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The WTO and the millennium round : between standstill and leapfrog

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KIELER DISKUSSIONSBEITRÄGE

KIEL DISCUSSION PAPERS

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The WTO and the Millennium Round: Between Standstill and Leapfrog

by Rolf J. Langhammer

CONTENTS

- The Third WTO Ministerial Conference in Seattle in November 1999 is expected to pave the way to the ninth multilateral round of trade negotiations, labelled Millennium Round (MR). Like the preceding Uruguay Round (UR), it will have the twin targets of preventing domestic measures from discriminating against foreign supply and of dismantling border measures such as tariffs and non-tariff barriers.
- The core challenge of the MR will be to defend the WTO framework against efforts to sacrifice its genuine target of guaranteeing and enforcing access to markets by compromising this target with other targets such as protecting the environment, workers' rights, foreign investors' rights and competition. The GATT experience with a contradictory and inefficient mixture of aid targets (special treatment for developing countries and least-developed countries) and trade principles (non-discrimination between all WTO member states) underlines the importance of clearly separating targets, instruments and responsibilities of actors through different institutional set-ups instead of forcing them into a single framework. This holds especially for the protection of the environment and of workers' rights, where existing frameworks should be used and/or new frameworks be founded. For competition and investment, existing elements of the WTO can be used to keep markets open and to level the playing field between foreign and domestic investors.
- Liberalising trade in services and enforcing free access to service markets through the General Agreement on Trade in Services (GATS) will be the most important concrete liberalisation objective in the MR. As the GATS principle is bottom-up (service-industry-specific liberalisation with many loopholes) while the GATT principle for goods is top-down (across-the-board cut of border measures), the best liberalisation results would be achieved if the top-down principle could be applied to services as much as possible. Linking services to goods as joint products bound to GATT rules and/or defining services as goods wherever possible (for instance, in e-commerce) could be instrumental to anchor the top-down principle in services.
- In traditionally highly protected sectors with special entitlements like agriculture and textiles (including clothing), the MR must counter efforts of big players like the EU and partly the US to play for time by postponing UR commitments to the latest possible date. In doing so, they will deliberately create an adjustment jam, which would trigger requests for further safeguards. Should the WTO fail to discipline the players in these sectors, frustration in developing countries can weld the vast majority of WTO members into a stumbling block against the MR.
- Further needs to reform the current WTO framework can be identified in disciplining mushrooming regional integration schemes, which undermine the most-favoured nation treatment principle, in dismantling still existing tariff escalation, which discriminates against manufactured goods exporters, in fundamentally redressing the abuse of contingent protection measures such as anti-dumping and safeguards and, finally, in solving the still pending issue of China's accession to the WTO. The MR without China refutes the WTO's claim to be a universal institution.
- In a mercantilist world, negotiation strategies matter. Notwithstanding the lack of a fast-track mandate for the US administration, it seems that the US together with Asian countries prefer sector-specific negotiations with a focus on agriculture, services, and government procurement. In contrast, the EU prefers negotiations on all issues in a so-called comprehensive round. Developing countries still hesitate to participate at all but their hesitancy can prove to be a promising strategy to push the EU and the US toward accelerating the implementation of UR commitments. All participants will experience that there are first-mover advantages and that leapfrogging technological progress in the cross-border movement of persons, goods and services will impose high costs on those who get stuck in old-style nitty-gritty trade diplomacy.

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Contents

List of Abbreviations

AMS	Aggregate measure of support
APEC	Asia Pacific Economic Cooperation Group
ASEAN	Association of Southeast Asian Nations
BOP	Balance of payments
CGE	Computable general equlibrium
EC/EU	European Community/European Union
EVSL	Early voluntary sectoral liberalisation
FDI	Foreign direct investment
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GSP	Generalised system of preferences
IEA	International environmental agreement
ILO	International Labor Organization
IMF	International Monetary Fund
MAI	Multilateral Agreement on Investment
MERCOSUR	Common market of the South
MFA	Multifibre Agreement
MFN	Most favoured nation
MR	Millennium Round
NAFTA	North American Free Trade Association
NGO	Non-governmental organizations
NTB	Non-tariff barriers
OECD	Organisation of Economic Co-operation and Development
OMA	Orderly marketing arrangements
OPA	Orderly production arrangements
PPM	Process and production methods
R&D	Research and development
TRAP	Trade-related antitrust principle
TRIM	Trade-related investment measures
TRIP	Trade-related intellectual property rights
UNCTAD	United Nations Conference on Trade and Development
UR	Uruguay Round
VER	Voluntary export restraint
WEO	World Environmental Organization
WTO	World Trade Organization

I. New Round, New Game

Six years after the conclusion of the Uruguay Round (UR), the Third WTO Ministerial Conference in Seattle in November 1999 is intended to lay the foundations for the ninth round of multilateral trade negotiations since the foundation of GATT in 1947. As this round will lead the multilateral trading system into the new millennium, it has been named Millennium Round (MR) as a working label.

It is hardly an exaggeration to argue that a substantial work has been done between the two rounds. After 1995, for instance, unfinished UR agenda items were concluded in basic telecommunications and financial services, and new sector-specific negotiations were started in information technology products, aiming at the elimination of tariffs on a broad range of products. But aside from such negotiations, the increasing number of dispute settlement procedures has revealed areas where more precise wording has become necessary to avoid even more such disputes in the future.

Despite such legal wrangling, the bottom line of the UR results seems to be reflected in the current account. That is, while the capital transactions in the balance of payments became exposed to volatility and shocks during the financial crises of the past few years, the current account transactions revealed a remarkable stability. Some argue that this was due to the legal discipline which the Contracting Parties had to comply to. Such a view neglects that the trading system can also be exposed to volatility and shocks and that stability can be transitory. Volatility and shocks might arise less from general political resistance against open markets, which seems to have declined in recent years, but more from occasionally emerging protectionist forces which are fuelled, for instance, by a widening gap between the US current account deficit and the Japanese and EU current account surpluses. The view that the buoyant US market has been assuming the role of the "world's importer of last resort" by absorbing the post-crisis export expansion of emerging Asian markets (which actually has not yet fully started) and that the two other major, but slowly growing markets shy away from "burden sharing", could easily culminate in protectionist actions and retaliatory responses. It is for this reason that launching a new round is timely in order to contain protectionist forces when the export expansion should reveal its full strength.[1]

There are three aspects which will influence the agenda of the MR from the very beginning. *First*, as the implementation of the UR commitments will be finalised much later than the start of the new round, there is some overlapping between the UR and the MR. The MR has to take account of some UR commitments, for instance, the liberalisation of trade in textiles and clothing until year 2005 and the implementation of UR commitments to the trade in agriculture, which are scheduled to begin in year 2000. Hence, part of the MR eventually will have to cope with "play for time"-strategies of major Contracting Parties in addition to the new "headline" issues. It cannot be excluded that trading partners abuse the evergreen issues as hostages for receiving specific privileges in the headline issues or vice versa.

Second, the complexity and heterogeneity of issues increases. This is a continuation of the trend which started at the UR in which, unlike the preceding rounds, tariff cuts for the first time were no longer in the centre of negotiations. This trend is not only due to splintering the negotiations into specific core sectors like agriculture and textiles or to including intellectual property rights (TRIPs) and trade-related measures (TRIMs). Heterogeneity and complexity is primarily due to the shift in attention from goods to services as the big remaining stumbling block to freer trade and to the fact that the dismantling of qualitative (non-numerical) border barriers often escapes quantification beyond the bottom line of the reciprocity prerequisite. Thus, Contracting Parties who are un-

Remark: The author would like to thank Dean Spinanger and Jörg-Volker Schrader for critical comments on earlier drafts.

1 To arrest never-ending protectionist tendencies is the key reason for sustaining the liberalisation momentum as argued by the so-called bicycle theory (Bergsten 1999).

able to quantify the value of their own liberalisation concessions might be reluctant to accept other Parties' concessions, thereby bringing the negotiations in a stalemate situation. The initial refusal of the United States in the post-UR period to accept concessions offered by Asian countries in financial services as an equivalent to own offers bears witness to the implications of non-quantitative trade barriers for speedy negotiations, which are still subject to the reciprocity criterion.

The *third* reason is perhaps the most far-reaching one: For both trade in goods and services, a shift in priorities from trade liberalisation to market access can be identified. As concerns merchandise trade on the one hand, tariff barriers and quantitative restrictions in particular as well as border measures in general have declined substantially. On the other hand, technical barriers such as health and phyto- sanitary standards as well as anti-dumping measures today have emerged as the major hurdles to accessing foreign markets. As concerns trade in services, border measures are relatively unimportant compared to domestic measures which restrict foreigners' presence in domestic markets or prevent residents from buying services in foreign markets unrestrictedly.

The crucial shift from trade liberalisation to market access with its impacts upon various policies and sectors will be discussed in more detail in Section II. Section III is devoted to the so-called evergreen issues, i.e. the unfinished agenda items from previous rounds. Section IV discusses likely negotiation strategies of the most important actors, which reflect a mercantilist tone in terms of ensuring best access to potential export markets while keeping concessions for access to the domestic markets at bay. Section V concludes with an optimistic note. It points out that technological innovations in moving goods, people and knowledge across borders can easily establish a new bottom line of first-mover advantages for traders. Against this bottom line, responsive tactics from mercantilists might still be able to play for time in order to postpone and slow down adjustment. However, they will not succeed in stopping the caravan of those who gain from freer trade and have technology on their side.

II. The Headline MR Issue: How to Defend Market Access against the Abuse of Domestic Policies

1. Services: The GATT "Swallowing" the GATS?

Until the UR, multilateral trade negotiations were based on the top-down principle: Tariff cuts for all industrial goods (except for specifically excluded products like textiles, clothing and processed agricultural goods) were proposed either across the board or with a non-linear tariff-cutting formula. Overall, common principles toward dismantling border measures were agreed upon. In the same vein, quantitative trade restrictions were generally banned; the use of domestic subsidies was restricted to non-discriminatory purposes in compliance with national treatment; and the application of contingent trade measures such as anti-dumping measures, safeguard clauses and countervailing duties was limited to strictly defined cases which were each subject to a non-arbitrary transparent procedure.[2] Price equivalents of non-tariff measures were calculated to allow for comparisons with tariffs. The entire effort of the top-down principle was to focus the GATT on its prime instrument of discrimination between domestic and foreign suppliers — the tariff. By putting a clear price tag on trade-restricting measures, transparency was facilitated, thus raising hurdles for domestic vested interests to defend and justify their claims for protection. Furthermore, the reciprocity requirement as a negotiation principle in a political environment of disciplined mercantilism could be met with such price tags becoming available and accepted.

