Putting 'Humpty' Together Again: Including Developing Countries in a Consensus for the WTO

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Executive Summary

Seattle was a mess. The failure of the WTO Ministerial meeting to initiate a new round of world trade talks in December 1999 reflected several negative forces: the parties' widely disparate positions; the lukewarm attitude of governments towards further trade liberalization; and a failure of the WTO as an institution. The trust necessary to span the large differences in attitudes and interests encountered in trade negotiations was completely absent, and among the worst fractures was that between the developed and the developing countries. The latter felt completely excluded from the process in Seattle, both procedurally and because they were unable to make their voices heard in the substantive debates and preparations.

If the WTO is to recover from Seattle, it will need to bring the developing countries much more securely into the trading system. After all, developing countries comprise a large majority of WTO membership and account for an increasing share of world trade and the bulk of its growth. They feel frustrated by the difficulties of implementing the Uruguay Round agreements and by the unsympathetic attitude of the developed countries towards their aspirations for the trading system. They were reluctant to come to Seattle and the mess there made it worse. Having torn the fabric of the system, it will be impossible to put it together again without the active enthusiasm of the majority of its members. But restoring the legitimacy of the world trading system in the eyes of the majority of its members is not mere charity; rather it is a matter of self-interest for the developed countries. They still have much to gain from both the further liberalization of world trade and the disciplines that an effective WTO imposes on domestic policy discretion.

An effective coalition in favour of the trading system must be put together before starting another serious round of talks. This requires both paying greater attention to the substantive needs of developing countries and procedural reform of the WTO. We argue that the best strategy for developing countries is not to resist a Round and liberalization, but to embrace them, and focus them on their development needs. They should approach a Round with a firm view of their development priorities and seek to ensure that WTO obligations will assist in achieving them. To be plausible in the current circumstances, however, that needs real concessions from the developed world.

To balance the needs of the developing and developed worlds, we propose an eight-point plan:

1. A broad based liberalization of trade in agriculture, manufactures and services

Agricultural liberalization is a job for developed countries – particularly the EU and Japan. It calls for reducing bound tariffs from their current 50-150% to the 0-15% range, a ban on agricultural export subsidies, and cuts in domestic support. Liberalizing manufactured imports into developing countries, where tariffs alone currently average over 10%, will stimulate mutual trade and provide 'specie' with which to 'buy' other concessions from developed countries. Among the latter, tariff escalation should be eliminated.

Developing countries have been reluctant to liberalize services, fearing that they have nothing to gain. This is wrong. As importers, a supply of reliable and cheap business services would aid efficiency in all sectors of their economies. As exporters of services, particularly through the temporary movement of natural persons to supply services in foreign markets, the potential gains are huge. The current success stories of developing countries exporting services, such as Indian software or Cuban health services, rely significantly on provider mobility, but this is severely constrained at present. The fundamental problem is that developed countries make almost no distinction between temporary and permanent labour movement. With suitable provision for short-term mobility of workers, many more developing countries could export services (such as construction, distribution and health and transport) to the great advantage of consumers and many businesses in the developed world.

It is premature to talk of numbers, but preliminary estimates suggest gains from 'ordinary' trade liberalization like this running into hundreds of billions of dollars per year.

2. Credit for past unilateral liberalization

Developed countries should treat part of developing countries' recent unilateral liberalizations as something to be reciprocated by their own concessions in a round. This would re-assure developing countries, who feel that they often have to 'pay twice' for developed country liberalization, and recognize that developed countries have also been beneficiaries from unilateral reforms. For their own sakes, however, developing countries should use credit not to avoid making cuts in actual tariffs, but as a means of encouraging deeper liberalization in the developed world.

3. Re-inventing special and differential treatment for the twenty-first century

This would recognize developing countries' needs for cheap and effective institutional routes to implementing liberalization and allow them greater procedural flexibility in some rules areas. Old style special and differential treatment, which just let the developing countries off many GATT obligations and offered extended adjustment periods at random, should be junked.

4. Legally binding promises of technical assistance

Where developed countries persuade developing ones to accept a policy with promises of technical assistance in implementing it, these promises should be legally binding. In the past, such assistance has not always been delivered *ex post.* Perhaps the developed countries should pay for the assistance when it is agreed, by depositing earmarked funds in the WTO.

5. Honour the agreement on phasing-out of the MFA

Developing countries need to make plain that there will be no settlement to the next Round if the textiles and clothing agreement negotiated in the Uruguay Round is not implemented in good faith. That means that quantitative barriers must be removed and not replaced by alternative restrictions such as anti-dumping duties. The intention, floated in Seattle, of a three-year Round was never very plausible, but developing countries have a clear interest in postponing its conclusion well into 2005, when the MFA quotas have all been off for some time.

6. Keep labour and environmental standards off the agenda

The fear that adding labour and environmental clauses into the WTO would foster protectionism is well grounded: think how anti-dumping measures have been abused. Labour discussions should be moved to the ILO, and if the latter's lack of teeth is a problem for developed countries, let the agenda include discussions on enforcement.

7. Drop investment and competition policy

These will certainly be contentious and they will divert political and bureaucratic attention from the more straightforward and rewarding business of trade liberalization. Comprehensive rounds are desirable because they increase the opportunities for trade-offs, but in the aftermath of Seattle it seems better not to burden developing country administrations with threatening and complex issues. The last thing they need is the external imposition of another set of institutions that they cannot operate effectively.

8. Dramatically improve the governance of the WTO

This clearly involves strengthening developing country capacity to deal with trade issues and with the WTO. In the WTO itself, more streamlined governance would be desirable. This would facilitate pre-negotiation explorations and discussions, but it could not create binding agreements, which, for sovereign governments, can only be agreed by consensus.

This plan is no walkover; indeed, it will require considerable courage. Developing country policy-makers will have to tackle fundamental institutional problems and confront domestic protectionist interests. Developed country leaders will need to get over their blind insistence that their own models of policy and institutions are the only acceptable ones. They will also need to confront their own interest groups in order to make the significant concessions necessary to ensure that, in the long-run, the trading system survives intact and that all countries can benefit from it.

