

THE WORLD TRADE ORGANIZATION, ITS FUTURE, AND RUSSIA'S FUTURE IN IT

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Ten years ago this month, trade ministers met in Marrakesh, Morocco, and signed the Uruguay Round agreements that created the World Trade Organization. Since formally opening its doors in January 1995, the WTO has served as the forum for new sectoral agreements on information technology products, telecommunications, and financial services. In addition, it has heard and ruled upon hundreds of disputes over the proper interpretation of WTO agreements. And it is currently hosting the Doha Round of global trade talks, which promises to make further progress on reducing trade barriers and trade-distorting subsidies in the organization's 146 (and counting) members.

During the past decade, the WTO has been the focus of incessant, swirling controversy. Its critics charge that the organization is a tool of exploitative multinational corporations, and that it undermines national sovereignty and democratic governance. Yet despite these charges, no original member has moved to exit the WTO, and since 1995 19 additional countries have joined the club. Among those new members are seven former Soviet republics: Armenia, Estonia, Georgia, Kyrgyzstan, Latvia, Lithuania, and Moldova. Russia, for its part, is actively pursuing WTO entry, although negotiations remain far from completion.

So who is right—the WTO's critics, or its members and would-be members? Does the WTO have a constructive role to play in a liberal international economic order? How well is it playing that role, and what does the future hold? Is joining the WTO a good idea for Russia—and under what terms? To address these questions, this paper first clarifies what the WTO does and does not do. Next, it looks ahead to identify some troubling threats to the WTO's continued efficacy. Finally, it examines Russia's accession negotiations and evaluates Russia's stake in joining the organization.

Demystifying the WTO

There is much less to the WTO than meets the eye. Its detractors depict it as immensely powerful, but in truth the WTO is exceptionally weak and fragile. Its functions—like those of its predecessor, the General Agreement on Tariffs and Trade—are basically two. First, it serves as a neutral forum in which member countries can agree to change their policies in a concerted manner, i.e., to reduce their trade barriers at the same time other countries do the same. Since its founding in 1947, the GATT organized eight rounds of multilateral tariff cutting and mutual reductions in other trade barriers; the WTO, as mentioned above, has brokered three sectoral deals and launched a ninth omnibus round of talks.

But the GATT could not and the WTO cannot impose these agreements by force. Deals are struck only if all members agree, and they apply only to those members that do agree. Despite the vocal complaints in the United States about the WTO's threat to national sovereignty, the fact is that every member, including the U.S., has veto power over every WTO agreement. Furthermore, no WTO agreement alters any U.S. law until Congress passes and the president signs the necessary implementing legislation.

The WTO's second function is to serve as a neutral forum for resolving disputes about previously signed agreements. A country that suspects another WTO member of failing to honor its obligations under an agreement can invoke dispute settlement procedures. Under the old GATT's toothless arrangements, the defendant country had to give its permission before an adverse verdict could be announced; WTO rules do not extend that courtesy to rule breakers. But once the WTO announces its decision, it has no coercive powers to force members to comply. Its last resort is to authorize aggrieved

countries to impose trade sanctions against recalcitrant violators—but countries have always had the power on their own to close their markets to each other. Here again the WTO is accused of undermining national sovereignty—this time by striking down national laws left and right like some rogue judicial tribunal. In reality, though, the only power the WTO wields lies in the moral authority of its reputation for fairness. If countries don't voluntarily mend their ways in compliance with adverse rulings, the WTO is powerless to press the issue.¹

The past couple of decades have witnessed dramatic reductions in trade barriers around the world, but these developments owe comparatively little to the GATT and WTO. The boldest moves toward opening markets have occurred outside the context of negotiations: countries as diverse as Australia, New Zealand, Chile, Thailand, and India decided unilaterally to forsake the old import-substitution model in favor of greater integration with the global economy. The driving force for sweeping change in those countries was not tough bargaining or the prospect of a quid pro quo, but rather the realization that protectionism was causing economic stagnation.²

Even when liberalization has occurred under GATT or WTO auspices, it has often deviated from the predicted path. Trade negotiations are thought to work on the principle of reciprocity: one country “gives up” trade barriers at home in order to “get” improved access to foreign markets. Official WTO parlance reflects this thinking. Offers to open

¹ For a discussion of the WTO's supposed threat to national sovereignty, see William H. Lash, III and Daniel T. Griswold, “WTO Report Card II: An Exercise or Surrender of U.S. Sovereignty?” Cato Institute Trade Briefing Paper no. 9, May 4, 2000, available online at <http://www.free-trade.org/pubs/briefs/tbp-009.pdf>.