Compared to the GATT, the situation in the General Agreement on Trade in Services (GATS) could not be more different. The GATS principle is bottom-up. Contracting Parties place those services they are prepared to liberalise on a

[2] It is commonly acknowledged among free traders that these limits could be drawn much more narrowly. See Leidy (1994).

"positive" list. The remaining services are excluded from liberalisation. Furthermore, trade-restricting measures maintained for those services listed for liberalisation (Krancke 1998) are placed on a "negative" list. To some extent, this procedure pays tribute to the peculiarities of non-factor services, i.e. the dominance of qualitative domestic measures over quantitative border measures and the heterogeneity of non-factor services. However, it also reflects strong resistance to the opening of service industries to international competition for obvious reasons. In many industrialised countries, such industries have enjoyed a level of protection similar to other highly protected sectors such as agriculture. As a result, resource allocation has become distorted in favour of excessively absorbing the relatively scarce factor, i.e. in this case unskilled labour. This process has lasted for the entire post-war period and today coincides with pressures on labour market adjustment due to de-industrialisation. Therefore, vested interests during the UR were strong enough to enforce the bottom-up principle which leaves sufficient room to ensure protection on service sectors against competing imports. Admittedly, the GATS in Art. XIX specifies a continuation of negotiations on liberalisation to begin not later than five years from the date of entry into force (i.e. not later than year 2000). In addition, negotiations concerning government procurement, subsidies and safeguard measures have also become obligatory. Finally, the GATS principle to encourage mutual recognition of national standards (equivalent to ex post harmonisation) and its multilateral application must be acknowledged as positive steps. Yet, the bottom-up principle remains the limiting factor. That means that any significant liberalisation step forward requires to weaken the bottom-up principle and to strengthen the top-down principle. In other words, the top-down principle is typical for border measures, while the bottom-up principle addresses the details of different national legal rules, for instance, for commercial presence as a prerequisite of one mode of providing services, the move of the producer to the consumer.

To speed up liberalisation of trade in services, the MR could aim at substituting border measures for domestic measures. For instance, Contracting Parties could be entitled to charge foreigners a fee for allowing them to supply commercial services domestically, dropping in return legal restrictions on the presence of foreigners. Reducing such fees would then become subject to negotiations. Moreover, negotiators could consider either binding as much services to goods and thus to the GATT provisions or defining services as goods as much as possible and then again apply GATT provisions.

The first approach departs from Grubel's proposition that all traded services are embodied in materials and people and that therefore "...free trade in goods assumes free trade in non-factor services. There is no need for a special treatment of trade in services under GATT" (Grubel 1987: 326). While this proposition has been strongly motivated by the target to apply the same rules for services as for goods and to maintain the liberalisation momentum and transparency of the trading system, it is untenable in its radical form (Arndt 1989: 4). Many services are not embodied in materials or people but constitute a separate item in terms of dissemination of knowledge or information. However, if the benefits from GATT provisions for goods are threatened to be impaired or nullified due to discriminatory measures in goods-related services such as transport, Contracting Parties should be allowed to demand that such services are subject to the same trade policy provisions as for goods. In short, one would establish a common policy treatment for a joint product consisting of a good plus a service.

The other approach is of more recent nature and stems from modern telecommunication devices. At the Second WTO Ministerial Conference in Geneva in May 1998, a decision was taken to continue not to impose tariffs on electronic transmission (WTO 1999a). While tariff collection was never intended nor thought to be feasible, the United States substantiated this decision by proposing to bind it as a standstill commitment on duty-free trade in electronic transmission. If the point of departure has been to argue that electronic transmission of information ultimately can (but must not necessarily) acquire a tangible form, then electronic trans-

mission includes the possibility to deliver goods such as designs, cards, movies, books or music. This transmission should then be bound to the rules which are relevant for this tangible form in order to treat the intangible form and the tangible form equally. These rules would be under the GATT and its ban of quantitative restrictions, and not under the weaker GATS. Both ways would be instrumental to generally anchor top-down rules of non-discrimination for services and would help to refocus the trading system on border measures.

It goes without saying that partner countries particularly competitive in exporting "goods" under the intangible form would find the possibility attractive to subsume intangibles under the GATT. However, the more operational issue of how to place customs officers in the internet in order to collect tariffs remains unsolved.

2. Environmental and Social Standards in the WTO: Barking up the Wrong Tree

Enforcing environmental and social standards which are consistent with absorptive capacities, preferences and income levels of countries is a legitimate concern. Since countries differ in these fundamentals, so do domestic environmental and social policies. Policies impact upon factor costs and thus may drive a wedge between competing goods produced under different policy conditions. Is there then a case for levelling the playing field through forced harmonisation by using trade measures against "sub-standards"? The borderline to be drawn is between the environmental and social standards having purely domestic implications on the one hand and those having cross-border spillovers on the other hand (Siebert 1996; Langhammer 1997).

In the purely domestic case, there are two arguments supporting trade measures. The *first argument* is to equalise the pollution tax over all WTO Contracting Parties through trade measures in order to countervail "unfair" competition through "environmental and social dumping". This argument is misleading, since it confuses the universal rule of the polluter-pays principle with a uniform pollution tax rate (Bhagwati 1999). To meet the former rule would be efficient but this does not require that the latter is fulfilled. With differences in fundamentals, the tax rate will be different "for the same carcinogen in the same industry" (Bhagwati 1999). The *second argument* relates to the "race to the bottom": sound policies in some countries are feared to be undermined by unsound policies in other countries, which thus attract "dirty" industries or industrialists eager to exploit labour. Theoretically, the argument is not unidirectional: there could be also races to the top if strict policies meet the preferences of people for environment protection and workers' rights. If races to the bottom should actually occur, host countries would rapidly impose a tax on inflowing capital in order to stop the degradation of human and environmental capital. Should such taxes not be levied, the adequate policy measures should be targeted to correct this suboptimality directly rather than taxing trade (Wilson 1996). However, the empirical validity of this argument is not strong. Either differences in the pollution tax are overshadowed by other locational factors to the detriment of countries with a low tax rate, or differences in tax rates are marginal. This evidence seems to hold both for environmental and social standards (Beghin et al. 1994; Bhagwati 1999). Alternative policy measures available as trade policies are either mandatory or voluntary codes to induce multinationals to adopt home country standards when going abroad or to initiate private competition in certificates and labels and leave it to the consumer to decide. For the latter, however, it is important to note that this competition should be outside governmental actions and that therefore governments should not privilege specific labels.

The case with cross-border spillovers is truly a thorny one which will be high on the agenda of the Millennium Round. Principally, trade measures can address negative spillovers. Yet, the current WTO understanding is such that these measures should be compared with alternative policy measures (including compensation payments and emission certificate auctioning) and, if applied, should be non-discriminatory, least

distortive to trade and subject to limits in scope and time. Negative spillovers may arise, for instance, for consumers if imports cause physical damages to them. The recent controversies between the United States and the European Union on possible consumer damages from consuming genetically modified or hormone-treated food has revealed the degree of uncertainty on long-term health effects of food consumption and to some extent also the degree of arbitrariness and vested interests as imports compete with domestic substitutes produced under different standards.

Dispute settlement decisions under the WTO have always stressed equal treatment of imports and domestic production if both show the same effects on health, for instance in tobacco consumption. However, consumer spillovers provide clearer policy guidelines than cross-border producer externalities, which arise from so-called process and production methods (PPM) objections.[3] Famous PPM examples of dispute settlement have been the dolphin-tuna and turtle-shrimp cases. In these cases, the WTO has opposed trade measures which aim to enforce PPMs that do not affect the characteristics of a product (Low 1998). However, it is evident that the pressure for harmonising national PPMs internationally rather than mutually recognising different national standards intensifies. In this respect, Art. XX GATT opens legal opportunities to ensure resource conservation by means of trade measures under the above-cited prerequisites of non-discrimination (equal treatment of imports and domestic production) and minimisation of the negative effects on trade. Concerning PPM objections, motivation to dispute other trading partner's PPMs can be labelled either "selfish" if competing domestic production are to be protected. Alternatively, the motivation would be "emotional", "altruistic" or "psychological" if no domestic production is involved, but if lower time preference rates in importing countries (compared to producing countries) lead to concerns about the depletion of the natural capital stock and to campaigns against imports. Such "emotional" spillovers have strongly influenced the debate on defending minimum social standards by the threat to impose trade measures as an *ultima ratio*.

Should "emotional" spillovers, however, become a legitimate reason for imposing trade measures, environmentalists and non-governmental organisations (NGOs) defending social standards risk to kill a cash cow and to bark up the wrong tree. As concerns the risk to kill a cash cow, it has been shown and witnessed time and again that freer trade offers poor countries the opportunity to catch up, to gain income and thus to collect financial resources, which are needed to implement resource-saving technologies. Likewise, it is known that openness promotes the inflow of new ideas and goods and thus will also shape attitudes and preferences of people toward the rising demand for resource-preserving goods and better social standards. Sustainable income increases, such is the message and experience, are only possible with a well-educated and highly motivated workforce and with a natural capital stock which is not irreversibly degraded.

As concerns the risk to bark up the wrong tree, mixing trade policy with environmental policy under the WTO roof may lead the institution into the same dilemma which the GATT incurred when aid targets and trade policies were mixed under the infant industry argument (Art. XVIII GATT) and special and differential treatment (Enabling Clause of 1979). This dilemma and the costs involved in terms of reaching a target half-way with inappropriate instruments and high opportunity costs are due to the violation of the assignment rule: There should be one institution responsible for achieving one target instead of two or more. Unlike in the GATT, there should not be distribution targets assigned to an institution which is designed to achieve allocation targets.[4] Nor should there

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3 PPM problems stem from the GATT principle of non-discrimination between imports and "like" domestic products (national treatment). The similarity of products, however, is only defined according to the physical pecularities of products and not according to the production method. Hence the national treatment principle does not allow to discriminate between similar products competing in the same market but produced with technologies using different intensities of environment.

4 This is exactly the dilemma with the EU banana policy. This policy is designed to redistribute income by abusing trade policies. It has been convincingly

be an institution facing a trade-off between protecting the environment and enforcing the non-discrimination principle in international trade.

