Australia’s interests in the WTO*

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Australia’s prosperity is highly dependent on international trade. Access to world markets has long been a staple for our farming and mining industries. It has also become the key to the performance of our manufacturing industries, helping to provide the scale economies and global integration necessary for their efficient operation. Our burgeoning services sector is also increasingly reliant on foreign markets, which have become more accessible through trade as well as foreign investment.

Equally, Australian businesses benefit from technology transfer and capital equipment sourced from abroad, and the domestic economy benefits from the disciplines for efficiency that international competition represents. And of course, as well as these ‘business efficiency’ benefits, the availability of a wide range of competitively priced imported consumer goods and services increases the value that all Australians get from their incomes.

These benefits can only be derived by Australia being open to trade and by supporting institutions like the WTO that promote open trade overseas.

Nevertheless, trade liberalisation and the WTO remain contentious for many people. The old debates about free trade vs protection have never completely gone away — even if many of the appeals for protection today are cloaked in the more alluring terminology of ‘fair trade’. Added to this, anti-globalisation protestors are now a common sight at international economic gatherings. In their sights is what one

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protest group has labelled “the anti-environmental, anti-worker, anti-democratic agenda of the corporate-dominated WTO”. And more recently, the US decisions on steel tariffs and farm subsidies have raised concerns in many countries, with some commentators seizing on them to suggest that we need to protect our own industries, or switch our focus to bilateral trade deals.

The Productivity Commission, while having a much broader policy and regulatory mandate than its predecessor organisations, retains a strong interest in trade policy issues and has examined aspects of the recent debate in various reports.

Today, I want to draw on that work to develop three themes:

- first, the WTO and the multilateral trading system *have* generated significant benefits for Australia as well as the world economy;
- second, Australia has a strong interest in continuing to support the WTO and shape its agenda; and
- third, if the WTO is to continue to play a positive role at the international level, it must be underpinned by better decision-making processes at the *national* level in its member countries.

But first I want to dispel a couple of the myths surrounding the WTO.

The global benefits of the World Trade Organization

Whatever its imperfections, many of the criticisms levelled against the WTO in recent years have been simplistic, and sometimes misleading.

Rather than a dictatorial global Leviathan, the WTO’s authority derives from agreement among its members about what behaviour is in their mutual interests. It is essentially an international forum where sovereign governments negotiate and execute agreements *among themselves* to secure the benefits that an open trading system offers. The WTO Secretariat has no executive power and has a budget a fraction of that of many NGOs, such as the WWF.

The multilateral trading system grew out of the economic chaos of the 1930s, when unilateral protection and discriminatory bilateral trade deals prevailed. The WTO’s predecessor — the GATT — and the Bretton Woods institutions established immediately following World War II, were not only about economic recovery and prosperity: they were also about international cooperation and avoiding the earlier ‘beggar thy neighbour’ policies that contributed to the conflict.

The GATT created a system of trade rules around the core principles of transparency and non-discrimination. It was as much about establishing *order* in international relations as achieving lower barriers to trade (though of course the two are linked).

The WTO was established in 1995 to strengthen and expand on the GATT's work. Membership of the WTO is not compulsory: governments can apply to join or can leave at any time. Presumably, the large number of governments that have joined the WTO — there are more than 140 today, compared to the original 23 members of the GATT — have done so because they believe the multilateral trading system benefits their countries.

It is true that, in entering GATT/WTO agreements, member governments accepted constraints on their own actions. Yet when constraints are similarly agreed to in multilateral arms control or pollution control agreements, these are generally seen as evidence of global cooperation for mutual benefit — not as disenfranchising the nation state.

Economic benefits

The multilateral trading system has generated substantial benefits worldwide. Since the GATT's establishment, average tariffs on manufactured goods in industrialised countries have fallen from 40 percent to 4 percent. And notwithstanding some growth in non-tariff barriers, world trade has increased 18-fold. This contributed to the unprecedented rise in average living standards during the second half of the twentieth century.

Of course, other factors such as technological change were also important, but a large body of economic research generally supports the view that liberal trade policies promote higher economic growth.

