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WTO: Building a Global Trading System for the 21st Century

As Pradeep Mehta’s friends and colleagues around the world celebrate his 65th anniversary, we are also celebrating that the multilateral trading system is 65 years old. Since the signing of the General Agreement on Tariffs and Trade (GATT) in 1947, its rules have significantly contributed to the coherence and stability of the international community by providing international economic agents with a framework for transparency and predictability.

The system underwent a significant revamp in 1995 with the establishment of the World Trade Organization (WTO), whose areas of work were expanded beyond tariffs to include topical issues, such as trade in services, the protection of trade-related intellectual property rights (TRIPs), a binding dispute settlement mechanism and the reform of trade in the most sensitive sectors of agriculture and textiles. In subsequent years, other issues were added to the WTO agenda, including telecommunications, information technology products, electronic commerce and financial services.

The institutional structure that was created in 1995 as a result of the Uruguay Round (UR) has served as a solid basis for global trade. Since the establishment of the WTO, international trade has seen a boost and its expansion rate for the period 1990-2008 has been six per cent on average. The rules and functions of the WTO have been of paramount importance in keeping markets open and resisting protectionism, especially in times of crisis. During the recent financial and economic crisis, the WTO responded by establishing a surveillance mechanism to track trade policy responses and restrictive measures put in place by governments.
We feared that weak recovery of the global economy and high unemployment rates would put pressure on governments to turn to inward-looking policies.

While a number of trade restrictive measures have been adopted, it is important to note that, overall, WTO Members have refrained from high intensity protectionism, reconfirming the organisation’s role as an anchor for trade policies. But the trade-restrictive measures introduced by governments since the beginning of the crisis show that there are still gaps and loopholes that members can exploit to the detriment of their trading partners. The launch of the Doha Development Round in 2001 was an attempt at correcting these imbalances and locking in and expanding members’ commitments. Over 10 years later, negotiations are stalled and the political, economic and social environment in which the WTO operates appears once again changed.

Over the past 20 years, the world has experienced a significant economic and geopolitical shift. Developing countries’ participation in international trade has risen considerably faster than world trade. WTO figures for 2011 show that their share of trade rose to 47 per cent on the export side and 42 per cent on the import side, the highest levels ever recorded since 1948. This growing share of trade is led by emerging countries such as India, China, Brazil, Malaysia or Mexico, all of which have become drivers of economic growth and are now asserting their role in global governance. These countries have made the most of their trade opening opportunities and their vibrant economies make them increasingly attractive markets for trade and investment. They are also proving relatively resilient to external shocks.

While the current crisis continues to frustrate demand and growth in industrialised countries, emerging economies recovered faster than the rest of the developed world and became sources of both demand and supply for other developing countries. It is telling that in 2009, China overtook Germany as the world’s leading merchandise exporter but more importantly, it recorded the fastest growing share of imports in 2011. The dynamism of emerging economies is shifting the axis of trade from North-South to South-South, and from West to East, with China taking up the role that
until recently had been of the US and the European Union as a major export destination.

Emerging economies’ dynamism and the level of competitiveness they have achieved, require the definition of a new equilibrium in international trade relations. As the gap between developed and emerging economies narrows, it requires a new balance of rights and obligations, of contributions between countries at different levels of development. Developed countries are growing more reluctant to make concessions to emerging economies that are in direct competition with them. On the other hand, developing countries are reluctant to accept much higher levels of commitments while they still face development challenges. This dichotomy is proving a hard challenge for the trading system and is stalling progress in multilateral negotiations, much as it is stalling progress in climate change or on the quota and voice within the International Monetary Fund (IMF).

The world is also witnessing an emerging trend in international trade relations: the geographical expansion of global value chains. This phenomenon has emerged from a changing demand structure that leads firms to locate various stages of their production process in the most cost-efficient markets through outsourcing and offshoring. The integration of production and trade networks finds its highest expression in what has come to be known as ‘Factory Asia’, where parts and components are traded across borders several times before being assembled for final consumption. The high degree of complementarity that characterises Asian economies has favoured specialisation and has opened market opportunities even for countries with narrow export bases. The emergence of China as a production hub has worked as a catalyst for the further integration of trade and production networks even beyond the Asian region, thus strengthening the interconnection of the world economy. We have moved from ‘trade in products’ to ‘trade in tasks’.

The expansion of global value chains is changing the way we think about trade. First of all, when products’ components are produced and assembled in a number of different countries, the concept of ‘country of origin’ becomes somewhat misleading. Products are more simply ‘Made in the World’. Second, with trade
in intermediate goods covering a significant share of international trade, a complementarity emerges between exports and imports. Each step of the value chain adds value to the final product, so that the competitiveness of a country’s exports is increasingly dependent on the competitiveness of its imports. In this scenario, there is no room for the traditional exports-imports opposition and protectionist measures become highly ineffective or even damaging to a country’s competitiveness.

Another important aspect of global value chains is the enhanced complementarity between goods and infrastructure and support services. The coherence of importing and exporting regulations is also one of the elements that supports the competitiveness of global value chains. In this area, multilateral cooperation is important and the multilateral trading system can play a crucial role by delivering on set of global rules on trade facilitation. Finally, to understand how global value chains work, we need to be able to analyse and measure their effects. Traditional statistics based on gross numbers on trade flows do not tell us the full story. Calculating trade flows on an added-value basis and grasping the real size and magnitude of domestic inputs, value addition and therefore employment is important to help explain the complexity of international transactions and stir trade policies—and trade politics—in the right direction.