Environmentalists and social rights' defenders would therefore be well advised not to bark up the wrong tree called WTO. Instead, they should head for special institutional set-ups exclusively designed to serve these purposes and endowed with the similar toolbox as the WTO to seek compliance with basic principles on the member countries' side. The ILO is the appropriate institution for subjecting countries to a multilateral discipline in labour market conditions in the same vein as the WTO does it for trade. Until now, this division of labour between the WTO and the ILO has been the common understanding reached at the Singapore Ministerial Meeting. Should the ILO find social aspects in trade disputes, for instance, due to Art. XX GATT which under specific conditions approves trade measures in order to protect the health of people, these aspects could be submitted to the ILO for conclusion while the WTO would adopt ILO's conclusions.[5] This procedure would neatly separate the responsibility of the two institutions.[6]

To extend the blueprint from the IMF/WTO interaction to the environment requires a new institutional set-up, a WEO (World Environmental Organization), which would commit the partner countries to basic principles in domestic environmental policies such as cost internalisation and polluter-pays principle.[7] In addition, the WEO would oversee international environmental agreements (IEAs) and the trade policy implications which arise from overlapping membership in the WTO and the IEAs. Art. XX GATT would not have to be revised if the assignment problem could be solved in the same way as in the case of Art. XII (balance of payments provisions). That means that the WEO would submit its judgments to the WTO concerning the appropriateness of invoking Art. XX GATT for environmental purposes.

In sum, the proposal to establish a new international set-up for the environment has been illustrated by Esty (1994) in the sense that the Greens were barking up the wrong tree, the WTO, while underrating the importance of a multilateral discipline for the protection of the environment as witnessed by the success of the GATT. Hence, instead of greening the GATT, the environment would gain more if the Greens were to be "GATTed" (Esty 1994: 73).

The alternative, which is more cumbersome and less comprehensive, is to gradually "develop" environmental law which is consistent with the trading system through current panel decisions in the WTO and through reforming Art. XX GATT and other legal norms concerning the environment in the WTO framework. It seems that the Working Committee on Trade and Environment, the work of which will play a major role in the MR, is heading for the internal piecemeal solution rather than for delegating the issue to an external institution. While the internal solution builds upon previous developments and thus avoids institutional breaks, it risks permanent trade-offs between two targets within an institution which has been designed to serve one target only. Hence, the internal solution misses the correct assignment of tasks and responsibilities.

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shown that a direct financial transfer to banana-producing countries with cost disadvantages is more efficient and cheaper for the taxpayer/consumer than a product-specific resource transfer via a discriminatory trade policy (Borrell 1996).

5 There is a blueprint of a division of labour between the WTO and another international institution, the IMF. Developing countries are entitled to take recourse to temporary trade restrictions for balance of payments purposes (BOP) under the GATT. On the other hand, the dismantling of trade restrictions belongs to one of the key foci of IMF-supported programmes. Therefore, coordination between the two institutions is necessary to ensure greater coherence being one of the work tasks agreed upon in the UR. In praxi, the WTO accepts the IMF assessment of the appropriateness of BOP-justified restrictions (IMF 1998: 1,24).

6 For a discussion of the need to separate different institutional set-ups see Siebert (1995) and Klodt (1999).

7 This proposal is introduced in more detail in Esty (1994:73–98), who recommends the foundation of a Global Environmental Organization and addresses also the fears concerning a new international bureaucracy.

3. Competition Policies in the WTO: Building upon Existing Rules or Designing New Ones?

There seems to be a common understanding on the positive role of opening markets to competition. Hence, both the removal of border measures and the enforcement of non-discrimination principles toward domestic measures such as subsidies and government procurement can be labelled pro-competitive. Should the WTO succeed in furthering trade liberalisation and access to markets, one could be tempted to call competition policies redundant. Unfortunately, this is not the end of the story. *First*, companies operating globally do not tend to see a maximum of trade as the optimum, but tend to shift the adjustment burden of opening markets to third parties by effectively making markets less contestable. Concerted actions are appropriate tools to close markets and to exploit rents above the price level which would have emerged under unimpeded competition. *Second*, governments may encourage concerted actions for social or political reasons either by actively promoting cartel behaviour or by passively accepting such behaviour through benign neglect, thereby reducing the gains from freer trade. *Third*, national competition policies sometimes do not exist, for instance in many developing countries, or are sometimes abused as competition-regulating instruments. *Fourth*, liberalisation in specific industries, such as basic telecommunications and other network industries, may not hinder suppliers from making markets less contestable. *Fifth*, specific trade measures which were initially designed to enforce "fair" trade in countries lacking national competition policies, have actually become discriminatory and anti-competitive, such as anti-dumping.

Both private activeness to contain competition and public indifference toward fighting concerted actions have led many people to demand multilateral competition rules. Arguments in favour of such rules come from different quarters (Hoekman and Mavroidis 1994). *First*, it is argued that the lack of national competition policies, for instance in developing countries, distorts trade to the detriment of these countries (and of their trading partners) and that tying the hands of their politicians internationally would help the pro-trade lobby groups in such countries more than a less credible national law. Related to this argument is a *second* one. As those countries lacking competition policies are often subject to anti-dumping procedures, an international agreement might be the way to abandon such procedures.[8] *Third*, existing national competition laws differ from each other (for instance between the United States and the European Union), and some deliberately exclude actions against market conduct which distorts trade, for instance export cartels.[9] Internationally agreed-upon minimum rules for competition policies could cure such shortcomings. *Fourth*, multinational companies operating under various jurisdictions might choose the jurisdiction with the lowest degree of pro-competitive discipline and thus circumvent tougher jurisdictions in order to abuse market power. *Fifth*, international rules might also help multinational companies to lower transaction costs if they could operate under a single international competition set-up.

Overall, the experiences with national competition policies cast doubts on the straightforward view that such policies promote competition per se. Hence, one should think twice whether an international agreement on harmonising national competition laws, assumed it might be politically feasible, cures the shortcomings of national laws. As doubts have been strong in recent years, a cautious approach seems a reasonable starting point for the MR. This approach would try to use existing WTO rules and commitments (Hoekman 1996). One of these rules is the nullification and impairment clause of Art. XXIII:1(b) GATT. It would allow Contracting Parties to notify cases where

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8 The argument has been forcefully put forward in the case of Central European transition countries where the adoption of the EU competition rules in the Europe Agreements helped them to bring anti-dumping procedures against companies originating from these countries to an end. However, the famous Norway-UK dispute on salmon pricing reveals that even a well-established competition law may not protect countries against anti-dumping procedures.

9 For a detailed discussion of different national competition policies and their impact upon trade, see WTO (1997).

governments tolerate anti-competitive behaviour of companies through benign neglect or open support and thereby risk that gains from WTO membership are lost or reduced for other parties. Other existing regulations to be used in this piecemeal approach are the national treatment and the state trading enterprise clauses in the GATT, the ban on voluntary export restrictions, similar export measures, compulsory import cartels in the Safeguards Agreement[10] and, finally, the reference to conditions of competition between new investment and established enterprises related to the notification requirement of trade-related investment measures (TRIMs agreement). Such cases may not be easily enforceable and may therefore be more an indirect way to address private market power abuse via filing public tolerance. Yet, it would help to improve transparency and induce governments to legitimate permissive behaviour toward restrictive business practices of private companies. A stronger form than simply to notify would be to open the dispute settlement mechanism to disputes on so-called TRAPs (trade-related antitrust principles) (Hoekman 1996). A minimum approach confined to transparency would be to widen the Trade Policy Review Mechanism to trade-related restrictive business practices. Other possibilities to introduce competition policies to the WTO go further than using the existing framework. They would either try to harmonise national competition laws at a minimum level[11] or to multilateralise existing bilateral agreements on cooperation in competition law enforcement. Such agreements, for instance between the European Union and the United States or between Canada and the United States,[12] could also comprise the exchange of specific concessions, for instance the right to apply national law to companies under foreign jurisdiction which operate on the domestic market or the right to be heard if foreign companies merge on their home market and if this affects domestic companies (for instance the merger between Boeing and MDD affecting Airbus).

The range between a "once and for all" solution by negotiating an international antitrust code with joint minimum requirements and the down-to-earth approach to gradually applying the existing WTO framework to competition issues is large. For the time being, the latter approach is more promising. It will benefit from work done in the 1996 established Working Group on the Interaction between Trade and Competition Policy.

4. A WTO-Based Multilateral Agreement on Investment: In Search of a Public Good

With the conclusion of the TRIMs Agreement, the multilateral trading order made a first essential step to open the door to investment policies.[13] This step comprises the impact of investment policies on the direction and volume of trade (see above) but does not address the rules under which investors operate in host countries. In the same year that the WTO began its operations, the OECD tried to enter the latter issue by inviting countries to negotiate a Multilateral Agreement on Investment (MAI). The MAI was intended to anchor basic principles such as MFN and national treatment and to supersede the large number of bilateral agreements which by 1997 had increased to more than 1300. One year later, a special report of the WTO on trade and investment recommended the WTO as the only appropriate institution to manage a shift from bilateral, regional or plurilateral agreements to a global and comprehensive framework with full participation of developing and least-developed countries (WTO

10 It is important to note that Art. 11:3 of the Safeguards Agreement commits Contracting Parties not to encourage or support the adoption or maintenance by public *and private* enterprises of non-governmental measures equivalent to those listed in Art. 11:1 (i.e. VERs and similar measures on the export and import side).

11 This was the approach of a Munich-based group of competition law experts, publishing a Draft International Anti Trust Code (Fikentscher and Immenga 1995).

12 For a detailed description of bilateral agreements, see WTO (1997: 81–82).

13 Other agreements, such as those on services, government procurement, TRIPs and subsidies also have investment provisions but they are not as far-reaching as in the TRIMs agreement.

1996: 77–78). In fact, this report touched upon a major shortcoming of the OECD initiative: it did not receive a positive response from non-OECD countries, which obviously feared to become handmaidens of OECD-based multinationals' interests.

By mid-1999, neither the OECD initiative nor the WTO report's recommendations have been implemented. The reluctance of developing countries is still alive but the issue will be on the agenda of the MR for a number of good reasons.

First, next to portfolio investment, foreign direct investment (FDI) has been the most rapidly growing entity in international goods and factor flows in the last decade. It has become more global in the sense that on average developing countries as hosts accounted for more than one-third of annual inflows in the nineties in contrast to the seventies and eighties when intra-OECD flows clearly dominated. A further new element with special importance for the WTO is that FDI seems to have become more complementary to trade flows than in the past due to shifts in relative importance from domestic-market-oriented investment to export-market-oriented investment.[14] Given that many developing countries abandoned import substitution policies, this shift was the logical consequence of changes in the incentive system toward exports. *Second*, the number of bilateral investment agreements has mushroomed. Mostly, these agreements guarantee the free transfer of investment income, non-expropriation and same access conditions to sectors as for domestic investors. Similarly, regional integration schemes such as NAFTA, MERCOSUR and recently ASEAN provide for rights of establishment not to speak of the EU Single Market. Interestingly, the majority of these agreements set conditions for the in-operation stage but not for the pre-entry stage. Here is the gap which a multilateral agreement is assumed to fill when anchoring MFN treatment and national treatment as common pre-stage principles in national investment regulation. *Third*, given the closer link between trade and FDI, liberalisation achievements in trade can become obsolete if investment regulations continue to discriminate not only between residents and non-residents but also between sectors. Hence, just what past trade liberalisation has achieved to reduce (but not yet fully abandoned; see Section III.5 below) — the discrepancy between nominal and effective subsidisation of individual sectors — can easily reemerge through discriminatory industrial policies. *Fourth*, there is a clear link between competition policies and investment policies. Hence, should the WTO succeed in introducing competition issues in the trading order, the need to anchor the non-discrimination principle in investment regulations increases. *Fifth*, while in many developing countries the hostile stance against multinational enterprises of the seventies has practically disappeared, the recent rise in FDI flows has alerted NGOs keeping an observer status in the WTO. They fear that such a rise has been fuelled by widening gaps in social and environmental standards, thus leading to "the race to the bottom". According to the NGOs, a multilateral agreement while fixing the two WTO principles should also fix minimum standards.