Introduction

Humpty Dumpty sat on the wall

Humpty Dumpty had a great fall

All the King's horses and all the King's men

Couldn't put Humpty together again

By common consent Seattle was a mess. The acrimonious failure of the Ministerial talks to initiate a new round of world trade talks in December 1999 represented a severe setback for hopes of harnessing the trading system as a stimulus for economic growth and development. It arose from a confluence of several negative forces: the parties' widely disparate positions and interests on most issues; the generally lukewarm attitude of governments towards trade liberalization; and a failure of the governance of the WTO as an institution. The high level of trust that is necessary to span the large differences in attitudes and interests encountered in trade negotiations was completely absent. The fractures ran in several directions, but prominent among them was that between the developing and the developed countries. The developing countries felt completely excluded from the process in Seattle, both procedurally and because they were unable to make their voices heard in the substantive debates and preparations.

Many policy-makers recognize that the job of creating a liberal world trade order is not complete, and have expressed a welcome determination to get the 'WTO-show' back on the road. High on the list of their priorities for repairing the damage done at Seattle must be to cement the developing countries more securely into the trading system.[1] After all, developing countries comprise a large majority of WTO membership and account for an increasing share of world trade and the bulk of its growth. Over the last few years developing countries have become increasingly frustrated with the operation of the WTO and the trading system in general. Having largely adopted the 'new' philosophy that openness is good – indeed vital – for development they found the agreements of the Uruguay Round less satisfactory than they had anticipated, and the uncompromising behaviour of major developed countries discouraging to any hopes that they may have had that the system would be sympathetic to their problems.

Given these frustrations, it was always going to be a challenge to bind the developing countries into a new round of trade talks. Now, however, it is both more challenging and more important. It is more challenging in that Seattle revealed so starkly the narrow

[1] Pascal Lamy, Trade Commissioner of the European Commission, recognized this in a recent letter to the *Financial Times* (31 January 2000) in which he wrote of developing countries' 'deep frustration and resentment', and noted that 'rebuilding confidence in the WTO is critical'.

self-interest that motivated the developed countries and that, having once missed an existing opportunity to strike a bargain, it will become more expensive to construct a new one. The failure in Seattle has reinforced the critics of open trade within the developing countries and moved even sympathetic comment towards the view that developing countries' needs in the WTO are for exemptions and exceptions to liberalization rather than the opposite. This makes bringing developing countries back into a system whose main virtue was to foster openness both politically and intellectually difficult. The concessions that the developing countries will initially seek as the price of return will tend to undermine the system's usefulness as a tool of development. The challenge will be to encourage good policy while at the same time winning the political support necessary to preserve – or perhaps, restore – the standing of an institution that helps governments to take beneficial but unpopular decisions.

It has also become more important to bring the developing countries actively into the coalition to preserve the trading system, because, having torn the fabric of the system, it will be impossible to put it together again without the active enthusiasm of the majority of its members. Rebuilding the legitimacy of the world trading system in the eyes of the majority of its members is not a matter of charity or development assistance, however, but one of self-interest for the developed world. The latter still has much to gain from both the further liberalization of world trade and the effective presence of the WTO in domestic political debate. The main contribution of the GATT (now WTO) system was to fortify governments against the narrow and sectoral interests of their domestic pressure groups. Any observer of the way the European Union kow-towed to its farm groups or the US government to its labour groups would conclude that this medicine is as much required in rich as in poor countries.

The timetable for resuming serious multilateral trade liberalization is uncertain, but in all probability governments will want to try again at, or before, the WTO's fourth Ministerial Conference in 2001. Thus the next year offers a respite during which the various pieces of the coalition for the trading system can be put back together. We argue that, in terms of the developing-developed country fracture line, this will require both greater attention being paid to the substantive needs of developing countries and procedural reform of the WTO. The latter is required to ensure that developing countries are no longer excluded from negotiations either formally, as (unforgivably) happened in Seattle, or informally through lack of voice in Geneva.

This Paper is about how to start to repair the system by addressing the substantive needs of developing countries. Even more so than before Seattle, any forthcoming round of trade talks must be a 'Development Round'. It does not argue for taking the line of least resistance by diluting WTO disciplines in line with the demands of many of its critics, but for the aggressive pursuit of those elements of the system that *genuinely* assist development coupled with the removal of other distractions. We present a realistic and balanced blueprint for negotiators from developed and developing countries, including significant trade liberalization for both (and from both), along with institutional and rules reforms. Its main elements are summarized in Box 1 (below).

The recommendations in Box 1 are no walkover; indeed, they will require considerable courage. Developing country policy-makers will have to tackle fundamental institutional problems and confront domestic protectionist interests. Developed country leaders will need to get over their blind insistence that their own models of policy and institutions are the only acceptable ones, and also confront their interest groups in order to make the significant concessions necessary to ensure that, in the long-run, the trading system survives in tact and that all countries can benefit from it.

BOX 1.1 A shopping list for the Development Round

Liberalize, liberalize, liberalize

– Agriculture
- slash bound tariffs
- ban export subsidies
- abolish subsidies that boost farm output

– Manufactures
- reduce bound tariffs, especially in developing countries
- eliminate tariff escalation and remove tariff peaks, especially in developed countries

– Services
- enhance access for foreign services suppliers to developing country markets
- liberalize developing country domestic regulations to encourage competition and enhance social goals
- liberalize the movement of 'natural persons', especially to allow developing country workers temporary entry to developed country service markets

Give credit for developing countries' unilateral trade liberalization

Re-invent special and differential treatment for the twenty-first century

- judge rules changes against a development yardstick
- allow greater procedural flexibility for developing countries

Make promises of technical assistance legally binding

Honour the agreement on the phasing-out of the MFA

- ensure textiles and clothing trade fall completely under the GATT-disciplines
- allow only extremely limited use of safeguards on textile and clothing trade

Labour and environment standards

- shift issues of labour standards out of the WTO and into the ILO
- permit environmental trade policy *only* when multilaterally sanctioned by an appropriate multilateral environmental agreement

Drop investment and competition policy off the agenda

Governance of the WTO

- strengthen developing countries' capacity to deal with trade and WTO
- stream-line WTO governance to facilitate pre-negotiation discussions but recognize that consensus is the only basis for binding agreements

1. Liberalize, liberalize, and liberalize [2]

The first and main requirement for developing countries is a thorough-going trade liberalization covering agriculture, manufacturing and services: not only liberalizing access to developed country markets, but to each others markets and, most importantly, each opening up its own market.