- A series of detailed country case studies sponsored by the World Bank, the OECD and others from the late 1960s to the early 1980s found that, after accounting for numerous country-specific variables, liberal trade regimes remained a significant factor in better economic performance.
- A recent World Bank study found that since 1980, 'globalising' economies have grown faster than 'non-globalising' economies. On a GDP per person basis, the globalisers outgrew the non-globalisers by more than 35 percentage points during the 1990s alone.
- Cross-country regression studies in the 1980s and 1990s — though not without their individual limitations — consistently found positive links between countries' growth record and their openness to trade.

Critics often respond that this is simply the rich getting richer as the poor get poorer.

This is a big topic in its own right and one that has been assigned to other speakers. Suffice it to say here that, contrary to popular perceptions, there is no robust research showing that global inequality has worsened over the last thirty years. In fact, many developing countries — notably China, India and several in East Asia — have been rapidly closing up on the living standards of the West.

While these developing countries have forged ahead, another group have remained mired in poverty. Yet countries such as Myanmar, Sierra Leone, Rwanda, Albania and North Korea are not in that state because they have liberal trade policies. Rather, responsibility lies with internal institutions and policies that are inimical to economic growth, including political instability and inadequate property rights. Zimbabwe, a country of abundant resources and great economic promise just a few years ago, is perhaps the most telling current example.

History tells us that countries that turn their backs on the world or on liberal domestic institutions can inflict great cost on their own peoples. To a large extent, poverty is a matter of national political choice. Liberal trade is part of the solution, not the problem.

The WTO has some blemishes

That said, the WTO is not without its own deficiencies. As the product of diverse constituent countries it would be surprising if that were not so.

Some of these defects have acted against the interests of developing countries. For example, the GATT essentially provided formal cover for two major sectoral exceptions from its rules — TCF and agriculture — which have particularly disadvantaged developing countries.

These ‘black holes’ are well known and have been the target of recent initiatives within the WTO. A less commonly acknowledged deficiency, however, has been the ‘special and differential treatment’ provisions which have allowed developing countries themselves to retain relatively high barriers to trade, and thus promote inefficiency within their own economies. Moreover, there are many ambiguities and loopholes in WTO rules which provide legal room for all countries to maintain or introduce measures which are fundamentally trade distorting. (Aspects of the Codes on Subsidies and Anti-dumping provide two examples.)

These simply illustrate the point that the WTO is more a servant than a master of its members. It can constrain, but not over-ride domestic political pressures. The recent US steel decision is just the latest illustration of that reality.

The US actions also underline what many would perceive as a key deficiency of the WTO — namely that larger economic powers retain more sway in trade relations than smaller countries.

But there is little doubt that smaller economies would fare much worse without the WTO. Indeed the WTO's rules were originally designed with power imbalances in mind, the MFN clause being the most important expression of this (a point to which I will return). In addition, the 'consensus' basis on which agreements are concluded in WTO negotiations give smaller countries a voice, and the WTO dispute settlement process provides an avenue through which all countries can seek to enforce agreed trade rights. Consequently, while larger players occasionally throw their weight around, they cannot altogether ignore the interests of other countries — which they might well do in the absence of the WTO system.

What's in it for Australia?

Let me illustrate some of the benefits for smaller players by turning specifically to the case of Australia.

Trade is important to Australia's economic prosperity. But since we account for just 1 percent of total world trade, we have little bearing on the prosperity of most other nations. So we could easily be sidelined in international trade relations.

Through our membership of the WTO we have been able to preserve and enhance our economic interests in several ways.

One is by influencing the evolution of WTO rules and the broad directions of its coverage. In my view, Australia has long been able to 'punch above its weight' in these respects. I attribute this in part to our 'honest broker' status on many issues (a role enhanced by our own liberalisation record), but also to the quality of Australian trade representation in Geneva over the years — something I witnessed from the 'other side' during a spell with the GATT Secretariat. Ideas can count as much in international forums as they do in domestic policy formulation.

Secondly, we contrived to compensate for our lack of economic bargaining clout by initiating the Cairns Group of agricultural exporters as a negotiating alliance. It was instrumental in making some progress in the Uruguay Round (notably tariffication) and in getting the EU to the table again in the Doha commitment.