These arguments, however, do not necessarily legitimate a MAI established under the roof of the WTO. One of the main arguments against it are doubts concerning the public good character. FDI are subject to private sector decisions on the one hand and policy decisions in host countries on the other hand. Host countries pursuing restrictive policies against FDI would be penalised in terms of being bypassed by foreign investors. They would lose in the "beauty contest" for mobile capital, and the costs of their policies would be entirely borne by themselves. This does not legitimate an international agreement. Only to the extent that national investment policies have negative international spillovers can an international agreement play a genuine role. Such spillovers can be contagion effects in the sense that a country pursuing "good" policies is neighboured by countries pursuing "bad" policies and that the latter policies impact upon the host through various transmission channels. Clusters of countries with discouraging investment conditions in Subsaharan Africa come to mind when this spill-

[14] The complementary issue of its implications for the trading system has been discussed in more detail in WTO (1996: Sections II and V).

over argument is raised. More frequently, however, a "bidding war" between finance ministers is mentioned as a negative spillover. In the "beauty contest", countries compete with fiscal and financial incentives, which they legitimate with positive in-border externalities. Such bidding wars are feared to ruin host countries' budgets. There are two opposing views against this argument. First, theoretically, the costs from ruining the budget can outweigh the gains from positive externalities for the host country, and then countries will stop bidding. Furthermore, participating in a bidding war has such negative allocative implications that countries which refrain from participation are better off (Hiemenz and Weiss 1984). Second, the empirical relevance of incentives vs. fundamentals as pull factors for FDI has so long been very much in favour of the fundamentals, though recently new findings seem to somewhat challenge this view.[15] Overall, the cross-border spillover argument does not carry far, especially if one concludes that a multilateral agreement would have to enter deeply into the taxation regulations of host countries in order to effectively subject host countries to a multilateral discipline in granting incentives.

Another argument in favour of multilateral agreements is directed toward market failure. Potential hosts with good policies fail to attract FDI because risk-averse investors extrapolate past policy failures and downrate the capability of the government to turn the tide. Obviously, this is an issue of capital market imperfections, and it is open to debate whether a commitment of a government to tie its hands internationally under a multilateral agreement would be sufficient to cure market imperfections to make good investment policies sustainable. In many cases, accession to a multilateral agreement was necessary but not sufficient for attracting FDI. Mexico's accession to the GATT in 1986 would have not been sufficient to attract investors, had the country not simultaneously made a number of substantial unilateral reforms in virtually all policy aspects.

In conclusion, heading for a multilateral agreement on investment under the WTO roof is an ambitious endeavour which cannot be easily launched given the reluctance of developing countries to the OECD initiative and given the requirements to fine-tune domestic tax regulations. Moreover, it does not even seem to be compelling because of doubts concerning its public goods character. In many cases, traditional policies to open markets in trade and capital are good substitutes, which can be pursued unilaterally at short notice. Furthermore, the various WTO agreements offer ways to bind investment issues more closely to trade so that at the end of the day the sum of many small steps would be at least as beneficial as the big MAI step, but with the advantage of being more likely to materialise.

III. The Evergreen Issues: Stepping Stones or Stumbling Blocks for Trade Liberalisation?

1. Agriculture: Old Problems Mixed with New Issues

Compared with agriculture, trade-restrictive measures in other sectors can be labelled minuscule. Since the beginning of multilateral trade negotiations and even more since the beginning of any negotiations on trade liberalisation, agriculture benefitted from the heavy hand of public shelter in industrial countries. To make this shelter waterproof, governments centred their measures within the triangle "price/income support — export subsidies — import protection". For many years, resistance from trading partners did not reach a critical mass. Many developing countries discriminated the domestic agricultural sector against the manufacturing sector, thus became net importers of agricultural products, booked a terms of trade gain in terms of (subsidised) lower world market prices to their account and therefore did not act as lobby groups to urge for reducing state support in industrial countries. Given their continuing domestic dis-

[15] For a discussion of recent empirical literature, see Hoekman and Saggi (1999).

tortions, they also failed to collect the welfare gains from any small step toward putting state support in industrial countries under multilateral discipline.

Such was the situation before the conclusion of the UR. The UR, however, has substantially reshaped the policy trend. This trend today points toward slowly but irreversibly integrating the agricultural sector in the same straightjacket of discipline and stepwise liberalisation as other sectors. A number of events and changes have contributed to this historical change. *First*, domestically, both taxpayers and the non-agricultural sector have finally understood the message that they were paying a high toll in terms of higher prices, higher tax burden and resource misallocation. Against these groups, even a well-organised lobby like the agricultural sector increasingly faced hurdles to legitimate state support, especially as this support divided the farmers into those who gained because of artificially rising land prices and those landless tenants who in spite of support saw themselves at the end of the income scale (Schrader 1998). *Second*, specifically the European Union had to cope with severe budget constraints even without new agricultural producers as prospective members from Central and Eastern Europe. With these new members, a radical reform remained the only viable option. *Third*, multilaterally, even without many net-importing developing countries, the UR saw the Cairns Group emerging as a strong lobby group pro multilateral discipline in subsidisation and better market access for the first time in the post-war history of trade negotiations. The Cairns Group found compatriots on the US side against the European Union and thus put the European Union in the position of the only scapegoat should the UR have failed. It was the European Union and the United States in the 1992 Blair House Agreement on Agriculture which prevented the UR from failing. This agreement became possible, since shortly before the EU-internal MacSharry Reform had paved the way toward differentiating between price support and direct compensatory payments. The European Union insisted on exempting these payments (like the US deficiency payments) from eventual GATT commitments to gradually reduce the support calculated on the basis of aggregate measure of support (AMS) as a prerequisite for coming to a GATT agreement (for more details see Tangermann 1998 and Swinbank 1999). *Fourth*, industrial countries including the European Union have become internationally competitive exporters of specific agricultural products, especially with a high value added, and thus are interested in gaining access to export markets. Hence, the mercantilist logic of trade negotiations is also relevant for agriculture: without reciprocity, no concessions. *Fifth*, linked to the fourth aspect, there is a technology argument. The emergence of technological innovations in food production, especially toward genetically modified food, may open industrial economies new markets either through direct exports or through FDI. Given the R&D intensity of such new goods, protection of investment and of intellectual property rights will require agreements on a bilateral, regional and multilateral level. The latter is particularly important for TRIPs, as many developing countries demand the anchoring of property rights for genetic raw materials deposited in their own resource base such as tropical rain forests.

These are just the new issues discussed in Section II which will also impact upon a traditional sector such as agriculture and which, unlike in the past, will induce industrial economies to become more attentive to reducing barriers to trade in agriculture.

In concrete terms, the MR will depart from the UR commitments, which cover liberalisation measures in market access, domestic support and export subsidies. 1999 is the year which was foreseen in the UR agreement on agriculture as the starting point for new negotiations. As regards *market access*, the target will be cutting the tariff equivalents, which in the UR were agreed upon as substitutes to variable levies (EU) and other quantitative restrictions. However, a simple across-the-board cut in the range of about one-third of the initial level will not be effective due to the fact that many tariff equivalents in industrial economies are redundant ("water in the tariff" or so-called dirty tariffication): the equivalents are higher than differences between domestic and world

market prices. Many developing countries which apply much lower tariffs than those which were bound in the UR still enjoy the same manoeuvring space for tariffs without having to fear competition. The solution could be either the application of a non-linear tariff-cutting formula like that in the Tokyo Round when higher tariffs were lowered more strongly than lower tariffs. This would have the advantage of reducing tariff dispersion and bringing effective rates of protection closer to the nominal rates. Another (more unlikely) possibility would be such a high across-the-board cut that tariff redundancy would disappear, and, thirdly, Contracting Parties could negotiate to cut tariffs for selected items to zero level as they negotiated in information technology items (Anderson et al. 1999). However, the latter would raise tariff dispersion, as countries would prefer duty-free trade for products which are not "sensitive" while maintaining tariffs on items such as sugar which are "sensitive". Thus, a non-linear tariff cut seems the best alternative viewed from the allocative point of view. An escape clause, which was negotiated as a special safeguard tariff-raising option when world market prices were low or imports were high, will probably also be tightened. It is important to note that cutting tariffs reduces the volume of imports for which price support in terms of fixing intervention prices makes sense.

For a number of agricultural items meeting the so-called minimum access requirement (part of domestic sales must be provided by imports), there are tariff quotas, i.e. tariffs within a certain quota are lower than above the quota. To relax these quota by expanding them is likely to meet resistance from those countries which benefitted from guaranteed access in country-specific quota. A far-reaching proposal to cancel tariff quota altogether and to agree on a non-linear high tariff cut above the quota is the best approach for improving market access. However, it is very unlikely to be achieved unless industrial economies will be offered some off-hands area which are exempted from a strict removal of state interventions. Such an area could be *domestic support.* As mentioned above, the European Union and other industrial economies were exempted from the commitments to include compensatory payments in the AMS which became subject to reduction. Instead, compensatory payments were placed in the "blue box" outside the reduction commitments. However, due to the fact that meanwhile the United States decoupled their deficiency payments from production and shifted payments from the blue to the green box, there is increasing pressure upon the European Union as the major "occupant" of the blue box to follow suit. Tangermann (1998: 450) points out that with these hitherto "blue box" measures included in the AMS commitments, the EU domestic support payments would exceed the WTO limit already by year 2000. To be prepared for this challenge in forthcoming WTO negotiations, the European Union could either *a priori* cut its price support and/or reduce compensatory payments or decouple payments from production by binding the payments to the historical area under cultivation (or to persons irrespective of their employment in agriculture) rather than stipulating how land must be used. Unfortunately, the European Union in May 1999, when deciding on the Agenda 2000, shied away from both cutting intervention prices substantially and decoupling income support from production. Hence, the May 1999 Agenda 2000 decisions leave the European Union much less well prepared for the WTO negotiations than it could have been the case. The argument to keep bargaining chips for the forthcoming negotiations instead of giving "everything away for free" neither witnesses insight into the macroeconomic allocative distortions of agricultural subsidies nor a realistic assessment of the defensive role the European Union will have to play in the WTO if there is no policy change. Furthermore, this "wait and see" attitude will deteriorate the chances the European Union has in enforcing the "new issues" in agriculture to the benefit of its competitive exporters.