1.1 Agriculture

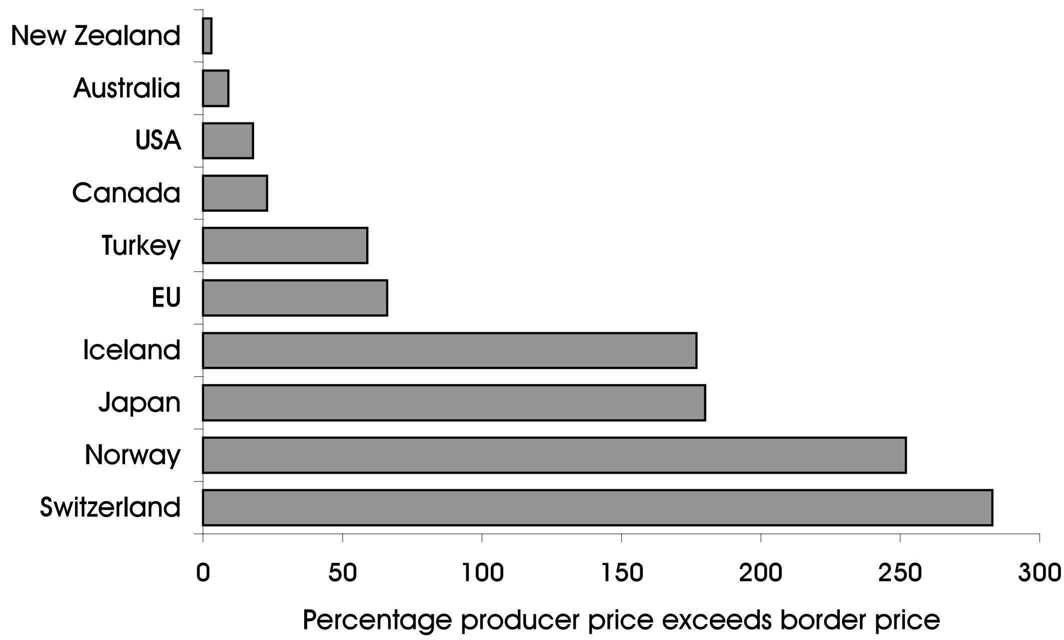
The Uruguay Round made good progress in bringing agriculture under regular GATT disciplines: the next round must continue the process by removing the remaining non-tariff barriers (NTBs) unique to agriculture and then liberalizing trade by reducing tariffs. At present, barriers to trade in agricultural products are several times higher than barriers to trade in manufactures: OECD estimates total levels of support at 18% of the value of output in the USA, 66% in the EU, and an outrageous 252% and 283% respectively in Norway and Switzerland (see Figure 1.1 below). Although the shares of agriculture in total world trade and production are much smaller than those of manufactures, the cost of agricultural protection to the world economy roughly equals that of the latter. For most farm products and countries, actual tariffs provide no less protection than did the non-tariff import barriers of the late 1980s and early 1990s. Tariffication of agricultural trade in the Uruguay Round has made restrictions to imports more transparent, but the degree of 'water' currently in those tariffs makes most bindings ineffective. Binding tariffs at such a high level allows countries to vary their actual (applied) protection as they wish in response to changes in domestic and international food market. This means that there has been little or none of the reduction in fluctuations in international food markets that tariffication was expected to deliver. Reducing bound tariffs from their current 50-150% to the 0-15% range that characterizes manufactures is one of the major challenges, and one of the major potential benefits, ahead.

Several non-tariff barriers (NTBs) are more-or-less unique to agricultural trade, e.g. tariff rate quotas, export subsidies and various forms of domestic support measures. The pernicious 'tariff-rate quotas' are when (mostly developed) countries reduce the tariffs charged on a given level of their imports of various commodities in order, ostensibly, to guarantee a (negotiated) minimum level of import penetration. In fact, the allocation of these (low-tariff) quotas across suppliers is arbitrary and biased, resulting in inefficiency (high cost suppliers got the quotas), favouritism, political pressures and, sometimes, under-shooting the minimum because the quotas go to countries that can't supply. It is estimated that rents from tariff rate quotas on agricultural imports to OECD countries

[2] This and subsequent sections draw heavily on the work of colleagues. Rather than pepper the text with references, we include brief Bibliographic Notes on p. 23.

amount to $25 billion per year based on 1996 international prices. Expanding tariff rate quotas – i.e. the quantity of imports permitted at low tariff rates - will reduce their importance, increase competition and lessen the impact of the excessively high above-quota tariffs.

Figure 1.1 Agricultural support in OECD, 1997



Source: Table 2 in Anderson, Erwidodo and Ingco (1999)

Export subsidies undercut local producers in developing countries but are not much help to consumers because they are unreliable and likely to disappear as soon as world prices rise. Nothing less than a ban on agricultural export subsidies is needed, bringing agriculture into line with non-farm products under the GATT.

A whole raft of domestic support measures expands agricultural output in developed countries (generally the less efficient producers), wasting resources there and undermining efficient production and income generation in developing countries. For both efficiency and equity, the general level of domestic support needs to fall further. The so-called 'blue box' (a set of subsidy policies permitted by the Uruguay Round even though they were known to boost farm output) needs to be abolished. The criteria for the 'green box' (for subsidies that do not affect output) ought to be tightened up in order to reduce the loopholes that currently still permit output-increasing subsidies.

Agricultural liberalization is predominantly a job for developed countries – particularly the EU and Japan, who went to great lengths in Seattle to shift the focus elsewhere by enlarging the agenda. If achieved, developing country suppliers of temperate products will see large export (and income) increases, and there will probably be some spill-over to tropicals. Agricultural growth is strongly pro-poor and so the benefits will flow to where they are most needed. World prices of agricultural products will probably rise with liberalization, but this is not likely to be a major problem even for net food importing developing countries. First, the increases are likely to be only a few percent, compared with regular fluctuations measured in tens of percent. Second, many developing countries currently import food only because of their own distortionary policies. Protection in the manufactures and services sectors bestows a significant anti-agriculture bias in many low- and medium-income countries, making it more difficult for them to benefit from the agricultural trade reform in developed countries. For such countries economic theory shows that, even though the prices of their imports rise, world food price rises make them better off: they are initially losing welfare by unnecessarily stimulating food imports and the price rise curtails that stimulus.