Thirdly, the up-graded dispute settlement provisions within the WTO, while raising the spectre of legalism within an institution founded on diplomatic interpretation, has helped keep some key markets open. Last year's backdown by the United States on lamb is perhaps the clearest example. Similarly, attempts by South Korea to keep our beef out of their market; by the EU to use health standards to discriminate against Australian grains; and by the USA to keep Australian shrimp off their shelves (and BBQs), have all been scuttled following WTO rulings. We will watch the progress of actions taken in the WTO against the recent US steel decision with interest.

Of course the flip-side to this enhanced litigation function of the WTO is that it can be (and has been) used against *us* when we break the rules. But that could be seen as a further source of benefit!

Fourthly, there are many other benefits of the WTO system which we don't hear about because, as most countries abide by most of their commitments most of the time, they are never the subject of a formal dispute.

A key example of the silent workings of the WTO is the most-favoured-nation principle, under which a country that offers a concession to one country must extend the same concession to all WTO members.

To illustrate the effect of this, during bilateral negotiations with China prior to its accession to the WTO, Australia was able to negotiate reduced Chinese tariffs on wine, cheese and various other items. However, the EU later negotiated far deeper tariff cuts. With China's accession, application of the most-favoured-nation rule means that those lower Chinese tariffs now apply to imports from all member countries, including Australia. So, in effect, as a result of the WTO most-favoured-nation principle, we and other smaller countries have been able to piggy-back on the EU's bargaining strength.

This is a specific example of the important general point that while the big countries may dominate in the deal making, the outcomes ultimately have to be shared with all WTO members. The converse implication of this is that, were we ever to withdraw from the WTO, overnight we could face higher trade barriers on a wide range of our exports.

Domestic reform is still the main game

Having said that, it is important to keep the benefits Australia gains from multilateral trade reform in perspective.

While Australia has an obvious interest in encouraging other countries to reduce their trade barriers and keep their markets open, we need to continue to see appropriate domestic economic reform as 'the main game'.

Australia has already undertaken significant reform of tariffs and other trade restrictions because of the benefits it brings to the Australian economy and Australian consumers. The average effective rate of assistance for manufacturing has fallen from 15 percent in the early 1980s to less than 5 percent today. Measured assistance to agriculture has also declined over the last decade, and mining has always received little assistance. We have also moved to liberalise certain restrictions on foreign supply in the services sector.

As well as reductions in border assistance, Australian governments have also undertaken a comprehensive program of pro-competitive reform across a range of areas, including infrastructure, utilities, public services and the labour market. Many of these have been stimulated by the increased competitive pressure on user industries from reduced trade barriers.

Commission research suggests that the microeconomic reforms of the last two decades have contributed to strong productivity and income growth, and to our economy's increased flexibility in the face of foreign economic disturbances. By a range of indicators, Australian firms have become much more innovative and productive. Over the 1990s, Australia's measured productivity growth accelerated to rates rivalling the so-called 'golden age' of the early post-war years, outstripping that of many of our economic peers. And despite the crisis which enveloped several of our major markets in Asia, rapid import growth has been matched by export growth, with Australia's trade participation as a proportion of GDP now a third higher than it was in the mid-1970s.

In general, the benefits we stand to gain from domestic reforms, including reform where appropriate to remaining trade barriers, justify our continuing efforts irrespective of progress internationally.

Against this view, it is commonly argued that Australia should retain trade barriers for strategic purposes — to use them as 'negotiating coin' in trade negotiations.

The value of negotiating coinage depends on the perceived worth of any additional access to our market. Our 1 per cent share of world trade tells much of the story. Our potential market share is larger for some countries in some sectors, but these are generally not key markets of interest to us.

Our inability to 'buy' foreign access — notably in agriculture — helped encourage us to do our sums on the domestic costs and benefits of Australia's own liberalisation, taking as given the position of other countries.

As it turns out, this strategy of 'unilateral' liberalisation has not eroded any of our negotiating leverage. Apart from the possible demonstrational value of our liberalisation efforts, we have been able to enter into agreements to 'bind' our tariffs at lower rates — and it is on such bindings that WTO reciprocity hinges. Thus in its relationship with the WTO, Australia could be said to have had the best of both worlds — benefiting from domestic liberalisation, while gaining recognition for its efforts in subsequent multilateral negotiations.