The third traditional playing field in the forthcoming MR negotiations in agriculture will be *export subsidies.* The UR specified binding maximum amounts for export subsidies both in terms of budgetary expenditures (36 per cent from the base period for industrial countries)

and volumes (21 per cent for industrial countries). Due to higher international food prices than in the base period, meeting the expenditure limits did not pose a problem to the industrial countries for the time being. They need less subsidies to export products than in the past. The binding constraint is the volume limit. Again, Tangermann (1998: Tables 3 and 7) exhibits the EU subsidies as the core challenge. In a number of products, they account for more than half of world entitlements to subsidies. In 1996/97 the European Union had already exhausted these entitlements in terms of volumes which would have been allowed by year 2000, thus requiring downward adjustments until 2000. It can thus be expected that it is the export subsidy issue in which the European Union will face the largest pressure from other Contracting Parties and in which it will have the least degree of manoeuvring space.

To summarise, the agricultural issue is a *mélange* of the three old stumbling block issues (export subsidies, domestic subsidies and market access) and the new stepping stone issues like standards on technology, TRIPs, investment and environment. The European Union has been overly passive during the first half of 1999 in overcoming the stumbling blocks and thus risks to pay for this passive stance in terms of missing chances in the stepping stones issues. Though being an important and competitive producer of technology-intensive agricultural goods, the European Union still allows itself to be taken hostage in its policies by those vested interests which would like to postpone import market opening in non-competitive products to the latest moment possible.

2. Textiles: How Playing for Time Erodes the Credibility of the Trading Order

Together with agriculture, textile and clothing has been the other sector which for many years enjoyed special treatment outside the GATT discipline, and like in agriculture, it was the UR which set the milestone for the phase-out of special treatment and special agreements. There are no other sectors which are still as heavily protected by above-average tariffs as agriculture and textiles and clothing. However, unlike in agriculture where the phase-out is still subject to uncertainties and is therefore open-ended, the D-day for the end of special treatment for textiles and clothing has already been fixed: on January 1, 2005, in the final step of four tranches, the Contracting Parties will have to liberalise the remaining 49 per cent of trade (measured in terms of 1990 import volume) which hitherto was regulated under the Multifibre Agreement. That means that within ten years (1995–2005), the MFA with its categorisation of products and its bewildering array of quotas and tariffs by categories of different degrees of "sensitivity" (in the case of the EU) will disappear.

After 2005, textiles and clothing will be under the same discipline of the WTO as telephones and clocks. This is the clear letter and spirit of the UR commitments. However, the way of implementing the in-between steps of liberalisation has given rise to strong doubts whether the major importing countries spell letters correctly and share the spirit behind the wording of the UR. During the first two liberalisation sub-periods after starting in 1995, these countries, notably the United States and the European Union, have tried to side-step commitments by both watering down and postponing the liberalisation process (Baugham et al. 1997; Spinanger 1999: 458). Watering down means that they include products never covered by quotas into the liberalisation coverage in order to have a broader sample of products available for the liberalisation to start. With this broader sample, countries have postponed the liberalisation of "sensitive" products to the last date possible, that is within the 49 per cent group to be liberalised in 2005.

Playing for time has three consequences. Each of them is detrimental for the trading system. First, the full welfare impact of the UR is seriously curtailed, since textile and clothing account for a large share of the entire UR welfare gains following CGE modelling.[16] Second,

[16] Spinanger (1999: Table 6) provides an overview of CGE model-based welfare effects from the UR by

the country group which from the very beginning of the UR has been most sceptical about liberalisation, the middle and lower-income developing countries, is just the group which would benefit most strongly from the liberalisation of textiles and clothing. This holds because the current MFA system allows established producers to capture rents and thus either closes the door to the newcomers or only permits them to participate by buying quotas. Many middle and low-income developing countries are such newcomers. Hence, by playing for time, industrial countries risk the re-emergence of old North-South conflicts (as they already showed up during the Singapore Ministerial), new barriers against universal acceptance of the trading system and finally a high mortgage for the MR. Third, it cannot be excluded that by postponing liberalisation of the most sensitive products to the last date possible, industrial countries deliberately create an import jam in early 2005, which they could use to invoke and legitimate the application of the regular GATT safeguard clause.[17]

Irrespective of whether or not these consequences materialise, textiles and clothing will keep its unrivalled position as the most heavily protected industrial sector. This holds in particular for labour-intensive clothing with its peak tariffs. Contingent protection measures[18] such as anti-dumping will continue to be applied to this sector, and it is not unlikely that real depreciation of Asian currencies after the 1997 crisis will be used as the starting point of new contingent protection measures. Furthermore, instead of the former OMAs (orderly marketing arrangements), OPAs (orderly production arrangements) could begin to plague this sector if industrial countries were to concentrate their early initiatives toward minimum environmental and social standards in developing countries on this sector. While they would have definitely chosen the wrong instrument, unfortunately, they would have not chosen the wrong sector, since problems of environmental protection and labour standards emerge in this sector like in a nutshell. Better instruments are domestic policies rather than trade policies.

3. Regional Integration: Preventing the Exception from Becoming the Rule

Free trade areas and customs unions are grandfather exceptions from the MFN commitment. With the second wave of mushrooming regional integration schemes in the nineties (after the first wave in the sixties), Art. XXIV GATT, which specifies the conditions for a GATT-consistent MFN exception, has become one of the most frequently invoked GATT articles. Many of the schemes launched by developing countries are far from meeting the strict clauses of Art. XXIV of liberalising "substantially" all trade,[19] not to speak of the initial idea of the GATT fathers that only countries should be eligible for the exception from MFN which are so deeply integrated with each other that they were virtually subject to a single economic policy. At that time, the analogy of political federations was used, and, in fact, some of the earliest schemes eligible for Art. XXIV were colonial federations.

When dealing with the issue of compatibility between multilateralism based on MFN and regionalism, one is reminded of the fact that compared to unilateralism this is an exercise in the theory of the second best (Frankel et al. 1996: 52). To bring the second-best situation close to the first-best requires the minimisation of trade diversion, i.e. the shift from non-pre-

sectors. Shares differ significantly between the various models but the consensus figure is about one-third whereas the two other thirds of welfare effects stem from liberalisation of agriculture and tariff dismantling.

17 The Agreement on Textiles and Clothing allows them to invoke a so-called transitional safeguard clause for the period until 2005.

18 Contingent protection measures will be discussed below in Section III.6.

19 This is not to speak of non-operative blueprints of ambitious bureaucracies sarcastically criticised by Bhagwati (1997). Many of the developing countries' schemes are notified under the special and differential treatment clause ("Enabling Clause" of 1979) and thus do not have to meet the Art. XXIV requirements of forming a free trade area or a customs union within due time for almost total trade. See for this notification procedure WTO (1995).

ferred to preferred trading partners due to discriminatory treatment. It is trade diversion which gives Contracting Parties the legitimacy to file a dispute case because WTO benefits have been multified and impaired by forming regional integration schemes. All proposals to discipline regional trading arrangements multilaterally focus on this target of minimising trade diversion.

As concerns the proposals made in the past, they can be listed into three categories: one principally opposing such schemes ("trans-systemic"), one going beyond the narrow framework of Art. XXIV but still leaving regional integration schemes as a strategy allowed within the trading system ("out-systemic") and the third one staying within Art. XXIV ("in-systemic").

The *"trans-systemic" proposals* centre on rollback and standstill of regional integration, for instance, by setting a sunset clause in Art. XXIV, which would bring external tariffs down to the internal tariffs within a time range (Bhagwati et al. 1998: 1146). In the same vein, reportedly, Srinivasan (WTO 1999b: 7) has argued in favour of a sunset clause whereby preferences available to members of regional agreements would be extended to all WTO members within five years. These radical proposals, which would also include cancellation of Art. XXIV, are unlikely to succeed given the existence and formation of many integration schemes and the small number of Contracting Parties in the WTO who as being outside of any preferential scheme could credibly and influentially promote such radical step.[20]

The *"out-systemic" proposals* have more leverage. First, they can depart from a natural erosion of preferences by accelerating the reduction of MFN tariffs. With zero tariffs as binding MFN tariffs, trade diversion (more precisely, trade diversion based on tariffs) would disappear. Ambitious proposals to drop tariffs altogether early next century signal that the "out-systemics" could benefit from a worldwide liberalisation initiative. An institutional proposal of "out-systemics" is to ban free trade areas and to allow customs unions only. Negative effects for non-members from forming a customs union would be completely ruled out by following the additional provision that the lowest pre-union national tariff serves as the common external tariff (Bhagwati 1991: 77). Customs unions have been found as welfare-superior relative to free trade areas because they the lack the rules of origin. Such rules designed to counter trade deflection in a free trade area formed by members with different external tariffs are essentially protective and trade-diverting (Lloyd 1993: 711; Krueger 1995). Furthermore, customs unions are found to enjoy enforcement advantages over free trade areas under the mercantilist rule already cited above: no reciprocity, no concession. They have market power that enables them to threaten the multilateral trading partners with setting higher tariffs should such threat be desired (Bagwell and Staiger 1998: 1179).

The *"in-systemic" proposals* centre on sharpening the preconditions set by Art. XXIV for GATT-consistent free trade areas *and* customs unions. These preconditions comprise three aspects[21]: the question of whether bound or applied tariffs are meant with the word "applicable tariff", the meaning of the scope of liberalisation as laid out in the provision that "substantially all the trade" should be liberalised and thirdly the definition of "other regulations of commerce" applied to trade with non-members which should not be higher or more restrictive than before the scheme was formed.

The first aspect has become a focal point, when Mexico raised applied tariffs on imports from non-NAFTA members in the aftermath of the December 1994 crisis within WTO-bound ceilings while keeping applied tariffs on NAFTA imports unchanged. The European Union felt discriminated vis-à-vis the United States, since it defined applicable tariffs as applied tariffs. The pending issue is particularly relevant for developing countries, which have frequently bound their tariffs to a higher level in the WTO framework compared to the tariffs they actually apply. The second aspect concerns the exclusion of agricultural products in free trade arrangements

[20] Among the large trading partners, it is only Japan which is not a member of a preferential trading scheme.

