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Multilateral Trade Regime: Conflicts between Developed and Developing Nations

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In the last fifty years, there has been a marked expansion of the multilateral trade regime—more commonly known as the World Trade Organization (WTO)—both in terms of coverage of issues and memberships. Yet even as the 6th WTO Ministerial meeting 2005 in Hong Kong finishes, there is still a raging debate as to the net benefits that developing countries gain from membership in this regime. Many in the developing world argue that different rounds of trade negotiations generated skewed benefits in favour of the industrialized countries. Still there are many who support further trade liberalization and expansion of this trade regime. This paper will shed some lights on different important issues regarding the conflicts between developed and developing countries as far as multilateral trade regime is concerned. It will also give some suggestions about the effective initiatives that can be taken by the governments of the developing countries to improve their conditions.

Field of Research: International Trade

1. Introduction

A rule-based multilateral trading system provides transparency, stability and predictability with respect to market access conditions and various other trade related issues. This system is intended not simply to promote the development of trade relations but also to foster the economic prosperity of trading partners. The preamble to the Agreement Establishing the World Trade Organization (WTO) states, “relations in the field of trade and economic endeavours should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world’s resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their [i.e. the Parties to the Agreement] respective needs and concerns at different levels of economic development”.

Like their trading partners, the developing countries view their participation in the multilateral trading system as a means of integrating into the global economy and maximizing their benefits from international trade (UN, 2004).

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But there seems to be inadequate attention given to whether and to what extent the trade regime has over-all coherence or consistency with the development goals of the countries it is intended to benefit, despite repeated policy statements by all member countries in the WTO to construct a regime that promotes development (Mendoza and Bahadur, 2002).

2. The Development of Multilateral Trade Regime

The multilateral trade regime - often referred to as the World Trade Organization – is primarily composed of the various trade agreements that serve as the legal ground rules for much of international trade today. It began in 1947 with 23 contracting parties for The Protocol of Provisional Application of the General Agreement on Tariffs and Trade (GATT). The main purpose was to lower barriers of trade among the contracting parties, mainly in the form of tariffs, and to create a forum for further trade liberalization and trade dispute settlement. In line with the liberal basic philosophy, the most favoured-nation principle, non-discrimination, multilateralism and reciprocity are the decisive fundamentals of GATT. (Engels, 1994). If we consider GATT-1947 a club, then both club membership and club rules have changed dramatically since its inception. Nine successive rounds of trade negotiations have since increased both the scope of membership in the trade regime as well as the range of areas covered within its discipline. With the changing world trade environment and a growing globalization, the GATT 1947 no longer was sufficient to regulate world trade. New areas of business were exploding, such as international investment and trade in services. In addition, the institutional structure of GATT and its dispute settlement system called for reform. In April 1994, the World Trade Organization (WTO) replaced GATT as the central institution for international trade cooperation in the world. Today the WTO has 149 member countries, with at least 30 more planning to accede.

3. The Principles of the Multilateral Trading System

The WTO Agreement contains some 29 individual legal texts- covering everything from agriculture to textiles, and from services to government procurement, rules of origin and intellectual property. Added to these are more than 25 additional Ministerial declarations, decisions and understandings which spell out further obligations and commitments for WTO members. However, a number of simple and fundamental principles run throughout all of these instruments which, together, make up the multilateral trading system. These are:

i) Trade without discrimination
ii) Predictable and growing access to markets
iii) Promoting fair competition
iv) Encouraging development and economic reform

4. Imbalances in the regime and the vulnerability of developing countries

Trade among non-equals (i.e. producers in developed vs. developing countries) can lead to different adverse outcomes such as the decimation of entire industries in some developing countries. Similarly, simply expanding the realm of free trade has, in many cases, resulted in an actual increase in poverty and environmental degradation, and in an adverse impact on women and food security across the developing world, undermining efforts to achieve sustainable human development (McCulloch ,2001). A Sri Lankan activist, when asked about free trade between developing and industrial countries, said, “It is like putting a rabbit and a tiger in the same cage."

