

# Between Intensive Care and the Crematorium: Where Next for the Global Trading System?

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When the Doha Round of multilateral trade negotiations was suspended indefinitely on 24 July, apparently due to irreconcilable differences over the liberalisation of agricultural trade, it marked the latest crisis in a trade round that the *Financial Times*' Alan Beattie described as a 'deal doomed from the beginning' (24 July 2006). News of the suspension naturally prompted the media to question the world's trade ministers about the future of the round. While they were understandably reluctant to pen Doha's obituary, their assessments were nevertheless bleak. Australia's trade minister, for example, described the round as hanging by a thread. But perhaps the most colourful assessment was made by India's Kamal Nath, who judged that while Doha was not dead, it was nevertheless somewhere between intensive care and the crematorium.

The July 2006 suspension of negotiations may or may not turn out to mark the death of the Doha Round: the history of multilateral trade negotiations shows that trade rounds have often been marked by repeated crises and breakdowns in negotiations, before eventually a compromise is forged. Certainly, that was the experience with Doha's predecessor, the Uruguay Round (1986-1994), which ran for almost eight years and suffered collapses in Montreal (1988) and Brussels (1990) before finally reaching a successful conclusion in the creation of the WTO. Still, the decision to toss

the current trade round into the deep freeze will almost certainly mark a watershed for the future of the international trading system. Even a 'good' outcome for the faltering trade round—and at this stage a good outcome is almost anything short of an outright collapse—is likely to deliver little in terms of new market access when set against the scale of negotiating resources devoted to Doha. As a result, the appetite of the world's trade ministers for any repeat performance will be limited. One implication is that the era of giant, set-piece trade rounds like Doha and the Uruguay Round may well be over.

Achieving progress in the current Doha round has proved to be 'painfully difficult and has raised questions about the process itself', according to a report to the WTO's director-general by a consultative board of 'wise men.'<sup>1</sup> One doesn't necessarily have to be an advocate of the bicycle theory of international trade policy—which asserts that momentum is all, with the world either moving forward towards freer trade or sliding backwards into more protectionism—to view this lack of progress as a source of real concern for the future of the system. As the WTO's own wise men have pointed out, since the WTO is basically a negotiating machine, to the extent it becomes unable to negotiate effectively, or even is perceived to be unable to do so, its position becomes fragile.

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1. Peter Sutherland, Jagdish Bhagwati, Kwesi Botchwey, Niall Fitzgerald, Koichi Hamada, John H. Jackson, Celso Lafer and Thierry de Montbrial 2005. *The future of the WTO: addressing institutional challenges in the new millennium. Report by the Consultative Board to the Director-General Supachai Panitchpakdi*, Geneva: World Trade Organisation.

## What Went Wrong?

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As in a good murder mystery story, there are a multitude of suspects when it comes to identifying who or what undermined the Doha Round.<sup>2</sup> Prominent among them are a United States that seemingly preferred no deal to a modest deal, a European Union unable to accept significant agricultural reform and some major emerging markets reluctant to accept the reciprocity required by multilateral negotiations.

There were also significant structural difficulties facing trade negotiators, not least a capacity crisis for the multilateral system that is a product of the growing number of WTO members, the requirement for consensus decision making and the increasing breadth and complexity of trade negotiations.

The WTO's membership has expanded dramatically: from the original 23 signatories to the GATT in 1947, the number of member economies has risen to 150 with the recent accession of Vietnam, and more are on the way. The WTO is now heading towards effective universal membership, its members now accounting for more than 95 per cent of world merchandise trade. While this expansion is a symbol of the system's success, a greater number of members makes achieving consensus a more difficult and time-consuming task. This is even more the case since the rise in membership numbers has been accompanied by an even bigger increase in diversity. Originally, the GATT was basically a rich countries' club that focused on liberalising trade in industrial products. The expansion of membership to emerging markets and developing countries brings new interests and new constituencies into the negotiations.

Along with more countries, the capacity challenge is also more issues. The advocates of large trade rounds argue that big is beautiful: negotiating over a large package of measures has two potential advantages. First, with a sizeable number of issues up for discussion, there is the possibility of securing bigger gains. Second, it might be easier to reach an agreement if participants can trade off concessions they have to make in one area against gains they can secure in another.<sup>3</sup> Yet the sheer size and complexity of trade rounds that are the ultimate outcome of this approach seem to be becoming increasingly counterproductive.

Not only are there more issues up for discussion, but the issues are often those on which it is difficult to reach agreement. Trade negotiators have already picked much of the lower hanging fruit, and that leaves the harder, more politically sensitive sectors like agriculture and services to be tackled. Not surprisingly, that makes for tougher negotiations.