Key elements of the Doha Round agenda

While we should therefore not let WTO negotiations deflect us from realising potential gains from domestic reforms, where such gains exist, there are important benefits to be had from further multilateral liberalisation and Australia has an interest in pursuing this agenda. The new WTO round launched at Doha in November presents an important opportunity.

Promoting development

The new round has been called the 'development round', and with good reason.

Many developing countries now realise that previous multilateral trade agreements did not yield their promised benefits. The Uruguay Round final agreement allowed developed countries to avoid many important reforms while imposing implementation costs on developing countries. Earlier rounds had also favoured trade growth among developed countries.

The Doha declaration included several provisions that proffer benefits for developing countries, although most of these matters still need to be finalised in detailed negotiations.

There are several reasons for Australia to support developing countries in their efforts to redress the perceived imbalance of past trade liberalisation initiatives.

First, Australia has common interests with many developing countries in the WTO agenda, including in agricultural reform, services and issues such as trade and the environment — which I will discuss shortly. Emphasising the importance of promoting the interests of developing countries could provide additional leverage for Australia in these important areas.

Second, given the ongoing benefits that the multilateral system offers, Australia has an interest is seeing the WTO remain as effective as possible. Developing countries now make up more than two thirds of WTO members, and their active participation in liberalisation of their own economies is important both for their own economic performance, and for developed countries that trade with them.

And third, supporting developing countries' participation in the world trading system, and working to ensure that the system promotes development, is one way in which Australia can contribute to its own goal of reducing poverty abroad.

Agriculture: maybe this *time?*

A key area in which Australia and many developing countries share a common interest is agriculture.

Agricultural reform is politically hyper-sensitive, particularly in the EU. Past trade agreements have done little to limit or reduce agricultural support programs. The WTO Ministerial Conference in Doha involved intense discussions on agricultural protection, with the EU most resistant to reform, and the Cairns group the strongest advocates. The final declaration states:

> …without prejudging the outcome of the negotiations we commit ourselves to comprehensive negotiations aimed at: substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support.

Although this negotiating mandate appears promising — and the Australian delegation was upbeat about this when returning from Doha — there is uncertainty about the extent to which it will translate into substantive reform. Among other things, the EU, which is the main user of export subsidies, has sought to interpret the words "without prejudging the outcome of the negotiations" as an assurance that it will not be driven by the WTO agenda in reforming its use of export subsidies. The history of the GATT/WTO tells us that language loopholes rarely appear by chance, and once there are rarely left unexploited.

The EU's case for maintaining assistance to agriculture, based on its so-called 'multi-functionality', is of dubious merit. While there are undoubtedly desirable social effects and environmental spillovers from supporting agricultural activity, there are also negative ones that have received little scrutiny in Europe — including impacts of high food prices on the poor and the harmful environmental effects of intensive agriculture. Where there are desirable features to be maintained, targetted subsidies which have less impact on trade will generally be preferable. Of course they will also be more visible, but that would provide a useful test of whether they are warranted.

Apart from its benefits to the EU, trade reform in agriculture would bring significant gains to Australian farmers. Australia is one of the world's most efficient producers of beef, wheat, sugar, and dairy products — which are all among the most highly protected agricultural products in global terms. These products also loom large in Australia's total rural production and are important to the fortunes of country Australia.

Quantitative studies have estimated that liberalisation of post-Uruguay agricultural trade barriers would enhance global welfare by at least US$50 billion per year. The bulk of these gains would accrue from a better allocation of resources within the economies of North America, the European Union and Japan.

For all these reasons, Australia has a strong interest in doing whatever it can to promote the liberalisation of agricultural trade.

The services frontier

An increasingly important area on the WTO agenda is services. In Australia, the services sector now accounts for around 80 percent of gross domestic product and employment. Services exports also account for over 20 percent of world trade.

Barriers to trade in services largely take the form of domestic regulations, such as licensing requirements, which restrict the access of service providers to the market. In some cases, there may be benefits associated with the restrictions that outweigh their costs. But in other cases, particularly in the case of discriminatory restrictions against foreigners, the effects are little different from a quota or tariff.