² For a detailed account of the global move toward economic liberalization generally, and trade liberalization in particular, see Brink Lindsey, *Against the Dead Hand: The Uncertain Struggle for Global Capitalism* (New York: John Wiley & Sons, 2002). This section of the present paper borrows from the discussion of the WTO in Chapter 11 of that book.

one's own market are referred to as "concessions," while other countries' offers to liberalize are called "benefits." The underlying assumption is that countries have no real interest in cutting their own trade barriers; they do so only to gain new markets for their exports.

But an examination of some of the WTO's recent successes in reducing trade barriers reveals the shakiness of that assumption. For example, dozens of developing countries agreed to participate in the WTO agreements on telecommunications and financial services—despite the fact that their own industries are in no real position to export such services or otherwise expand abroad. These countries were motivated not by reciprocity but by the recognition that more open domestic markets would promote economic development at home. Likewise, consider China's bold offer of market-opening commitments in its bid for WTO membership. China had first sought membership in the GATT back in 1986, but talks went nowhere until 1999, when suddenly China began to agree to sweeping liberalization of its market. Why the change of heart? It seems clear that China's leadership came to the conclusion that a new burst of market reforms was necessary to reverse the country's flagging economic performance. Wrapping those reforms in a package of international obligations, it judged, would make them easier to get past domestic political opposition and then insulate them from subsequent reversal.

These examples show that while the WTO can facilitate trade liberalization, it is not the main engine. Trade negotiations can strengthen the political prospects for dismantling domestic barriers by sweetening the pot. Liberalization always provokes opposition from domestic import-competing interests; trade agreements help to overcome

that opposition by adding a new partner to the pro-trade lobbying coalition—namely, exporters eager for better access to foreign markets. Furthermore, trade agreements are especially useful in consolidating and institutionalizing prior liberalizing gains. Once countries decide to open their own markets in their own national interest, those decisions are harder to undo by subsequent protectionist-minded governments if liberalization has been enshrined as an international obligation. Trade agreements can thus “lock in” reforms by imposing additional political constraints on their reversal.³

But even if the WTO were wiped from the face of the earth, the ongoing worldwide process of reducing trade barriers would still continue. Progress would be slower and more selective, but it would not come to a halt. That is because the fundamental impetus for market-opening comes, not from international agreements and institutions, but from national-level decisions regarding national economic interests.⁴

Does the WTO Have a Future?

The modest assistance that the WTO does lend to trade liberalization cannot be taken for granted. An institution as weak and fragile as the WTO is never far from paralysis and irrelevance. At present, as usual, it is possible to spy a number of dark clouds looming on the WTO’s horizon.⁵

³ For a recent evaluation of the WTO’s record in promoting trade, see Arvind Subramanian and Shang-Jin Wei, “The WTO Promotes Trade, Strongly But Unevenly,” International Monetary Fund Working Paper 03/185, September 2003, available online at <http://www.imf.org/external/pubs/ft/wp/2003/wp03185.pdf>.

⁴ For an extended argument on the relative merits of liberalization “from above” and “from below,” with a decided preference for the latter, see Razeen Sally, *Classical Liberalism and International Economic Order: Studies in Theory and Intellectual History* (London: Routledge, 1998).

⁵ For a more extended discussion along similar lines, see Razeen Sally, “Whither the WTO? A Progress Report on the Doha Round,” Cato Institute Trade Policy Analysis no. 23, March 3, 2003, available online at <http://www.free-trade.org/pubs/pas/tpa-023.pdf>.

When all is said and done, the WTO is only as effective as its leading members are willing to make it. Unfortunately, the major trading powers are presently displaying little commitment to the institution's continued success. Consider the Doha Round as a case in point. The round has been in trouble almost from the moment it started in November 2001. Since then, a number of early deadlines were missed, and plans for what could be accomplished at the September 2003 ministerial meeting in Cancun, Mexico had to be scaled back because of all the delays. Even with reduced ambitions, the Cancun meeting ended in dismal and rancorous failure, and the initial schedule for completing the round by the end of 2004 has been abandoned. Negotiators are still struggling to pick up the pieces after the Cancun debacle, and the negotiations remain in disarray.