Another challenge for the multilateral trading system in the 21st century is the rise of preferential trade arrangements (PTAs). The stalling of the Doha Development Round and the uncertainty it brings about has led countries to seek trade openings bilaterally or regionally. As of January 2012, over 500 regional trade agreements had been notified to the WTO, of which more than 300 are currently in force. The proliferation of PTAs demonstrates an appetite for trade opening and can be a blessing for the multilateral trading system as they can be the forerunners of further opening at the multilateral level. However, as their number increases, the risk also grows that members of different trade agreements would implement increasingly divergent regulatory systems. As the global economy becomes more integrated, regulatory divergence
poses further obstacles for businesses that seek more coherent and predictable rules that can only be achieved multilaterally.

Next to these structural changes in trade dynamics, new emerging issues—often dubbed as ‘21st century issues’—are changing the perception of international trade. As the reality of trade is decoupling from the mere consideration of exchanges in goods and services, its linkages to other areas of international cooperation are becoming more evident. Some of the issues that the WTO is being called to look upon include the relationship between trade and climate change, exchange rate policies, food security, energy policies, competition and investment.

Some of these issues have been on the WTO agenda for some time. For example, some aspects of the trade and environment debate are already addressed under the Doha Development Agenda: trade opening for environmentally-friendly technologies, the elimination of environmentally-harmful fisheries subsidies that are depleting the world’s fish stocks and greater coherence between WTO rules and Multilateral Environmental Agreements (MEAs). Other issues are starting to attract renewed attention. For example, the relationship between trade and exchange rates and the impact of trade-related measures—in particular, export restrictions and trade distorting agriculture subsidies—on food security are being raised by members in various formats.

Although some of these issues are not entirely new, their implications for the multilateral trading system are taking new forms as more challenging and complex links emerge. In this context, some observers are wondering whether the WTO should not step up its engagement in the debate about the future structure of global governance. Indeed, the organisation has achieved considerable progress since its establishment. The interest shown by acceding countries in joining the organisation speaks volumes about the value of its rules and agreements. With Russia becoming a WTO member, about 97 per cent of world trade will be under the aegis of the WTO, making it even more attractive to the present and prospective members. Even as the mere repository of trade rules, the WTO will continue to play a role in global governance,
but its relevance would be greatly diminished if it fails to keep up with this changing trade environment.

Undoubtedly, a successful conclusion of the Doha Development Round would be the best overhaul for the multilateral trading system. The issues contained in the negotiating agenda, including disciplines for trade-distorting agriculture subsidies, elimination of export subsidies, reduction of industrial tariff peaks, efficient customs procedures, further opening in services and deeper integration of least-developed countries in the trading system, are as relevant today as they were 10 years ago. These issues need to be resolved. However, currently the Doha Round is at an impasse. At the Eighth WTO Ministerial Conference in December 2011, WTO members recognised the need to strengthen the WTO and to look at innovative ways of solving the negotiating impasse without striding away from the original Doha mandate. Amongst the suggested approaches, there have been calls for a pragmatic, step-by-step approach that would deliver small but steady results, thus reinstating confidence in the multilateral trading system.

In the meantime, the WTO should reinforce its rule-enforcing and surveillance functions, where the WTO operates as a forum for the consideration of trade-related issues of interest to the members. This deliberative function is a less celebrated and underutilised aspect of the multilateral trading system, but one that can offer the opportunity for members to discuss and explore sensitive—at times controversial—issues in a non-confrontational way. This would foster understanding of the complexities of these issues while not shifting the attention away from Doha.

The WTO should also continue to press for building trade capacity in developing and least developed countries through ‘Aid for Trade’, which in reality should be renamed ‘Investment for Trade’. For many countries the trade opportunities that the WTO offers can only be transformed into realities if an investment is made through development assistance, to build trade capacity at home.

To help WTO members identify the present and future challenges that are having—or are likely to have—an impact on the
multilateral trading system, I have recently convened a Panel on Defining the Future of Trade composed of a group of trade experts from diverse backgrounds. The panel, which includes Pradeep Singh Mehta, can offer an outside perspective on what role is expected from the WTO in the 21st century. I am convinced that through Pradeep, CUTS will continue to be a leading voice for a stronger, rules-based global trading system, more attentive to the needs and aspirations of developing countries.

Inaction is not an option. For the WTO to remain relevant in the new century, it needs to keep advancing. The world of the 21st century needs a global trading system that is relevant, dynamic and comprehensive; a system that is responsive to the needs of its members and to the expectations of the world citizens that it serves; a system that contributes to development, poverty alleviation and growth through enhanced economic opportunities, a system for the 21st century that is able to lead the world out of the stalemate that it is in and reinject trust and confidence in international cooperation. Even in the 21st century, the WTO needs to be able to make a difference in the world economy for the benefit of all, especially for the poorest amongst us. “The difference between rich and poor is not wealth, but opportunity,” says Nobel Laureate Prof Muhammad Yunus. By equipping the WTO with a 21st century software, the organisation will continue to contribute to global prosperity by ensuring that the new opportunities created by a changing global context are available to all.