Services are part of the 'built-in' agenda agreed at the conclusion of the Uruguay Round, which was mainly concerned with the framework of rules relating to services trade rather than actual liberalisation.

Recent modelling work by Commission staff, while still experimental, provides some indication of the benefits that could flow from successful negotiations to improved access to services markets. World income is projected to increase by some US$250 billion annually as a result of eliminating all post-Uruguay Round trade barriers. More than half of the gain would come from liberalising services trade. While services restrictions are not as high in Australia as in many other countries, we could still stand to gain about $4 billion annually from global liberalisation of services trade.

Liberalising services trade can be even more politically fraught than goods trade, given the equity and other non-economic dimensions of some services (eg. health, education). Indeed, whether and how competition should be introduced at all is in some cases far from obvious. However where competition is found to be appropriate domestically, treating foreign service providers in a comparable way (‘national treatment’) will generally bring greater benefits.

Unlike merchandise trade, the scope for “concession swapping” within the services sector is inhibited by there being less scope for achieving tradeoffs, favouring (on the traditional reciprocity logic) a cross sectoral approach. For example, it may be that the EU, Japan and the USA might be more willing, or politically able, to offer concessions in agriculture if it buys them access to key services markets in developing countries.

Threats and opportunities for the WTO

The success of the WTO in achieving relatively robust agreements, and its emerging ability to enforce them through dispute settlement processes, have made it an attractive forum for pursuing other agendas with trade connections.

Some of these may be able to be accommodated, but others pose significant risks for the institution’s core business.

Investment liberalisation?

With the growth of the services sector and its inclusion within the WTO, the question of that institution’s ability to make progress on the liberalisation of international direct investment has come into prominence — especially following the failure of the MAI initiative within the OECD. But, as that experience demonstrated, the domestic political obstacles in this area can be substantial. This after all was the issue that first galvanised NGOs opposition to ‘globalisation’ prior to the WTO debacle in Seattle.

That is not to say that barriers to investment should not be tackled through an international agreement, nor that the WTO could not eventually be an effective forum to do it. But as a recent Commission survey has shown, FDI is growing rapidly already. Some of it is being driven by the need to get behind barriers to conventional trade (automotive investments in Asia being a case in point). What is clear is that more preparatory work will be needed before negotiations on a new investment agreement could begin among WTO members.

Environmental standards

The EU's push to have environmental matters placed on the WTO agenda also poses some difficulties for the organisation.

There *are* some specific cases in which the non-discriminatory nature of WTO agreements can constrain the ways in which environmental objectives can be pursued. For example, WTO rules limit the extent to which governments can discriminate among imports according to methods of production, including environmentally unsustainable production processes (although recent decisions by the WTO's Appellate Body have made this area a little grey). The consistency of trade sanctions provided for in multilateral environmental agreements with WTO rules is also unclear.

However, the Commission has found that many of the environmental concerns about the WTO — such as it promoting a 'race to the bottom" in standards — do not stand up to close scrutiny. Further, trade sanctions are generally poor means of addressing environmental problems, which have their origin in production and consumption decisions that are much more effectively targeted at source.

While WTO rules constrain environmental policy makers to a degree, it is not clear that the balance struck is inappropriate from the view of overall community welfare. Moreover, moves to modify the WTO agreements could open the door to protectionist abuse. Developing countries, in particular, have indicated their opposition to environmental policies linked to trade agreements.

Consequently, loading such issues onto the WTO agenda threatens to frustrate trade reform, potentially to the detriment of the environment as well as the global economy.

Labour standards

Developing countries are even more strongly opposed to embodying labour standards provisions in WTO agreements, particularly where failure to comply could provide grounds for trade sanctions. The linkage of labour standards to trade measures was of course the issue that brought the Seattle meeting unstuck. It is notably absent from the Doha declaration. The Commission's recent examination of the issue would suggest that that omission is not to be regretted. This reflects not only the risks for the trading system of such an approach, but also its likely ineffectiveness relative to other options for generating better living and working conditions in developing countries.

