

Handout # 10
Multilateral Trade Agreements

I. Preliminary

Huge expansion of trade
Some presumptions that trade is good for countries
Yet strong opposition movements to trade liberalization and globalization

- **Basic trade theories:**

Aggregate gains from trade (almost always)

Two categories of arguments:

Comparative advantage: Two countries will gain from trade whenever their relative prices of goods differ in absence of trade.

Economies of scale: Expansion of the market through trade makes it possible to attain economies of scale

Theories ignore non-tradable goods, i.e., all goods will be either exported or imported.

Distribution effects of trade: gainers and losers

By and large consumers will gain from lower prices of the imported goods. Most concerns about the different producers.

Examples:

- Oil or mineral exports, coffee/cocoa: In aggregate: beneficial for the country. Yet, as with any export, it produces an appreciation of the real exchange rate.
- Labor intensive goods for skill/capital intensive goods. Unskilled labor “rare” and skilled “abundant” in DCs, and the reverse in LDCs.

Dynamic issues, industrialization strategies and trade policies

- Problems with the primary exports model: sluggish demand, declining terms of trade, fluctuating export earnings, few linkages, weak productivity growth.
- Creating dynamic comparative advantage: Industrialization policies

II. Brief historic

Collapse of international trade ~1930s, with tariffs around 60% and retaliation

Creation of GATT (General Agreement on Tariff and Trade) in 1947.

Objective: Coordination mechanism to reduce tariffs.

Works by “round” of negotiation, 8 rounds between 1947 and 1994

By mid-1980s average tariffs in industrialized countries ~6%, but still many NTBs (non tariffs barriers). Only on manufactured goods, not on agriculture and services.

Previous to last round, the Uruguay round 1986-94 created the WTO.

Last round launched at Qatar in Nov 2001: Doha Development Round, expectedly for 3 years, with 143 - now 168 countries. Negotiation on Agricultural subsidies, reduction of discriminatory government procurement practices, trade in services; TRIPs to allow poor countries to override patent protection for health issues; TRIMs (trade related investment measures); rules regarding the use of anti-dumping.

Cancun Ministerial conference . 10-14 Sept 2003

International commodity agreements:

MFA (Multi-Fiber Agreement)

III. Basic functioning of the WTO

Trade rules

- Non-discrimination:
Most Favored Nation principle. same tariffs vis-à-vis all members
Except for regional trade agreement partners and former colonies.
Ex: Bananas war
National treatment principle: Equal tax and regulation treatment of domestic and imported goods. Ex: Tuna with Mexico.
- Toward freer trade
Agreement to cut and “bind” tariff rates (agreement on maximum rates). At each round agreement on an average tariff rate reduction in sectors. Then flexibility of countries within each sub-sector.
Elimination of quotas, except:
 - “Safeguards” for balance of payment problems
 - “Temporary escape clause relief” for specific industry facing “serious injury”
 - “Development goal” for developing countriesMajor remaining quotas on sugar, textiles (multifiber agreement).
Elimination of export subsidies, except:
 - in agriculture, under certain rules (de-coupling).
- Special provisions
Regulation of anti-dumping (similar to US rule), based on sales at price below cost. Big issue is the establishment of “costs”.
Health/safety protection: “Precautionary principle”. Countries can protect their citizens from perceived risks. Used to be that WTO had to prove the safety. Now countries have to scientifically prove the risk.
TRIPs (Agreement on Trade-Related Aspects of Intellectual Property Rights) oblige all WTO members to adopt a core set of intellectual property rights.
- Note: two US trade laws implemented by ITC at odd with WTO regulations
Countervailing duties: in response to export subsidies by foreign countries, even if no injury.
Section 301: Retaliation by US government against unfair practice by foreign government vis-à-vis imports from the US. (Retaliation ≠ WTO dispute resolution scheme)

Forum for negotiation

- Avoid trade war. WTO seen as an intermediary between countries that would engage in trade dispute anyway.
- Schedule of negotiations, “rounds”, to agree on mutual reduction of protection.
Last round Uruguay on agriculture, textile, and services. Largely perceived as having favored industrialized nations over developing countries (insufficient in ag and textile which represent 70% of their exports, services are interests of the North)
New round agreed on in Qatar: Doha Development Round, planned for 3 years
Agenda, beyond tariff reduction:
 - Negotiation on textile quotas (accelerate the scheme from Uruguay)
 - Negotiation on tariffs on ag. products (still ~ 40%)
 - Reduction with a view to phase out of agricultural subsidies
 - Discuss anti-dumping
 - No discussion on labor standard
 - Intellectual property rights (TRIPs): exception for drugs when public health needs justify it.
 - Discussion on environmental, investment, and competition issues.
 - Eco-labeling of goods
 - “Precautionary principle”
 - Extension of TRIMS (Trade related investment measures, regarding domestic content, requirement on exports matching imports). Establishment of a “national treatment principle” for FDI.
- New commodity: Pollution rights?