Developing countries have a significant stake in the process of farm policy reform. One simple model of the world economy suggests that a reduction of 40% in the barriers to world farm trade will generate economic gains of at least $15 billion per year by 2005.[3] OECD countries are estimated to gain about $55 billion per year from the same liberalization – greater than developing countries' gains because it is mainly developed country inefficiencies that are removed by the reduction in barriers. Other estimates are of substantially higher gains for developing countries, which seems plausible given the difficulties of capturing all the complexities of agricultural policy and the extremely high rates of protection that particular agricultural products receive.

1.2 Manufactures

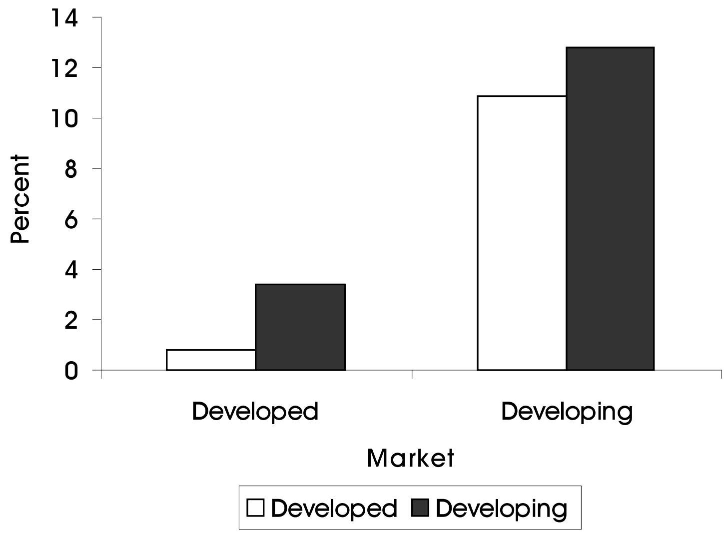
The share of manufactures in developing country exports has increased dramatically, from around 30% in early 1980 to over 70% in 1995 and probably approaching 80% by 2005. Manufactures trade between developing countries has also been increasing steadily over time. About 40% of developing country exports of manufactures went to other developing countries in 1995.

Figure 1.2 (see below) shows that developed country tariffs on manufactured imports are quite low on average (1.5%), but that they impinge more heavily on exports from the developing world (3.4%) than on those from other developed countries (0.8%).

[3] These results (and all the other forecasts of the effects of future rounds) are based on computable general equilibrium models. Their absolute sizes should not be taken too seriously, and it should always be remembered that they reflect their authors' assumptions and approximations. However, provided they are carefully conducted and honestly reported, the results of such exercises are useful in suggesting the *relative* importance of different policies and in terms of highlighting broad issues.

Moreover, within the average there are both peaks of 15, 20 or 25% on goods in which developing countries are competitive and significant escalation. Escalation means that tariffs rise with the degree of processing, which makes it more difficult for developing countries to export processed goods. There are also some residual non-tariff barriers of various sorts. Thus there are significant areas such as steel, leather, footwear, textiles and clothing in which developing countries can benefit from important concessions from developed ones.

Figure 1.2 Average tariffs on developed and developing country exports of manufactures



Much more important, however, are developing countries' own barriers to manufactures. These average 10.9% on developed countries' manufactured exports and 12.8% on developing countries' (see Figure 1.2 above). Liberalizing these will have immediate consumer gains in developing countries and longer-term efficiency benefits as industry adjusts. It will stimulate growth in trade between developing countries and also, in the present context, provide specie with which to 'buy' other concessions from developed countries in the negotiations.

Developing countries stand to make substantial gains from further liberalizing manufactures trade, much larger, in fact, than those accruing to developed countries ($52 billion vs. $18 billion per year from a 40% reduction in barriers). This imbalance reflects a combination of the facts that, facing higher tariffs to start with, developing countries get larger absolute improvements in access to exports markets, and that starting with much higher tariffs of their own, developing countries get much greater efficiency gains from a given proportionate liberalization.

1.3 Services

The service sector is far larger than manufacturing or agriculture and almost certainly more protected. Developing countries have been reluctant to liberalize services, fearing that they have nothing to gain. This is wrong. As importers a supply of reliable and cheap business services would aid efficiency in all sectors of their economies, while consumers would stand to gain from liberalization of some other services. Moreover, importing services (or allowing foreign firms to establish at home) is quite consistent with prudential or quality regulation.[4] However, liberalizing foreign supply is not sufficient. Developing countries need also to liberalize domestic services markets at the same time. This should entail improved rules and domestic regulations – first to encourage economic efficiency by remedying market failures and, second, to pursue social goals.

Policy-makers should emphasize competition rather than ownership when negotiating services markets because larger welfare gains arise from increased competition than from simply changes of ownership: increased competition brings benefits through both allocative and internal efficiency. Liberalizing imported services markets by eliminating explicit trade restrictions and implicit regulatory barriers to foreign services can increase effective competition strongly, and this is clearly business for a round of trade talks. But reforming the regulations governing domestic firms can often go further and this too can be aided by placing it in an international context. Developing countries should use strengthened multilateral disciplines on domestic regulations to promote and consolidate domestic reform, as they did in telecommunications over the 1990s. Also, such disciplines give developing country exporters the means to address regulatory barriers to their exports in foreign markets.

However, there are limits to what can be achieved at multilateral level: multilateral trade rules are designed to ensure market access, rather than directly to promote competition. Thus, in parallel with any trade talks, developing countries should strengthen their purely domestic rules to encourage economic efficiency in remedying market failure and pursing social goals.

Developing countries also have as much to gain as exporters of services, particularly with regard to the temporary movement of natural persons to supply services in a foreign market. Under the General Agreement on Trade in Services (GATS) (negotiated in the Uruguay Round) the liberalization commitments were very limited in this area. Of the four modes of supply recognized by the GATS – cross-border supply, consumption

[4] Note that liberalizing the provision of banking services is *not* the same as liberalizing capital flows.

abroad, commercial presence (i.e. foreign direct investment), and presence of natural persons – the last attracted the fewest commitments. Those that were made were of very limited sectoral coverage and were conditional on things such as the length of stay, the state of the labour market and the 'economic need' for imports. Even where commitments were made to freeze existing regulations, the latter are so obscure that it is unclear what has been gained.