Where it is feasible, there is clearly a justification for policies to enable the players to become more equal. For instance, there is a need to enable developing countries to enhance their producers’ ability to compete in world markets. This is especially compelling when one considers that even primary exports from developing countries still face numerous barriers in developed countries’ markets. For instance, developing country exports of chocolate to the developed countries often face tariff barriers that are up to eight times higher than those that apply to unprocessed cocoa. Such elements in the multilateral trade regime contribute to the factors that lock-in the developing countries’ comparative advantage in low value-added products, seriously impeding development efforts. (Mendoza and Bahadur, 2002)

Hong Kong trade talks declaration scripted by WTO speaks of the tired mantra and discredited rhetoric of structural adjustment, free trade, open market, investment and privatisation, precisely the language of globalization and Washington consensus prescribed by the World Bank and IMF as panacea to accelerate the economic growth of the developing countries. But the prescription is far from bringing equilibrium and balance in the existing economic disparity between the rich and poor countries. Rather, it has widened the disparity between the rich and the poor within the society exacerbating the misery, sufferings and destitution of the poor (Hannan, 2005).

5. Explosion of Trade Disputes

Since the establishment of the World Trade Organization (WTO), trade disputes between its country members have escalated sharply. An increasing number of developing countries have become involved in trade disputes, while more conflicts have arisen between the developed countries. In addition, more of these disputes have been related to non-tariff barriers and as such, have been more difficult to settle under the WTO than under its predecessor, the GATT. These developments have caused public concern about the consequences of the WTO and this has led to calls for more serious research attention (Yin and Lee, 2004). Often, one nation defends its policy as a rightful exercise of national sovereignty, while another challenges it as an unfair barrier to trade. Ideally, such disagreements have been settled by appeal to the WTO whose new dispute resolution panel hears trade disputes and determines whether national behaviour is consistent with international rules (Moon, 1998).

Until 1995, the new protectionist tariff and non-tariff trade barriers (e.g., excise taxes, quotas, “voluntary export restraints”, sanitary regulations) imposed by rich nations on the commodity exports of poor ones were the most significant obstacle to the expansion of the latter’s export-earning’s capacities. Moreover, as we have seen, many of these tariffs increased with the degree of product processing; that is they were higher for processed foodstuffs than for basic foodstuffs (e.g., peanut oil compared with peanuts), higher for, say, shirts than for raw cotton. These high effective tariffs inhibited LDCs from developing and diversifying their own secondary-export industries and thus acted to restrain their industrial expansion. It has been estimated that the net impact of trade barriers on all products reduced developing-world foreign exchange earnings by more than $100 billion in 2000. (Todaro and Smith, 2003)

In the process of implementing the WTO Agreement (of the Uruguay Round), developing countries experienced various difficulties and had increasing conflicts with developed countries on different issues like anti-dumping, intellectual property rights protection, market opening in services and in the financial industries and restrictions on subsidies. The failure of the Seattle Millennium Round negotiation in 1999 demonstrated that significant gaps existed on wide range of issues between developing and developed economies.

Moreover, when weighted by import volumes, developing countries face average manufacturing tariffs of 3.4 percent on their exports to developed countries—more than four times the 0.8 percent average tariff they impose on goods imported from developed countries (Hertel and Martin 2000). Tariffs on fully processed food are 65 percent in Japan, 42 percent in Canada, and 24 percent in the European Union. By contrast, tariffs on the least processed products are just 3 percent in Canada, 15 percent in the European Union, and 35 percent in Japan (World Bank 2002). Such tariffs are manifestly unfair and have a particularly pernicious effect on development by restricting industrial diversification in the poorest countries.

The Uruguay Round focused on the liberalization of service industries of primary interest to firms in OECD countries, such as financial services. Much less attention was given to low-skilled, labour-intensive services, in which developing countries have a comparative advantage. Therefore, progress on different development rounds has been slow and marred by disagreement over whether the evolving agenda reflects the real concerns and interests of developing countries.

