Whither the Multilateral Trading System? A Case for Plurilaterals

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Executive Summary

So far the WTO has acted as a constraint on the worst protectionist pressures building in the global trading system following the global financial crisis, a testament to the system's constraining power. But the combination of those pressures with fundamental changes in global economic power has implications for what countries will be prepared to concede in the context of multilateral negotiations in the future, and therefore for the shape of the multilateral trading system. Overall it appears that the current world of multilateral impasse on the trading front is likely to endure and potentially deepen if the US does not provide the necessary leadership, which seems unlikely as the US is increasingly unwilling to underwrite the costs of maintaining the global trading system whereas China is unwilling to step up to the plate in the short to medium term. Therefore, the future of the WTO's negotiating mechanism lies in plurilateral agreements negotiated under its auspices and subject to a 'code of conduct agreed to by the broader membership. These and the proliferation of trade-related discussions in other multilateral forums mean that the negotiating capacities of all countries will be increasingly stretched. Since emerging middle powers are viewed and to some extent see themselves as "representing" developing country interests, the degree of negotiating stretch will extend further than the narrow national self interest. Consequently they need to identify their core priorities in this connected set of trade-related negotiations and organize negotiating resources and coalitional formations accordingly.

Background

Most analysts of the World Trade Organization (WTO) and (discretely) many senior trade negotiators, agree that the Doha Round is not likely to conclude soon. That has serious implications, as would the Round collapsing. Nonetheless, this briefing assumes a "Doha Light" outcome[1] at some point in the future, and speculates about where that would leave the WTO and the multilateral trading system. Specifically, what are the likely contours of the WTO beyond the Doha Round; and what implications does that hold for developing countries - especially 'emerging middle powers' and the countries they ostensibly 'represent'?[2]

Economic Drivers

The WTO's underlying difficulties have economic roots in the ongoing and far-reaching structural adjustment of global economic geography, specifically the shift of economic power from west to east. These countries emergence is transforming global power relations, and causing considerable anxiety mixed with anxious optimism both in the west and the developing world.

The global economic crisis has sharpened these tensions and in some parts of the world has strengthened the backlash against unilateral economic liberalization à la 'Washington Consensus'.[3] The crisis has also prompted calls for re-regulation of key economic sectors, notably finance, and has been accompanied by huge financial bailouts of some manufacturing sectors, especially automotive. These policy measures closely followed the food crisis of 2008 which saw many countries resort to export taxes in order to retain domestic food supplies. The overall picture is one of an escalating pattern of protectionism[4] by no means confined to the developed world, encompassing *inter alia* 'buy local' government stimulus packages, subsidies to key sectors, tariff increases, and increasing resort to trade remedies. Underpinning the protectionist impulse is the accumulation of huge global economic imbalances between chronic deficit and surplus countries and associated currency alignments. The tensions this generates manifest in the trading system and raise sharp questions, particularly around exchange rate management and its impact on trade.

Global climate negotiations sharpen these underlying distributional conflicts. With growth and development imperatives at centre stage in the crisis, many in developed and developing countries alike are asking: who will pay the costs of mitigation? Will the developed world lead by example? What burden will major developing countries take on? These questions are underpinned by a 'competitiveness' agenda rooted in the underlying economic geography shift, which permeates the climate talks. Whatever is agreed in Mexico and beyond will feed back into the WTO and the multilateral trading system.[5]

So far the WTO has acted as a constraint on the worst protectionist pressures building in the system, but the combination of those pressures has implications for what countries will be prepared to concede in the context of multilateral negotiations in the future, and therefore for the shape of the multilateral trading system.

Politics

Political leadership will be essential to manage the underlying economic adjustments. The first port of call still, and for the foreseeable future, is the United States. However, the Obama Administration is confronted by a plethora of challenges, and faces capacity constraints of its own as its 'policy bandwidth' is severely stretched into the foreseeable future. Trade policy and negotiations are low on the radar screen. If and when the Administration does get around to trade policy it will encounter a hostile Congress exercised by a recent history of large current account deficits and a domestic manufacturing sector in relative decline. Furthermore, US elites' willingness to underwrite the costs of maintaining the post World War Two multilateral trading system is arguably diminishing in proportion to rising competitiveness concerns and diminishing corporate interest[6] in WTO negotiations. Therefore, it is difficult to foresee the US providing much leadership to the multilateral trading system in the absence of securing US preferences on a range of regulatory issues that may be anathema to many developing countries.

The European Union (EU) is not better placed to provide the necessary leadership. Whilst trade is a European Commission (EC) competency, the EU lacks the US's geopolitical clout. Like the US but more so it is hamstrung in the WTO by its unwillingness to substantially free up its agricultural markets, and relative lethargy on the part of corporate interests that stand to gain through opening up export markets for trade and investment.