[21] For a detailed discussion of these aspects, see Nagarajan (1998).

in the sense that part of trade must not be subject to internal liberalisation. But which part? The normal practice was that agricultural trade was excluded. Yet, special treatment of agriculture is inconsistent with the above-discussed trend to treat agriculture in the world trading system like other sectors. Reforms in this respect could have substantial implications. By dropping the word "substantially", the EU, for instance, would have to revise their numerous bilateral "hub and spoke"-type free trade agreements[22] in order to include agricultural trade unless the exclusion in past agreements would be "grandfathered" and thus treated as a *fait accompli.* It is obvious that the EU would have difficulties to comply with such a substantial reform.[23] The third aspect primarily refers to preferential rules of origin in regional trade agreements as well as to other regulations of commerce such as variable levies or anti-dumping duties (Sampson 1996). In some cases, regional provisions do not refer to WTO provisions as the binding provision and, actually, deviate from the latter. It has been correctly argued that special regional rules of origin[24] could curtail third-country rights under the WTO (Roessler 1993; Palmeter 1993).

In short, it cannot be denied that the "out-systemic" proposals have much appeal as they would automatically extinguish a number of problems which are dealt with in "in-systemic" proposals. The former proposals could follow Bhagwati's proposal to allow customs unions as the only exception from MFN for newly founded schemes and to fix a timetable during which the lowest national tariff would have to be approached as the common external tariff. "Grandfather" clauses could protect the established free trade agreements with a sunset clause that also these agreements should be converted into customs unions within a pre-specified timeframe. Internal liberalisation could be approved by binding it to the commitment of external MFN-based liberalisation in order to maintain the preference margins and at the same time not to impair third-country rights under the WTO.

Overall, with decreasing MFN tariffs and ongoing liberalisation of non-tariff barriers, Art. XXIV is likely to lose much of its relevance. To put it differently, Art. XXIV is devoted to coping with problems of "old regionalism" in which trade was the dominating issue. In contrast, the "new regionalism" stresses the shift in relevant issues from trade to investment and harmonisation of regulations and underlines that its emergence has been due to the success of multilateralism in removing tariff barriers on MFN basis and not to its failure (Ethier 1998: 1161).

4. Special Treatment for Developing Economies: Has Free-Riding Helped the Free-Riders?

Throughout its history, the world trading system influenced by the Havana Charter has paid tribute to special treatment of economies in development. Infant industry arguments were considered in the 1947 GATT (Art. XVIII) and elaborated further in the so-called Part IV Extension (Arts. XXXVI–XXXVIII) of 1965. They allowed developing countries to opt out of MFN liberalisation commitments, thus legitimating the countries to protect their industries more than would have been possible under full participation in multilateral trade negotiations. Moreover, industrial countries' tariff preferences for non-traditional products originating from developing countries, the so-called Generalised System of Preferences (GSP), were introduced in the early seventies and became approved in the GATT first through a ten-year waiver and finally, in 1979, through the Enabling Clause on "Differential and More Favourable Treatment, Reciprocity and Fuller Partici-

22 Hub-and-spoke agreements misleadingly suggest free trade for the spoke. In fact, this holds only for trade with the hub. Over the rest of the region, the spoke becomes an outsider as there is no free trade between the spokes. See Wonnacott (1996).

23 An alternative to dropping the word "substantially" would be to quantify it in terms of minimum percentage of intra-regional trade to be liberalised such as 75 per cent (a figure mentioned by Bhagwati (1990)). For a number of reasons which, for instance, refer to inapproriate manoeuvring space for governments to exclude "sensitive" sectors from liberalisation commitments, this is unsatisfactory as well.

24 The European Union operates the most sophisticated system of rules of origin such as the donor country content or different "cumulation rules" in the hub-and-spoke agreements with European transition countries and within the European Economic Area.

pation of Developing Countries". It is the Enabling Clause which today serves developing countries as the permanent legal foundation for being unequally treated within the trading system. The term "fuller participation" in the Enabling Clause is a misnomer. What it stands for is actually the result of a deal: developing countries have an incentive to participate in trade negotiations more actively than in the past only if differential treatment continues to be guaranteed.

Economically, special treatment brings aid aspects into an allocative framework. Development and trade are two separate issues linked together in a single institutional framework. This is highly problematic again because of the assignment problem, discussed above for the link between environment and trade. There are aid institutions with adequate instruments but the WTO does not belong to them. It neither has the appropriate instruments nor is the appropriate institution for channelling public resources to developing countries (either in terms of industrial countries' tariff revenues foregone or in terms of subsidising domestic industries through infant industry protection).

The implications of special treatment for the trading system have been far-reaching. *First*, 80 per cent of WTO members are developing economies and the consensus principle requires industrial countries to take developing countries' interests into consideration.[25] Qualified (two thirds) majority voting, which is principally possible, could mean that industrial countries could easily be voted down. This would threaten the existence of the WTO. *Second*, developing countries enjoy special treatment in all sub-aspects and special agreements under the WTO roof, mostly in terms of longer transition periods. *Third*, the UR created an additional group of particularly privileged Contracting Parties, the least-developed countries. The idea behind this new grouping, namely to upgrade the developing countries and to merge developing and industrial countries in order to confine preferences to the poorest countries only, was well-intended but not good. There is no clear distinction line between poor and poorest countries and hence arbitrariness will continue. Nor will poor countries become more eager to participate in the world trading system as equals because poorer countries receive more privileges. It is more likely that members eligible for either group will stick to their group-specific entitlements.

The economic results from unequal treatment have been disenchanting. Trade preferences of industrial countries failed to compensate for supply-side-originating disincentives to export and additionally became a suitable tool for the donors to divide and rule (Langhammer and Sapir 1987; Bhagwati et al. 1998: 1145). Rent-seeking was encouraged in the same way as fuller participation of the poorest members was discouraged. The African countries, for instance, while enjoying the highest preferences have largely refrained from committing themselves to binding trade liberalisation in the UR and thus remain the most heavily protected markets (Sorsa 1996). That means that the implicit tax on exports through import taxation is the highest for the poorest countries. This is a result which flies in the face of those seeing privileged treatment as a key to world market integration.

At a High Level Symposium on Trade and Development held by the WTO in March 1999 (WTO 1999b), the hesitancy of developing countries in entering the Millennium Round was discussed on the basis of the disappointing opening of developed countries' markets since the UR. While this can be confirmed following the textiles and clothing debate, the mercantilist tone underlying this argument is notable. Instead of following the many partial and general equilibrium studies, which stress the importance of welfare effects derived from the opening of the *own* import market, developing countries supported by NGOs and UNCTAD have argued in favour of fully exploiting the options of privileged access to developed countries' markets especially for the poorest countries. Proposals to cut tariffs for least developed countries' exports to zero, for instance, seem to oversee various hurdles, such as supply-side induced disincentives to exports (due to "wrong"

[25] The controversies on agreeing to a new WTO Director-General following Renato Ruggiero after March 1999 bear witness to this point.

exchange rates), the incentives for developing countries to bypass trade barriers by establishing "screwdriver" factories with miniscule domestic value added in least-developed countries and the redundancy of preferences due to MFN duty-free treatment.

A major impulse for the debate on development and trade will come from the decision on China's application for WTO membership. As China is by far the largest and most competitive developing country (and not a least-developed country) some industrial countries have demanded that China should give up all claims for privileged treatment under the Enabling Clause (Anderson 1997: 764), especially the rights of temporary import protection under the balance of payments provision (Art.XII GATT) and the infant industry protection following Art. XVIII GATT. It is evident that invoking the two provisions would largely erode all the benefits WTO members are expecting to collect from having freer access to the Chinese market. Likewise, it is evident that China is a developing country and that giving up this claim as a precondition for approving its application would be a signal for the complete revision of preferential treatment for developing countries. Should China insist on this status and be nevertheless allowed to accede to the WTO, the debate would very likely shift to the direction of standstill and sunset clauses of preferential treatment, probably with long transition periods and some sort of compensation. This would be a development which warrants support in order to strengthen the responsibility of the WTO for enforcing the non-discrimination principle in international trade rather than being a widely imperfect substitute to aid.

5. Tariffs: Abandoning the Evils of Escalation and Non-Binding

One of the oldest impediments to international trade is the unequal tariff treatment of sectors, usually described as the positive escalation effect.[26] Tariffs increase with the stage of production and thus effectively protect domestic value added in downstream industries higher than is shown by the nominal rate of protection. It is the group of countries exporting "finishing touch" labour-intensive manufactures which primarily suffers from positive escalation. These are basically the advanced developing countries plus few low-income countries which have managed to shape their trade policies from import substitution strategies to a more neutral incentive system. Interestingly, the culprits in escalation are basically all WTO members: the industrial countries as the major markets for developing countries but also the developing countries themselves and among them primarily the low-income countries insisting on the validity of the infant-industry argument.[27]

Whether or not escalation is still a pending issue for the MR depends on the extent of its dismantling in the UR. The GATT measured the change in tariff escalation due to the UR by the change in the absolute difference between the tariffs at the higher and lower stages of processing (GATT 1993: 28;1994: 14; Safadi and Laird 1996: 1227).[28] Three stages were used: raw materials, semi-manufactures and finished goods.

The results are unambiguous. Tariff escalation has declined but still continues to exist especially in the more advanced stages of production. Disaggregated by stages, it has been eliminated in the first stage of raw-material-based products and even reversed for tropical finished goods in the sense that tariff cuts on finished goods were larger than those on goods at the preceding stage (semi-manufactures). An

26 Negative escalation effects are possible if agriculture and services are included as upstream industries. In many countries, both sectors today still enjoy higher protection than manufacturing industries which were liberalised under the GATT rounds. If this discrepancy continues, many manufacturing industries with an export potential will become unable to materialise this potential because of negative escalation: costly inputs of services and agricultural goods will prevent them from collecting the fruits of liberalisation in manufactures.

27 For detailed analysis of low-income trade regimes and their reforms, see Sharer (1998) and IMF (1998)

28 Following this definition, tariff escalation declines when the absolute decline in the tariff on the more processed good exceeds the absolute decline in the tariff on the less processed good. A reduction in tariff escalation as defined above is a sufficient condition for a decline in the effective rate of protection when tariffs are reduced.

even more detailed analysis by major importing countries has revealed some exceptions from the general trend of de-escalation. This occurs if the decline in intermediate-goods tariffs exceeds the decline in final goods tariffs. Rubber in the European Union, Japan and the United States, jute in Canada, the European Union and the United States, lead in Japan and the United States, zinc in Canada as well as hides, skins and leather in Japan belong to those products where escalation has increased (GATT 1994: 15). Hence, tariff escalation will remain on the agenda.