Negotiations in the Uruguay Round centred on increasing market access for developing countries in protected developed country agriculture and textiles markets in exchange for trade agreements in intellectual property rights, services, and investments, all of which primarily benefited developed countries through increased rents and market access (Ostry, 2000). The idea behind this “grand bargain” was that member countries could trade off costs of one agreement with benefits gained on another. However, it was an inherently unequal exchange. While both developed and developing countries benefit from lower protection in the developed countries, agreements on intellectual property, services and investment do not unambiguously promise efficiency gains for the developing countries. In fact they generate both large wealth transfers and adjustment costs that are asymmetrically distributed (Panagariya, 1999). This raises serious questions about the net benefits for the developing countries in the multilateral trade regime.

Concerns about the use of natural resources and environment on one side and about the trade effects of environmental policies on the other are becoming increasingly prominent in trade and trade policy discussions, including those involving the WTO. Many developing countries perceive the entwining of environmental and trade issues as a threat to their sovereignty and their economies, while influential groups in industrial countries consider it unfair, ecologically unsound and even immoral to trade with and invest in countries adopting much lower environmental standards than theirs. But the environmental standards of the developing countries do tend to be lower simply because they are poorer. These countries are vulnerable to being pressured to enforce stricter standards or to facing less market access for their exports and less foreign investments from countries with stricter standards. On the other hand, effective environmental protection is not even possible for the poorer developing countries in the absence of economic development (Jahan, 2001).

6. Causes of trade disputes

Lee (2000) conducted a statistical analysis of 897 bilateral trade cases involving 45 WTO country members during 1995-99 and found the following conventional economic factors that tend to be related to trade disputes:

1. Trade disputes are positively related to trade volume. This conforms to common reasoning: The more trade a country conducts, the more conflicts and frictions it is likely to encounter. However there are some empirical exceptions. For example, even though India was the 22nd largest country in terms of trade volume, it was ranked as the 4th largest country in terms of the number of trade disputes in which it was involved.
2. A country is more likely to be involved in trade disputes if its trade volume, income and trade deficits are large and if its trade regime is less open.
3. Two countries are more likely to engage in trade disputes when there is a gap in income and their trade imbalance is large.
4. Trade disputes between two countries will be less if their trade relations are complementary.

Most countries, particularly developing countries are now dissatisfied with the progress of WTO because most of the promises of the Uruguay Round agreement to expand global trade has not materialized in practice. Particularly for developing countries, the promised expansion of trade in three key areas of agriculture, textiles and services has been dismal. Moreover, early protectionism and lack of willingness among developed countries to provide market access on a multilateral basis has prompted many developing countries to look for regional alternatives. The North-South divide which is appearing in the WTO ministerial meets is strengthening the apprehension of developing countries about the prospect of trade expansion under the WTO regime (Pal, 2004).

7. What Developing Countries Should Do?

The establishment of an open, fair, rational and transparent international multilateral trade regime that is non-exclusive and non-discriminatory will contribute to the stability and growth of regional and global trade, promote a balanced and sustained expansion of world economy and serve the interests of all parties. As developing members account for 85 percent of WTO membership, negotiations should take full account of the development level and tolerance of the developing members and leave them with necessary policy leeway in terms of special and differential treatment to implement development strategies consistent with their own conditions. Developing countries will have to reform their policies to take advantage of open markets in developed countries and strengthen regional trade.(Zamir, 2005) Moreover, they should take the following initiatives in order to progress in terms of development and stability:

7.1 Continue building alliances

Given that developing countries are a fairly heterogeneous group, building stronger and larger alliances remains one of the key challenges that they need to face. Alliances amongst several large groups of countries have flourished: the 13 countries in the “like minded group” (LMG), the 14 countries in the Caribbean Community (CARICOM), the 48 countries in the least developed countries (LDC) group, the 78 countries in the Africa, and the Caribbean and Pacific (ACP) Group are some notable examples. Furthermore, the Group of 77 countries has already demonstrated commendable unity in a host of trade issues. Such efforts need to be continued.