Platform for dispute resolution

Process:
Countries submit their complaint, and ask for talk.
If talks fail, the country can ask for a panel of trade officials to adjudicate.
If the panel finds rules have been broken, the “guilty” country is asked to amend its behavior.
It can appeal. But once appeals are exhausted, the decisions can only be reversed by consensus of all members (and not one single country as before).
The panel authorizes the offended country to retaliate by “withdrawing a concession of equivalent value which it had previously negotiated with that country).
Countries remain sovereign in determining how to respond. Conformity to WTO rule and decisions cannot be compelled by external force.
Example: the Hormone-treated beef.

Issues on the WTO institution

Inter-governmental entity, not supra-governmental.
Inefficient: all decisions taken by consensus. (168 countries)
Trade negotiation kept secret. Choice of governments that prefer to remain away from corporate interests?
Dispute resolution mechanism: small number of officers, secret procedure, some opportunity for countries to appeal, but no open discussion.

IV. Regional trade agreements

- Different level of regional integration
 - Preferential trade agreement: loose preference scheme. Ex: British commonwealth
 - Free trade area: All barriers removed within the area, but each country deals individually with the rest of the world. Ex: NAFTA
 - Risk of triangular trade and trade deflection: Japan goods could enter the US through Mexico. Hence in NAFTA, “Regional content requirement” clause.
 - Custom Union: Free trade + harmonization w.r.t. rest of the world. Ex: European community, until 1992
 - Common Market: Custom union + free movement of labor and capital. European Union, 1992-99
 - Free movement of capital requires a good harmonization of other issues, to avoid downward spiral to the bottom, with lowest wage, safety standard, taxes, etc.
 - Economic Union: Common market + harmonization of monetary and fiscal policies. Ex: Benelux, European Union since 99.
- Economic static gains/losses
 - Welfare effects of regional trade agreement ambiguous
 - Example: Spain entering the European Union.
 - Before, could buy wheat from the US at $p_{US} + \text{tariff}$
 - After, buys wheat from France at $p_F < p_{US} + \text{tariff}$. Efficiency gains, because the price is lower but loss of tariff revenue (France captures the difference $p_F - p_{US}$).
 - Trade creation- trade diversion
 - Some trade creation, because lower price induce increase of imports.
 - But some of that is diverted from imports from Canada
 - Gains expect to be large when custom union with a country substantially more efficient than home. But little gain or even loss if custom union with country too similar.
- Other benefits of regional agreements
 - Greater negotiation power in international negotiations.
 - Dynamic effects similar to any trade opening: increased competition, economies of scale, stimulus to investment
- Are regional trade agreements a step toward freer trade or an impediment to free trade?
 - By proponents: complement to WTO, easier to achieve not much diversion since tariffs are low anyway. More innovative negotiated rules and commitments that go beyond what is possible multilaterally (agreements on environmental standards, investment, and competition policies). Can pave the way for discussion in the WTO.
 - By opponents: undermine the WTO, induce trade diversion.
- Examples:
 - European Community: far more than a trade agreement. Include a development plan for its weaker regions.

- NAFTA. Interesting special provisions:
 - rules of origin
 - two side-agreements on environmental and labor issues
 - mechanism to monitor members' compliance with their own national laws
 - Funding for labor retraining and environmental clean-up
- FTAA (Free Trade Area of the Americas) – Negotiations to be completed by 2005
- The European Free Trade Association (EFTA),
- The Southern Common Market (MERCOSUR),
- The Association of Southeast Asian Nations (ASEAN) Free Trade Area (AFTA)
- The Common Market of Eastern and Southern Africa (COMESA).

V. Points of debate

- Is the WTO going too far beyond a trade agreement?
 - Long list of admission requirements. Enforce global integration at a speed and with priorities that are not necessarily those of a genuine development strategy. Undermines the choice of development strategy
- Can openness deliver growth as expected.?
 - Some argue it requires a whole array of other policies (from administrative reforms to social security; from banking regulations to corporate governance.!)
 - Others that “globalization above all crowds out alternatives that are potentially more development friendly (Rodrik).
 - Controversy on all cross-sectional analyses. (Relationship depends on the control. “ceteris paribus” interpretation of regression results).
 - Successful countries (South Korea and Taiwan in the 60s and 70s, India and China in the 80s and 90s) have used very unorthodox strategy. Liberalized trade gradually, and not until growth had taken place

References: Dani Rodrik “Trading in Illusions”, Foreign Policy, April 2001. http://www.foreignpolicy.com/issue_marapr_2001/rodrik.html. Arvind Panagariya. “Think Again: International Trade”. Foreign Policy. November/December 2003. (<http://www.foreignpolicy.com/story/story.php?storyID=13920>)