While tariff escalation has been a traditional conflict in South-North direction of trade, non-binding of tariffs opens conflicts in North-South direction. The industrial countries have almost completely bound their tariffs (99 per cent of their imports) while the developing countries still have more than 40 per cent of their imports unbound. In particular, Asian and African economies have refrained from fully surrendering the scope for tariff manoeuvring. In addition, as mentioned above, many developing countries apply tariffs at much lower rates than their bound tariffs. Both elements, unbound tariffs and the application of tariffs at lower rates than the bound ones, inject an element of uncertainty into the trading system. One might be tempted to positively assess unilateralism in terms of being released from the WTO straightjacket of reciprocity. In fact, however, in a mercantilist world such unilateralism can backfire. It opens the door to counter-unilateralism from the industrial countries' side if these countries should find developing countries' bound tariffs generally too high and non-binding as a way to arbitrarily deny a guarantee on market access. Hence, the MR should and will aim at full tariff binding and convergence of applied and bound tariffs to the benefit of developing countries.

6. Non-Tariff Barriers: The Race between the Hare and the Hedgehog

In a legalist understanding of the trading system, non-tariff barriers (NTBs) have been narrowly defined as specific issues like quantitative restrictions (now generally banned) or rules on pre-shipment inspection. Remaining barriers other than tariffs have been listed either under specific agreements (technical standards, subsidies, anti-dumping), under specific sectors (agriculture, textiles and clothing) or under the broad umbrella "market access". Yet, analytically, this fragmentation is not helpful as all these barriers have a price equivalent impacting upon the difference between domestic and world market prices for different industries and sectors. The example of the AMS approach in agriculture could easily be extended to manufacturing. Given the tactical games in negotiations, the fact that fragmentation impedes transparency might not be a random outcome of sophisticated issues but a deliberately pursued target in order to hide what can be called a hare-hedgehog race: Parallel to the constructive destruction of old NTBs, a destructive build-up of new NTBs is under way so that traders will face new hurdles much faster than they expected to see them after just having succeeded in overcoming old ones.

With respect to NTBs in the MR, the priority challenges will be to establish more discipline in so-called contingent protection instruments. These are trade measures the quantitative dimension of which is not known a priori like a tariff or a quota. Their extent depends on the outcome of an investigation either launched against countries (countervailing duties, safeguards, for instance) or against companies (anti-dumping). It is the latter measure which exemplarily can serve as the reason for the re-emergence of a problem which seemed to have been contained after the UR. The 1979 Tokyo Round Anti-dumping Code was tightened with respect to dumping margin calculations, injury determination, investigation procedures, specification of *de minimis* provisions (determining a threshold level for negligible injury), no approval for anti-circumvention measures, revision clauses in order to terminate anti-dumping provisions etc. Yet, from an economic rather than legal point of view, these reforms have been marginal. Neither has a macroeconomic impact analysis been negotiated in order to consider interests of consumers and downstream

industries injured by anti-dumping measures against intermediates, nor were penalties approved for the case of unjustified complaints. The misleadingly vague and subjective term "unfair", which accompanies anti-dumping action, was not removed. Anti-trust authorities were not called upon to comment on the competition effects of anti-dumping measures, and no alternative to protective tariffs was offered (for instance pure trade-adjustment assistance).[29]

What is worse is the increase of anti-dumping measures after the conclusion of the UR and the wider geographical coverage of such measures. Since 1995 developing countries have — after passing their own WTO-based anti-dumping legislation — been applying anti-dumping measures faster than the industrial countries. This could well stimulate the four main initiators (United States, European Union, Canada and Australia)[30] to introduce more such measures (Spinanger 1998).

Apart from the contingent protection measures, non-tariff barriers find ideal breeding conditions to mushroom in technical standards including health and phytosanitary standards. Endeavours toward "deep" integration like in the EU Single Market, but to some extent also within a "shallow" scheme like NAFTA normally lead to harmonisation of measures at a higher level, and only rarely can third countries choose between different national standards which are mutually recognised among the member states of such schemes.

As in all other rounds, non-tariff barriers will be dealt with in the above-discussed fragmented way of different agreements. This impedes cross-comparisons and compatibility. It would be a useful effort to launch studies intended to quantify an AMS in selected non-agricultural products combining the most important NTBs in a single price equivalent. But even then the hare-hedgehog race cannot be won. The scope of non-tariff barriers seems like space: indefinite and all the more expanding, the more barriers are identified and made transparent.

29 For detailed discussion of the UR reforms and deeper reform proposals, see Leidy (1994).

30 The order reflects the ranking in terms of measures in force in 1997 (Spinanger 1998: Table 1).

7. Universality: What Is a New Round Worth without China?

By mid-1999, thirty countries having applied for WTO membership are at various stages of negotiating the terms of their accession.[31] Some of them, such as Algeria and China, first applied for membership more than ten years ago. The applicants, including the "Big Three" China, Russia and Saudi Arabia, account for about 9 per cent of world merchandise exports, 7 per cent of world merchandise imports, 30 per cent of world population and about 5 per cent of world GDP (at current exchange rate). Hence, while many applicants, being island states or successor states of the former Soviet Union, are rather unimportant in world trade, the aggregate weight of the applicants is not negligible due to China.

It has been criticised that the procedures for application have been arbitrary, double-standard driven, lengthy, cumbersome, intransparent, volatile and very much influenced by the WTO consensus principle. Co-optation to the WTO requires the approval of all major trading partners, and this is a particular problem with respect to China whose economic and political weight seems to have become more a stumbling block than a building block for accession. In a nutshell, all uncertainties and volatilities of policy-making in a transition and developing country are concentrated in China, as has been shown exemplarily above for the free-riding conduct of China as a developing country. For Russia, it is "only" the transition aspect of severe shortcomings in market-based institution building which seems to be the most formidable barrier.

As long as the accession problem is not solved, for China (and to a lesser extent for Russia) the MR cannot be labelled "universal" or "global" since non-members do not enjoy the legal protection of non-discrimination. In fact, there is blunt discrimination against non-members as concerns quota restrictions and anti-dumping provisions. On the other hand, the benefits of the MR are seriously curtailed if

31 This sub-section draws on Langhammer and Lücke (1999) and the literature discussed there.

China cannot be committed to comply with the WTO rules. To put it differently, China's WTO membership would be the most significant example of "tying hands internationally" for a single economy in the post-war period. Unfortunately, in the mercantilist world in which the WTO operates, WTO accession of important trading countries is always linked to losses in economic rents for competing countries. In the short run, developing countries like India have reason to fear the erosion of rents, for instance in trade in textiles and clothing, although the long-term benefits weigh more. Furthermore, NGOs exert pressure upon governments to demand far-reaching political reforms from the applicants to be implemented prior to accession. This has led to frustration on the applicants' side fuelled by the resistance of domestic interest groups, which for selfish reasons have opposed WTO membership. In such a stalemate situation, it is possible that a new round starts without having solved the accession issue. This could lead to a situation of *rebus sic stantibus,* i.e. applicants could withdraw from their applications if the members would demand more concessions prior to accession following the MR proposals for deeper liberalisation. It is this "moving goal post" situation (already being in force) which could seriously impede progress in accession negotiations. It could make the MR much less meaningful than it could be with the MR starting from a truly universal position with China as a member.

IV. On Strategies: The Political Economy of Disciplined Mercantilism

1. The US Strategy: Focusing the Millennium Round on Preferred Topics

The GATT has a long record of struggling with mercantilism, and there is no evidence that at the eve of a new round the WTO will be exempted from such a struggle. Securing access to export markets and curtailing foreign government practices that could give imports in domestic markets an advantage have been and are major negotiation targets for each Contracting Party. The reciprocity requirement and the MFN principle are responsible for the conversion of mercantilist attitudes into welfare gains and for a wide geographical spread of such gains.

Sharing the same philosophy of "exports first and imports second" does not mean that Contracting Parties agree on strategies. In fact, they do not, and this is fairly obvious given different specialisation profiles of their economies.

To begin with the United States, identifying a mid-1999 strategy is hampered by the fact that the President by that time had not yet sought to get an approval from Congress for a fast-track negotiating authority. This is not a unique situation just a few months before the Third WTO Ministerial, since such a mandate did not exist in 1986 when the UR was launched and was approved only one and half years later when negotiations were already underway. However, given that Republican fast-track negotiating authority proposals failed twice in Congress between 1997 and early 1999, there is some reason to assume that the US legislative body is divided over what issues the President should concentrate on in his negotiation strategy. While the Republicans have continued to concentrate on traditional market-access issues like tariffs, the Democrats (jointly with NGOs and organised labour) are determined to give similar attention to the new issues like environment, social standards and investment.[32] With a widening current account deficit, opposition against a new round has gained momentun in the United States, thus making it unlikely that Congress will approve a fast-track mandate just in time when the Third WTO Ministerial starts.

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32 The two views have been clearly exposed in the addresses given by Rep. Gephardt, US House of Representatives minority leader on the one hand, and Senator Roth, Republican Chairman of the Finance Committee on the other hand. The addresses were given at the Economic Strategy Institute Conference on April 28, 1999 (Internet-address: http://usis-israel.org.il/publish/press/congress/archive/1999/April/).

Overall, the US administration so far has revealed few priority topics which were also exposed in bilateral US-EU discussions on trade facilitation: a further reduction of industrial tariffs, the removal of high tariffs and subsidies in agriculture, the expansion in coverage of GATS and the Government Procurement Agreement and the strengthening enforcement of TRIPs (Morici 1999). This sectoral focus on agriculture, some services (preferably financial and audio-visual services) and government procurement mirrors US export interests as well as a continuation of the approach to pick up specific industries as front-runners in liberalisation which was started with the information technology products after the UR conclusion. Within the industrial sector, a sectoral focus has also been displayed in proposals which were suggested within the Asia Pacific Economic Cooperation Group (APEC) as so-called early voluntary sectoral liberalisation (EVSL).[33] This suggestion was made by the United States in order to initiate a liberalisation momentum for the 2010 Bogor target of free trade among APEC's advanced member states. As a result of APEC's self-understanding as a non-discriminatory arrangement, internal liberalisation within APEC would be extended to non-APEC members, subject to the reciprocity requirement (conditional MFN). Any group action of APEC would thus automatically become a subject of WTO negotiations under the Millennium Round.

Economic costs of sectoral liberalisation are evident. Unequal treatment of sectors could lead to diverging effective rates of protection between sectors and trigger misallocation (Dee et al. 1998). Non-sensitive ("easy") sectors would be liberalised first, sensitive sectors later. This would create an adjustment jam and further ground for special treatment (see above for the discussion of playing-for-time strategies in the textiles and clothing sector). Finally, focusing on agriculture and special services as US "pet" liberalisation sectors can easily lead the negotiations into an early deadlock, since trading partners would oppose sector-specific negotiations.