Furthermore, one lesson from the Doha Ministerial is that building alliances amongst developing countries may be bolstered further by building alliances with both Northern and Southern civil society organizations (CSOs). For example, the broad based support by developing countries, CSOs - and even some developed countries like Holland and Norway - for unambiguous language on the primacy of public health concerns over TRIPS clearly pushed this issue, despite initial resistance by some countries. Such “public interest coalitions” could potentially be built around issues of clear importance to the least developed countries in particular. (Mendoza and Bahadur, 2002)

7.2 Exercise leadership

Very little emphasis has been made on the “leadership deficit” among the developing countries. In order to advance the broad concerns of the developing world, key developing countries must demonstrate support for issues beyond their immediate national concerns. Arguably, this is a small price to pay, in exchange for a more unified negotiating front. Just as the United States and the European Union (EU) have taken on more of a leadership role in facilitating increased global trade, some of the larger developing countries can also play a similar role in facilitating a more balanced construction of the multilateral trade regime. In this regard, Brazil, India and China are prime candidates for this role, owing to their relative economic and political weight in their respective regions.

It is important to note that all these reforms are not only in the interest of the developing countries, by helping strengthen their bargaining positions, but developed countries should also find these reforms conducive to the construction of a more stable and legitimate trade regime, anchored in a more participatory WTO. (ibid)

7.3 Bargain more effectively

Effective bargaining may be a necessary element of international cooperation. Yet one must also recognize the inherent limitations in such an approach. Relying on such a process alone may prove quite detrimental to the balanced and complete development of a broadly beneficial trade regime.

The trade regime is currently constructed through a cross-issue bargaining process, wherein negotiators are invariably locked on to a mercantilist mindset where concessions are “traded” in the process of expanding market access or setting the rules of the game. In fact the WTO, to some extent, can be considered a market for exchanging commitments to liberalized trade (Hoekman and Kostecki 2001). The bargaining and negotiations process has the likely result of an incomplete trading regime, because the agreements and components of the trade system are being developed and bargained for in a piece-meal manner. Often, each agreement is not evaluated and developed as a self-contained and mutually beneficial arrangement. Instead one agreement - with all its flaws- is accepted in exchange for concessions in another agreement, often dealing with a totally unrelated sector.

Bargaining works best for those who have most to bargain with, immediately placing the developed countries at an advantage. North America, Western Europe, Japan, Australia, and New Zealand alone collectively accounted for 63% of world merchandise trade in 1948, and little has changed since. These same countries accounted for 66% of world merchandise trade in

2000 (WTO 2001). The results of the Uruguay Round of negotiations clearly show how the developed countries were able to extract very costly concessions from the developing countries, notably TRIPS, reforms on trade procedures (i.e. import licensing procedures, customs valuation, etc.), and reforms on regulations (i.e. sanitary standards, intellectual property law, etc.). It is therefore not surprising that the outcome was stacked heavily in favour of the developed countries. Developing countries should concentrate on the effective bargaining process that will enable them to gain more in the negotiating tables of WTO.

7.4 Increase Trading Capacity

Business, whether foreign or domestic, want a business environment that is stable and predictable, supported by transparent laws, fair competition, reliable legal systems, predictable and honest public institutions, and reliable transport and communications infrastructure.(Benn, 2005) The key economic challenge for any developing country is to become, and remain, internationally competitive. This requires a host of things: building up educational and skill levels, becoming technologically innovative, improving productivity, and managing a more open market economy. However, not everything can be done at once; nor does it need to be. It’s essential to prioritise. The key to increase a country’s ability to benefit from the opportunities arising from international trade is to get the investment climate right-to give people confidence to invest. Only then the economic misery would be diminished. Employment would be increased. Income, consumption and savings of the people would be improved. (Dev, 2005)

8. Conclusion

We must not forget that if development is the objective, then trade is the tool with which to achieve it. Developed and developing countries have to work together to achieve this goal. The governments have to serve as a helping hand in facilitating trade and maximising the benefits of market forces. Promoting growth and development, improving the standards of living and tackling poverty have to be at the heart of using trade for development purposes. One of the WTO’s biggest challenges will be to continue moving ahead with a purposeful agenda, while maintaining cohesion among a steadily growing number of members, at widely different stages of economic development.

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