The 'BICs' (Russia not being a WTO member and looking unlikely to join for some time) have major domestic development challenges of their own. As such they are not yet ready to play the kind of global leadership role the US traditionally has; at the same time they have a number of defensive concerns that mirror US and EU offensive interests. Those defensive concerns are echoed by a host of developing countries concerned with maintaining domestic policy space especially concerning behind-the-border regulations.

Overall it appears that the current world of multilateral impasse on the trading front is likely to endure and potentially deepen for the foreseeable future.

Implications for the WTO

Taken together these developments imply convergence towards less ambition in WTO negotiations, paralleled by acceleration of regional and bilateral talks. This is likely to be accompanied by growing recourse to WTO dispute settlement to settle a probable escalation in disputes, particularly if the negotiating mechanism remains stalled. Hence multilateral forums outside of the WTO may gain in relative importance as negotiating forums. Therefore, the WTO may be headed for a period of consolidation with the attendant risk of being increasingly bypassed by the major trading powers.

The WTO negotiating mechanism's prospects lie substantially in plurilateral agreements negotiated by like-minded subsets of WTO members.[7] This would be consistent with the current WTO practice of allowing multiple distinctions amongst members, including several extant plurilateral codes, and would have the added benefit of allowing the major trading powers – developed and emerging - to deepen rules in issues of core interest to them by avoiding the blocking power of the broader membership, thereby securing the WTO's relevance. This offers the prospect of reviving the WTO's negotiating mechanism, but for this approach to work it has to be contingent on not harming the interests of the broader developing country membership.

Therefore, it would be necessary to negotiate a 'code of principles' to govern plurilateral accords; such a code could reassure many developing countries that are nervous of having plurilateral agreements foisted upon them and could include, inter alia:[8]

1. that membership is voluntary;
2. the subject of the plurilateral is a core trade-related issue;
3. that those participating in plurilateral negotiations should have the means, or be provided the means as part of the agreement, to implement the outcomes;
4. the issue under negotiation should enjoy substantial support from the WTO's membership;
5. the 'subsidiarity' principle should apply in order to minimize intrusion of club-rules into national autonomy.

Flowing from these principles plurilateral codes should also be governed by a set of rules. These could include, inter alia, the following:

1. Only parties to the agreement could participate in WTO dispute settlement and, flowing from this, cross-agreement retaliation should not be allowed since it would reduce the incentives to join the agreement;
2. Any WTO member could participate in the negotiations on a voluntary basis subject to demonstrating sufficient capacity to implement the outcomes;

3. Provision of benefits to non-members should not be required since that would reduce the incentives to negotiate the plurilateral, but could be allowed.

Two obvious and linked dangers are that a small group of developed country members negotiates an agreement that sets the bar so high that poorer WTO members are unable to join; and that the plurilateral(s) – as happened to the Tokyo codes in the Uruguay Round – are subsequently multilateralised in later negotiating rounds via the single-undertaking. These are powerful objections and developing countries in particular need to take them seriously.

The first problem would be minimized through active participation of developing countries in negotiating the codes, especially emerging middle powers. Since they are active participants in economic globalization they also have a strong interest in defining the rules that govern it, and therefore are likely to do so. Furthermore, they have learned from the Uruguay round experience and are unlikely to simply accept agreements being foisted upon them in the context of a single undertaking – nor indeed would the majority of developing countries – as they demonstrated during the Cancun ministerial. Nevertheless, the price of policy space is eternal vigilance.

A third potential problem is that the codes would reduce the need for a single undertaking, with consequent reduction of possibilities for cross-issue trade-offs. To take one practical potential consequence, developed countries could simply ignore demands for agriculture policy reform whilst forging ahead with a code on competition policy. In this scenario the reforms to developed country agricultural policy regimes which many developing countries are pushing for may simply never make it onto the agenda.

The obvious riposte is that cross-issue trade-offs can still occur in the absence of a single undertaking. Emerging middle powers with substantial markets could withhold participation in plurilaterals in return for developed country participation in agriculture negotiations, for example. Emerging middle powers could also contemplate launching their own plurilateral negotiations, impelling developed countries to participate. This logic could even propel the membership towards the single-undertaking approach, thus obviating the need for plurilaterals altogether. In this scenario initiating plurilaterals provides the spark to reignite the WTO's negotiating mechanism.

So what issues could form the basis for an emerging set of plurilateral agreements? Two seem particularly obvious and are underpinned by dynamics emerging from the financial crisis: transparency in government procurement, and financial services. The former is already covered by a plurilateral code, so the key issue is to expand the agreement to major non-signatory trading powers especially emerging markets (including South Africa), and deepen it, on terms agreeable to potential signatories. Financial services are covered by the General Agreement on Trade in Services and its ensuing market access commitments are extended unilaterally on a country-specific basis. In the wake of the financial crisis and the many regulatory interventions agreed by G20 Leaders it may be sensible to build a WTO agenda around the work of the Financial Stability Board and IMF.

