberalisation permanently, with regional agreements achieving the greatest advances. The developing countries would lose out twice from this. Some would find themselves cut of agreements due to their geographic or political position. Others would suffer fully from the asymmetrical balance of power which always arises when regional agreements are concluded between major powers and developing countries. This is the paradox Brazil faces today. Having played a role in blocking the Round, the country might be constrained to accept US conditions in the conclusion of the Free Trade Agreement of the Americas.

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10. Duties are said to be progressive when they rise with the degree to which products are transformed.

11. In April 2000, 47 countries belonging to the WTO signed an Accord on information technology, relating to the suppression of all customs duties on these products. Mauritius is the only African member country of this Accord.

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