So success—more members, more trade, more issues and greater diversity—has come at a cost: trade negotiations are tougher and take longer. And time is important. For example, the longer the time required to reach a successful result at the multilateral level, the more likely that trade ministers will end up looking elsewhere for politically visible 'deliverables'. Questions of time might also explain what appears to be the fading interest of the business community in international trade rounds: several press reports have cited trade negotiators bemoaning a lack of corporate interest in the Doha Round. Certainly, there is now a clear contrast between the accelerating pace of the international product cy-

2. For a more general discussion of the problems facing the global trading system overall, see Mark P. Thirlwell 2005. *The New Terms of Trade*, Lowy Institute Paper 07, Sydney: Lowy Institute for International Policy.

3. C. Fred Bergsten 2001. 'Fifty years of trade policy: the policy lessons', *World Economy* 24 (1).

cle—powered by the forces of globalisation—and the relatively glacial pace of trade negotiations.<sup>4</sup> From the point of view of a corporate lobbyist, the cost-benefit equation for multilateral negotiations may be looking steadily less attractive than some of the alternatives on offer.

Along with the difficulties posed by success, the system has to cope with structural change in the global economy. In particular, the growing economic strength of emerging markets has quite naturally caused them to become more assertive negotiating partners, and hence less willing to accept a deal imposed by the major developed economies. For their part, the latter are becoming more reluctant to afford generous concessions to what they see as increasingly potent competitors in global markets. The reciprocal bargaining framework of WTO negotiations—under which domestic trade liberalisation is treated as a concession that has to be ‘purchased’ with similar concessions by the country’s trading partners—means that stalemate is always a potential risk. In the case of the Doha Round, while some emerging market economies and developing countries feel that rich country concessions on agriculture are overdue after the disappointments of the Uruguay Round’s supposed grand bargain, their counterparts in the developed world are reluctant to offer a substantive deal on agriculture in the absence of sig-

nificant progress in areas of interest to their constituents, such as improved access for services or investment to the dynamic emerging markets.

Finally, it seems likely that the twin decisions to give the round a focus on agriculture and on development may also have made the negotiations more difficult. In fact, a focus on agriculture makes a great deal of sense: the sector remains one of the most distorted in the global economy, and economic modelling suggests that significant reform has the potential to deliver very large welfare gains.<sup>5</sup> Unfortunately, a major reason that agriculture is such a problematic sector is its immense political sensitivity: delivering significant gains in this area was always going to be extremely difficult.

What about the focus on development? Again, there was a fair degree of logic here, with the Doha Round seeking to offer something to those developing countries that felt the Uruguay Round’s focus on issues such as intellectual property and investment had advanced the interests of the developed economies while offering little in return. Yet the rhetoric of a development round has also been interpreted as providing a free ride for both the least developed countries and, at least in some cases, for emerging markets. This in turn has been a significant stumbling block given the current requirement for reciprocity in negotiations.

### Does Doha Matter?

Does any of this matter? After all, one possibility is that even the complete failure of the round will turn out to have little or no adverse impact on international trade: Doha has looked increasingly unlikely to deliver much *additional* liberalisation, and

previous trade rounds have already lowered many of the most significant barriers to cross-border exchange, progress which the WTO will continue to defend through its dispute settlements mechanism.

4. Aaditya Mattoo and Arvind Subramanian 2005. ‘Why prospects for trade talks are not bright’, *Finance and Development*.
5. Kym Anderson and Will Martin 2005. *Agricultural market access: the key to Doha success*, Trade Note 23, Washington DC: World Bank.

Stephen Roach, chief economist of Morgan Stanley, penned a piece on 4 August, shortly after the suspension of negotiations with the title *Doha doesn't matter*. Roach argued that the 'fundamentals of IT-enabled globalization have become far more important than multilateral agreements in driving the global trade cycle.'<sup>6</sup> He pointed out that during five years of multilateral negotiations that have as yet delivered no significant progress (the modest achievements announced after the Hong Kong ministerial largely remain conditional on the round reaching a successful conclusion), the world economy had nevertheless continued to become more integrated, with a steady rise in the ratio of world trade to GDP.

It is certainly the case that there are other forces besides the WTO that are driving international trade integration. According to calculations by World Bank economists (who looked at the trade-weighted tariff rates of the 33 largest developing country importers) roughly two-thirds of the decline in average tariffs over the past two decades has come from *unilateral* liberalisation.<sup>7</sup> This compares to just 25 per cent from multilateral liberalisation (the Uruguay Round) and only 10 per cent from preferential trade agreements (PTAs). So perhaps the world

economy can rely on the powerful forces unleashed by international global competition and the business incentives that it creates, along with the fruits of technological progress (in the form of lower transport and communications costs) to continue to drive world trade.