A third plurilateral agreement seems theoretically plausible, if politically fraught: investment. Since a core group of emerging market countries are now actively engaging in outward foreign direct investment (FDI) as well as being recipients of FDI, their interest in multilateral investment rules may be converging with established investors in the developed world. Underpinning this is the escalation in investment nationalism in recent years, associated with national security considerations and resource, especially food and energy, security. Even poor developing countries in Africa have an interest in enforceable multilateral disciplines provided the right balance is struck between investor obligations and rights, and host nation policy space. Whether this could be translated into a plurilateral investment code is an entirely different matter, as would be its relationship to the 1,500 or so bilateral investment treaties, but one that should not be lightly dismissed.

Beyond plurilaterals there are at least two other issues that will require attention, although it is likely these would have to ultimately be negotiated across the entire membership: environment, and exchange rates. The former is managed through a host of multilateral environmental agreements, some of which have trade implications. The big picture item is the UNFCCC process and the competitiveness agenda cited above. But the Doha round also has a process underway to liberalize trade in environmental goods and services, which could be harnessed into a plurilateral agreement as an 'early harvest' of the Doha round.

Exchange rates are much trickier, and fall under the purview of the IMF. The main protagonists are those large economies practicing flexible exchange rate regimes, particularly the US, EU, Brazil and India; and those pegging or closely managing their exchange rate regimes – principally East Asian countries and especially China. The IMF lacks an enforcement mechanism and must rely on the consent of its powerful members, who lie at the centre of the issue. Hence the WTO, with its dispute settlement mechanism, is regarded as attractive by some within the flexible exchange rate regimes 'zone'. The danger with introducing such a matter into the WTO is that it could overload the system since a case would essentially revolve around currency management and monetary policies – not exactly traditional territory for the WTO.

Implications for Developing Countries

To summarise: a number of core issues concerning global trade should move into plurilateral negotiations within the WTO, or they will move to similar groupings in forums outside of the WTO. It is likely that the negotiating capacities of all countries will be increasingly stretched, but particularly for our purposes those emerging middle powers that potentially will be invited to the high table. Since those middle powers are viewed and to some extent see themselves as "representing" regional and developing country interests, the degree of negotiating stretch will extend further than narrow national self interest since the majority of poor countries cannot engage effectively across this widening front.

Therefore, coalitional possibilities will become increasingly important, and particularly those amongst 'middle powers' and 'emerging middle powers' on specific issues. Consequently developing countries as a whole need to position themselves for the hard-bargaining that undoubtedly lies ahead.

Endnotes

[1] For the implications of such an outcome for South Africa, see Draper P 'Towards Doha Lite? Consequences for South Africa', an electronic briefing to SAIIA members, 2007, June 19.

[2] Schoeman distinguishes traditional (developed country) 'middle powers' from 'emerging middle powers'. The former are not regional hegemons, are developed, and historically have played bridging roles between the great powers (Canada and Australia are good examples) in international negotiations. The latter are major emerging markets that exert regional dominance if not hegemony. Schoeman, M. (2003) 'South Africa as an emerging middle power', in Daniel, J, Habib, A, and Southall, R *State of the Nation: South Africa 2003-2004*. Cape Town: HSRC Press.

[3] Sally R 'The Political Economy of Trade Liberalization: What Lessons for Reforms Today?' SAIIA Trade Policy Report, 18, 2007.

[4] See the collection of essays in Baldwin, R and Evenett, S (2008) 'What world leaders must do to halt the spread of protectionism', VoxEU.org and CEPR.

[5] The UNFCCC process also has implications for other multilateral institutions connected to global finance, particularly the IMF, multilateral development banks and the G20 Leaders' Forum.

[6] Mattoo A and Subramanian A 'Multilateralism beyond Doha', Peterson Institute for International Economics, Working Paper Series, 8, 2008. There are divergent views on the extent of corporate interest in the Doha round; from the standpoint of many developing countries certain US corporate interests remain strongly connected to the negotiating process and broadly determinative of US government positions.

[7] Khumalo N 'Looking beyond the Doha round: Reforming the WTO negotiating process', SAIIA Policy Briefing, 4, 2009.

[8] This discussion is based on the paper developed by the World Economic Forum's Global Agenda Council on Trade, in which the author participated. World Economic Forum (2010) Everybody's Business: Strengthening International Cooperation in a More Interdependent World – Report of the Global Redesign Initiative, PP159-166. Available at http://www.weforum.org/pdf/grs2010/GRI_Report_2010.pdf