Almost inevitably, the least liberal commitments (or the complete absence of commitments) are in sectors or areas where developing countries have a comparative advantage, i.e. in low- and medium-skill related labour-intensive activities. The commitments that have been made generally have only limited significance for developing countries because they refer almost exclusively to higher level of personnel who are typically associated with commercial presence in capital intensive activities. If the GATS is to effectively promote trade in services and address the interests of developing countries, the industrial countries must negotiate in *good faith* in this key area of the 'movement of natural persons'.

Four classes of continuing constraints on the movement of natural persons need to be negotiated:

1. Immigration related regulations concerning the entry and stay of service providers.
2. Regulations concerning the recognition of qualifications, work experience and training.
3. The differential treatment of domestic and foreign personnel.
4. Regulations covering other modes of supply, particularly commercial presence, which indirectly limit the scope for the movement of natural persons.

The fundamental problem is that there is no separation between temporary and permanent labour movement, even though GATS is meant to cover only temporary labour flows in services. At present, the temporary movement of labour comes under the purview of immigration legislation and labour market conditions. In a new round it will be important to separate temporary movement of labour from permanent movement of labour and provide suitable provision for short-term mobility of workers. The multilateral discussions should also aim at sector-specific commitments (especially in sectors such as professional and business services) and on expanding the categories of service providers, to remove the current bias towards higher level personnel. It is important to include middle- and low-skill level providers and make the commitments more relevant to the interests of developing countries with capacity in these categories.

All in all, with suitable provision for *short-term* mobility of workers (*not migration*), developing countries could greatly expand the supply of services to developed country consumers and businesses. With greater liberalization, many more developing countries could export services such as construction, distribution, environment and transport. The current success stories of developing countries exporting services, such as Indian software or Cuban health services, rely significantly on provider mobility. Indian software exports grew from $225 million in 1992-3 to $1.75 billion in 1997-8.[5] Despite the growing importance of cross-border electronic delivery, the movement of natural persons remains a critical part of the equation. In the early 1990s, the US government introduced rules that obliged foreign workers to acquire temporary work visas (H1- B visas). The number of visas issued during a year was limited to 65,000. In 1998, in response to mounting labour shortages experienced in the information and technology sector, the US relaxed its temporary visa requirements for skilled workers and the annual visa cap was raised to 115,000 for both 1999 and 2000. This shows the sort of advantages that developed country producers perceive in relaxing the movement of natural persons and suggests the sort of allies that developing countries could find in pursuing this issue.

Figure 1.3 Gains from 40% reduction in trade barriers

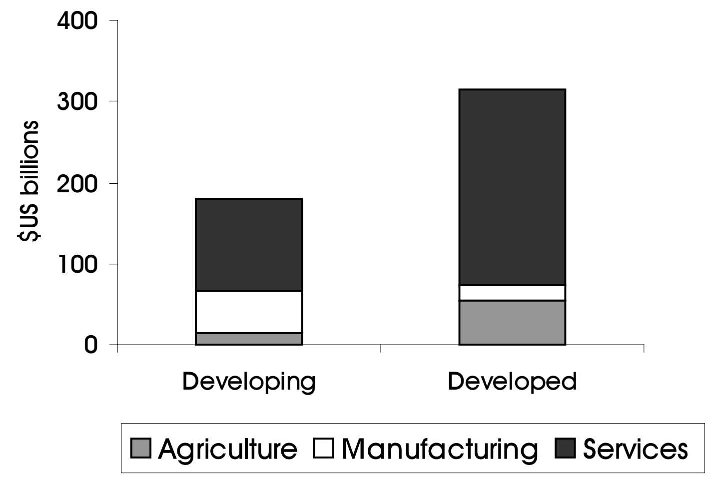


Figure 1.3 (see above) summarizes one set of estimates of the benefits of reducing world trade barriers by 40% in 2005. It suggests significant gains for both developing and developed countries of roughly $180 billion and $320 billion respectively. One should certainly not take these figures literally – especially in services – but they are an indication that there are still significant benefits to be reaped through simple trade liberalization. They also suggest the relative importance of services markets in both developed and developing countries and the familiar result that trade policy reform mainly benefits the countries doing it rather than their partners. Developed countries gain more than developing countries from agricultural liberalization because they have furthest to go: developing countries gain more than developed countries from manufactures liberalization for the same reason.

[5] It is reported that it will reach $6.32 billion in 2000-1 (*Financial Times*, 7 February 2000).

2. Credit for unilateral liberalization

Many developing countries have liberalized their trade unilaterally since the end of the Uruguay Round, frequently lowering applied tariffs well below the rates they agreed ('bound' in WTO-speak) in the Round. They fear that such reductions will erode their bargaining power in any forthcoming talks. Developed countries must re-assure them that this is not so. They must treat reductions in bound rates (which are the subject of WTO negotiations) as concessions to be reciprocated, even if the bindings do not come down to the rates actually applied and hence do not imply an immediate reduction in the tariffs charged on the ground.

Reductions in bound rates are valuable even if they do not immediately lower applied rates because they remove uncertainty: they lower the maximum legal tariff. Besides, by offering credit, developed countries will help to foster further unilateral liberalization, which, in the past, has benefited developed countries as well as the developing countries undertaking the liberalization. For their own sakes developing countries should not use credit to avoid making cuts in actual tariffs, but as a means of encouraging deeper liberalization in the developed world. If they do this making provision for credit in the Round would be both equitable and constructive as well as a useful gesture towards developing countries.

3. Re-inventing special and differential treatment

'Special and differential treatment' referred to GATT/WTO rights and privileges given to developing countries, but not extended to developed countries. It covered both special rights for developing countries to protect their domestic markets and producers, and special market access (tariff preferences) for their exports to developed countries. In the 1980s intellectual opinion on economic development shifted away from import substitution and many developing countries started unilateral trade liberalization. The Uruguay Round agreements reduced the scope of special and differential treatment, but did not completely eliminate it. Instead, they focused it on the adjustment and implementation capacity problems facing developing countries. Special and differential provisions were included in many WTO agreements, including more flexible terms such as longer transition periods to implement the agreements/rules, smaller liberalization commitments and technical assistance. Rights to preferences in developed markets were not reduced at all.

