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# MULTILATERALISM AND REGIONALISM: THE NEW INTERFACE

## Chapter III: Comments on Dynamism in the Interface of Multilateral Trading System and Regional Trade Agreements: A Post-Cancún Perspective



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## Chapter III

### COMMENTS ON DYNAMISM IN THE INTERFACE OF MULTILATERAL TRADING SYSTEM AND REGIONAL TRADE AGREEMENTS: A POST- CANCÚN PERSPECTIVE

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The adoption of the Uruguay Agreements and the establishment of the World Trade Organization in 1995 is acknowledged as a significant milestone in the Multilateral trading system. Prior to that, GATT laid down rules, which countries applied among themselves when trading in goods. In the Uruguay Agreements those rules were broadened to cover agriculture, trade in 'services', trade-related aspects of 'intellectual property' and trade-related aspects of investment measures.

The basic objective of WTO rules is to promote greater integration of the world economy by encouraging countries to pursue 'open and liberal policies'. It is assumed that the resulting export-oriented growth would create more employment and in the long run result in poverty reduction.

It is recognized that regional trade arrangements are an important aspect of the strategy for development. Hence, the ministers gathered in Doha while stressing that the WTO 'was a unique forum for global trade rule making', also recognized 'that regional trade arrangements can play an important role at promoting liberalization, expansion of trade and in fostering integration'.<sup>1</sup> Furthermore, it was agreed that negotiations aimed at clarifying and improving procedures under existing provisions applying to regional trade agreements be undertaken and that these negotiations would take into account their developmental aspects.<sup>2</sup> The expectation was that both the multilateral trading system (MTS) and regional arrangements should be complementary and mutually reinforcing. There has been an exponential growth of regional trade arrangements. Virtually all members of WTO are today party to, or are in the process of, negotiating a regional trade agreement; this explains the need for coherence between the two processes if the potential benefits are to be maximized.

The failure of the Cancún Ministerial Conference, whose declared purpose was to take stock of progress in negotiations, provide the necessary political guidance and take decisions where necessary, was a great disappointment to all member states. While the breakdown was a major setback, its impact on the functioning of the multilateral system has been exaggerated. This is not the first time that the multilateral trade negotiations have failed to meet the agreed schedule. Some thought that this situation would result into the demise or serious impairment of the MTS. They envisaged that the major trading powers would resort to bilateral and regional trade arrangements which would be of great disadvantage to developing countries and which the Doha Round had been expected to forestall. The Economist Magazine<sup>3</sup> observed that the Cancún outcome "is going to leave most of the people in the world worse off and that

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<sup>1</sup> Paragraph 4 of the Doha Declaration.

<sup>2</sup> Paragraph 29 of the Doha Work Programme.

<sup>3</sup> Herald Tribune, 23 September 2003, "Failed Cancun Talks give impetus to bilateral deals", p.16.

those who would no doubt suffer the worst are the world's poor". It was further observed that, "The developing countries will come to regret the consequences". This fear was reinforced by a flurry of activities to negotiate bilateral and RTAs (i.e., USA, Australia, Morocco, Bahrain, etc.).

The apprehension that the failure in Cancun would divert most countries and especially the USA and EU away from multilateralism to bilateralism and regionalism in trade negotiations was given reinforced by statements made by both EU and US. The US Trade representative was quoted as saying that they would more vigorously pursue bilateral agreements. The EU Trade Commissioner, on the other hand, described the WTO as medieval and wondered whether they should maintain multilateralism, which was the basic tenet of EU commercial policy as their privy.

While the failure of Cancún was disappointing, it should be put in perspective. It was not the first time that the multilateral trade negotiations have failed to live up to their agenda. Indeed the road to Cancún and the preparatory process was full of 'bumps' and 'roadblocks' coupled with missed deadlines on issues of development. Developed countries made numerous speeches supporting the Doha Round as a development agenda, they were extremely frugal when responding to proposals on special and differential treatment (SDT) and implementation on agriculture, both of which were seen as a lynchpin of success by developing countries. The 'crash' of Cancún has not, in itself, dented the credibility of the multilateral system.

Cancún simply highlighted the major concerns of developing countries, which the multilateral system had hitherto not addressed. Instead, the system has been used by major players to push their own policy agenda on other countries. As they continue to carry out highly protectionist policies in agriculture and textiles, which they are reluctant to liberalize, they were, at the same time, pushing developing countries to open up their markets to imports. However, a number of empirical studies on the trade liberalization experiences of developing countries at a lower stage of development and by least developing countries have showed that, unless the physical and human infrastructure necessary for development are first put in place, liberalization can lead to de-industrialization and unemployment. Yet these countries are being pressured to carry out substantial reductions of their tariffs. Those that are reluctant to carry out reforms in agriculture have been forcefully pushing for negotiation on new issues, such as the multilateral agreement on investment and competition policy whose impact on economies of developing countries remains to be clarified.