This optimistic assessment may turn out to be right. But a completely defunct Doha would be a defining moment for the global trading system, marking as it would the first irrevocable breakdown in trade negotiations since the GATT was established in 1948. A complete and total collapse in negotiations could damage the credibility not just of the current trade round, or even trade rounds in general, but of the WTO and the multilateral trading system overall. Without the prospect of *future* progress with trade liberalisation, the result could be an increasing reluctance to abide by *existing* commitments, leaving the world's great trading powers feeling increasingly entitled to dictate their own rules for international trade. Under such circumstances, the end game could be an unwinding of the very process of globalisation on which the optimistic scenario is counting. Such a world would be a very uncomfortable place for all but the largest and most powerful economies.

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### **What Comes Next?**

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In the absence of progress through negotiation, the temptation will be to seek liberalisation by litigation, with countries turning to the disputes settlement mechanism to try to prise open markets and deal with outstanding trade problems. While the dispute mechanism has been an effective tool for keeping markets open, however, its efficiency as the sole tool for driving further liberalisation is questionable, not least because of the likely domestic political back-

lash that sustained use of a legalistic approach would engender.

Instead, the most obvious development in prospect would involve countries spending even more of their time and energy negotiating various forms of PTAs—bilateral, regional and cross-regional. This would merely take the world economy further down an already well-trodden path, as the number of such

6. Stephen Roach 2006. *Doha doesn't matter*, Morgan Stanley Research Global, 4 August.

7. World Bank 2004. *Global economic prospects 2005: trade, regionalism and development*, Washington DC: World Bank.

agreements has already surged since the 1990s.

The prospect of a world economy enmeshed in an expanding network of overlapping trading arrangements is a worrying one for many economists. One risk is that, rather than supporting world trade, the resulting web or spaghetti bowl or noodle soup of agreements, with their inconsistent rules of origin and differing product coverage and content, will turn out at best to impede international economic integration and at worst to actively undermine it. Some economists even look back to the poisonous economic nationalism of the 1930s, when the world economy fragmented into competing trade blocs, as a warning of what the worst case scenario could entail. Such fears are almost certainly overdone, and it is quite possible that some PTAs will turn out to have a positive impact on trade integration. Still, the bottom line is that there is no clear theoretical or empirical consensus as to whether the mass proliferation of PTAs is likely to complement the multilateral system or undermine it. This is far from reassuring given that the world is about to charge off even further down the PTA route.

The potential problems associated with proliferating PTAs have at least prompted a series of proposals that seek to reduce the risks. Some of these look to promoting better or cleaner PTAs, for example by making it easier for other economies to join in, or by proposing the use of less distorting types of rules of origin, or, more modestly, by encouraging the adoption of best practice guidelines for such agreements. An example of the former approach is Profes-

or Ross Garnaut's proposal for open trade arrangements that would use the simplest and most liberal rules of origin available, and which would extend membership to any country willing to meet the conditions of the agreement.<sup>8</sup> An example of the latter approach is APEC's list of best practice rules for PTAs.<sup>9</sup>

Another alternative that is often canvassed is for the WTO itself to enforce greater external discipline on its members' pursuit of PTAs, for example by tightening up the language of, and then enforcing, Article XXIV of the GATT, which is supposed to regulate such agreements. But the idea of toughening Article XXIV and/or its application is a proposal that has been around for some time, and experience indicates that making any significant progress along this route is very difficult.<sup>10</sup>

Another suggestion is to go for regional or even larger PTAs. One example of this approach would be the proposed APEC-wide free trade area for the Asia-Pacific (FTAAP). Yet another would be Japan's proposal for a regional trade agreement that would take in the 16 members of the East Asian Summit.<sup>11</sup>

At least part of the thinking behind these proposals for supersized PTAs seems to be that they would at least minimise the distortions associated with having a large number of smaller agreements, by incorporating a substantial portion of the world economy under the same rules and arrangements. Other advocates of such agreements see them as being large enough to force countries back to the multilateral system through fear of exclusion (supporters of NAFTA sometimes

8. Ross Garnaut 2004. "A new open regionalism in the Asia Pacific", paper presented at the International conference on world economy, Colima, Mexico.
9. APEC 2004. *Best practice for RTAs/FTAs in APEC: agenda item: v.2, 16th APEC ministerial meeting, Santiago, Chile, 17-18 November 2004*. [http://www.apec.org/etc/medialib/apec\\_media\\_library/downloads/ministerial/annual/2004.Par.0004.File.tmp/04\\_amm\\_003.pdf](http://www.apec.org/etc/medialib/apec_media_library/downloads/ministerial/annual/2004.Par.0004.File.tmp/04_amm_003.pdf).
10. See, for example, the discussion in World Bank, *Global economic prospects 2005: trade, regionalism and development*. A similar conclusion is reached in Sutherland *et al.*, *op. cit.*
11. On the FTAA see C. Fred Bergsten, "Toward a Free Trade Area of the Asia Pacific", paper presented at the APEC CEO Summit, Santiago, Chile, 19 November 2004.