Before Seattle, developing countries were generally reluctant to contemplate a Round. Despite special and differential treatment, they felt over-burdened with implementing the Uruguay Round and insisted that, if there were a new round, they be exempt from much of its likely liberalization and new rules. In effect they were looking back towards the special and differential treatment of the past, which had tended to deflect them from trade liberalization and which, as a result, left them largely outside the GATT-system and frequently outside the huge increase in prosperity that it engendered.

Special and differential treatment has not been a constructive force in the past. Letting developing countries off the liberalization of their own barriers undermined liberal forces at home and left developing country negotiators nothing to negotiate with in the Rounds. Neither have the preferences, which developing countries have fought so hard to preserve, been a success overall. Under the General System of Preferences (GSP) or, for the EU, the Lomé Convention for ACP countries, industrial countries grant preferential tariffs to developing countries' exports. In most goods the margins of tariff preference are small because tariffs are low in industrial countries. Where they are not small, the preferences are constrained either quantitatively (formally or informally) or by stringent rules of origin and a threat of graduation (i.e. that the exporter has become too effective to be treated specially). The complicated procedures of the rules of origin cost poor country exporters dearly in terms of paperwork. In certain areas where developing countries have comparative advantage they may have no preferences at all; for example, the USA's GSP excludes clothing.

In the few cases where preference margins are material, they are no basis for investment and development because they are insecure.[6] Preferences teach developing country negotiators to focus on short-term quasi-rents (i.e. pocketing the revenue from the tariffs they have been let off while the concession lasts) rather than to focus on the long-term needs of assured access for commercially viable products. It also opens them up to pressure on unrelated issues such as labour standards. It is for the best interest of developing countries that they stick with the basic rules of trade liberalization – non-discrimination (most favoured nation and national treatment), binding tariffs in all sectors and cutting bound tariffs through negotiations.

However, there is still scope for a new form of special and differential treatment that enhances effective liberalization rather than stymies it. This would recognize the genuine differences in institutions and objectives between developed and developing countries and tailor liberalization and new regulations to these. Thus, for example, if future trade talks introduce measures that genuinely require more difficult or more costly transitions for developing countries, these should be recognized in terms of longer periods, more flexible rules, and in specific offers of technical assistance. To prevent longer transition periods from being used merely to put off adjustment, however, developing countries should agree to phased transitions with monitorable mileposts, so that both the international community *and their own citizens* can see that adjustment is actually occurring.

[6] Conditions such as rules of origin, eligibility (if a country becomes competitive in certain products, GSP status granted by the USA may be withdrawn), renewal and graduation are attached to all GSP schemes (see Whalley (1999)).

Special and differential treatment might also be extended to some rules changes on a more permanent basis. The Uruguay Round included commitments to modernize trade procedures such as import licensing and customs valuation, and to reform areas of regulation which relate to domestic business environment. Given the disparities in negotiating power and resources, negotiations on rules tend to reflect the agenda of rich countries and their specific interest groups. Therefore, the existing WTO rules are in large part a codification of the rules and institutions in developed countries. They work well there, but not necessarily so well in poor countries.

In some cases the requirements of the WTO agreements, while not harmful *per se*, are not well suited to developing countries' development objectives. One example is the customs valuation agreement. Customs valuation is only one part of the customs process. Given the initially weak situation in many developing countries, changing the valuation method without overall customs reform is not likely to improve the predictability of the customs process, nor to mitigate significantly the possibility of using the customs process as a non-tariff barrier. For example, nearly all developing countries face difficulties over customs administration, but inappropriate valuation methods rank far behind things like corruption, lack of codification and mechanization, and unreliable timing. Thus the WTO Customs Valuation Agreement, which prescribed how imports are to be valued, is more or less irrelevant for many developing countries. A global regime more sympathetic to an honest and verifiable reference price system (which is banned under the current Agreement) would be better. It would leave over more developing country resources, and effort, for reforms that are more important. [7]

In future, rules changes should be judged against a development yardstick. Many reforms would pass the test and apply to all WTO members, but some would not and would need to be modified for poor countries. In many of the new negotiating areas on domestic regulation and institutions, there is no developing country trial and error experience from which to infer the development implications of multilateral rules. WTO rules should allow for such experimentation and learning. Creating such flexibility, while at the same time preserving predictability and transparency for traders would be a useful form of special and differential treatment for developing countries in the next round. One approach might be to allow greater (although not complete) procedural flexibility, while requiring that outcomes be fair. Criteria for assessing the fairness of outcomes and procedures without overburdening the Dispute Settlement process would need to be developed. Perhaps, for example, the right to use unorthodox procedures could be made conditional upon agreeing to a fast-track administrative review of contentious policies.

Rule-mandated reform will cost money and many developing countries will need extra funding and technical assistance (see below). However, the question of where to spend

[7] Finger and Schuler (1999) characterize the customs valuation agreement as addressing only a small proportion of developing countries' customs problems, providing no remedy over the remainder, and being inappropriate in the areas it does cover.

the limited resources deserves attention. If the development dimension is absent in the rules, money spent on implementing them might be wasted. For example, an extra dollar in most poor countries might be more productively spent on health care or education than on implementing intellectual property rules.

4. Binding technical assistance

For the many new areas of regulation introduced in the Uruguay Round effective implementation and compliance involves heavy investment. For example, the introduction of legislation, the creation of administrative bodies, staff training, equipment, buildings, etc, all cost money. It is estimated that it averages $130-150 million per country to meet the WTO rules in just three areas (intellectual property, sanitary and phyto-sanitary standards and customs valuation). This exceeds an entire year's development budget in many of the least developed countries!

The Uruguay Round Agreement is replete with promises of technical assistance to developing countries to help them undertake the agreed reforms, but most of these promises were not binding and many have not been delivered. Since the developing countries clearly saw such assistance as a quid pro quo for certain agreements/concessions, this is hardly fair. Neither is it efficient. Given their limited human resources and institutional capacity, many developing countries, particular the poor and small ones, have significant difficulties implementing the Round and integrating themselves into the world trading system. Solving these difficulties is likely to benefit both the countries themselves and their trading partners. The next Round needs to find a means of making promises of technical assistance binding – justiciable and subject to complaint/retaliation. One solution might be to establish a fund from which developing countries could draw agreed amounts by right. The Trade and Development Committee of the WTO may be authorized to manage the fund.