Developed countries have been reluctant to remove restrictions on the movement of national persons (mode four) in the In the negotiation of services, especially with regard to the movement of skilled and unskilled labour in which the developing countries have a comparative advantage. Whether it is this context of multilateral or bilateral arrangements these are the concerns of developing countries, which have to be addressed.

What the failure of Cancún showed was that the days are gone when the major powers could exercise full dominance over negotiations and impose solutions, which only served their objectives and interests, without taking into account the interests of developing countries. Developing countries have become more proactive, better informed, and better-organized players. This is due to the assistance of organizations like UNCTAD, South Center and Civil Society, who have provided informative studies and research. It has also become clear that the Doha Agenda round cannot successfully be concluded unless the problems with agriculture are satisfactorily addressed; those who have asked for new issues to be placed on the table should

also scale back their ambitions. Unfortunately, at the Fifth Ministerial Meeting in Cancún, developed countries lacked the political will to resolve the developmental aspects of the Doha agenda, which would make the multilateral trading system more fair and equitable.

What is needed after Cancun is not to engage in a blame game, but to pause and constructively consider how to move the process forward. This requires a genuine effort to address issues such as agriculture, cotton, implementation issues, special and differential treatment, etc., which developing countries have put on the table, rather than attempting to create divisions in the groups of developing countries. The leaders of developing countries have continuously reaffirmed their support of multilateralism. It is therefore encouraging that both the US trade Representative and the EU Trade Commissioner have since taken a leading role in ensuring that the discussion in WTO are back on track. This has paved the way for General Council to continue dialogue. Hopefully this will result into a solution that genuinely addresses the concerns of all countries.

As indicated above, the question of whether the Cancun failure could promote bilateralism or regionalism at the expense of multilateralism was, in my view, an exaggerated fear. Free trade, preferential and regional trade arrangements have always run parallel to WTO processes. These arrangements are now an integral part of international trade and they account for almost half of the world trade. The decision by USA and Latin America to negotiate free trade of the Americas and by the EU to negotiate partnership agreements with ACP were taken a decade ago. These arrangements are pursued for a variety of economic and underlying geopolitical and security interests. With or without Cancún, they would have been pursued anyway.

They, however, present both challenges and opportunities. An OECD study (*Regionalism and the Multilateral Trading System*) exploring the relationship between the MTS and RTAs concluded that these arrangements can compliment one another, but could not replace a coherent set of multilateral rules and a process of progressive liberalization. It is clear in the evolving world trade system regional arrangements and regional preferences will continue to play an important role. However it is necessary to ensure that they are consistent with the MTS, and are supportive of the development of developing countries.

There are three levels in which there is an interface between the MTS and RTAs.<sup>4</sup> The first level of WTO rules define the specific conditions under which these arrangements are allowed to exist – namely article XXIV of GATT, Article V of GATS and the enabling clause as regards South-South preferential arrangements. At the second level, MFN market access commitments where the MTS determines the margin of preference that can be obtained at the regional level. At the third level, the multilateral disciplines constitute a floor which all members are committed to observe, and which determine the conduct of their trade policy. In short, the MTS provides the framework for negotiating RTAs. Within this framework, RTAs could impose certain obligations to parties or provide certain benefits, which go beyond existing multilateral rules. They may also divert or converge with the multilateral system and may impact on third parties if there is a trade diversion.

In parallel to WTO negotiations, the European Union and ACP countries have, within the framework of the Cotonu Agreement, been involved since 2002 in negotiations on economic partnership agreements with the aim of establishing new WTO-compatible trading arrangements. They are aimed at progressively removing barriers of trade between EU and

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<sup>4</sup> Paragraph 25 of the issues paper

ACP countries which "would build on the regional integration initiatives of ACP States" and promote sustainable development and contribute to poverty eradication in ACP countries. This in essence would be a free trade agreement between the developed (EU) and developing ACP region or country. This would fall under the provision of Article XXIV of GATT requiring substantial coverage of all trade in a reciprocal manner within a period of "10-12 years". Furthermore, the negotiations are expected to cover investment, competition, trade facilitation, data protection and services. This would mean a WTO plus as there are no disciplines on some of those issues in WTO. The ACP countries in carrying out simultaneous negotiations in WTO and under Cotonu face considerable challenge of coordination and consistence of their positions in the two processes.

ACP countries are justifiably worried that the interpretation of "substantially all" under article XXIV may give more advantage to European producers given their advanced stage of development. Article XXIV of GATT assumes agreements between equals and it is not clear whether it allows SDT parties that are not equals. As originally envisaged SDT provisions were intended to enhance market access conditions of beneficiary countries and permitted derogation from certain multilateral disciplines. The derogation was intended to ensure that countries had the tools to strengthen their supply capacity and be able to take full advantage of the preferential market access that has been granted to them. It is in the light of this that the ACP countries have submitted a proposal for special and differential treatment in GATT Article XXIV in the negotiating group on rules<sup>5</sup>. They proposed that members should agree that SDT treatment for developing countries be formally and explicitly made available to developing countries in meeting the criteria of paragraphs 5 to 8 of GATT Article XXIV in the context of regional agreements between developing and developed countries. They proposed appropriate flexibility with regard to duties covering substantially all trade and in interpretation of 'other restrictive regulations of commerce.'