What went wrong? There are many complex issues in play, but the bottom line is that all of the major players in the WTO have been more concerned with defending their own anti-trade policies than with obtaining improvements in the policies of their trading partners. For the European Union and Japan, the political pain of reforming their egregious agriculture subsidies and trade barriers far exceeds any political benefit to be gained from expanding commercial opportunities for their exporters and multinational corporations. Consequently, they have made even the slightest "concessions" only grudgingly, and they have stuck to impractical demands for new investment and competition rules as a diversionary tactic to draw attention away from agricultural issues.

The United States, the other farm-subsidy superpower, is at least willing to talk about significant changes in its agricultural policies. However, in the weeks prior to Cancun, the U.S. abandoned its more ambitious proposals and sided with the EU in favor of a minimalist agricultural agenda—a critical misstep that helped to set the stage for

Cancun's failure. In addition, the United States is the leading opponent of increased discipline on the abusive use of antidumping laws; on this issue, the U.S. government has decided that the interests of the protectionist American steel industry trump all other considerations.⁶

The major developing countries, meanwhile, are stridently insisting on “special and differential treatment”—WTO-speak for ambitious liberalization by rich countries and as little reform as possible by poor countries. In other words, their position is that rich countries should stop the disgraceful practice of immiserizing poor countries with subsidies and trade barriers, but that poor countries should receive *carte blanche* to immiserize themselves with the same kinds of policies. In taking this stance, it appears that many developing-country leaders are more interested in avoiding politically difficult reforms at home than in bettering the prospects of their people through reforms at home and abroad.

The WTO's other main job besides hosting negotiations is settling disputes. And here again, the WTO's biggest members are putting short-term political considerations ahead of the long-term vitality and effectiveness of the institution. Specifically, both the United States and the European Union have dragged their feet in changing policies found to violate WTO rules. The EU revised its discriminatory preferences for bananas imported from former colonies only under the pressure of U.S. retaliation; it decided to endure retaliation rather than revisit its WTO-inconsistent ban on hormone-treated beef. The U.S., for its part, persisted with unjustified steel tariffs to the very brink of retaliation by the EU; years of U.S. paralysis in the face of a WTO ruling against tax preferences for

⁶ For a detailed discussion of antidumping policy, see Brink Lindsey and Daniel J. Ikenson, *Antidumping Exposed: The Devilish Details of Unfair Trade Law* (Washington, D.C.: Cato Institute, 2003).

American exporters finally forced a reluctant EU to begin imposing trade sanctions last month. In other cases involving the so-called Byrd amendment to the antidumping law and the old and seldom-used 1916 Antidumping Act, Congress has failed to respond to adverse WTO rulings and the threat of more retaliation is growing.⁷

What message, then, are the U.S. and EU sending to the rest of the world? Might makes right is the message, and it is a grim one indeed for the future prospects of a rules-based trading system. If the WTO's two biggest members will live up to their WTO obligations only under the threat of punitive duties, we cannot be surprised if other countries start following our bad examples. It is a very real possibility that more and more WTO agreements will be honored in the breach—much like the old GATT whose toothless ineffectiveness the WTO was supposed to cure.

The WTO's troubles do not end with the current difficulties in enforcing and expanding needed disciplines on trade barriers and subsidies. In addition, the WTO is menaced by efforts to extend the organization's mandate to new issue areas. This tendency toward “mission creep” threatens to mire the WTO in intractable controversies that will only frustrate progress in the traditional mission of eliminating policy biases against trade.

From its inception in 1947 to its end in 1994, the old GATT system focused on imposing negative obligations on its members. In other words, its rules generally took the form of prohibiting bad things—in particular, discriminating against foreign goods and services—rather than compelling good things. The Uruguay Round agreements that

⁷ See Dan Ikenson, “‘Byrdening’ Relations: U.S. Trade Policies Continue to Flout the Rules,” Cato Institute Free Trade Bulletin no. 5, January 13, 2004, available online at <http://www.freetrade.org/pubs/FTBs/FTB-005.html>.

created the new WTO system contained a decisive break from that pattern with the agreement on trade-related intellectual property. The main thrust of the TRIPS agreement was to impose positive obligations on WTO members, i.e., to require them to enact and enforce specific protections for intellectual property rights.