The next question is what kind of mechanism should be put in place in order to ensure effective use of resources. The current model, the Integrated Framework,[8] may form a suitable basis, although, in truth, it has several shortcomings. It involves six international agencies – WTO, IMF, World Bank, The International Trade Centre (ITC), UNCTAD and UNDP. The process begins with the identification of needs by each country, followed by a joint response to those needs by participating agencies. Each country develops an integrated assistance plan. The Integrated Framework seems a sound approach as it is demand-driven and avoids overlapping among international organizations. However, its effectiveness depends on the follow-up and co-ordination among the participating international agencies; the quality of the needs assessments at the start; and the

[8] This was developed in 1997 as part of the High-Level Meeting on Integrated Initiatives for the Least Developed Countries' Trade and Development (for more detail see www.idcs.org).

resources which are available to meet these needs. In fact, all these aspects are causes for concern, especially the last, given that no new resources were earmarked for the programme.

The European Commission has suggested that, when an agreement is being concluded in the WTO, it is accompanied by a framework to support its implementation in light of country specific requirements. This would require the definition of steps for implementation plus each developing country member's identification of its own specific requirements. The Commission argues that as technical assistance needs are so country specific, depending, for example, on the level of development, existing regulations and the trade regime of the country, technical assistance requirements would not be laid down in the agreement itself, but would somehow be 'identified in relation to the agreement'. We agree that developing countries clearly should not sign any agreement until their requirements for implementing the agreement are known. But we would also argue that if they need assistance to make implementation possible or desirable, neither do they sign until these needs are recognized, and the resources to meet them have been identified and guaranteed by developed country members. Given that many developing countries lack human resources and have little experience in international negotiations or in administering policy in the new areas of the WTO, they will need assistance in identifying their needs. This assistance might include independent specialist help during negotiations, but should also extend to strengthening developing countries' capacity to analyze their interests in proposed international trade rules.

Overall, the message here is clear. As other negotiated commitments are binding, technical assistance commitments should be binding too.

5. Genuinely phasing out the MFA

The Uruguay Round agreed to phase-out the quantitative restrictions on textile and clothing trade by the end of 2004. The liberalization was hugely end-loaded, with the result that there is due to be a huge bonfire of controls on 31 December 2004. Given developed countries' poor record in liberalizing this sector in the past, and given China's likely accession to WTO by then, one can legitimately doubt whether the bonfire will catch alight at all. One even hears rumours of plans for mass anti-dumping or safeguards actions in 2005, so that even if textiles and clothing trade is returned to GATT-discipline there is little effective liberalization. This would be a massive, and wholly unacceptable, breach of faith.

Ideally the developed countries should pre-empt such worries by making public commitments that this will not happen – perhaps agreeing to limit safeguards in clothing to, say, a maximum of five tariff headings. But in the meantime, developing countries need to make plain that there will be no settlement to the next Round if the textiles and clothing agreement from the last is not implemented in good faith. The intention, floated in Seattle, of a three-year Round was never very plausible, but developing countries have a clear interest in postponing its conclusion well into 2005, when the MFA quotas have all been off for some time.

6. Avoiding labour and environmental standards

The fear that labour and environmental clauses in the WTO world foster protectionism is well grounded: think how anti-dumping has been abused. Moreover, if the WTO legitimized trade sanctions for social or environmental reasons, the WTO Appellate Body could become, de facto, the final arbiter of such standards. This seems both undesirable per se and potentially so divisive that WTO's traditional role in fostering trade could be undermined. Developing countries are right to resist these additions to the WTO competence absolutely for labour standards and nearly absolutely for the environment. If they have to give ground on the latter, it should only be to consider multilateral sanctions for breaches of multilateral environmental agreements where the breaches have been identified by a large majority of the countries in the world.

One of the reasons for the Seattle collapse was Bill Clinton's call for labour standards with trade sanctions to be inserted into the WTO. Seattle failed and everybody went home. But the issue of labour standards will not go away. Rather than just being obstructive, it may be more constructive for developing countries and supportive international organizations such as UNCTAD and the World Bank to invite their developed country partners to discuss the issue in the International Labour Organization (ILO). This is a far more appropriate forum for a labour debate. The ILO's lack of teeth has made it less attractive than the WTO to developed countries, but the agenda could include discussions on enforcement and teeth. Moreover, the ILO's traditional mechanism of naming and shaming transgressors has increased greatly in effectiveness with the advent of the internet and the increased influence and organizational ability of the NGOs.

7. Dropping investment and competition policy

There is no stomach for an investment negotiation so soon after the demise of the OECD's Multilateral Agreement on Investment (MAI). The causes that led to the abandonment of the MAI – the differences between, and lack of commitment of, the developed countries – have not disappeared. Moreover, the liberalization of capital flows in general, and foreign direct investment (FDI) in particular, has been going on in many developing countries regardless of the OECD machinations. Since the MAI essentially aimed to mandate the fair and liberal treatment of inward investment, developing countries can achieve most of what it promised on FDI unilaterally. The investment negotiation should be dropped for now.

On competition policy, the chances of a successful negotiation look no better, but here developing countries could usefully seek means to manage international collusion and to control anti-dumping actions, which are, ostensibly, about predatory competition. On collusion, they might extract agreement that firms' (developed) home governments would act against export market power (a sort of positive comity). On anti-dumping, the need is for substantive reform not greater procedural complexity and it must curb not only developed but also developing countries' activities. What developing countries do *not* need is an obligation to create complex competition authorities: they will typically have the resources neither to create nor to run them. Moreover, if such organizations are to have legitimacy and operate effectively they must emerge from domestic concerns about domestic consumers, not from international concerns about market access.

Not only are investment and competition policy likely to yield little concrete progress in the next few years, but they could derail a Round. They will certainly be contentious and they will divert political and bureaucratic attention from the more straightforward and rewarding business of trade liberalization. Comprehensive rounds are desirable in that they increase the opportunities for trade-offs, but in the aftermath of Seattle it seems better to keep the agenda within fairly tight bounds in order not to overburden developing country administrations with threatening and complex issues.

8. The governance of the WTO

The disorganization at Seattle was not only embarrassing and insulting to developing country delegations: it was also dysfunctional. By excluding most of them from every negotiating session,[9] opposition to any deal was virtually assured. No provision was made even for effective informal communication. Moreover, in the Pre-Conference discussions in Geneva developing countries also were substantially ignored. On one occasion their contributions to a list of possible topics for discussion was, contrary to all previous practice and diplomatic nicety, excised by the Secretariat, allegedly at the behest of the USA.