argue that it helped convince otherwise reluctant European trade negotiators to complete the Uruguay Round). Yet many of the same issues that have caused Doha to run into the ground would appear to be almost

equally as likely to dog any such large-scale negotiations at present. To date, for example, there appears to have been little appetite on the part of several major APEC members to negotiate an FTAAP.

### ***Reforming the Multilateral System?***

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The best way to get economies to turn away from PTAs and back to the multilateral system is, of course, to increase the attractiveness of the latter. What might this entail?

While the WTO grants a say to all of its members (in principle on a one member, one vote basis), in practice the overwhelming majority of world trade is accounted for by a minority of countries: 30 countries account for almost 90 per cent of all merchandise exports and more than 85 per cent of all merchandise imports.<sup>12</sup> In other words, to deliver a meaningful result for world trade, only a subset of the WTO's membership is needed, or indeed relevant.

One implication is that it might not be necessary to take all of the WTO's members forward on a particular issue, allowing more ambitious members to press ahead with their own agendas while staying within the multilateral system. Alternatively, given the problems with large trade rounds, it might be possible to turn to single-issue negotiations. One option therefore would be a retreat from the idea of a single undertaking introduced by the Uruguay Round, whereby all the issues up for negotiation are treated as a total package. This would basically represent a step back in time, to when some agreements were negotiated that were adopted only by those GATT members that chose to be bound by them. Such optional or 'plurilateral' agree-

ments were a feature of the Tokyo Round (1973-79). However, many of these were amended in the Uruguay Round and turned into multilateral agreements, leaving only two such arrangements still operational (covering government procurement and trade in civil aircraft). Indeed, a major objective of the Uruguay Round was precisely to move away from this approach, although even post-Uruguay there are some examples to be found, such as the 1997 Information Technology Agreement.<sup>13</sup>

Placing a greater emphasis on a plurilateral approach would have the advantage of allowing those members with more ambitious agendas to advance them within the existing WTO-based framework. But it would achieve this at the cost of creating a multi-class membership structure and hence possibly losing some of the current system's legitimacy.

A second group of proposals would look to an even more fundamental reform of the multilateral system. The logic here is that the idea of reciprocity on which the current system is based, whereby domestic trade liberalisation is treated as a concession that must be made in order to purchase market access overseas, runs directly counter to the ideal of free trade, which would have countries cutting their own trade barriers because it is in their best interest to do so. This approach would therefore seek to change the foundations of the system, by re-emphas-

12. Data are for 2004. If the EU is counted as a single reporter, then trade flows are even more concentrated.

13. The Information Technology Agreement provides for participants completely to eliminate duties on the information technology products covered by the agreement. Originally signed by 29 participants accounting for 88 per cent of world trade in IT products, the agreement entered into force in 1997 after several other countries had joined. At present the ITA has 68 participants and accounts for about 97 per cent of global IT trade.

ing the benefits of domestic liberalisation and, by being more transparent about the costs of protection, reinvigorating the domestic political case for liberalisation. For example, Andrew Stoeckel has argued for an augmented role for the WTO's Trade Policy Review Mechanism to carry out economy-wide analyses of the costs and ben-

efits of trade policies, and so encourage a political constituency for liberalisation. Similarly, Bill Carmichael has stressed the importance of securing a domestic commitment to liberalisation, arguing for institutions to promote domestic transparency for trade policy along the lines of Australia's Productivity Commission.<sup>14</sup>

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### ***Conclusion: Intensive Care or the Crematorium?***

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At the time of writing, the future of the Doha Round remained uncertain. Indeed, perhaps the only grounds for optimism rested on the fact that trade rounds have come back from the brink before, and therefore that Doha might be able to repeat the trick. Either way, reform of the

global trading system now looks to be a pressing task for international policymakers. Reform is needed to take not just the Doha Round, but also the multilateral system itself, from intensive care and into the infirmary, where the recovery process can begin. Otherwise, the crematorium beckons.

14. Andrew Stoeckel 2004. *Termites in the basement. To free up trade, fix the WTO's foundations*, Barton: Rural Industries Research and Development Corporation. Bill Carmichael 2005. *Trade policy at the cross-roads*, Pacific Economic Papers No. 351, Canberra: Australian National University.