2. The EU Strategy: Toward a "Comprehensive" Round

The EU Commission has already set out its preferred approach to the MR (EU Commission 1999). It calls for a so-called comprehensive round similar to the UR and rejects a narrow sectoral approach. Explicitly, the two critical sectors agriculture and services are exposed when the latter approach is criticised. Broad negotiations should be time-bound, and results should already be achieved after three years, since — unlike in the previous round when the GATT was integrated into the WTO — no systemic questions would be expected to arise this time.

Apart from the broad coverage of issues to be discussed, the EU pleads for considering development aspects in more depth than before. This includes special treatment for least-developed countries (tariff-free treatment of essentially all industrialised countries' imports from them), assistance to capacity building in developing countries in order to trigger more participation in the WTO (Michalopoulos 1999), better coherence in different institutional settings (WTO and the Bretton Woods institutions) and, finally, better operationalisation of special and differential treatment. It is evident that the European Union seeks to draw developing countries on its side and that the EU challenge to find a WTO-compatible solution for reconciling preferential relations with low-income developing countries (Lomé Agreement) is reflected in its proposals. In short, the European Union continues the *mélange* between aid and trade aspects in spite of critics from economic quarters.

In a sectoral view, the EU has announced its defence of blue box measures. That would mean that compensatory payments would remain outside the AMS definition and thus

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33 Initially, the list of designated sectors for EVSL comprised fifteen industrial sectors (Yamazawa 1998). However, as no consensus could be achieved concerning implementation, the 1998 Kuala Lumpur Ministerial Meeting of APEC reduced the list to eight sectors to be pursued in the WTO. Yet, given the non-committing forms of cooperation within APEC, the Kuala Lumpur Meeting stated also that APEC members while expanding the EVSL beyond APEC would not be restricted in their freedom to act independently in the WTO negotiations (EC 1999: 4).

would not be subject to reductions. The renewal of the so-called peace clause in agriculture beyond 2003 is important for the European Union, since it would protect subsidies compatible with the Agreement on Agriculture against WTO-internal claims to dismantle them. Finally, the "multifunctional" role of agriculture which the European Union would like to see accepted aims at getting WTO endorsement for subsidies which following the European Union are still necessary to enable the agricultural sector to meet social and environmental functions in rural areas.

As concerns services, the European Union clearly pursues the bottom-up approach (see Section II.1 above). This approach acknowledges the peculiarity and hence sensitivity of individual service sectors and links further market opening to regulatory discipline. In reading the EU proposals, the development of a transparent and predictable regulatory environment seems at least as important as the opening of markets.

Quantifiable proposals of the EU include the harmonisation of tariff levels in non-agricultural products with three tariff bands (low, medium and high level), but again subject to flexibility according to the development level of partner countries and according to the sensitivity of sectors. Furthermore, the European Union still sees "trade defence" measures (including anti-dumping measures) as a necessary instrument to implement its export interests. Under non-quantifiable proposals, calls for international frameworks concerning competition, investment, environment and core labour standards can be mentioned.

Overall, the EU proposals mirror its traditional strategy to merge distribution and allocation targets and to burden all trade-related aspects of other issues upon WTO shoulders. Concessions to open markets are qualified with respect to domestic interests (sensitivity, non-economic issues) as well as presumed foreign interests (better treatment of developing countries). Hence, the proposals are open to critics concerning the assignment problem (non-separation of allocation and distribution targets) and the watering of trade liberalisation. Evidently, the target to make a new round "comprehensive" also reflects EU-internal problems of rising heterogeneity. This is partly due to forthcoming enlargement, but also due to different economic structures emerging through the deepening of integration. Risking more "incomprehensiveness" in terms of a more narrow but economically more coherent approach seems to have been non-reconcilable with the current political mainstream.

3. The Developing Countries: Hesitancy Can Become a Strategy

The role of developing countries in the world trading system is bound to increase as there is no industrial country left outside the WTO while all prospective members including China are either from the developing world or are in transition to either industrial or developing countries. Even with the consensus principle still prevailing in WTO decision-making, developing countries can no longer be ignored. This fact has found acceptance in the label used by many observers of the 1999 WTO High Level Symposium on Trade and Development for the next round: Development Round (WTO 1999b).

Both the European Union and the United States have already paid tribute to this role by linking a number of countries to them through hub-and-spoke trade agreements. The European Union has been the forerunner through its myriad of bilateral and regional preferential integration schemes in the Mediterranean and Africa. The United States has followed late but is now propagating a Free Trade Area of the Americas and APEC, both departing from NAFTA and the Canada-United States Free Trade Agreement as core schemes. The geographically clear separation between the Americas and the Eurafricas has recently been broken by the renewed interest of the United States in African countries' natural resource potential on the one hand and the designs of free trade agreements between the European Union and Mercosur and between the European Union and Mexico on the other hand. Such "Spaghetti bowl or criss-crossing of preferences", as

Bhagwati et al. (1998) have correctly labelled this development, can undermine the effectiveness, credibility and enforceability of the multilateral trading system, should the developing countries believe that more benefits could be collected from regional than from multilateral agreements.

Unfortunately, both the lack of implementing the UR and the systemic flaw of GATT/WTO to mix aid with trade issues have made developing countries at best hesitant to agree on a new round and at worst hostile to do so. Hesitancy and hostility are rooted in the lack of UR implementation of textiles and clothing liberalisation, the continuation of anti-dumping procedures, the existence of peak tariffs and tariff escalation, the pressure (as seen by developing countries) to comply with industrial countries' standards on environment, investment, labour and competition, the protectionist abuse of rules of origin and the ongoing protectionism in agriculture. What adds to these complaints is the inherent fear of developing countries to be overrun by leapfrogging improvements in technology, including services and agriculture. Finally, special and differential treatment traditionally rules the way many developing countries' policymakers perceive the WTO. Regrettably, political constraints facing the WTO chief officials have prevented them from calling the presumed fruitful *mélange* between trade and aid issues in the WTO what it actually is: a chimera.[34] Such constraints may include the growing importance of NGOs, many of which simply disagree with the straightforward nexus between more trade and higher economic growth.

Interestingly, economists like Srinivasan, reportedly have supported developing countries' hesitancy in entering a new round by pointing to the many pending issues in the implementation record of the UR (WTO 1999b: 7).

At first glance, it seems that the focus of many developing countries on a more even distribution of the gains from trade liberalisation as highlighted in the WTO Symposium could lead to a stalemate situation in the pre-stage of the Millennium Round. Yet, hesitancy for whatever reasons can also have a positive payoff for the new round. In many cases, gains are unevenly distributed simply because they could not materialise at all. The current system without full UR implementation favours few relatively advanced developing countries collecting rents from their position as established producers relative to the lower-income newcomers. Should hesitancy favour the acceleration of UR implementation, including trade facilitation and the dismantling of obsolete technical barriers to trade, poorer countries would be among the main beneficiaries.

However, even with such gains, many developing countries will continue to hesitate following the bicycle theory of keeping the world trade policy engine going (Bergsten 1999). The reason is simple: To esteem the achievements of trade liberalisation requires a thinking in counterfactuals, i.e. what would happen without open markets. For many policymakers in developing countries, it is still unperceivable that this counterfactual would have shown a much worse situation for their countries than the actual one.

V. Outlook: Technology Beats Tactics

All preceding multilateral rounds (like all rounds on "disarmament") were characterised by periods of standstill and leapfrogging, by deliberately planned delays in negotiations and likewise planned accelerations, by withdrawals from offers of concessions and by threats, in short: by tactical games. Understandably, the entire toolbox of cooperative and non-coopera-

34 Such constraints become visible when the former WTO Director-General Ruggiero mentions "...the wide consensus that trade liberalisation was not on its own sufficient for development" (WTO 1999b: 9) without mentioning that without trade liberalisation, there would be hardly any development at all. Likewise, empirical evidence rejects those who argue that special preferences for least-developing countries would be helpful. They would either trigger transhipment of components from advanced developing countries to least-developing countries to circumvent trade barriers against more advanced developing countries and consequently would induce donor countries to meticulously check origin certificates in order to discourage such transhipment. Alternatively, special treatment would be obsolete because of supply-side-induced obstacles to exports from least-developing countries.

tive games and the underlying theory found an excellent playing field in the world of disciplined mercantilism or — coined more neutrally — trade diplomacy. It is a safe bet that the MR will see similar endeavours of trade diplomats as before. Yet, whether the endeavour will be crowned by success is no longer sure for two reasons.

First, in the trade in "visibles" (goods), the pro-trade lobby groups have gained in enforcement capabilities. In agriculture, the shift from price to income support has made the extent of subsidies transparent and politically less defendable. Producers are increasingly divided over their stance toward international trade due to their different affiliation to processing intermediates or producing import-competing goods, or to landless or landrich farmers. Consumers demand goods locally which they have consumed abroad as visitors, for instance. Budget constraints have put a cap on subsidy expansion. Moreover, R&D investment in processed agricultural products have made just those countries internationally competitive which traditionally have adhered to restrictive trade policies. They now learn the lesson of reciprocity: without own concessions, there are no concessions on the export side either. Yet, the most important driving force towards freer trade in visibles is the success of learning in those sectors which indirectly were discriminated against because of subsidies paid to the protected sectors.[35] This success makes competition for subsidies much less clearer in outcome for the hitherto protected sectors than in the past.

Second, in the trade in "invisibles" (services), unprecedented technological progress opens the door to first-mover advantages which the beneficiaries will defend against those who would like to regulate and contain trade in invisibles for various reasons. With innovations coming first to stimulate cross-border trade and regulations coming later to control such trade, one is reminded of the hare-hedgehog race. What matters is that the borderline between invisibles and visibles becomes porous as seen in the e-commerce debate on goods versus services. To some extent, services can be defined as goods and vice versa or can be substituted for one another. It is in this trade primarily where technology beats tactics.

Still, however, there is no golden age of unlimited trade even if the trade diplomats were only to seal what traders had already achieved. Particularly, many NGOs are concerned about real and emotional negative spillovers concerning environmental and labour standards, and they are no longer political light-weights. Unlike in the past, their role in the MR has been politically accepted. Some developing countries fear to be marginalised in the trade and technology nexus and hence are more sympathetic to regulations and special treatment than others. Though both players are far from being natural allies, they will sit close to the brake lever in the MR. And finally, there is the immobile factor of unskilled labour in industrial countries, gaining as consumer but eventually losing as wage earner. How he defines himself and how he succeeds to form cross-border pressure groups, this will decide on whether the pro-traders will have a home game or an away game in the MR.

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35 A few years ago, for instance, the German industry raised in open debate the question on the bill they had to pay in terms of resources foregone because of protection conceded to the agricultural sector.

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