It is clear that means have to be found of involving developing countries more effectively in the WTO without allowing pressure of numbers to allow the organization to degenerate into a mere talking shop. This clearly involves strengthening developing country capacity to deal with WTO issues – mainly, we suggest, in national capital,

[9] Negotiating sessions were restricted to thirty participants – chosen from among the largest traders in each sector. Thus some countries attended all sessions; most attended none.

where experts can review trade issues in general, rather than in Geneva. In the WTO itself a more streamlined governance would be desirable. This could be based on a smaller body with multi-country constituencies (as in the World Bank and IMF Executive Boards) or revolving membership (as in the US Federal Reserve Board's Monetary Policy Committee). However, given the high value that governments place on sovereignty and given the domestic sensitivity of trade issues, it is plain that such smaller bodies could have only exploratory and preliminary roles. Governments will accept only trade agreements that they have signed themselves (and, in many cases, have been approved by their legislatures).

The WTO Secretariat might play a more active role than previously, but it must ultimately be seen to remain neutral in negotiations. Moreover, it is developing country delegations as much as developed country ones that have kept the Secretariat so closely under the control of members in the past. Thus, there will need to be both a broad agreement between members and a much greater sense of tolerance and trust in Geneva before the Secretariat can start to explore and develop initiatives independently as a means to resolving some of the conflicts that a round will throw up.

Governance clearly requires a great deal of careful thought and analysis over the next few months. We cannot resolve the problems here, but conclude with two observations. First, the answer probably lies in creating greater capacity for technical and non-negotiating discussions to map out alternatives and probe the boundaries of feasibility. Straight decision-taking seems likely to remain based on consensus among all members. Second, while there is plainly a case for wide debate on many issues and for hearing the views of many parties, there seems little virtue in allowing non-governmental actors into decision-making or adjudication, nor, indeed, even of allowing them to observe the Council or Intergovernmental negotiating sessions. To be sure publics observe their parliaments at work first hand, but they never observe their executives.

9. Conclusions

Even before Seattle it was going to be a challenge to enthuse the developing countries sufficiently to achieve a successful round of trade talks. The WTO works essentially by consensus and so, while huge pressure can be brought to bear on small and isolated holdouts on particular issues, it is no longer possible to proceed in the face of concerted antipathy by the developing countries. In seeking to build such a consensus, Clare Short, UK Secretary of State for International Development, and Michael Moore, the Director General of the WTO christened the prospective round the 'Development Round'. Not only is development the most pressing of humanity's problems and open trade part of the answer, but this rhetoric also recognized the need for a direct pay-off for developing countries if they were to maintain faith in the system. If they lost faith and withdrew into protectionism again it would be a blow not only to the world trading system, but also to their own development prospects (Short (1999)).

In this paper we discuss how to incorporate the developing countries securely into the world trading system and make the next round a truly 'Development Round'. Building developing countries' confidence and bringing them back to WTO negotiations requires, to quote Pascal Lamy's,[10] words, 'something of substance for developing countries'. We argue that the best strategy for developing countries is not to resist a Round and liberalization, but to embrace them, and focus them on their development needs. To be plausible in the current circumstances that will need real concessions and contributions from the developed world. Developing countries should approach WTO negotiations with a firm view of their development priorities, and seek to ensure that WTO obligations will assist in the realization of development objectives. We provide a shopping list for developing and developed countries, including significant liberalization for both plus some institutional/rules-based suggestions. We recognize that each side needs to 'buy' the concessions it seeks from the other by making their own.

We also give a warning to the major developed countries of what they have to consider if they are serious about repairing the fractures inside the WTO. We emphasize a realistic recognition that developing the institutions to lock in the advantages of markets takes time and resources, and a sensitivity to the environment in which those institutions have to be developed and operate. 'Recognition' calls for resources and assistance from developed countries, while 'sensitivity' requires more flexibility in the rules parts of the WTO agreements than was shown previously. In addition, given the recent history, we shall also need some measures to re-assure developing country members of the WTO that they have a significant role to play and significant benefits to reap.

[10] Pascal Lamy, Trade Commissioner of the European Commission, *Financial Times*, 31 January 2000.

We recommend:

- A broad based liberalization of trade in agriculture, manufacturing and services.
- Giving credit for developing countries' past unilateral liberalization.
- Re-inventing special and differential treatment to recognize developing countries' needs for cheap and effective institutional routes to implementing liberalization: old styles of special and differential treatment which let the developing countries off many GATT obligations and offered extended adjustment periods at random should be junked.
- Legally binding promises of technical assistance.
- A firm commitment to liberalize textiles and clothing trade by 2005.
- Keeping labour and environmental standards off the agenda.
- Dropping investment and competition policy off the agenda.
- Dramatically improving the governance of the WTO and the organization of its meeting.

Bibliographic Note

This paper has drawn on the work of many colleagues, particularly the World Bank international trade research work and various papers commissioned by the World Bank.

Section 1.1 is based on work by Hertel, Anderson, Francois, Hoekman and Martin (1999), Anderson, Erwidodo and Ingco (1999), Elbehri et al (1999). The data on welfare gain of agricultural liberalization is from Anderson, Erwidodo and Ingco (1999), the rent of tariff quotas from Elbehri et al (1999). Section 1.2 draws on Hertel and Martin (1999). The general discussion of Section 1.3 is based on Mattoo (1999) and the discussion of movement of natural person draws on Chanda (1999). The quantitative estimates in Figure 1.3, and elsewhere, are derived from Hertel, Anderson, Francois, Hoekman and Martin (1999) and Hertel and Martin (1999).

Section 3, re-inventing special and differential treatment benefits from Wang and Winters (1997) and Whalley (1999). The discussion of rules changes against a development yardstick and allowing procedural flexibility in the WTO draws on Finger and Hoekman (1999) and Finger and Schuler (1999). The latter also provides the estimates of the costs of implementing the Uruguay Round agreements.

The EU proposal on technical assistance comes from WTO document (WTO, WT/GC/W/297).

The arguments on labour and the environment draw on Rollo and Winters (forthcoming).

Henderson (1999) provides an excellent analysis of MAI affairs.

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