The TRIPS precedent has since been cited by various groups that want to use the WTO to advance their own regulatory agendas, whether in the realm of environmental protection, labor rights, or competition policy. The expansion of the WTO into these areas would move the institution in precisely the wrong direction: increasing government intervention in economic life rather than reducing it.

But the prospect of a new layer of international regulatory mandates is not the most pressing concern, since it is extremely unlikely that, for the foreseeable future, WTO members will come to any kind of meaningful agreement on these controversial subjects. Rather, the main threat is that the campaign to transform the WTO into an international regulatory body will end in an impasse between the rich countries that support such a move and the poor countries that are leading the resistance. That impasse will then block, not only misguided initiatives, but also badly needed progress in reducing trade barriers and subsidies. In this regard, it was a deadlock over labor and environmental issues that was the primary reason for the failure to launch a new trade round in Seattle in 1999. And in Cancun, unresolvable differences over competition policy and other so-called “Singapore issues” (investment, government procurement, and trade facilitation) were the proximate cause for the meeting’s collapse.

Finally, the WTO runs the risk of being overwhelmed by political grandstanding—what could be called the “UN-ization” of the institution. During its

nearly half-century of existence, the old GATT was remarkably effective for an international institution because it was small, focused, and low-profile. Its purpose was to get things done, not to create photo opportunities or provide a platform for sterile speechifying. As the WTO has grown in size, membership, and prominence, it is vulnerable to being taken over by elements more interested in symbolism and point-scoring than in actually improving trade rules.

The emergence prior to the Cancun meeting of a new bloc of developing countries—known as the Group of 20, and led by Brazil, China, and India—bears watching in this regard. On the one hand, a relatively cohesive bloc of developing countries could facilitate real progress in the WTO by creating an effective counterweight to the U.S. and EU—a counterweight that could exert salutary pressure on rich countries to reform their shameful agricultural policies. However, there is a significant risk that the Group of 20 or some successor group could wind up as a soapbox for self-appointed champions of the “global South” to denounce all the various sins, real and imagined, of the advanced economies. Polarization of the WTO along North-South lines was featured with dismal results during the Cancun meeting; if the future holds more of the same, it offers diminished prospects for constructive negotiations.

The problems facing the WTO are real, but by no means is doom inevitable. The Doha Round’s flagging progress is hardly unprecedented: trade talks usually look all but hopeless until the very moment when a breakthrough has been reached. The prior Uruguay Round required 12 years to launch and complete, with many crises and breakdowns along the way. The dispute settlement system, for all its flaws, remains an enormous improvement over the old GATT procedures, and the fact is that the vast

majority of the disputes heard to date have been settled successfully without any need to threaten retaliation. Critical attention to the WTO's shortcomings is not intended to promote defeatism; rather, such attention is necessary if those shortcomings are to be remedied and growing threats to this valuable organization are to be headed off.

Russia and the WTO

In addition to hosting negotiations and settling disputes, the WTO has one other method, selective but occasionally powerful, to encourage liberalization. That method consists of setting a high price for membership in the club. Countries that haven't yet joined the WTO can be required to make ambitious liberalization commitments as part of the accession process.

China's accession experience is the most spectacular instance of this phenomenon. The world's most populous country was not allowed to enter the WTO until it had made sweeping commitments to open its markets—commitments that went far beyond those that apply to many existing members. Of course, these differential and higher standards for China should not be seen as burdensome: fulfilling its entry requirements will be good for China's economic health. Furthermore, subjection to high international standards aids China's reform-minded leaders in their domestic battles against vested interests and other opponents of pro-market policy changes.

Now Russia is struggling with the negotiation of its accession commitments. Policymakers with an interest in modernizing Russia's economy should welcome this process as an opportunity to advance their agenda. At the same time, however, Russian authorities would be well advised to resist those occasional demands from WTO members that are not consistent with Russia's best interests.