In the MTS negotiations on agriculture, the broad objective is to secure the complete elimination of export subsidies, substantial reduction in domestic support and substantial reduction of the MFN tariffs applied to imports. The proposals on the table with regard to Non-Agricultural products, Market Access (NAMA) aim to reduce MFN tariffs, and more especially at ensuring that high or peak tariffs applied by developed countries are substantially reduced, if not eliminated. The outcome of such negotiation would have a significant impact on the benefits that ACP countries could derive from Cotonu.

Both Cotonu and "Everything But Arms" (EBA) allow imports of both agriculture and industrial products in EU markets on preferential rates. The margin of preferences would be narrowed and affect the competitiveness of ACP countries. A joint study by UNCTAD and the Commonwealth Secretariat found that the benefits of preferential access to LDCs under the "Everything But Arms" proposal are likely to be significant especially in such products as horticulture, textiles and leather products.

This is why the ACP countries have insisted that the techniques and modalities to be adopted take account of the needs of preference beneficiary countries. This could for instance be achieved by exclusion from MFN reduction products on which the margins of preferences are meaningful in trade terms providing longer terms for tariffs reductions agreed in the negotiations than the normal 5 to 8 years, and providing compensatory arrangements.

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<sup>5</sup> WTO Document TN/RL/W/155 of 28 April 2004.

Whether in this context of EPA or MTS, it is crucial that the question of agricultural subsidies be addressed. Given the requirement of reciprocity between the Cotonu agreements and the WTO there is a danger that subsidized agricultural products could be dumped in ACP countries, thereby undermining their food security and competitiveness in their local markets. Developing countries should, therefore, not lose sight of their strategic objective of using trade for development, and not as an end in itself.

Services constituted a significant share of the GDP of developing countries and are a major input for production of goods and services. Liberalization in banking, insurance and telecommunication sectors could improve the capacities of manufacturing industries in marketing their products abroad. The issue, however, is whether liberalization should be achieved through MTN participation, other arrangements, or on autonomous basis. Despite the fact that Article V of GATS allows a measure of flexibility to developing countries, countries involved in MTN negotiations only make reciprocal commitments when they are able to get secure improved access for their services and products. In the case of developing countries particularly Africa, service products which could be exported in cross-border mode, have not yet been developed. The only services in which those countries have a comparative advantage are those that can be provided through the movement of natural persons.

Developed countries have been reluctant to liberalize mode 4, which allows movement of such persons. It appears that progress can be more forthcoming in a regional context. Within the context of RTA, arrangements have been made for mutual acceptance of each country's qualification.

RTAs have acquired increased prominence in the context of rules development. As indicated earlier, the new trade agreements currently in the process of being negotiated envisage liberalism to encompass investment, competition policy, the protection of intellectual property, as well as trade and labour standards.

ACP countries have opposed these issues in the WTO. There is a clear danger that they will end up taking in a regional context of standards that are higher than the WTO and later on be pressed by the same rules at the multilateral level.

In the current multilateral trade negotiations the developed countries have emphasized that developing countries would gain most from tariff reductions of other developing countries. The question is the mechanism for achieving this objective of South-South cooperation. The preferred mechanism is the Global System of Preferences negotiated under UNCTAD. This system has two special benefits for the developing countries over the reducing tariffs in the WTO framework. Firstly, a developing country while reducing tariffs under the GSTP does not have to extend this benefit to the developed countries; thus there is less revenue loss for the committing importing developing country. Secondly the beneficiary exporting developing country will face less competition from the developed country, as the latter will not get the advantage of this lower tariff in the developing countries. Over a course of time, this process is likely to enhance investment in the developing countries in manufactures and agriculture, because of larger market access opportunities among the developing countries.

UNCTAD is the focal point in the United Nations system for the integrated treatment of trade and the interrelated issues of finance, technology and development. Developing countries in the post-Cancún period are faced with the challenges of concurrent negotiations at the

multilateral level, regional trade arrangements and in the case of ACP/EU, a new generation of trade agreements involving reciprocal rights and obligations.

Many developing countries need capacity strengthening for effective negotiations. In addition they need the necessary technical information to determine their negotiating options. UNCTAD through its research analysis and technical cooperation programs has an important role to clarify the implication of the interface between RTAs and MTS and help to ensure that these processes are complimentary, promote development and leave these countries with sufficient policy space to implement development measures.

Lastly I wish to take this opportunity to thank UNCTAD Secretariat, BNDES and Rio for organizing this forum, and facilitating our participation.