Regional trade arrangements

A more direct challenge for the WTO is posed by the escalation in regional (typically bilateral) trading arrangements over the past decade. Such arrangements are sometimes seen as building blocks for multilateral liberalisation, but they can also constitute stumbling blocks. The exchange of tariffs or other preferences may generate new trade, to the benefit of members and their trading partners. It may also divert trade from more efficient producers to less efficient RTA members, to the detriment of both members and third parties.

It is in Australia's interests to see WTO rules enforced that would prevent the formation of the sort of RTAs that would harm third parties.

But what about Australia's interests in *participating* in RTAs? The emerging conventional wisdom is that, in a world of trading blocs, it could prove costly to be left out. But whether or not it pays for us to join depends on who the other members are — and who is left out — and what sort of preferential deal is on offer. A deal with a major trading partner like the USA or Japan which excluded agriculture, for example, is unlikely to be in our economic interests.

The reality of RTAs is that unless there is an overriding political imperative, they tend to happen between economies that do not pose significant competitive threats for each others' industries. But a good rule of thumb for RTAs is 'no pain, no gain'. In these circumstances, multilateral agreements still look the best option — as they can provide more scope for tradeoffs. When considering bilateral or other regional agreements, Australia needs to be clear about what we want, and about the wider costs and benefits of achieving it.

Shoring up national support

Beyond the positions that governmental negotiators might take on particular agenda items, the success of trade liberalisation and the WTO ultimately depends on community understanding and support for such policies among the populations of WTO member countries.

Such understanding and support will almost never predominate without some systematic help from governments. Otherwise the old political calculus of concentrated losers from liberalisation dominating over the more diffuse winners will generally prevail. Political leadership is clearly an important ingredient, as President Bush appears to have recognised in the following passage from a recent speech:

> By failing to make the case for trade, we have allowed a new kind of protectionism to appear. It talks of workers, while it opposes a major source of new jobs. It talks of the environment, while opposing the wealth-creating policies that will pay for clean air and water in developing nations. It talks of the disadvantaged, even as it offers ideas that will keep many of the poor in poverty.

However as the subsequent US protective action on steel (and many previous actions) attests, such leadership needs to be underpinned by processes that can enable the tradeoffs in policy choices to be more apparent when decisions are actually being made.

Without mechanisms to make and remake the case for trade liberalisation, and to highlight the costs of protection to the inhabitants of the country considering protection, sectional interests in those countries — whether they be American steel millers, French cheese farmers or Japanese rice growers — will continue to meet with success at the cost of their own economies as well as ours.

The WTO is in a weak position to influence domestic political opinion. In fact, while the commitments made in the WTO act as a constraint on ad hoc protectionism, the WTO negotiations themselves can exacerbate misunderstandings about the benefits of trade liberalisation. The reciprocal exchange of 'concessions' between countries — "I'll cut my tariffs if you cut yours" — allows politicians to sell the benefits of WTO deals to particular domestic constituencies. But it simultaneously reinforces a mercantilist view of the gains from trade liberalisation — that increased exports are good for a country whereas imports are not.

A further difficulty for the WTO, is that concerns about its effects on 'national sovereignty' have been reinforced as governments have extended its rules beyond barriers to merchandise trade to include more ostensibly 'domestic' issues — such as trade in services, rights to provide services from within foreign countries, and regulation to do with domestic subsidies, quarantine and intellectual property.

The concerns of NGOs about this extension of the WTO's realm have spilled over into the international arena in protests at successive forums from Seattle on. This has happened in large part because these groups have felt disenfranchised at the national level. NGOs probably have a point when they argue that in most countries corporations have more opportunity to consult with governments about trade policy matters than they do. If NGOs do not have an input at the national level, they will continue to target the WTO — which as a forum for negotiation among sovereign governments is neither designed nor equipped to accommodate them.

There is a clear need for better decision-making processes in WTO member countries, to identify and debate the domestic tradeoffs in the increasingly sensitive areas of international trade and investment policy. What arrangements are put into effect are of course a matter for each government. It is an area, however, where Australia's own experience over the years in publicly assessing the costs and benefits of trade restrictions has something to offer. Indeed, I believe that this conference itself is a tangible expression of the importance of a well-informed domestic debate in achieving better outcomes at the national and international levels.

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