The WTO accession process proceeds along two tracks. First, there is a formal WTO process in which Russia's generic trade-related policies are examined and evaluated, issues of concern to various members are raised and ventilated, and official accession protocols are ultimately drafted.⁸ Much of the real action, however, occurs on the informal, bilateral track, where the prospective entrant negotiates one-on-one with interested WTO members. Under WTO rules, each existing member has the right to limit its WTO obligations with respect to a new member at the time of that new member's entry. Armed with this leverage, existing members are able to extract commitments from the acceding country as the price for assuming full WTO obligations with respect to the new entrant. The bigger the WTO incumbent, the greater its leverage over an acceding country—and so it is no surprise that the bilateral negotiations with the U.S. and the EU are the two biggest obstacles that stand between Russia and WTO membership.

For the most part, the U.S. and EU are targeting trade barriers that Russia would be better off without. In the financial sector, foreign participation in insurance firms is now capped at 15 percent, and foreign bank branches are currently prohibited. Efforts to grant Rostelecom a six-year monopoly over inter-city and international calls have come under fire, and rightly so. Russia's screening procedures for food imports, which have attracted U.S. ire, act as a significant and nontransparent trade barrier. Both the U.S. and EU are urging Russia to sign the Civil Aircraft Code, which binds tariffs for aircraft and aircraft parts at zero, but Russia is balking for purely protectionist reasons. On all of these

⁸ See World Trade Organization, "Draft Report of the Working Party on the Accession of the Russian Federation to the World Trade Organization," WT/ACC/SPEC/RUS/25/Rev.2, May 26, 2003, available online at <http://www.wto.org>.

issues, there is a happy coincidence between the U.S. and EU positions and Russia's national economic interest.

In some cases, however, the U.S. and EU negotiating positions are questionable. The U.S., in particular, is insisting on more aggressive moves by Russian authorities to protect intellectual property rights. As mentioned above, the inclusion of intellectual property rights enforcement in trade agreements represents a dubious expansion of the scope of such agreements. Acceding to U.S. demands on these issues would surely result in the transfer of resources (in the form of royalty payments) from Russian firms to American firms, but whether that loss would be compensated for by greater foreign investment and domestic innovation is unclear. This is not to say that Russia's intellectual property rights regime is perfect—hardly. Rather, the point is that the U.S. approach to such matters is not above reproach, either, and so Russia should be cautious about uncritically adopting the U.S. model.

The EU, meanwhile, is demanding a thoroughgoing restructuring of Russia's natural gas industry. In particular, the EU objects to the fact that domestic gas prices in Russia are a fraction of the prices that Gazprom, the Russian gas monopoly, charges in export markets. Without a doubt, Russia's natural gas sector is plagued by corruption and market distortions. Nevertheless, the overhaul of this gigantic and thoroughly politicized industry extends well beyond the WTO's proper concerns. Moreover, the EU's motives in raising this issue are largely protectionist: the idea is to protect EU steel and fertilizer producers from low-cost Russian competition by raising the latter's energy costs. Such parochial concerns are a poor excuse for blocking Russia's entry into the WTO. After all, the EU already has the authority to impose countervailing duties against subsidized

Russian imports; if artificially low natural gas prices constitute a subsidy as the EU contends, then a remedy is already at hand.

While the details are often complex, the bottom line is clear: Russia has a strong interest in joining the WTO. First, joining this club would be an important symbolic step in Russia's ongoing modernization efforts. And once inside, it would have recourse to WTO agreements that limit other countries' ability to discriminate against Russian goods and services. But most important, Russia can use the accession process to achieve important and badly needed economic policy reforms. Admittedly, the market-opening commitments needed to secure Russia's entry into the WTO would leave many of the country's deepest problems unaddressed. Nevertheless, making and fulfilling those commitments would push Russia in the right direction. Accordingly, pro-market policymakers in Russia should seize this chance to make some real if limited progress.

Conclusion

The World Trade Organization is a weak and fragile organization with an uncertain future. That said, it is far from useless. The WTO lends modest encouragement to the progress of international economic integration; in addition, and perhaps more important, it erects obstacles that hinder backtracking from progress already made. Consequently, supporters of free and open markets should count themselves supporters of the WTO as well. In that role, they should encourage their home-country governments to promote the institution's effectiveness—by participating constructively in negotiations, upholding the integrity of WTO rules in dispute settlement, and guarding against ill-advised expansions of the WTO's mission.